ClearOne®

# 2016 ANNUAL REPORT

# WHAT WE DO

**ClearOne** enhances communication and collaboration for organizations worldwide, from the Fortune 500 to small and medium businesses and institutions. We design, develop, and sell conferencing, collaboration, network streaming & signage solutions through a global network of expert AV and IT practitioners who specify, install, and support our advanced hardware, software, apps, and cloud solutions.

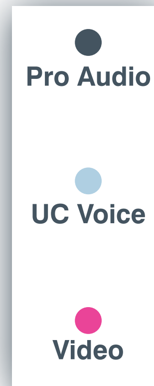
The performance and simplicity of our comprehensive product lines enable unsurpassed levels of functionality, reliability, and scalability.

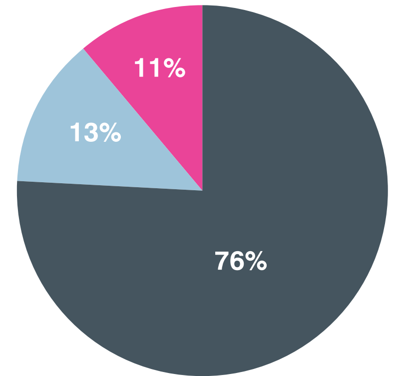
From ad-hoc work spaces and mobile conferences to the largest meeting venues and boardrooms, ClearOne is the best-in-class option for any industry or organization that relies on teamwork and collaboration to be successful.

# 2016 AT-A-GLANCE

## Investment Rationale

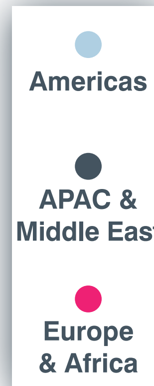
The only Pro AV source that connects, interoperates and scales across enterprises of any size, for any workspace, for all conferencing, collaboration and network streaming applications.

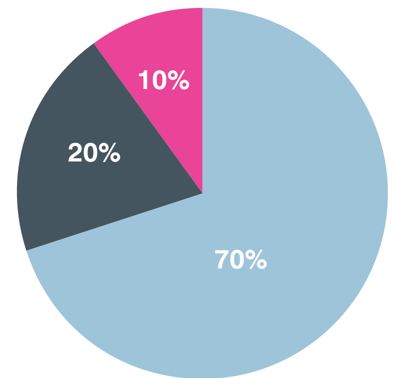



## The ClearOne Opportunity

+ Delivering disruptive solutions
+ Expanding into adjacent markets
+ Leveraging software-based video platforms that complement our audio
+ Increasing the ClearOne value chain for partners
+ Addressing multiple customer needs — any time, any place, anywhere




"ClearOne continues to strike a balance between competitive pricing and top notch technologies which sets it apart from competitors."

Frost and Sullivan, Mar. 2017

| | | | | |
|---|---|---|---|---|
| $48.6 Total Revenue (millions) | 61% Gross Margin | $38.5 Cash & Investments at Year End (millions) | $0.20 Dividends Per Share | $1.8 Dividends Paid (millions) |
| $0.53 Non-GAAP Diluted EPS* | $8.6 Non-GAAP Adjusted EBITDA (millions)* | $0 Debt at Year End | 542,000 Number of Shares Repurchased | $6.1 Shares Repurchased (millions) |

* The non-GAAP measures discussed above exclude certain costs and expenses from GAAP results. A reconciliation between the GAAP and non-GAAP financial measures can be found at the end of this document.

# PROFESSIONAL VOICE CONFERENCING

## *State-of-the-art audio technology*

ClearOne's professional audio conferencing systems bring state-of-the-art audio technology to large-scale conferencing venues such as boardrooms, conference rooms, courtrooms, training centers, and telemedicine facilities.

These voice conferencing systems handle multiple audio inputs and outputs and perform various sophisticated audio processing functions, to deliver the high-quality and immersive audio conferencing critical for enabling productive meetings.

CONVERGE® Pro 2

CONVERGE® Pro

INTERACT® Pro

# PROFESSIONAL MICROPHONES

*Most innovative in the market*

Beamforming
Arrays
Ceiling Arrays
Wireless Systems
Tabletop

ClearOne's professional microphones are the most innovative in the market. Optimized for our professional voice conferencing, media collaboration, and audio distribution products, the game-changing beamforming microphone arrays, the scalable wireless microphone systems, and the powerful ceiling microphone arrays deliver seamless, crystal-clear voice for any conferencing venue.

# UC VOICE

## *Award-winning rich audio*

ClearOne offers a broad portfolio of award-winning products designed to enhance the user's unified communications experience, from the desktop to the small working conference room—each solution boasting ClearOne's unmatched, rich audio performance.

- CHAT®
- CHATAttach®
- MAX®
- MAXAttach®
- INTERACT® AT

# MEDIA COLLABORATION

*Software-based for cloud or room*

COLLABORATE®

SPONTANIA™

UNITE®

ClearOne's software-based media collaboration solutions set themselves apart from anything available in the market. Our portfolio features award-winning cloud-based services for video, audio, and data collaboration using any device and low-cost appliances for conference rooms.

Without the burden of expensive hardware or infrastructure investments, our media collaboration solutions also include wireless presentation and whiteboarding, streaming, recording, and multi-party conferencing.

# NETWORK MEDIA STREAMING AND SIGNAGE

## *Highest-quality for IP networks*

ClearOne's IP-based media streaming solutions provide the highest-quality media streaming on existing IP networks, unmatched in scalability, ease of implementation, and lowest total cost of ownership.

Powerful new features can be added via fast and easy software license purchases to ensure that one-time hardware investments are "future proof", and can be continuously upgraded as needed.

VIEW®

MagicBox®

*Flexible & scalable architecture*

CONVERGE® Pro 2 SR

CONVERGE® Pro SR

CONVERGE® Matrix

CONNECT®

ClearOne provides Sound Reinforcement Audio DSP mixers and Dante based Audio Distribution mixers. Audio distribution is based on Dante digital networking technology, which increases the scalability and interoperability with any Dante based devices.

## A sample of our blue-chip customer base...

All product names, logos, and brands are property of their respective owners and are for identification purposes only.

Dear Fellow Shareholders,

2016 was a pivotal year. We launched a number of new, very strategic products. We solidified our position as a conferencing and collaboration solutions provider and as a leader in the installed audio conferencing market. According to Frost & Sullivan's latest analysis released in December 2016, ClearOne captured a 55.8 percent share of 2015 global installed audio conferencing endpoints revenue, up from 51.5 percent the previous year. We continued to create shareholder value through our generous dividend and stock repurchase programs. Overall, we fortified our underlying fundamentals and set the stage for a better 2017. Today, ClearOne is the only source that brings the full value chain to the AV conferencing, collaboration, and network streaming markets. This achievement was enabled by the benefits from our strategic acquisitions and internal technology development. We are confident in ClearOne's business and long-term prospects given the momentum in our video solutions and the market's strong positive response to our next-generation flagship audio conferencing platform launched in June.

**Financial Results**

2016 revenue was $48.6 million, compared to $57.8 million in 2015. The decrease reflects that the transition to our new audio conferencing platform, announced in June 2016, took longer than expected to ship, and delayed customer purchasing decisions. Further, demand in all our geographies except some parts of Asia was dampened by continued challenging global economic conditions and political uncertainty including Brexit and US elections. Regardless, our newer video products contributed over $5 million in revenue in 2016, growing 40% over 2015. We are extremely pleased with video's performance and believe it will continue to grow in contribution in 2017. Also, our balance sheet remains very strong with cash, cash equivalents and investments at $38.5 million and no debt at December 31, 2016.

**Investment in Shareholder Value**

ClearOne continued to create value with dividend and share repurchase programs. In 2016, the company paid a $0.05-per-share quarterly dividend, which amounted to $1.8 million in dividend payments, and repurchased $6.1 million of our common stock. In addition, in March 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. The board also extended our stock repurchase program for up to an additional $10 million over the next twelve months.

**New Product Development**

We invest in new ideas and technology that enable market transformation in our industry. During 2016, we strengthened the IP portfolio, increasing our patent count to 74 and pending applications to 31. These important core assets protect our groundbreaking technology and represent significant value for the company covering cutting-edge technologies in the fields of

audio and video signal processing, audio and video streaming, and communication technologies including cloud-based video conferencing. This ongoing development of new patents continues ClearOne's market leadership position and our strong history of product innovation.

We also introduced the following new products during the year:

- At InfoComm in June 2016, we unveiled our CONVERGE® Pro 2 platform that delivers stunningly clear audio, thanks to the world's most advanced audio signal processing. It is scalable, reliable and competitively priced and will outperform any competitive product in any sized room, any audio environment and any application. Its versatility is second to none. We expect our new fourth-generation platform will reinforce our dominant leadership position in the installed audio conferencing market. This immensely powerful and competitive platform has generated phenomenal excitement from our channel partners and our end-users. We began shipping a limited number of SKUs in the fourth quarter, and by the end of first quarter 2017, we were shipping all 10 SKUs of CONVERGE Pro 2 as well as our award-winning Beamforming Microphone Array 2.

- The new Beamforming Microphone Array 2 is optimized to complement and operate with ClearOne's next-generation CONVERGE Pro 2 audio platform. Representing the apex of voice conferencing, the Beamforming Microphone Array 2 comprises the industry's most sophisticated audio beamforming by delivering significantly enhanced echo cancellation for the most demanding acoustic environment, faster convergence and more advanced adaptation to changes in room acoustics. It provides dramatically enhanced mic pick up, sharpening the capability to detect softer voices as well as natural and clearly intelligible audio even when two people speak at the same time.

- The new DIALOG® 20 is a compact two-channel wireless microphone system packed with innovative features that increases the breadth of ClearOne's wireless microphone product line. The new wireless microphone system targets usage in which only a few wireless mics are required, such as in classrooms, presentation and training venues, huddle rooms and other smaller spaces.

- The new VIEW® Pro E110 encoder and new D310 decoder complement our existing network media streaming solution. The E110 video encoder is a single-channel alternative to the popular dual-channel encoder and provides the lowest-cost encoder for customers preferring a single-channel option. The D310 decoder enables basic display of a single-image video application while delivering superb price-to-performance value.

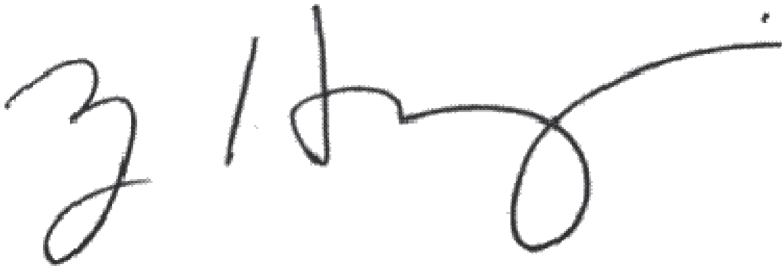
ClearOne's strength, exceptional audio, is the cornerstone and springboard for effective conferencing and collaboration. Just as the telephone handset served the need of communications a generation or more ago, today, the winning combination of great audio with rich video applications for dispersed teams, wherever they are — on the road, at their desk, in a huddle space or a conference room of any size — is the key for market adoption and success.

While there are solution providers who can provide audio or video or both, ClearOne uniquely differentiates itself in the market. We are the only player in the Pro AV market that can connect, interoperate, and scale across enterprises of any size, for any workspace, for all conferencing, collaboration and streaming applications. These capabilities extend our addressable market to more workspaces and more businesses worldwide. We are building positive sales momentum with our newly introduced core audio platform and the investments we have made in video, including media collaboration for cloud or premise, and network media video streaming. Now, we are ready to invest in broadening our sales and marketing reach through a variety of initiatives and activities to accelerate our momentum in the market in 2017. Through our end-to-end product portfolio, exceptional product quality, longstanding commitment to industry innovation and strong partner ecosystem, we are positioned to grow as we enter the emerging market of team collaboration and communication solutions for cloud or premise with our disruptive solutions.

We are forging ahead with utmost confidence in our products, people and the execution of our strategies. We are excited by the responses from our partners who have been evaluating our next-gen audio platform and who are giving it phenomenal reviews which match the enthusiasm of our sales and marketing team. As a distinguished brand bringing the full value chain to the professional AV market, ClearOne is well positioned to return to growth in 2017 while our strong balance sheet enables us to pay dividends and repurchase stock, and invest in our future; continuing to create shareholder value.

On behalf of the board and management, we thank you for your continued interest in ClearOne.

Sincerely,



Zee Hakimoglu
Chairman, President and Chief Executive Officer
March 29, 2017

## SELECTED FINANCIAL DATA

(Dollar in thousands, except per share data)

| Year Ended December 31, | 2016 | 2015 | 2014 | 2013 | 2012 |
|---|---|---|---|---|---|
| Revenue | $ 48,637 | $ 57,796 | $ 57,909 | $ 49,592 | $ 46,417 |
| Gross margin | 29,487 | 36,719 | 35,323 | 29,897 | 27,328 |
| Operating income | 3,566 | 10,262 | 7,975 | 7,622 | 42,521 |
| Net income | 2,444 | 6,776 | 5,596 | 5,179 | 26,647 |
| Diluted earnings per share | 0.26 | 0.71 | 0.58 | 0.55 | 2.89 |
| Cash dividends declared per share | 0.20 | 0.155 | 0.10 | — | — |
| Cash, cash equivalents, and short-term investments | 17,130 | 20,573 | 14,434 | 20,392 | 55,509 |
| Working capital | 30,819 | 36,539 | 30,202 | 39,417 | 56,467 |
| Total assets | 88,124 | 93,529 | 88,860 | 81,061 | 91,939 |
| Long-term obligations | 1,354 | 1,353 | 2,089 | 2,077 | 2,451 |
| Stockholders' equity | 77,449 | 82,569 | 76,016 | 70,335 | 66,668 |

## QUARTERLY STOCK PRICE

Our common stock has traded on the NASDAQ Capital Market under the symbol CLRO since August 14, 2007. The following table sets forth high and low sale prices (or high and low bid quotations) of our common stock for each fiscal quarter indicated as reported on the NASDAQ Capital Market.

| | First Quarter | Second Quarter | Third Quarter | Fourth Quarter | Full Year |
|---|---|---|---|---|---|
| **2016** | | | | | |
| High | $ 13.15 | $ 11.68 | $ 12.36 | $ 11.40 | $ 13.15 |
| Low | 10.60 | 10.21 | 10.32 | 10.40 | 10.21 |
| **2015** | | | | | |
| High | $ 11.32 | $ 14.65 | $ 14.05 | $ 13.45 | $ 14.65 |
| Low | 9.25 | 10.07 | 9.95 | 11.36 | 9.25 |

On March 15, 2017, the closing price for our common stock as reported on the NASDAQ Capital Market was $10.50.

As of March 15, 2017, there were 8,746,870 shares of our common stock issued and outstanding and held by approximately 322 shareholders of record. This number includes each broker dealer and clearing corporation that holds shares for customers as a single shareholder.

## DIVIDENDS

During 2016 and 2015, our Board of Directors declared the following dividends:

| Declaration Date | Record Date | Payment Date | Dividend per share | Dividends (S thousands) |
|---|---|---|---|---|
| March 12, 2015 | May 04, 2015 | May 15, 2015 | $ 0.035 | $ 319 |
| July 15, 2015 | July 27, 2015 | August 10, 2015 | 0.035 | 320 |
| October 21, 2015 | November 04, 2015 | November 18, 2015 | 0.035 | 320 |
| November 12, 2015 | December 04, 2015 | December 21, 2015 | 0.050 | 457 |
| 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 |

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 expected to be paid on or about June 1, 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.

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.

During the twelve months ended December 31, 2016 we acquired the following shares of common stock under the current stock repurchase program:

| Period | Total Number of Shares Purchased | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (in $ millions) |
|---|---|---|---|---|
| March 9 to March 31 | 33,600 | $ 12.02 | 33,600 | $ 9.6 |
| April 1 to June 30 | 330,515 | 11.25 | 330,515 | 5.9 |
| July 1 to September 30 | 91,965 | 11.16 | 91,965 | 4.9 |
| October 1 to December 31 | 86,179 | 11.00 | 86,179 | 3.9 |
| Total | 542,259 | 11.25 | 542,259 | |

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.

## 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 and 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 the captions “Business Description” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations” included in this Annual Report. 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 our Annual Report on Form 10-K for the year ended December 31, 2016 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.

## BUSINESS DESCRIPTION

References in this Annual Report 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.

### 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; Israel, Spain and United Arab Emirates.

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

We design, develop, market, and service a comprehensive line of high-quality conferencing 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.

### Acquisitions

On April 1, 2014, we completed the acquisition of Spontania from Spain-based Dialcom Networks, S.L. in an all-cash deal for €3.66 million (approximately US$5.1 million). Spontania, a software-based cloud collaboration solution, combines the benefits of video conferencing and web conferencing into an enterprise solution that can scale to tens of thousands of users. The addition of Spontania was made with the intent to make us the only company offering an entirely software-based video conferencing product line and to provide on-premise cloud-based Software-as-a-Service (SaaS) and Platform-as-a-Service (PaaS) solutions complementing our existing premise-based, enterprise video conferencing offering, COLLABORATE®.

On March 7, 2014, we completed the acquisition of Sabine, Inc. ("Sabine") through a stock purchase agreement ("SPA"). Sabine manufactured, designed and sold Sacom professional wireless microphone systems for live and installed audio. It also manufactured the FBX Feedback Exterminator for reliable automatic feedback control. With the addition of Sabine, we have reliable and exclusive access to the wireless microphones that are a critical component of our complete microphone portfolio. Pursuant to the SPA, we paid initial consideration of $6.89 million in cash and approximately $1.68 million in ClearOne shares. In addition, we paid off Sabine debt of $1.25 million and may be required to make earn-out payments over a three-year period from the acquisition date based on achievement of certain performance criteria.

On February 16, 2012, we completed the acquisition of the video conferencing business of Israel-based VCON Video Conferencing, Ltd. ("VCON"). VCON was a pioneer in software based video conferencing solutions with product offerings that include group video conferencing endpoints, desktop video conferencing endpoints, video conferencing infrastructure solutions and software development kits. This acquisition and the combination of our streaming and digital signage technologies has provided us with complementary technology opportunities allowing us to enter new growth markets. Pursuant to the asset purchase agreement, ClearOne paid consideration of $4.6 million in cash to VCON in consideration for all the assets, including intellectual property, fixed assets and inventory, and assumed no debt.

**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" in our Annual Report on Form 10-K for the year ended December 31, 2016.

**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 and training tools;
- Network streaming and digital signage which includes audio and video networking, media streaming, video walls and digital signage; 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 enter new growth markets;
- Focus on the small and medium business (SMB) market with scaled, lower cost and less complex products and solutions;
- Capitalize on the growing adoption of information technology channels 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; and
- 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.

## 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, and
- 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 78%, 80% and 77% of our consolidated revenue in 2016, 2015 and 2014, 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, CONVERGE Pro 2 and CONVERGE SR product lines.

Our flagship CONVERGE Pro product line leads 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. CONVERGE Pro 2's 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 and/or the new DIALOG® 20 Wireless Microphone system; and
- New software that includes both a traditional matrix view and the unique ClearOne FlowView™.

*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 adaptive steering technology 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, adaptive steering, 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.

Beamforming Microphone Array 2, the next generation Beamforming Microphone Arrays started shipping in the last quarter of 2016. 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 DSP mixer.

*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*

ClearOne also 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. The wireless system combines ease-of-use with the most reliable security and power. ClearOne began shipping the WS800 Wireless Microphone Systems in January 2013. Through the Sabine acquisition, we also began shipping Sacom branded Wireless Microphone Systems in 2014. During 2015, 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.

***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 11%, 13% and 17% of our consolidated revenue in 2016, 2015 and 2014, respectively.

*Traditional Tabletop Conferencing*

Our MAX® product line is comprised of the following product families: MAX EX and MAXAttach® wired phones; MAX Wireless and MAXAttach Wireless; and MAX IP and MAXAttach IP VoIP 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.

*Personal Conferencing Products*

Our CHAT® product line includes affordable and stylish personal speakerphones and USB headsets. CHAT speaker phones 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 speaker phones are offered as personal speakerphones and group speakerphones.

CHAT personal speakerphones are approximately the size of a deck of cards, and connect to PCs and MACs, laptops, tablets, enterprise handsets, smartphones, cell phones, and MP3 players for rich, clear, hands-free audio and playback. CHAT 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 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 group speakerphones which can be daisy-chained together to function as a single conferencing system.

***VISUAL COMMUNICATIONS***

Our visual communication products include media collaboration and network streaming products. Our visual communication products contributed 11%, 7% and 6% of our consolidated revenue in 2016, 2015 and 2014, respectively.

*Media Collaboration*:

Our comprehensive portfolio of industry-leading COLLABORATE® branded HD videoconferencing solutions bring cutting-edge software-based full HD (1080p) video conferencing technology with H.264 High Profile encoding that reduces bandwidth utilization up to 50 percent. COLLABORATE is comprised of feature-rich room systems and desktop video applications, as well as enhanced network management, infrastructure solutions and software development kits.

COLLABORATE Infrastructure is for customers who desire an on-premise infrastructure solution. ClearOne offers a single-unit infrastructure server that will serve the needs of both the small to mid-sized businesses and enterprise customers hoping to expand locations. The heavy burden of adding video collaboration pervasively has always been the cost of expensive infrastructure solutions. ClearOne's single-unit solution provides the infrastructure component at a low price, including directory services, firewall traversal, MCU, H.323 gatekeeper, SIP registrar, license server, call control, and a full management system.

COLLABORATE Desktop is a versatile application for any PC or laptop user in organizations of any size. Available with up to 1080p resolution, the COLLABORATE Desktop offers multiple media transmitting capabilities for video, audio and data. Using ClearOne's DualStream™ technology, the application has the ability to send and receive video and data streams simultaneously. With its additional streaming capability, ClearOne's Simulcast™ allows COLLABORATE Desktop users to chair or participate in corporate broadcasts.

COLLABORATE Room is a best-in-class video conferencing and collaboration solution offering a price-point and feature set vastly superior to that of competing room conferencing solutions. Designed for small and medium businesses and corporate meeting rooms, the COLLABORATE Room features software-based and server-less embedded multipoint (up to 9-way) video conferencing, SIP/H.323 bridging interoperability, built-in recording and streaming, built-in remote content and data sharing, and interactive multicast.

The new COLLABORATE® Room Pro all-in-one appliance combines high-definition 1080p60 video with ClearOne's wildly popular Beamforming Microphone Array for the best audio available on any self-contained video conferencing solution, without using an external DSP unit for audio processing. This new system, available with a 9-party MCU, also includes many media collaboration tools that usually purchased separately, such as: streaming, recording and content creation, and presentation.

UNITE™ PTZ Camera complements the COLLABORATE product line, and comes with DVI-I (for digital and analog output) and USB 3.0 connectivity that enables users to easily add Full-HD video to UC or video applications running on desktop/laptop. With powerful optical zoom and wide field of view make this camera more suitable for medium to large meeting spaces. Full high definition video in up to 1080p60 resolution helps the remote sites in video conferencing see every detail, even when displayed on a large screen. During the first quarter of 2016 we launched the ClearOne UNITE® 200 PTZ Camera, a superbly versatile, professional-grade, HD video camera complete with USB, HDMI, and IP connections that can be used for the widest possible range of applications at a price significantly lower than competitive models.

Through the Spontania acquisition in 2014, ClearOne started offering Spontania cloud-based Media Collaboration solutions. Spontania empowers customers to deploy video collaboration without the heavy burden of expensive infrastructure. It also allows service providers and partners to expand their offerings by deploying the technology within their own networks. Spontania complements ClearOne's premise-based COLLABORATE enterprise video collaboration portfolio. The complete ClearOne video portfolio now can serve a full range of video collaboration needs for enterprise, SMB, healthcare, education, and other customers, whether they are seeking those solutions deployed in their private data centers or in the ClearOne Spontania cloud. ClearOne now offers its partners and end users a clear choice between public cloud, private cloud, and on-premise solutions.

*Network Streaming and Digital Signage*:

Our network streaming products 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.

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 and single output decoder with balanced audio, general purpose control ports and clock synchronized video output. VIEW Pro system also provides multi-view video composition and video-wall features 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 and D210 decoders. VIEW Pro solution also comes with multiple license options including audio mixing, video composition, video wall, multicast RTSP, local playback and USB HID.

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 installations using an easy, and 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.

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.

## MARKETING AND SALES

We primarily use a two-tier channel model through which we sell our commercial products to a worldwide network of independent 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 | 2016 | | 2015 | | 2014 | |
|---|---|---|---|---|---|---|
| | Revenue | % | Revenue | % | Revenue | % |
| In the United States | $ 31.8 | 65 % | $ 39.6 | 68 % | $ 39.8 | 69 % |
| Outside United States | 16.8 | 35 % | 18.2 | 32 % | 18.1 | 31 % |
| | $ 48.6 | 100 % | $ 57.8 | 100 % | $ 57.9 | 100 % |

We sell directly to our distributors, resellers and end-users in approximately 60 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 341 distributors and direct resellers throughout the world during 2016. 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 and our MagicBox branded digital signage products on our website www.magicboxinc.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 16.3% of consolidated revenue during the year ended December 31, 2016 with no other customer accounting for more than 10 percent. During the year ended December 31, 2015 sales to Starin Marketing and VSO Marketing represented approximately 14.2% and 10.4% of consolidated revenue, respectively. During the year ended December 31, 2014 sales to Starin Marketing represented approximately 16% 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 $3.9

million and $4.5 million as of December 31, 2016 and 2015, respectively. We had a backlog of unshipped orders of approximately $0.6 million and $0.2 million as of December 31, 2016 and 2015, respectively.

**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.

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, Biamp, Bose, Crestron, Extron, Harman, Peavey, Phoenix Audio, Polycom, QSC, 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, Beyerdynamic, Biamp, Clock Audio, Lectrosonics, Media Vision, Nureva, Phoenix Audio, Polycom, Sennheiser, Shure, TeachLogic, TOA and Yamaha 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 and Yamaha and their OEM partners.

Our video conferencing products face tremendous competition from well established players as well as emerging players, including Acano, Avaya, Aver, Barco, Blue Jeans, Cisco, Citrix, FuzeBox, Huawei, InFocus, Kramer, Logitech, Magor, Microsoft, Pexip, Polycom, Starleaf, Telylabs, UNIFY, Vidyo, Yealink, Zoom and ZTE. 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 Atlona, Aurora Multimedia, Barco, Biamp, Broadsign, Cisco, Crestron, Extron, Gefen, Goopie, Haivision, Hall Research, Infocus (Jupiter), Key Digital, Kramer, Liberty AV, Magenta Research, Matrox, Mediasite, Ncast, RGB Spectrum, Scala, Spinetix, SVSi Volante, Teracue, Tightrope, tvONE, UCView, VBrick, Visionary Solutions, Visix, WyreStorm and ZeeVee. We believe that our pioneering and patented StreamNet technology delivers superior audio and video streaming performance and flexibility and provides us with a competitive edge over other industry players.

**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.

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 except a few digital signage 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**

Our revenue has historically been the strongest in the fourth quarter and the weakest in the first quarter, even though a consistent pattern could not be established for seasonality between the quarters. There can be no assurance that any historic sales patterns will continue and, as a result, sales for any prior quarter are not necessarily indicative of the sales to be expected in any future quarter.

**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 $8.6 million, $8.3 million and $9.0 million, during the years ended December 31, 2016, 2015 and 2014, 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.

**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. The laws of foreign countries may not protect our intellectual property to the same degree as the laws of the United States.

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.

**Employees**

As of December 31, 2016, we had 151 full-time employees. Of these employees, 93 were located in our Salt Lake City location, 31 in other U.S. locations, and 27 in locations outside the U.S. None of our employees are subject to a collective bargaining agreement and we believe our relationship with our employees is good. We also hire contractors with specific skill sets to meet our operational needs.

## 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 in our Annual Report on Form 10-K for the year ended December 31, 2016 and elsewhere in this report.

## OVERVIEW

ClearOne is a global Company that designs, develops and sells conferencing, collaboration, and network streaming & signage solutions for voice and visual communications. The performance and simplicity of our advanced, comprehensive solutions offer unprecedented levels of functionality, reliability and scalability.

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

During 2016, we devoted most of our attention to the introduction of our full line of next-gen DSP conferencing platform and Beamforming Microphone Array. We also fine-tuned our product and go-to-market strategy for our media collaboration and network streaming products. On the operations side, we successfully transitioned our wireless microphones manufacturing operations from Alachua, Florida to an outsourced contract manufacturing facility in Singapore.

Overall revenue declined in 2016 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 gross profit margin decreased in 2016 to 61% compared to 64% in 2015 primarily due to the decrease in the mix of higher margin products and the price reductions associated with transition from CONVERGE Pro 1 to CONVERGE Pro 2. Net income decreased to $2.4 million from $6.8 million in 2015. Net income in 2016 decreased primarily due to decrease in gross margins.

*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 global economics conditions through 2016 were challenging due to a number of reasons, including conditions related to the Brexit vote and uncertainty surrounding the outcome of the U.S. presidential election. The decline in oil prices and commodity prices continued to affect certain countries and the operating budgets of large companies in the oil and gas industry.

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 Converge Pro 1 platform to the next generation Converge Pro 2 platform. Our strength in this space is largely due to our professional microphone products, especially Beamforming Microphone Arrays. Despite our strong leadership position in the professional audio communications products market, we face challenges to revenue growth due to the limited size of the market and pricing pressures from new competitors attracted to the commercial market due to higher margins.

Revenue from our video products in the overall revenue mix has been improving on the back of a strong growth for our video products in 2016. 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 provide high growth in revenue in the near future. 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 (about 35%) from international operations and expect this trend to continue in the future. Most of our revenue from outside the U.S. are 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 continues to be 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 decreased by $0.7 million to $3.9 million in 2016. In 2015 deferred revenue decreased by $0.5 million from $5.0 million at the end of 2014 to $4.5 million at the end of 2015.

**DISCUSSION OF RESULTS OF OPERATIONS**

The following table sets forth certain items from our consolidated statements of operations for the years ended December 31, 2016, 2015 and 2014, together with the percentage change each item represents. Throughout this discussion, we compare results of operations for the year ended December 31, 2016 ("2016") to the year ended December 31, 2015 ("2015" or "the comparable period") and to the year ended December 31, 2014 ("2014" or "the comparable period").

| (In thousands, except percentages) | 2016 | 2015 | 2014 | Percentage Change 2016 vs 2015 | Percentage Change 2015 vs 2014 |
|---|---|---|---|---|---|
| Revenue | $ 48,637 | $ 57,796 | $ 57,909 | -16% | 0% |
| Cost of goods sold | 19,150 | 21,077 | 22,586 | -9% | -7% |
| Gross profit | 29,487 | 36,719 | 35,323 | -20% | 4% |
| Sales and marketing | 10,032 | 10,646 | 11,227 | -6% | -5% |
| Research and product development | 8,564 | 8,318 | 8,969 | 3% | -7% |
| General and administrative | 7,325 | 7,493 | 7,152 | -2% | 5% |
| Operating expenses | 25,921 | 26,457 | 27,348 | -2% | -3% |
| Operating income | 3,566 | 10,262 | 7,975 | -65% | 29% |
| Income before income taxes | 3,878 | 10,551 | 8,229 | -63% | 28% |
| Provision for income taxes | 1,434 | 3,775 | 2,633 | -62% | 43% |
| Net income | 2,444 | 6,776 | 5,596 | -64% | 21% |

**Revenue**

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 2015 to 12% in 2016.

During 2016, revenue declined across all major markets except parts of Asia. The decline was pronounced in Australia, Canada, Middle East and all regions of Europe. Asia Pacific including Middle East decreased by 12%; Europe and Africa declined by 31% and Americas declined by about 14%. 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 offered to stimulate customer interest and sales in the current generation of products. Revenue was also negatively affected by less than robust infrastructure and capital equipment spending and political uncertainty – first in Europe with Brexit and then in the fourth quarter with US elections. We believe we will return to growth path as key products forming part of the new audio platform has already started shipping in early 2017 and the overall investor confidence and consumer confidence have started improving in the US. However, the growth will depend on the speed at which our customers transition to the new platform and the economic recovery in certain key markets like Europe, Canada and Australia which remains weak.

Our revenue remained essentially the same at $57.8 million in 2015 compared to $57.9 million in 2014. While the revenue from professional audio conferencing products increased by 4%, and the video products increased by 11%, the revenue from unified communication end points declined by 22%. The share of professional audio communications products (which includes microphone products but not premium products) showed an increase to approximately 80% in 2015 from approximately 77% in 2014. This increase was due to an increase in the revenue from microphone products and also due to licensing fees included in professional audio revenue. During 2015, revenue from Asia Pacific including Middle East increased by 4% while Europe and Africa declined by 2% and Americas declined by about 1%.

**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 2016 was approximately $29.5 million or 61% compared to approximately $36.7 million or 64% in 2015. Gross margin declined due to the following reasons: (1) Price reductions made to CONVERGE Pro 1 products to encourage CONVERGE Pro 1 sales while customers were awaiting CONVERGE Pro 2 products, (2) Decline in higher margin professional audio conferencing products in the mix, (3) Higher inventory obsolescence costs, (4) Increased overhead absorption due to sharp declines in inventory, and (5) Scrap of inventory related to transition of wireless microphones manufacturing.

Our gross profit during 2015 was approximately $36.7 million or 64% compared to approximately $35.3 million or 61% in 2014. 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, or income from operations, is the surplus 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 $25.9 million in 2016 compared to $26.5 million in 2015 and $27.3 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.

**Sales and Marketing.** 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 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 and commissions.

S&M expenses were approximately $10.6 million in 2015 compared to $11.2 million in 2014. The decrease in S&M expenses in 2015 was primarily due to a reduction in employee-related costs and commissions paid to employees.

**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 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.

R&D expenses decreased by 7% in 2015 from $9.0 million in 2014 to $8.3 million in 2015. The decrease was primarily due to reductions in R&D project costs, consulting expenses and employee related costs.

**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 $7.3 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.

G&A expenses were approximately $7.5 million in 2015 compared with approximately $7.2 million in 2014. As a percentage of revenue, G&A expenses were 13% in 2015 compared to 12% in 2014 The increase in G&A expenses was primarily due to the increases in various expenses including audit fees incurred on re-audit and reviews of previously filed financial information, information technology costs, legal expenses, stock based compensation and allowance for bad debts. These increases were partially offset by amounts credited for reduced earn-out payments.

**Provision for income taxes**

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.

The tax expense of $3.8 million during 2015 was primarily the result of tax on current year income. This increase compared to a tax expense of $2.6 million during 2014, was also primarily the result of tax on current year income. This increase of $1.2 million resulted from a decrease in the estimated research and development credit, as well as increases in the losses of foreign jurisdictions for which no benefit can be claimed. In addition, overall pre-tax income increased $2.3 million from 2014, resulting in additional tax expense.

## LIQUIDITY, CAPITAL RESOURCES AND FINANCIAL POSITION

As of December 31, 2016, our cash and cash equivalents were approximately $12.1 million compared to $12.5 million as of December 31, 2015. Our working capital was $30.8 million and $36.5 million as of December 31, 2016 and 2015, respectively.

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.

Net cash flows provided by operating activities were approximately $7.6 million during 2015, an increase of approximately $0.9 million from $6.7 million provided by operating activities in 2014. The increase was primarily due to increased net income of $1.2 million and an increase in non-cash charges of $0.8 million, partially offset by changes in operating assets and liabilities of $1.1 million. Net cash flows used in investing activities were $0.6 million during 2015 compared to net cash flows used in investing activities of $14.4 million during 2014. During 2015, the cash outflows on investing activities consisted of purchases of property, plant and equipment of $0.4 million and net outflow of $0.3 million on account of marketable securities. During 2014, the cash outflows for investing activities consisted of outflows of $13.1 million for the acquisitions of Sabine and Spontania, net outflow of $0.6 million on account of marketable securities and $0.6 million for the purchase of property and equipment and $90 thousand for the purchase of intangibles. Please refer to Note 3 - Business Combinations, Goodwill and Intangibles in the Notes to Consolidated Financial Statements for details on the Company's acquisitions.

Net cash used in financing activities in 2015 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 2014 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.

At December 31, 2016, we had open purchase orders related to our electronics manufacturing service providers of approximately $13.6 million, primarily related to inventory purchases.

At December 31, 2016, we had inventory totaling $13.0 million, of which non-current inventory accounted for $1.7 million. This compares to total inventories of $15.5 million and non-current inventory of $2.0 million as of December 31, 2015.

### 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 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.

### 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 depends 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 2016, 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, | | |
|---|---|---|---|
| | 2016 | 2015 | 2014 |
| Deferred revenue | $ 3,882 | $ 4,549 | $ 5,004 |
| Deferred cost of goods sold | 1,530 | 1,628 | 1,698 |
| Deferred gross profit | $ 2,352 | $ 2,921 | $ 3,306 |

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.

**Impairment of Goodwill and Intangible Assets**

The Company tests goodwill and other intangible assets with indefinite lives for impairment at least annually at the beginning of the fourth 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.

There were no related impairments recorded in 2016, 2015 or 2014 as no impairment indicators existed. However, due to uncertainty in the industrial, technological, and competitive environments in which we operate, we might be required to exit or dispose of the assets acquired through the past acquisitions, which could result in an impairment of goodwill and intangible assets.

**Impairment of Long-Lived Assets**

We assess the impairment of long-lived assets, such as property and equipment and definite-lived intangibles subject to amortization, annually or 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.

### Lower-of-Cost or Market Adjustments and Reserves for Excess and Obsolete Inventory

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, 2016 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 $1.4 million. Please refer to Note 12 - Income Taxes in the Notes to Consolidated Financial Statements for additional information.

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

In May 2015, the FASB issued Accounting Standards Update No. 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 2019, and it is currently evaluating the impact of this accounting standard update on the consolidated financial statements.

On February 25, 2016, FASB released ASU 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 will take effect for the Company for fiscal years, and interim periods within those 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 2016-09, Compensation - Stock Compensation: Improvements to Employee Shared-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 is effective for the Company on January 1, 2017. This is expected to affect our income statement, balance sheet and cash flow statements for all periods starting January 1, 2017, especially with respect to the tax benefit from the exercise of stock options.

## CONSOLIDATED BALANCE SHEETS
## (Dollars in thousands, except par value)

| | December 31, 2016 | December 31, 2015 |
|---|---|---|
| **ASSETS** | | |
| Current assets: | | |
| Cash and cash equivalents | $ 12,100 | $ 13,412 |
| Marketable securities | 5,030 | 7,161 |
| Receivables, net of allowance for doubtful accounts of $187 and $54, as of December 31, 2016 and 2015 respectively | 7,461 | 8,692 |
| Inventories | 11,377 | 13,447 |
| Distributor channel inventories | 1,530 | 1,628 |
| Prepaid expenses and other assets | 2,642 | 1,806 |
| Total current assets | 40,140 | 46,146 |
| Long-term marketable securities | 21,365 | 19,204 |
| Long-term inventories, net | 1,664 | 2,018 |
| Property and equipment, net | 1,513 | 1,589 |
| Intangibles, net | 5,677 | 6,638 |
| Goodwill | 12,724 | 12,724 |
| Deferred income taxes | 4,654 | 5,093 |
| Other assets | 387 | 117 |
| Total assets | $ 88,124 | $ 93,529 |
| **LIABILITIES AND SHAREHOLDERS' EQUITY** | | |
| Current liabilities: | | |
| Accounts payable | $ 3,545 | $ 2,815 |
| Accrued liabilities | 1,894 | 2,243 |
| Deferred product revenue | 3,882 | 4,549 |
| Total current liabilities | 9,321 | 9,607 |
| Deferred rent | 103 | 150 |
| Other long-term liabilities | 1,251 | 1,203 |
| Total liabilities | 10,675 | 10,960 |
| Shareholders' equity: | | |
| Common stock, par value $0.001, 50,000,000 shares authorized, 8,812,644 and 9,183,957 shares issued and outstanding as of December 31, 2016 and 2015 respectively | 9 | 9 |
| Additional paid-in capital | 46,669 | 46,291 |
| Accumulated other comprehensive loss | (205) | (166) |
| Retained earnings | 30,976 | 36,435 |
| Total shareholders' equity | 77,449 | 82,569 |
| Total liabilities and shareholders' equity | $ 88,124 | $ 93,529 |

*See accompanying notes*

## CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
**(Dollars in thousands, except per share amounts)**

| | Year ended December 31, | | |
|---|---|---|---|
| | 2016 | 2015 | 2014 |
| Revenue | $ 48,637 | $ 57,796 | $ 57,909 |
| Cost of goods sold | 19,150 | 21,077 | 22,586 |
| Gross profit | 29,487 | 36,719 | 35,323 |
| | | | |
| Operating expenses: | | | |
| Sales and marketing | 10,032 | 10,646 | 11,227 |
| Research and product development | 8,564 | 8,318 | 8,969 |
| General and administrative | 7,325 | 7,493 | 7,152 |
| Total operating expenses | 25,921 | 26,457 | 27,348 |
| | | | |
| Operating income | 3,566 | 10,262 | 7,975 |
| Other income, net | 312 | 289 | 254 |
| Income before income taxes | 3,878 | 10,551 | 8,229 |
| Provision for income taxes | (1,434) | (3,775) | (2,633) |
| Net income | $ 2,444 | $ 6,776 | $ 5,596 |
| | | | |
| Basic earnings per common share | $ 0.27 | $ 0.74 | $ 0.61 |
| Diluted earnings per common share | $ 0.26 | $ 0.71 | $ 0.58 |
| | | | |
| Basic weighted average shares outstanding | 9,021,980 | 9,127,385 | 9,166,769 |
| Diluted weighted average shares outstanding | 9,306,034 | 9,594,659 | 9,581,326 |
| | | | |
| Comprehensive income: | | | |
| Net income | $ 2,444 | $ 6,776 | $ 5,596 |
| Other comprehensive income: | | | |
| Unrealized gain (loss) on available-for-sale securities, net of tax | (1) | (81) | 14 |
| Change in foreign currency translation adjustment | (38) | (77) | (45) |
| Comprehensive income | $ 2,405 | $ 6,618 | $ 5,565 |

*See accompanying notes*

# CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
## (Dollars in thousands, except per share data)

| | Common Stock | | Additional Paid-in | Accumulated Other Comprehensive | Retained | Total Shareholders' |
|---|---|---|---|---|---|---|
| | Shares | Amount | Capital | Income (Loss) | Earnings | Equity |
| Balances at December 31, 2013 | 8,986,080 | $ 9 | $ 41,311 | $ 23 | $ 28,992 | $ 70,335 |
| Exercise of stock options | 234,432 | — | 1,337 | — | — | 1,337 |
| Stock repurchased | (272,767) | — | — | — | (2,598) | (2,598) |
| Cash dividends, $0.10 per share | — | — | — | — | (914) | (914) |
| Stock issued - Sabine acquisition | 150,000 | — | 1,679 | — | — | 1,679 |
| Tax benefit - stock option exercises | — | — | 211 | — | — | 211 |
| Stock-based compensation expense | — | — | 401 | — | — | 401 |
| Proceeds from employee stock purchase plan | 82 | — | — | — | — | — |
| Unrealized gain on available-for-sale securities, net of tax | — | — | — | 14 | — | 14 |
| Foreign currency translation adjustment | — | — | — | (45) | — | (45) |
| Net income | — | — | — | — | 5,596 | 5,596 |
| Balances at December 31, 2014 | 9,097,827 | 9 | 44,939 | (8) | 31,076 | 76,016 |
| Exercise of stock options | 56,143 | — | 308 | — | — | 308 |
| Proceeds from employee stock purchase plan | 14,982 | — | 155 | — | — | 155 |
| Cash dividends, $0.155 per share | — | — | — | — | (1,417) | (1,417) |
| Stock-based compensation expense | 15,005 | — | 848 | — | — | 848 |
| Tax benefit - stock option exercises | — | — | 41 | — | — | 41 |
| 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 |
| Options repurchased | — | — | (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 |

*See accompanying notes*

## CONSOLIDATED STATEMENTS OF CASH FLOWS

| | Year ended December 31, | | |
|---|---|---|---|
| | 2016 | 2015 | 2014 |
| Cash flows from operating activities: | | | |
| Net income | $ 2,444 | $ 6,776 | $ 5,596 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Depreciation and amortization expense | 1,873 | 2,058 | 1,972 |
| Amortization of deferred rent | (73) | (95) | (79) |
| Stock-based compensation expense | 667 | 848 | 401 |
| Provision for (recoveries of) doubtful accounts, net | 132 | (4) | (71) |
| Write-down of inventory to net realizable value | 653 | 496 | 946 |
| Loss on disposal of assets | 54 | 7 | - |
| Tax benefit from exercise of stock options | (690) | (41) | (211) |
| Deferred income taxes | 439 | (4) | (495) |
| Changes in operating assets and liabilities: | | | |
| Receivables | 1,085 | 1,201 | (251) |
| Inventories | 1,869 | (2,249) | (2,614) |
| Prepaid expenses and other assets | (209) | 824 | 844 |
| Accounts payable | 733 | (242) | (84) |
| Accrued liabilities | (319) | (1,219) | 1,451 |
| Income taxes payable | (207) | 323 | (947) |
| Deferred product revenue | (665) | (447) | 858 |
| Other long-term liabilities | 48 | (638) | (606) |
| Net cash provided by operating activities | 7,834 | 7,594 | 6,710 |
| | | | |
| Cash flows from investing activities: | | | |
| Payment towards business acquisitions | — | — | (13,068) |
| Purchase of property and equipment | (730) | (359) | (642) |
| Purchase of intangibles | (161) | — | (90) |
| Proceeds from maturities and sales of marketable securities | 9,795 | 7,341 | 4,650 |
| Purchase of marketable securities | (9,826) | (7,630) | (5,266) |
| Net cash used in investing activities | (922) | (648) | (14,416) |
| | | | |
| Cash flows from financing activities: | | | |
| Net proceeds from equity-based compensation programs | 773 | 463 | 1,337 |
| Repurchase and cancellation of stock options | (1,752) | — | — |
| Tax benefits from equity-based compensation programs | 690 | 41 | 211 |
| Stock registration costs | — | — | (55) |
| Dividend payments | (1,817) | (1,417) | (914) |
| Payments for stock repurchases | (6,086) | — | (2,598) |
| Net cash used in financing activities | (8,192) | (913) | (2,019) |
| | | | |
| Effect of exchange rate changes on cash and cash equivalents | (32) | (61) | (27) |
| Net increase (decrease) in cash and cash equivalents | (1,312) | 5,972 | (9,752) |
| Cash and cash equivalents at the beginning of the year | 13,412 | 7,440 | 17,192 |
| Cash and cash equivalents at the end of the year | $ 12,100 | $ 13,412 | $ 7,440 |
| | | | |
| **Supplemental disclosure of cash flow information:** | | | |
| Cash paid for interest | $ — | $ — | $ 3 |
| Cash paid for income taxes | $ 1,154 | $ 3,730 | $ 3,017 |
| Supplemental disclosure of non-cash investing and financing activities: | | | |
| Issuance of common stock in connection with acquisition of Sabine | $ — | $ — | $ 1,679 |

*See accompanying notes*

## 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 includes consolidated balance sheets for the years ended December 31, 2016 and 2015 and the related consolidated statements of income and comprehensive income, cash flows, and shareholders' equity for each of the years 2016, 2015 and 2014.

*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.

*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, 2016, 2015 and 2014.

*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, | | |
|---|---|---|---|
| | **2016** | **2015** | **2014** |
| Balance at beginning of the year | $ 54 | $ 58 | $ 129 |
| Allowance increase (decrease) | 148 | 36 | (49) |
| Write offs, net of recoveries | (15) | (40) | (22) |
| Balance at end of the year | $ 187 | $ 54 | $ 58 |

*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 $21 and $75, as of December 31, 2016 and 2015, respectively.

*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. In accordance with the provisions of FASB ASC Topic 350, *Intangibles – Goodwill and Other*, the Company tests goodwill and other intangible assets with indefinite lives for impairment at least annually at the beginning of the fourth 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 (See Note 3 – Business Combinations, Goodwill and Intangibles). ClearOne and all of its subsidiaries are considered as one reporting unit for this purpose.

*Impairment of Long-Lived Assets* – Long-lived assets, such as property, equipment, and definite-lived intangibles 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.

*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.

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, | |
|---|---|---|
| | **2016** | **2015** |
| Deferred revenue | $ 3,882 | $ 4,549 |
| Deferred cost of goods sold | 1,530 | 1,628 |
| Deferred gross profit | $ 2,352 | $ 2,921 |

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, | | |
|---|---|---|---|
| | **2016** | **2015** | **2014** |
| Balance at the beginning of year | $ 288 | $ 331 | $ 338 |
| Accruals/additions | 361 | 442 | 511 |
| Usage/claims | (403) | (485) | (518) |
| Balance at end of year | $ 246 | $ 288 | $ 331 |

*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, 2016, 2015 and 2014 totaled $836, $728, and $768, 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.

*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, 2016 and 2015, the Company had a valuation allowance of $1,404 and $1,071, respectively against foreign net operating losses, foreign intangible assets, capital losses carryforwards, and state research and development credits.

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.

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

| | Year Ended December 31, | | |
|---|---|---|---|
| | **2016** | **2015** | **2014** |
| Numerator: | | | |
| Net income | $ 2,444 | $ 6,776 | $ 5,596 |
| Denominator: | | | |
| Basic weighted average shares | 9,021,980 | 9,127,385 | 9,166,769 |
| Dilutive common stock equivalents using treasury stock method | 284,054 | 467,274 | 414,557 |
| Diluted weighted average shares | 9,306,034 | 9,594,659 | 9,581,326 |
| Basic earnings per common share: | $ 0.27 | $ 0.74 | $ 0.61 |
| Diluted earnings per common share: | $ 0.26 | $ 0.71 | $ 0.58 |

| | Year Ended December 31, | | |
|---|---|---|---|
| | 2016 | 2015 | 2014 |
| Weighted average options outstanding | 885,163 | 1,053,785 | 975,696 |
| Anti-dilutive options not included in the computation | 323,644 | 177,125 | 209,751 |

*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.

*Recent Accounting Pronouncements* - In May 2015, the FASB issued Accounting Standards Update No. 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 2019, and it is currently evaluating the impact of this accounting standard update on the consolidated financial statements.

On February 25, 2016, FASB released ASU 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 will take effect for the Company for fiscal years, and interim periods within those 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 2016-09, Compensation - Stock Compensation: Improvements to Employee Shared-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 is effective for the Company on January 1, 2017 and it is currently evaluating the impact that ASU 2016-09 will have on our consolidated financial statements.

## 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, 2016 and 2015 were as follows:

| | Amortized cost | Gross unrealized holding gains | Gross unrealized holding losses | Estimated fair value |
|---|---|---|---|---|
| **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 |
| **December 31, 2015** | | | | |
| Available-for-sale securities: | | | | |
| Corporate bonds and notes | $ 20,827 | $ 50 | $ (133) | $ 20,744 |
| Municipal bonds | 5,608 | 18 | (5) | 5,621 |
| Total available-for-sale securities | $ 26,435 | $ 68 | $ (138) | $ 26,365 |

Maturities of marketable securities classified as available-for-sale securities were as follows at December 31, 2016:

| | Amortized cost | Estimated fair value |
|---|---|---|
| Due within one year | $ 5,029 | $ 5,030 |
| Due after one year through five years | 21,353 | 21,256 |
| Due after five years through ten years | 109 | 109 |
| Total available-for-sale securities | $ 26,491 | $ 26,395 |

Debt securities in an unrealized loss position as of December 31, 2016 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, 2016 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, 2016** | | | | | | |
| Corporate bonds and notes | $ 10,294 | $ (112) | 1,029 | $ (9) | $ 11,323 | $ (121) |
| Municipal bonds | 3,910 | (45) | — | — | 3,910 | (45) |
| | $ 14,204 | $ (157) | $ 1,029 | $ (9) | $ 15,233 | $ (166) |

## 3. Business Combinations, Goodwill and Intangibles

### *Acquisition of Sabine*

On March 7, 2014, the Company completed the acquisition of Sabine, Inc. ("Sabine") through a stock purchase agreement ("SPA"). Sabine manufactures, designs and sells Sacom professional wireless microphone systems for live and installed audio. It also makes FBX Feedback Exterminator for reliable automatic feedback control. With the addition of Sabine, ClearOne will have reliable and exclusive access to the wireless microphones that are a critical component of ClearOne's complete microphone portfolio.

Pursuant to the SPA, the Company (i) paid initial consideration of $8,141 in cash, (ii) accrued for possible additional earn-out payments over the next two years, estimated to be $657, and (iii) issued 150,000 shares of restricted common stock of the Company, valued at $1,679 (determined on the basis of the closing market price of the Company's stock on the acquisition date). The purchase price was paid out of cash on hand. The SPA contains representations, warranties and indemnifications customary for a transaction of this type.

The following table summarizes the consideration paid for the acquisition:

| | Consideration |
|---|---|
| Cash | $ 8,141 |
| Common stock | 1,679 |
| Contingent consideration | 657 |
| Total | $ 10,477 |

The fair values of Sabine assets acquired and liabilities assumed are based on the information that was available during the measurement period of twelve months from the date of acquisition. The fair value of identified assets and liabilities acquired and goodwill is as follows:

| | Fair value |
|---|---|
| Cash | $ 125 |
| Accounts receivable | 255 |
| Inventories | 844 |
| Prepaid and other | 105 |
| Intangibles | 3,970 |
| Property and equipment | 292 |
| Other long-term assets | 11 |

| | Fair value |
|---|---|
| Goodwill | 5,510 |
| Deferred tax asset | 245 |
| Trade accounts payable | (420) |
| Accrued liabilities | (405) |
| Stock registration costs | (55) |
| Total | $ 10,477 |

The goodwill of $5,510 related to the acquisition of Sabine is composed of expected synergies in utilizing Sabine technology in ClearOne product offerings, reduction in future combined research and development expenses, and intangible assets including acquired workforce that do not qualify for separate recognition. The goodwill balance of $5,510 related to the acquisition of Sabine is expected to be deductible for tax purposes.

***Spontania business of Spain-based Dialcom Networks, S.L.***

On April 1, 2014 ClearOne closed on the acquisition of the Spontania business of Spain-based Dialcom Networks, S.L. The Spontania cloud-based service empowers customers to deploy HD video conferencing, web collaboration, and more with equipment most businesses have and use every day - video-conferencing endpoints, desktops, laptops, web browsers, tablets, and smartphones. With Spontania there is no hardware investment and the service operates off of a reservation-less model, enabling on-demand video communications from virtually anywhere, anytime, with anyone on any device.

The aggregate purchase price under the terms of the transaction was approximately €3.66 million in cash (approximately US$5.1 million), after certain closing adjustments. ClearOne did not assume any debt or cash. The cash purchase price was paid out of cash on hand. The addition of this technology was an integral part of the Company’s strategy to build an all-inclusive video collaboration portfolio.

The fair value of identified assets and liabilities acquired from the Spontania acquisition was as follows:

| | Fair value |
|---|---|
| Intangibles | $ 1,335 |
| Property and equipment | 47 |
| Goodwill | 3,741 |
| Accrued liabilities | (71) |
| Total | $ 5,052 |

The goodwill of $3,741 relates to the acquisition of Spontania cloud-based technology and intangible assets including acquired workforce that does not qualify for separate recognition.

***Acquisition Expenses***

The Company incurred $588 in acquisition related expenses for the Sabine and Spontania acquisitions, all of which were categorized under general and administrative expenses in the Consolidated Statement of Income and Comprehensive Income for the year ended December 31, 2014.

***Goodwill***

Changes in the carrying amount of the Company’s goodwill for the years ended December 31, 2016, 2015, and 2014 were as follows:

| | 2016 | 2015 | 2014 |
|---|---|---|---|
| Balance as of January 1, | | | |
| Goodwill | $ 12,724 | $ 12,724 | $ 3,472 |
| Accumulated impairment losses | — | — | — |
| | 12,724 | 12,724 | 3,472 |
| Goodwill acquired during the year | — | — | 9,252 |
| Balance as of December 31, | | | |
| Goodwill | 12,724 | 12,724 | 12,724 |
| Accumulated impairment losses | — | — | — |
| | $ 12,724 | $ 12,724 | $ 12,724 |

***Intangible Assets***

Intangible assets as of December 31, 2016, and 2015 consisted of the following:

| | Estimated useful lives | As of December 31, 2016 | As of December 31, 2015 |
|---|---|---|---|
| Tradename | 5 to 7 years | $ 555 | $ 555 |
| Patents and technological know-how | 10 years | 6,010 | 5,850 |
| Proprietary software | 3 to 15 years | 4,341 | 4,341 |
| Other | 3 to 5 years | 324 | 324 |
| | | 11,230 | 11,070 |
| Accumulated amortization | | (5,553) | (4,432) |
| Total intangible assets, net | | $ 5,677 | $ 6,638 |

During the years ended December 31, 2016, 2015 and 2014, amortization of these intangible assets were $1,121, $1,258, and 1,210 respectively.

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

| Years ending December 31, | |
|---|---|
| 2017 | $ 928 |
| 2018 | 853 |
| 2019 | 781 |
| 2020 | 602 |
| 2021 | 602 |
| Thereafter | 1,911 |
| | $ 5,677 |

## 4. Inventories

Inventories, net of reserves, consisted of the following:

| | As of December 31, 2016 | As of December 31, 2015 |
|---|---|---|
| Current: | | |
| Raw materials | $ 2,291 | $ 2,735 |
| Finished goods | 9,086 | 10,712 |
| | $ 11,377 | $ 13,447 |
| Long-term: | | |
| Raw materials | $ 599 | $ 375 |
| Finished goods | 1,065 | 1,643 |
| | $ 1,664 | $ 2,018 |

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 $1,530 and $1,628 as of December 31, 2016 and 2015, 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 $653, $496 and $946 during the years ended December 31, 2016, 2015 and 2014, respectively.

## 5. Property and Equipment

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

| | Estimated useful lives | As of December 31, 2016 | As of December 31, 2015 |
|---|---|---|---|
| Office furniture and equipment | 3 to 10 years | $ 4,835 | $ 4,412 |
| Leasehold improvements | 1 to 6 years | 1,495 | 1,488 |
| Manufacturing and test equipment | 2 to 10 years | 2,537 | 2,483 |
| | | 8,867 | 8,383 |
| Accumulated depreciation and amortization | | (7,354) | (6,794) |
| Property and equipment, net | | $ 1,513 | $ 1,589 |

Depreciation expense on property and equipment for the years ended December 31, 2016, 2015 and 2014 was $723, $801, and $761, respectively.

## 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 $1,099, $1,420 and $1,236, including amortization of deferred rent of $73, $95, and $79 for the years ended December 31, 2016, 2015 and 2014, 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.

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 7,070 square-foot facility in Austin, Texas under the terms of an operating lease expiring in October 2019. This facility supports 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.

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

| **Years ending December 31,** | |
|---|---|
| 2017 | $ 928 |
| 2018 | 872 |
| 2019 | 467 |
| 2020 | 239 |
| 2021 | 204 |
| Total minimum lease payments | $ 2,710 |

## 7. Accrued Liabilities

Accrued liabilities consist of the following:

| | As of December 31, 2016 | As of December 31, 2015 |
|---|---|---|
| Accrued salaries and other compensation | $ 1,098 | $ 1,170 |
| Sales and marketing programs | 319 | 477 |
| Product warranty | 246 | 288 |
| Other accrued liabilities | 231 | 308 |
| Total | $ 1,894 | $ 2,243 |

## 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 $13,563 as of December 31, 2016.

*Uncertain Tax Positions.* As further discussed in Note 12, we had $1,189 of uncertain tax positions as of December 31, 2016. 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.

*Legal Proceedings.*

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 alleges 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"). The Company denies the allegations in the OSHA complaint, has not discovered any evidence of wrongdoing with respect to the allegations previously made by the former employee, and is vigorously defending the claims. On March 2, 2017, the Company received notice that the same former employee who initiated the OSHA Complaint also has filed a complaint with the Utah Labor Commission, Anti-Discrimination & Labor Division (the "Utah Complaint") 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 Company is in the process of assessing the Utah Complaint and intends to vigorously defend it.

In 2016, the Company recorded $927 of pretax gross expenses related to the defense of the OSHA Complaint and review of the allegations underlying the former employee's OSHA complaint.

We expect to incur additional expenses related to legal and other professional services rendered in connection with the defense of OSHA Complaint and/or related matters in future periods and will recognize these expenses as services are received. Expenses related to the defense of the OSHA Complaint and/or related matters may include additional liabilities from OSHA's expected investigation; future governmental investigations and/or enforcement proceedings; future civil litigation; and future unspecified expenses.

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.

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, 2015. Provisions of the restated 2007 Plan include the granting of up to 2,000,000 incentive and non-qualified stock options, stock appreciation rights, restricted stock and restricted stock units. Options may be granted to employees, officers, non-employee directors and other service providers and may be granted upon such terms as the Compensation Committee of the Board of Directors determines in their sole discretion.

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, 2016 had contractual lives of ten years.

Under the 1998 Plan, 2,500,000 shares were authorized for grant. As of December 31, 2016, there were 150,000 options outstanding under the 1998 Plan, which includes the cliff vesting and 3 or 4-year vesting options discussed above.

As of December 31, 2016, there were 700,232 options outstanding under the 2007 Plan. As of December 31, 2016, the 2007 Plan had 826,268 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, | | |
|---|---|---|---|
| | 2016 | 2015 | 2014 |
| Risk-free interest rate, average | 1.52% | 2.00% | 2.20% |
| Expected option life, average | 6.1 years | 6.1 years | 8.2 years |
| Expected price volatility, average | 43.75% | 44.30% | 47.60% |
| Expected dividend yield | 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 compensation cost net of an expected forfeiture rate and recognized 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.

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, 2013 | 1,111,274 | $ 5.15 | | |
| Granted | 193,500 | 8.83 | | |
| Expired and canceled | (29,532) | 6.87 | | |
| Forfeited prior to vesting | (729) | 8.88 | | |
| Exercised | (234,432) | 5.72 | | |
| 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 |
| Vested and Expected to Vest at December 31, 2014 | 1,040,081 | $ 5.65 | 5.60 | $ 4,286 |
| Vested at December 31, 2014 | 730,016 | $ 4.67 | 4.15 | $ 3,271 |
| 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 |

The weighted average per share fair value of options granted during the years ending December 31, 2016, 2015 and 2014 was $4.27, $5.27, and $ 4.85 respectively. The total intrinsic value of options exercised during the years ended December 31, 2016, 2015 and 2014 was $2,824, $404, and $1,337 respectively.

The total pre-tax compensation cost related to stock options recognized during the years ended December 31, 2016, 2015, and 2014 was $628, $552 and $401, respectively. Tax benefit from compensation cost related to stock options during the years ended December 31, 2016, 2015 and 2014 was $107, $41 and $211, respectively. As of December 31, 2016, the total compensation cost related to stock options not yet recognized and before the effect of any forfeitures was $1,127, which is expected to be recognized over approximately the next 2.19 years on a straight-line basis.

*Employee Stock Purchase Plan*

During 2016, the Company issued shares to employees under the Company's 2015 Employee Stock Purchase Plan (the "ESPP"). The ESPP was approved by the Company's shareholders on December 12, 2015. As of December 31, 2016, 475,893 of the originally approved 500,000 shares were available for offerings under the ESPP. Offering periods under the ESPP commence on each January 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.

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

| | 2016 | 2015 | 2014 |
|---|---|---|---|
| Shares purchased under ESPP plans | 9,140 | 14,982 | 82 |
| Plan compensation expense | $ 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, 2015, the Company announced the discontinuance of the stock repurchase program along with the initiation of a cash dividend plan. On January 31, 2017, the Company declared its most recent dividend under this plan of $0.05 per share of ClearOne common stock, payable on March 1, 2017 to shareholders of record on February 15, 2017. 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 expected to be paid on or about June 1, 2017.

On March 9, 2016, the Board of Directors of the Company authorized the repurchase of up to $10,000 of the Company's outstanding shares of common stock under a 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.

During the twelve months ended December 31, 2016, we acquired the following shares of common stock under the current stock repurchase program:

| $ 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) |
|---|---|---|---|---|
| March 9 to March 31 | 33,600 | $ 12.02 | 33,600 | $ 9,596 |
| April 1 to June 30 | 330,515 | 11.25 | 330,515 | 5,885 |
| July 1 to September 30 | 91,965 | 11.16 | 91,965 | 4,861 |
| October 1 to December 31 | 86,179 | 11.00 | 86,179 | 3,914 |
| Total | 542,259 | $ 11.25 | 542,259 | |

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.

## 10. Significant Customers

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

| | Year ended December 31, | | |
|---|---|---|---|
| | 2016 | 2015 | 2014 |
| Customer A | 16.3% | 14.2% | 16.0% |
| Customer B | —%* | 10.4% | —%* |
| Total | 16.3% | 24.6% | 16.0% |

* Sales didn't exceed 10% of the revenue.

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

| | As of December 31, | |
|---|---|---|
| | 2016 | 2015 |
| Customer A | 13% | 18% |
| Customer B | 12% | 16% |
| Total | 25% | 34% |

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, 2016 and 2015:

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| **December 31, 2016** | | | | |
| Corporate bonds and notes | $ — | $ 19,970 | $ — | $ 19,970 |
| Municipal bonds | — | 6,425 | — | 6,425 |
| Total | $ — | $ 26,395 | $ — | $ 26,395 |
| **December 31, 2015** | | | | |
| Corporate bonds and notes | $ — | $ 20,744 | $ — | $ 20,744 |
| Municipal bonds | — | 5,621 | — | 5,621 |
| Total | $ — | $ 26,365 | $ — | $ 26,365 |

### 12. Income Taxes

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

| | Year ended December 31, | | |
|---|---|---|---|
| | 2016 | 2015 | 2014 |
| Domestic | $ 6,332 | $ 13,295 | $ 9,615 |
| Foreign | (2,454) | (2,744) | (1,386) |
| Total | $ 3,878 | $ 10,551 | $ 8,229 |

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

| | Year ended December 31, | | |
|---|---|---|---|
| | 2016 | 2015 | 2014 |
| Current: | | | |
| Federal | $ (593) | $ (3,386) | $ (2,750) |
| State | 63 | (344) | (173) |
| Foreign | (37) | — | (109) |
| Total current | (567) | (3,730) | (3,032) |
| Deferred: | | | |
| Federal | (633) | (220) | 379 |
| State | (17) | (10) | 27 |
| Foreign | 115 | 470 | 401 |
| | (535) | 240 | 807 |
| Change in valuation allowance | (332) | (285) | (408) |
| Total deferred | (867) | (45) | 399 |
| (Provision) for income taxes | $ (1,434) | $ (3,775) | $ (2,633) |

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

| | Year ended December 31, | | |
|---|---|---|---|
| | 2016 | 2015 | 2014 |
| Tax (provision) at Federal statutory rate | $ (1,318) | $ (3,587) | $ (2,798) |
| State income tax (provision), net of federal benefit | (148) | (408) | (257) |
| Research and development tax credits | 423 | 456 | 549 |
| Foreign earnings or losses taxed at different rates | (292) | (231) | (102) |
| Other | 233 | 280 | 383 |
| Change in valuation allowance | (332) | (285) | (408) |
| Tax (provision) | $ (1,434) | $ (3,775) | $ (2,633) |

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

| | 2016 | 2015 |
|---|---|---|
| Deferred revenue | $ 845 | $ 1,019 |
| Basis difference in intangible assets | (56) | 26 |
| Inventory reserve | 2,650 | 2,452 |
| Net operating loss carryforwards | 1,391 | 1,347 |
| Research and development tax credits | 88 | — |
| Accrued expenses | 92 | 165 |
| Stock-based compensation | 584 | 672 |
| Allowance for sales returns and doubtful accounts | 70 | 20 |
| Difference in property and equipment basis | (350) | (423) |
| Other | 743 | 886 |
| Total net deferred income tax asset | 6,057 | 6,164 |
| Less: Valuation allowance | (1,403) | (1,071) |
| Net deferred income tax asset (liability) | $ 4,654 | $ 5,093 |

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, 2016 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 $755 (pre-tax), Hong Kong NOL carryforwards of approximately $255, and Spain NOL carryforwards of approximately $855. The federal NOL carryforwards will begin to expire in 2029. The Hong Kong and Spain NOL carryforwards do 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, 2016 and 2015, that would favorably impact our effective tax rate if recognized was $233 and $176, respectively. As of December 31, 2016 and 2015, we accrued $87 and $55, 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.

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

| | Year ended December 31, | |
|---|---|---|
| | 2016 | 2015 |
| Balance - beginning of year | $ 1,126 | $ 1,678 |
| Additions based on tax positions related to the current year | 16 | 52 |
| Additions for tax positions of prior years | 47 | 5 |
| Reductions for tax positions of prior years | — | (503) |
| Settlements | — | — |
| Lapse in statutes of limitations | — | (106) |
| Uncertain tax positions, ending balance | $ 1,189 | $ 1,126 |

The Company's U.S. federal income tax returns for 2012 through 2015 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 2012. The Company completed its audit by the Internal Revenue Service ("IRS") for its 2006 tax return in 2010. As a result of the audit by the IRS, there were no material adjustments made to the Company's tax return. The IRS commenced an examination of the Company's 2012 tax return. We do not anticipate the examination will result in a material change to its financial position.

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, 2016. 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, | | |
|---|---|---|---|
| | 2016 | 2015 | 2014 |
| United States | $ 31,838 | $ 39,563 | $ 39,837 |
| All other countries | 16,799 | 18,233 | 18,072 |
| Total | $ 48,637 | $ 57,796 | $ 57,909 |

## 14. Subsequent Events

On January 31, 2017, the Company declared a stock dividend of $0.05 per share of ClearOne common stock payable on March 1, 2017 to shareholders of record on February 15, 2017.

In March 2017, the Company renewed and extended its common stock repurchase program of $10,000 to continue through March 9, 2018.

# MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

***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 Principal Financial Officer, 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 Principal Financial Officer, of the effectiveness and the design and operation of our disclosure controls and procedures as of December 31, 2016. Our disclosure controls and procedures are designed to provide reasonable assurance of achieving their objectives and, based upon this evaluation, our Chief Executive Officer and Principal Financial Officer concluded that, as of the end of the period covered by this Annual Report, our disclosure controls and procedures are effective at a reasonable assurance level.

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, 2016 based on the framework set forth in *Internal Control - Integrated Framework* (2013 framework) issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our assessment using that criteria, management concluded that the design and operation of our internal control over financial reporting were effective as of December 31, 2016.

***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.

## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of ClearOne, Inc.

We have audited the accompanying consolidated balance sheets of ClearOne, Inc. and subsidiaries (collectively, ClearOne) as of December 31, 2016 and 2015, and the related consolidated statements of income and comprehensive income, shareholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2016. We also have audited ClearOne's internal control over financial reporting as of December 31, 2016, based on criteria established in *Internal Control-Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). ClearOne's management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying form 10-K. Our responsibility is to express an opinion on these financial statements and an opinion on ClearOne's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A Company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A Company's internal control over financial reporting includes those policies and procedures that (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.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of ClearOne, Inc. and subsidiaries as of December 31, 2016 and 2015, and the consolidated results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2016 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, ClearOne Inc. and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on criteria established in *Internal Control-Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

*/s/ TANNER LLC*

Salt Lake City, Utah
March 16, 2017

## UNAUDITED RECONCILIATION OF GAAP MEASURES TO NON-GAAP MEASURES

(Dollars in thousands, except per share values)

| | Year ended December 31, | |
|---|---|---|
| | 2016 | 2015 |
| **GAAP gross profit** | $ 29,487 | $ 36,719 |
| Inventory scrap related to wireless manufacturing move | 494 | — |
| Stock-based compensation | 26 | 21 |
| **Non-GAAP gross profit** | $ 30,007 | $ 36,740 |
| | | |
| **GAAP operating income (loss)** | $ 3,566 | $ 10,262 |
| Inventory scrap related to wireless manufacturing move | 494 | — |
| Stock-based compensation | 667 | 848 |
| Amortization of intangibles | 1,122 | 1,258 |
| Legal expenses, acquisition expenses, re-audit expenses, restructuring expenses, etc. not related to regular operations | 1,711 | 914 |
| **Non-GAAP operating income** | $ 7,560 | $ 13,282 |
| | | |
| **GAAP net income (loss)** | $ 2,444 | $ 6,776 |
| Inventory scrap related to wireless manufacturing move | 494 | — |
| Stock-based compensation | 667 | 848 |
| Amortization of intangibles | 1,122 | 1,258 |
| Legal expenses, acquisition expenses, re-audit expenses, restructuring expenses, etc. not related to regular operations | 1,711 | 914 |
| Loss on disposal of assets related to wireless microphones manufacturing | 53 | — |
| Tax effect of non-GAAP adjustments | (1,497) | (1,081) |
| **Non-GAAP net income (loss)** | $ 4,994 | $ 8,715 |
| | | |
| GAAP net income (loss) | $ 2,444 | $ 6,776 |
| Number of shares used in computing GAAP income per share (diluted) | 9,416,085 | 9,594,659 |
| **GAAP income (loss) per share (diluted)** | $ 0.26 | $ 0.71 |
| | | |
| Non-GAAP net income (loss) | $ 4,994 | $ 8,715 |
| Number of shares used in computing Non-GAAP income per share (diluted) | 9,416,085 | 9,594,659 |
| **Non-GAAP income (loss) per share (diluted)** | $ 0.53 | $ 0.91 |
| | | |
| **GAAP total net income (loss)** | $ 2,444 | $ 6,776 |
| Inventory scrap related to wireless manufacturing move | 494 | — |
| Stock-based compensation | 667 | 848 |
| Depreciation | 723 | 808 |
| Amortization of intangibles | 1,122 | 1,258 |
| Legal expenses, acquisition expenses, re-audit expenses, restructuring expenses, etc. not related to regular operations | 1,711 | 914 |
| Loss on disposal of assets related to wireless microphones manufacturing | 53 | — |
| Provision for income taxes | 1,434 | 3,775 |
| **Non-GAAP Adjusted EBITDA** | $ 8,648 | $ 14,379 |

## CORPORATE INFORMATION

### BOARD OF DIRECTORS

**Zeynep Hakimoglu**
Chairman
President and CEO
ClearOne

**Brad R. Baldwin**
President and CEO
First Utah Bank

**Larry R. Hendricks**
Formerly VP of Finance and GM
Daily Foods, Inc.

**Eric L. Robinson**
General Counsel and CFO
ActiveCare, Inc.

General Counsel and CFO
MicroPower Global Corp.

### CORPORATE OFFICERS

**Zeynep Hakimoglu**
Chairman
President and CEO

**Narsi Narayanan**
Senior Vice President of Finance
and Corporate Secretary

**Michael J. Braithwaite**
Senior Vice President of
Network Streaming Business

### CORPORATE HEADQUARTERS

Edgewater Corporate Park
South Tower
5225 Wiley Post Way
Suite 500
Salt Lake City, UT 84116
801.975.7200

### CORPORATE COUNSEL

Seyfarth Shaw, LLP
700 Milam St.
Suite 1400
Houston, TX 77002
713.225.2300

### INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Tanner LLC
36 South State Street
Suite 600
Salt Lake City, UT 84111
801.532.7444

### TRANSFER AGENT

Broadridge Corporate
Issuer Solutions
P. O. Box 1342
Brentwood, NY 11717
877.830.4936

### SECURITIES LISTING

The company's common stock trades on the NASDAQ Capital Market under the symbol of CLRO

NASDAQ LISTED

### INVESTOR RELATIONS

LHA Investor Relations
44 Montgomery Street
Suite 200
San Francisco, CA 94104
415.433.3777

**FORWARD-LOOKING INFORMATION** Statements contained in this Annual Report, which are not historical facts, are forward-looking statements, as defined in the Private Securities Litigation Reform Act of 1995, and as such, are subject to risk and uncertainties which can cause actual results to differ materially from those currently anticipated. Readers are referred to the documents filed by ClearOne Communications with the Securities and Exchange Commission, specifically the most recent reports on forms 10-K and 10-Q, including amendments thereto, which identify important risk factors that could cause actual results to differ from those contained in the forward-looking statements.

Great ideas need to be heard and seen

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**clearone.com**