
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, D.C. 20549

FORM 10-Q

(Mark one)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2019

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to .

Commission file number 001-36017

Control4 Corporation

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of incorporation or organization)

42-1583209
(I.R.S. Employer Identification No.)

11734 S. Election Road
Salt Lake City, Utah
(Address of principal executive offices)

84020
(Zip Code)

(801) 523-3100
(Registrant's telephone number, including area code)

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, \$0.0001 par value per share	CTRL	The NASDAQ Stock Market LLC

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

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

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company Emerging growth company

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

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

On May 3, 2019, 26,660,960 shares of the registrant's Common Stock, \$0.0001 par value, were outstanding.

Control4 Corporation

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Control4 Corporation
PART I — Financial Information

ITEM 1. Condensed Consolidated Financial Statements

CONTROL4 CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except share data)

	March 31, 2019	December 31, 2018
	(unaudited)	
Assets		
Current assets:		
Cash and cash equivalents	\$ 19,828	\$ 40,395
Restricted cash	264	259
Short-term investments	48,789	52,794
Accounts receivable, net	30,316	33,016
Inventories	45,867	42,684
Prepaid expenses and other current assets	9,633	6,100
Total current assets	154,697	175,248
Property and equipment, net	9,540	9,663
Operating lease right-of-use assets	10,567	—
Long-term investments	3,201	—
Intangible assets, net	25,389	20,651
Goodwill	31,403	21,530
Other assets	22,560	25,456
Total assets	\$ 257,357	\$ 252,548
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	\$ 23,083	\$ 26,213
Accrued liabilities	7,151	9,142
Current portion of deferred revenue	5,588	5,507
Current operating lease liability	3,924	—
Total current liabilities	39,746	40,862
Long-term operating lease liability	7,924	—
Other long-term liabilities	5,838	5,339
Total liabilities	53,508	46,201
Commitments and contingencies (Note 14)	—	—
Stockholders' equity:		
Common stock, \$0.0001 par value; 500,000,000 shares authorized; 26,655,506 and 26,516,912 shares issued and outstanding at March 31, 2019 and December 31, 2018, respectively	3	3
Additional paid-in capital	234,999	235,529
Accumulated deficit	(30,355)	(28,385)
Accumulated other comprehensive loss	(798)	(800)
Total stockholders' equity	203,849	206,347
Total liabilities and stockholders' equity	\$ 257,357	\$ 252,548

See accompanying notes to condensed consolidated financial statements (unaudited).

CONTROL4 CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share data)

	Three Months Ended	
	March 31,	
	2019	2018
	(unaudited)	
Revenue	\$ 60,425	\$ 59,149
Cost of revenue	31,142	28,410
Gross margin	<u>29,283</u>	<u>30,739</u>
Operating expenses:		
Research and development	11,817	10,940
Sales and marketing	13,342	12,535
General and administrative	7,117	6,293
Total operating expenses	<u>32,276</u>	<u>29,768</u>
Income (loss) from operations	<u>(2,993)</u>	<u>971</u>
Other income (expense), net:		
Interest, net	344	236
Other income (expense), net	(87)	(357)
Total other income (expense), net	<u>257</u>	<u>(121)</u>
Income (loss) before income taxes	(2,736)	850
Income tax benefit	(766)	(116)
Net income (loss)	<u>\$ (1,970)</u>	<u>\$ 966</u>
Net income (loss) per common share:		
Basic	\$ (0.07)	\$ 0.04
Diluted	\$ (0.07)	\$ 0.04
Weighted-average number of shares:		
Basic	26,563	25,904
Diluted	26,563	27,526

See accompanying notes to condensed consolidated financial statements (unaudited).

CONTROL4 CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(in thousands)

	Three Months Ended	
	March 31,	
	2019	2018
	(unaudited)	
Net income (loss)	\$ (1,970)	\$ 966
Other comprehensive income (loss):		
Foreign currency translation adjustment, net of tax	(53)	(51)
Net unrealized gains (losses) on available-for-sale investments, net of tax	55	(64)
Total other comprehensive income (loss)	2	(115)
Comprehensive income (loss)	\$ (1,968)	\$ 851

See accompanying notes to condensed consolidated financial statements (unaudited).

CONTROL4 CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(in thousands, except share data)
(unaudited)

	Stockholders' Equity							Total Stockholders' Equity
	Common Stock		Treasury Stock		Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive (Loss) Income	
	Number of Shares	Amount	Number of Shares	Amount				
Balance at December 31, 2018	26,516,912	\$ 3	—	\$ —	\$ 235,529	\$ (28,385)	\$ (800)	\$ 206,347
Net loss	—	—	—	—	—	(1,970)	—	(1,970)
Other comprehensive income	—	—	—	—	—	—	2	2
Stock-based compensation	34,854	—	—	—	3,529	—	—	3,529
Issuance of common stock upon exercise of stock options and vesting of restricted stock	243,522	—	—	—	(1,537)	—	—	(1,537)
Repurchase of common stock for treasury	(139,782)	—	139,782	(2,522)	—	—	—	(2,522)
Retirement of treasury stock	—	—	(139,782)	2,522	(2,522)	—	—	—
Balance at March 31, 2019	26,655,506	\$ 3	—	\$ —	\$ 234,999	\$ (30,355)	\$ (798)	\$ 203,849

	Stockholders' Equity							Total Stockholders' Equity
	Common Stock		Treasury Stock		Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive (Loss) Income	
	Number of Shares	Amount	Number of Shares	Amount				
Balance at December 31, 2017	25,832,895	\$ 3	—	\$ —	\$ 242,281	\$ (72,226)	\$ (531)	\$ 169,527
Net income	—	—	—	—	—	966	—	966
Other comprehensive loss	—	—	—	—	—	—	(115)	(115)
Stock-based compensation	—	—	—	—	2,921	—	—	2,921
Issuance of common stock upon exercise of stock options and vesting of restricted stock	475,399	—	—	—	(1,525)	—	—	(1,525)
Repurchase of common stock for treasury	(300,000)	—	300,000	(7,448)	—	—	—	(7,448)
Retirement of treasury stock	—	—	(300,000)	7,448	(7,448)	—	—	—
Balance at March 31, 2018	26,008,294	\$ 3	—	\$ —	\$ 236,229	\$ (71,260)	\$ (646)	\$ 164,326

See accompanying notes to condensed consolidated financial statements (unaudited).

CONTROL4 CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	Three Months Ended	
	March 31,	
	2019	2018
	(unaudited)	
Operating activities		
Net income (loss)	\$ (1,970)	\$ 966
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation expense	1,109	969
Amortization of intangible assets	1,620	1,446
Loss on disposal of fixed assets	—	14
Provision for doubtful accounts	8	71
Investment discount and premium amortization, net	(169)	(83)
Stock-based compensation	3,529	3,335
Changes in assets and liabilities:		
Accounts receivable, net	2,064	3,235
Inventories	(1,741)	(2,003)
Prepaid expenses and other current assets	(3,034)	(916)
Other assets	1,784	194
Accounts payable	(3,887)	(3,923)
Accrued liabilities	(3,395)	(3,083)
Deferred revenue	25	163
Other long-term liabilities	(650)	84
Net cash provided by (used in) operating activities	<u>(4,707)</u>	<u>469</u>
Investing activities		
Purchases of available-for-sale investments	(27,171)	(19,501)
Proceeds from sales of available-for-sale investments	1,800	1,000
Proceeds from maturities of available-for-sale investments	26,399	18,200
Purchases of property and equipment	(1,171)	(892)
Business acquisitions, net of cash acquired	(11,695)	—
Net cash used in investing activities	<u>(11,838)</u>	<u>(1,193)</u>
Financing activities		
Proceeds from exercise of options for common stock	310	2,089
Payments for withholding taxes related to net share settlement of equity awards	(1,847)	(3,614)
Repurchase of common stock	(2,522)	(7,448)
Payment of debt issuance costs	—	(113)
Net cash used in financing activities	<u>(4,059)</u>	<u>(9,086)</u>
Effect of exchange rate changes on cash and cash equivalents	42	48
Net change in cash and cash equivalents	<u>(20,562)</u>	<u>(9,762)</u>
Unrestricted and restricted cash and cash equivalents at beginning of period	40,654	30,034
Unrestricted and restricted cash and cash equivalents at end of period	<u>\$ 20,092</u>	<u>\$ 20,272</u>
Supplemental disclosure of cash flow information		
Cash paid for interest	\$ 81	\$ 25
Cash paid for taxes	184	167
Supplemental schedule of non-cash investing and financing activities		
Settlement of accounts receivable and other assets in business combinations	4,250	—
Business acquisitions holdback liability	1,310	—
Purchases of property and equipment financed by accounts payable	61	207
Net unrealized gains (losses) on available-for-sale investments	55	(64)

See accompanying notes to condensed consolidated financial statements (unaudited)

Control4 Corporation
Notes to Condensed Consolidated Financial Statements
(unaudited)

1. Description of Business and Summary of Significant Accounting Policies

Control4 Corporation (“Control4” or the “Company”) is a leading provider of professionally-installed smart home and business solutions that are designed to personalize and enhance how consumers engage with an ever-changing connected world. The Company’s entertainment, smart lighting, comfort and convenience, safety and security, and networking solutions unlock the potential of connected devices, making entertainment systems easier to use and more accessible, homes and businesses more comfortable and energy efficient, and individuals more connected and secure. The Company’s premium smart home and small business solutions provide consumers with the ability to integrate audio, video, lighting, temperature, security, communications, network management and other functionalities into a unified automation solution, customized to match their lifestyles and business needs. The Company’s advanced software, delivered through the controller and user-interface products together with various cloud services, power this customized experience, enabling cohesive interoperability with thousands of connected Control4 and third-party devices. The Company was incorporated in the state of Delaware on March 27, 2003.

Unaudited Interim Financial Statements

The accompanying condensed consolidated financial statements are unaudited. These unaudited condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) and, in the opinion of management, reflect all adjustments, consisting only of normal recurring adjustments, considered necessary to present fairly the Company’s financial position, results of operations and cash flows. The results of operations for the three months ended March 31, 2019 are not necessarily indicative of the results that may be expected for the year ending December 31, 2019, or any other future interim or annual period.

These unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes included in the Company’s Annual Report on Form 10-K filed with the SEC on February 11, 2019. The December 31, 2018 condensed consolidated balance sheet included herein was derived from the audited financial statements as of that date.

Basis of Presentation

The unaudited condensed consolidated financial statements include the accounts of the Company and its subsidiaries. All intercompany balances and transactions have been eliminated in the unaudited condensed consolidated financial statements.

Segment Reporting

Operating segments are identified as components of an enterprise about which separate discrete financial information is available for evaluation by the chief operating decision-maker, the Chief Executive Officer, in making decisions regarding resource allocation and assessing performance. To date, the Company has viewed its operations and manages its business as one operating segment.

Concentrations of Risk

The Company’s accounts receivable are derived from revenue earned from its worldwide network of independent dealers and distributors. The Company’s sales to dealers and distributors located outside the United States are generally denominated in U.S. dollars, except for sales to dealers and distributors located in Australia, Canada, the European Union, New Zealand, Switzerland, and the United Kingdom, which are generally denominated in Australian dollars, Canadian dollars, euros, New Zealand dollars, Swiss francs, and pounds sterling, respectively. There were no individual account balances greater than 10% of total accounts receivable as of March 31, 2019 and December 31, 2018.

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No dealer or distributor accounted for more than 10% of total revenue for the three months ended March 31, 2019 and 2018.

While the Company partners with many manufacturers, generally one manufacturer is the Company's sole source for a particular product or product family. A significant disruption in the operations of one of these manufacturers would impact the production of the Company's products for a substantial period of time, which could have a material adverse effect on the Company's business, financial condition and results of operations.

Use of Accounting Estimates

The preparation of financial statements in conformity with U.S. Generally Accepted Accounting Principles ("GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. On an ongoing basis, the Company evaluates its estimates, including those related to revenue recognition, sales returns, provisions for doubtful accounts, product warranty, inventory obsolescence, litigation, determination of fair value of stock options, deferred tax asset valuation allowances and income taxes. Actual results may differ from those estimates.

Limited Product Warranties

The Company provides its customers a limited product warranty of two, three, or ten years depending on product type and brand. The limited product warranties require the Company, at its option, to repair or replace defective products during the warranty period at no cost to the customer or refund the purchase price. The Company estimates the costs that may be incurred to replace, repair or issue a refund for defective products and records a reserve at the time revenue is recognized. Factors that affect the Company's warranty liability include the cost of the products sold, the Company's historical experience, and management's judgment regarding anticipated rates of product warranty returns, net of refurbished products. The Company assesses the adequacy of its recorded warranty liability each period and makes adjustments to the liability as necessary. Warranty costs accrued include amounts accrued for products at the time of shipment, adjustments for changes in estimated costs for warranties on products shipped in the period, and changes in estimated costs for warranties on products shipped in prior periods. It is not practicable for the Company to determine the amounts applicable to each of these components.

The following table presents the changes in the product warranty liability for the three months ended March 31, 2019 (in thousands):

	Warranty Liability
Balance at December 31, 2018	\$ 2,524
Warranty costs accrued	905
Warranty claims	(1,030)
Balance at March 31, 2019	<u>\$ 2,399</u>

Net Income (Loss) Per Common Share

Basic net income (loss) per share is computed using the weighted-average number of common shares outstanding during the period. Diluted net income (loss) per share is computed using the weighted-average number of common shares outstanding and potentially dilutive common shares outstanding during the period that have a dilutive effect on net income (loss) per share. Potentially dilutive common shares result from the assumed exercise of outstanding stock options and settlement of restricted stock units.

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The following table presents the reconciliation of the numerator and denominator used in the calculation of basic and diluted net income (loss) per share (in thousands):

	Three Months Ended March 31,	
	2019	2018
Numerator:		
Net income (loss)	\$ (1,970)	\$ 966
Denominator:		
Weighted average common stock outstanding for basic net income (loss) per common share	26,563	25,904
Effect of dilutive securities—stock options and restricted stock units	—	1,622
Weighted average common shares and dilutive securities outstanding	<u>26,563</u>	<u>27,526</u>

Potentially dilutive securities, including common equivalent shares, in which the assumed proceeds exceed the average market price of common stock for the applicable period, were not included in the calculation of diluted net income (loss) per share as their impact would be anti-dilutive. The following weighted-average common stock equivalents were anti-dilutive and therefore were excluded from the calculation of diluted net income (loss) per share (in thousands):

	Three Months Ended March 31,	
	2019	2018
Options to purchase common stock	1,065	—
Restricted stock units	1,114	166
Total	<u>2,179</u>	<u>166</u>

Restricted Cash

Restricted cash as of March 31, 2019 and December 31, 2018 is composed of a guarantee made by the Company's subsidiary in the United Kingdom to HM Revenue & Customs related to a customs duty deferment account.

Leases

In February 2016, the FASB issued ASU 2016-02, "*Leases (Topic 842)*," which supersedes the guidance in ASC 840, "*Leases*." The guidance requires balance sheet recognition for assets and liabilities associated with rights and obligations created by leases with terms greater than twelve months. The Company adopted the standard effective January 1, 2019 and elected the package of practical expedients available under the standard. The Company also elected to apply the simplified transition option that allows entities to not apply the new leases standard in the comparative periods presented in financial statements in the year of adoption. Internal controls have been implemented to enable the preparation of financial information on adoption.

The adoption of the standard resulted in recording right-of-use ("ROU") assets of \$10.0 million and lease liabilities of \$11.9 million as of January 1, 2019. The ROU assets are lower than the lease liabilities as existing deferred rent and lease incentive liabilities were recorded against the right-of-use assets at adoption in accordance with the standard. The standard did not materially affect our condensed consolidated statements of operations or condensed consolidated statements of cash flows.

The Company determines if an arrangement is a lease at inception. Operating lease activity is included in operating lease right-of-use assets, and current and long-term operating lease liabilities on the condensed consolidated balance sheets for leases with terms greater than 12 months.

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Operating lease ROU assets and operating lease liabilities are recognized based on the present value of the future minimum lease payments over the lease term at commencement date. As most of the leases do not provide an implicit rate, the Company uses its incremental borrowing rate based on information available at the commencement date in determining the present value of future payments. The operating lease ROU asset also includes any lease payments made and excludes lease incentives and initial direct costs incurred. Lease terms may include options to extend or terminate the lease when its reasonably certain the Company will exercise that option.

Recent Accounting Pronouncements

In August 2018, the FASB issued ASU 2018-14, “*Compensation—Retirement Benefits—Defined Benefit Plans—General (Topic 715-20): Disclosure Framework—Changes to the Disclosure Requirements For Defined Benefit Plans.*” The new standard modifies the disclosure requirements for employers that sponsor defined benefit pension or other postretirement plans by removing and adding certain disclosures for these plans. The new standard is effective for public business entities for annual periods ending after December 31, 2020; early adoption is permitted, and the amendments are applied on a retrospective basis to all periods presented. The Company is currently evaluating the impact of this update on the consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, “*Financial Instruments – Credit Losses (Topic 326)*” which introduces new guidance for the accounting for credit losses on instruments within its scope. The new guidance introduces an approach based on expected losses to estimate credit losses on certain types of financial instruments. For trade receivables, the Company will be required to use a forward-looking expected loss model rather than the incurred loss model for recognizing credit losses which reflects losses that are probable. Credit losses relating to available-for-sale debt securities will also be recorded through an allowance for credit losses rather than as a reduction in the amortized cost basis of the securities. The guidance is effective for fiscal years beginning after December 31, 2019, including interim periods within those years. Early application of the guidance is permitted for all entities for fiscal years beginning after December 15, 2018, including the interim periods within those fiscal years. Application of the amendments is through a cumulative-effect adjustment to retained earnings as of the effective date. The Company is currently evaluating the impact of this update on the consolidated financial statements.

2. Balance Sheet Components

Inventories consisted of the following (in thousands):

	March 31, 2019	December 31, 2018
Finished goods	\$ 42,213	\$ 39,142
Component parts	3,630	3,490
Work-in-process	24	52
	<u>\$ 45,867</u>	<u>\$ 42,684</u>

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Prepaid expenses and other current assets consisted of the following (in thousands):

	March 31, 2019	December 31, 2018
Income tax receivable	\$ 4,215	\$ 2,073
Prepaid expenses	2,436	1,683
Other	2,982	2,344
	<u>\$ 9,633</u>	<u>\$ 6,100</u>

Property and equipment, net consisted of the following (in thousands):

	March 31, 2019	December 31, 2018
Leasehold improvements	\$ 6,426	\$ 5,954
Lab and warehouse equipment	6,137	5,938
Computer equipment and software	5,788	5,380
Manufacturing tooling and test equipment	4,697	4,598
Furniture and fixtures	4,645	4,670
Other	1,159	1,159
	<u>28,852</u>	<u>27,699</u>
Less: accumulated depreciation	(19,312)	(18,036)
	<u>\$ 9,540</u>	<u>\$ 9,663</u>

Accrued liabilities consisted of the following (in thousands):

	March 31, 2019	December 31, 2018
Compensation accruals	\$ 3,054	\$ 5,444
Sales returns and current portion of warranty liability	2,564	2,539
Other accrued liabilities	1,533	1,159
	<u>\$ 7,151</u>	<u>\$ 9,142</u>

Other long-term liabilities consisted of the following (in thousands):

	March 31, 2019	December 31, 2018
Deferred revenue	\$ 3,156	\$ 3,192
Other	1,855	1,272
Warranty	827	875
	<u>\$ 5,838</u>	<u>\$ 5,339</u>

3. Financial Instruments

Fair Value Measurements

The Company's financial assets that are measured at fair value on a recurring basis consist of money market funds and available-for-sale investments. The following three levels of inputs are used to measure the fair value of financial instruments:

Level 1: Quoted prices in active markets for identical assets or liabilities;

Level 2: Observable inputs other than quoted prices in active markets for identical assets and liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; and

Level 3: Unobservable inputs are used when little or no market data is available.

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The fair values for substantially all of the Company's financial assets are based on quoted prices in active markets or observable inputs. For Level 2 securities, the Company uses a third-party pricing service which provides documentation on an ongoing basis that includes, among other things, pricing information with respect to reference data, methodology, inputs summarized by asset class, pricing application and corroborative information.

Cash, Cash Equivalents and Marketable Securities

The Company determines realized gains or losses on the sale of marketable securities on a specific identification method. During the three months ended March 31, 2019 and 2018, the Company did not record significant realized gains or losses on the sales of available-for-sale investments.

The following tables show the Company's cash and available-for-sale investments' adjusted cost, gross unrealized gains, gross unrealized losses and fair value by significant investment category, recorded as cash and cash equivalents or short- or long-term investments as of March 31, 2019 and December 31, 2018 (in thousands):

March 31, 2019							
	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value	Cash and Cash Equivalents	Short-term Investments	Long-term Investments
Cash	\$ 14,782	\$ —	\$ —	\$ 14,782	\$ 14,782	\$ —	\$ —
Level 1:							
Money market funds	5,046	—	—	5,046	5,046	—	—
U.S. government notes	15,083	1	—	15,084	—	15,084	—
Subtotal	20,129	1	—	20,130	5,046	15,084	—
Level 2:							
Corporate bonds	22,098	9	(5)	22,102	—	18,901	3,201
Commercial paper	14,804	—	—	14,804	—	14,804	—
Subtotal	36,902	9	(5)	36,906	—	33,705	3,201
Total	\$ 71,813	\$ 10	\$ (5)	\$ 71,818	\$ 19,828	\$ 48,789	\$ 3,201

December 31, 2018							
	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value	Cash and Cash Equivalents	Short-term Investments	Long-term Investments
Cash	\$ 30,501	\$ —	\$ —	\$ 30,501	\$ 30,501	\$ —	\$ —
Level 1:							
Money market funds	6,903	—	—	6,903	6,903	—	—
U.S. government notes	10,420	—	(14)	10,406	—	10,406	—
Subtotal	17,323	—	(14)	17,309	6,903	10,406	—
Level 2:							
Corporate bonds	21,612	1	(37)	21,576	—	21,576	—
Commercial paper	23,803	—	—	23,803	2,991	20,812	—
Subtotal	45,415	1	(37)	45,379	2,991	42,388	—
Total	\$ 93,239	\$ 1	\$ (51)	\$ 93,189	\$ 40,395	\$ 52,794	\$ —

As of March 31, 2019, the Company considers the declines in market value of its investment portfolio to be temporary in nature and does not consider any of its investments other-than-temporarily impaired. During the three months ended March 31, 2019 and 2018, the Company did not recognize any significant impairment charges. The Company invests in highly-rated securities, and its investment policy limits the amount of credit exposure to any one

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issuer. The policy requires investments to be investment grade, with the primary objective of minimizing the potential risk of principal loss. Fair values were determined for each individual security in the investment portfolio. The maturities of the Company's long-term investments range from one to two years. When evaluating an investment for other-than-temporary impairment the Company reviews factors such as the length of time and extent to which fair value has been below its cost basis, the financial condition of the issuer and any changes thereto, changes in market interest rates, and the Company's intent to sell, as well as the fact it is not more likely than not that the Company will be required to sell the investment before recovery of the investment's cost basis, which may be maturity.

Fair Value of Other Financial Instruments

The carrying amounts reported in the accompanying condensed consolidated financial statements for restricted cash, accounts payable and accrued liabilities approximate their fair value because of the short-term nature of the accounts.

Derivative Financial Instruments

The Company has foreign currency exposure related to the operations in Australia, Canada, the European Union, New Zealand, Switzerland, and the United Kingdom, as well as other foreign locations. The Company has entered into forward contracts to help offset the exposure to movements in foreign currency exchange rates in relation to certain U.S. dollar denominated balance sheet accounts of its subsidiaries in the United Kingdom and Australia. The foreign currency derivatives are not designated as accounting hedges. The Company recognizes these derivative instruments as either assets or liabilities in the accompanying condensed consolidated balance sheets at fair value. The Company records changes in the fair value (i.e. gains or losses) of these derivative instruments in the accompanying condensed consolidated statement of operations as other income (expense), net. Gains and losses on derivative instruments are included in operating activities in the accompanying condensed consolidated statement of cash flows.

The Company settles its foreign exchange contracts on the last day of every month and enters into a new forward contract for the next month. As a result, there are no assets or liabilities recorded in the accompanying condensed consolidated balance sheets related to derivative instruments as of March 31, 2019.

The following table shows the pre-tax income (losses) of the Company's derivative instruments not designated as hedging instruments (in thousands):

	Income Statement Location	Three Months Ended March 31,	
		2019	2018
Foreign exchange forward contracts	Other income (expense), net	\$ (420)	\$ (548)

4. Leases

Operating Leases

The Company leases office and warehouse space under operating leases that expire between 2019 and 2025. The terms of the leases include periods of free rent, options for the Company to extend the leases (typically three to five years) and increasing rental rates over time. The Company recognizes rental expense under these operating leases on a straight-line basis over the lives of the leases.

Operating lease cost was approximately \$1.1 million and \$0.8 million for the three months ended March 31, 2019 and 2018, respectively.

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Other information related to leases was as follows (in thousands):

	Three Months Ended
	March 31,
	2019
Cash paid for amounts included in the measurement of lease liabilities:	
Operating cash flows from operating leases	\$ 1,274
Right-of-use assets obtained in exchange for new operating lease liabilities	1,088
Weighted-average remaining lease term - operating leases	3.2 years
Weighted-average discount rate - operating leases	5.8 %

Future minimum rental payments due under non-cancelable operating leases with initial or remaining terms in excess of one year consist of the following as of March 31, 2019 (in thousands):

One year	\$ 5,140
Two years	4,730
Three years	2,000
Four years	902
Five years	482
Thereafter	610
Total lease payments	13,864
Less landlord paid tenant improvements	(597)
Less imputed interest	(1,419)
Total	\$ 11,848

5. Acquisitions

NEEO Acquisition

On February 1, 2019, Control4 acquired all the outstanding shares of common stock of the Switzerland-based, NEEO AG (“NEEO”) for total consideration transferred of \$14.5 million. In accordance with the purchase agreement, \$1.3 million of the purchase price will be held for up to 18 months from the acquisition date to cover any of the sellers’ post-closing obligations, including without limitation any indemnification that may arise. The Company has classified the \$1.3 million holdback in other long-term liabilities.

Total consideration transferred for the NEEO acquisition was allocated to tangible and identifiable intangible assets acquired and liabilities assumed. The Company has adjusted the preliminary allocation of consideration as included in Exhibit 99.2 of Form 8-K/A filed with the U.S. Securities and Exchange Commission on April 16, 2019, with corresponding impacts to the pro forma adjustments reported in the unaudited pro forma condensed combined balance sheet as of December 31, 2018. First, total consideration transferred was increased from \$11.0 million to \$14.5 million due to a pre-existing relationship between Control4 and NEEO that was effectively settled as a result of the acquisition. Second, a measurement period adjustment was made to remove the deferred tax liability of \$1.7 million due to NEEO’s net deferred tax asset position.

The preliminary amount of consideration transferred is subject to potential adjustments in the event that the preliminary estimates of accrued liabilities or intangible assets are adjusted pending final valuation, and due to tax-related matters that could have a material impact on the consolidated financial statements. The Company expects the allocation of the consideration transferred to be final within the measurement period (up to one year from the acquisition date).

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The following reflects the Company's preliminary allocation of consideration transferred for the NEEO acquisition (in thousands):

	NEEO Acquisition
Cash	\$ 445
Accounts receivable	17
Inventory	577
Other assets acquired	542
Intangible assets	6,384
Goodwill	9,242
Total assets acquired	<u>17,207</u>
Accounts payable	758
Accrued liabilities	1,478
Pension liability	488
Total net assets acquired	<u>\$ 14,483</u>

Identifiable Intangible Assets

The Company acquired intangible assets that consisted of remote-control technology and other internally developed technologies, which had estimated fair values of \$5.8 million and \$0.6 million, respectively. The Company will amortize the intangible assets on a straight-line basis over their estimated useful lives of 5 years for the remote-control technology and 2-3 years for the other internally developed technologies. The amortization of these intangible assets is not deductible for income tax purposes.

Goodwill

Goodwill of \$9.2 million represents the excess of consideration transferred over the fair value of assets acquired and liabilities assumed and is attributable to NEEO's assembled workforce, expected synergies and new products. This goodwill is not deductible for income tax purposes.

Other

From the date of acquisition through March 31, 2019, the Company recorded losses of \$0.2 million associated with NEEO but did not record any revenue. In addition, the Company incurred approximately \$0.5 million in total acquisition-related costs, which are included in the accompanying condensed consolidated statements of operations as research and development and general and administrative expenses for the three months ended March 31, 2019.

Pro Forma Information

The unaudited pro forma information for the three months ended March 31, 2019 and 2018 presented below includes the effects of the NEEO acquisition as if it had been consummated as of January 1, 2018, with adjustments to give effect to pro forma events that are directly attributable to the acquisition, including adjustments related to the amortization of acquired intangible assets, stock-based compensation expense, interest expense and estimated tax impacts. These adjustments are based upon information and assumptions available at the time of filing this Quarterly Report on Form 10-Q. The unaudited pro forma information does not reflect any operating efficiency or potential cost savings that could result from the consolidation of NEEO. Accordingly, the unaudited pro forma information is presented for informational purposes only and is not necessarily indicative of the actual results of the combined company if the acquisition had occurred at the beginning of the period presented, nor is it indicative of the future results of operations.

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	Three Months Ended	
	March 31,	
	2019	2018
Revenue	\$ 60,447	\$ 59,306
Income (loss) from operations	(3,242)	(247)
Net income (loss)	\$ (2,386)	\$ (241)
Net income (loss) per common share:		
Basic	\$ (0.09)	\$ (0.01)
Diluted	\$ (0.09)	\$ (0.01)

Distributor Acquisitions

During the three months ended March 31, 2019, the Company began working directly with home automation integrators in Ireland, New Zealand, and Switzerland to better serve and support customers in those countries. The Company transferred \$1.4 million in consideration for the acquisition of these distributors. This consideration was allocated to \$0.7 million of inventory, \$0.1 million of other assets, and \$0.6 million of goodwill.

The Company determined these acquisitions were not significant.

6. Goodwill and Intangible Assets*Goodwill*

Changes in the carrying amount of goodwill consisted of the following (in thousands):

	Amount
Balance at December 31, 2018	\$ 21,530
Current period acquisitions	9,874
Foreign currency translation adjustment	(1)
Balance at March 31, 2019	<u>\$ 31,403</u>

Goodwill represents the excess of consideration transferred over the fair value of assets acquired and liabilities assumed.

[Table of Contents](#)*Amortizable Intangible Assets*

The Company's intangible assets and related accumulated amortization consisted of the following as of March 31, 2019 and December 31, 2018 (in thousands):

	March 31, 2019		
	Gross Carrying Amount	Accumulated Amortization	Net
Developed technology	\$ 23,854	\$ (11,251)	\$ 12,603
Customer relationships	12,009	(4,424)	7,585
Trademark/trade name	6,776	(1,575)	5,201
Total intangible assets	<u>\$ 42,639</u>	<u>\$ (17,250)</u>	<u>\$ 25,389</u>

	December 31, 2018		
	Gross Carrying Amount	Accumulated Amortization	Net
Developed technology	\$ 17,495	\$ (10,145)	\$ 7,350
Customer relationships	12,009	(4,050)	7,959
Trademark/trade name	6,776	(1,434)	5,342
Non-competition agreements	295	(295)	—
Total intangible assets	<u>\$ 36,575</u>	<u>\$ (15,924)</u>	<u>\$ 20,651</u>

The weighted average amortization period for developed technology, customer relationships, and trademarks/trade names is 5.2 years, 8.4 years, and 12.0 years, respectively; and 7.0 years for all amortizable intangible assets in total.

The Company recorded amortization expense during the three-month periods ended March 31, 2019 and 2018 for these intangible assets as follows (in thousands):

	Three Months Ended March 31,	
	2019	2018
Cost of revenue	\$ 864	\$ 921
Research and development	259	28
Sales and marketing	497	497
Total amortization of intangible assets	<u>\$ 1,620</u>	<u>\$ 1,446</u>

Amortization of finite lived intangible assets as of March 31, 2019 for the next five years is as follows (in thousands):

	Amount
Remainder of 2019	\$ 5,355
2020	6,051
2021	3,457
2022	3,243
2023	3,183
Thereafter	4,100
	<u>\$ 25,389</u>

7. Long-Term Obligations*Loan and Security Agreement*

On February 6, 2018, Control4 entered into the 2018 Loan Amendment with SVB, which amends the 2013 Loan Agreement.

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In the 2018 Loan Amendment, Control4 increased the revolving credit facility from \$30.0 million to \$40.0 million under the terms of the 2013 Loan Agreement (the “New Credit Facility”). All borrowings under the New Credit Facility are collateralized by the general assets of the Company. Amounts borrowed under the New Credit Facility are due and payable in full on the maturity date, which is January 29, 2020. Advances made pursuant to the New Credit Facility depend on Control4’s leverage ratio and are either: (i) Prime Rate Advances, which bear interest at the Prime Rate plus a Prime Rate Margin of either 0% or 0.25%, or (ii) LIBOR Rate Advances, which bear interest at the LIBOR Rate plus a LIBOR Rate Margin of either 2.50% or 2.75%.

Control4 will be assessed an unused revolving line facility fee of 0.25% in any quarter wherein the amount of advances under the New Credit Facility is less than \$15.0 million. As of March 31, 2019, Control4 had no outstanding borrowings under the revolving credit facility.

The 2018 Loan Amendment contains various restrictive and financial covenants, and the Company was in compliance with each of these covenants as of March 31, 2019.

8. Revenue Recognition

Revenue is recognized upon transfer of control of promised products or services to customers in an amount that reflects the consideration expected to be received in exchange for those products or services. Revenue is recognized net of allowances for returns and any taxes collected from customers, which are subsequently remitted to governmental authorities.

Shipping charges billed to dealers and distributors are included in product revenue and related shipping costs are included in cost of revenue. The Company has elected to account for shipping and handling activities performed after control has been transferred to the customer as a fulfillment cost and accrues for these costs if revenue is recognized before contractually agreed-upon shipping and handling occurs.

Solution Products Revenue

The Company sells its solution products through a network of independent dealers, distributors and retailers. These dealers, distributors and retailers generally sell the Company’s products as part of a bundled sale, which typically includes other third-party products and related services, project design, installation services and on-going support.

The Company’s products are generally highly dependent on, and interrelated with, the underlying operating system and cannot function without the operating system. In these cases, the hardware and software license are accounted for as a single performance obligation and revenue is recognized at the point in time when ownership is transferred to dealers, distributors, and retailers, which is typically at the time the product is shipped. In cases where revenue is allocated to software updates and technical support, primarily because the updates and technical support are provided at no additional charge, revenue is recognized as the updates and technical support are provided, which is ratably over the estimated life of the related device.

Certain customers may receive cash-based incentives or credits; which are accounted for as variable consideration. The Company records estimated reductions to revenue for dealer incentives at the time of the initial sale. The estimated reductions to revenue are based on the sales terms and the Company’s historical experience and trend analysis. The most common incentive relates to amounts paid or credited to dealers for achieving defined volume levels or growth objectives.

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Subscription Service Revenue

The Company offers a subscription service that allows consumers to control and monitor their homes remotely and allows the consumer's respective Control4 dealer to perform remote diagnostic services. Subscription revenue is deferred at the time of payment and recognized ratably over the contract period which is typically one year.

Third-Party Product Revenue

The Company recognizes revenue net of cost of revenue for non-inventoried, third-party products sold through the Company's online ordering system. The Company's primary role is to arrange for another entity to provide the goods or services and the Company does not control the promised good or service before it is transferred to the customer.

Significant Judgments

The Company's contracts with dealers, distributors, and retailers can include promises to transfer multiple products and services. Determining whether multiple products and services are considered distinct performance obligations that should be accounted for separately versus together may require significant judgment.

Judgment is required to determine the stand-alone selling price ("SSP") for each distinct performance obligation. The Company uses a single amount to estimate SSP for items that are not sold separately, including software updates and technical support provided at no additional charge. In instances where SSP is not directly observable, such as when the Company does not sell the product or service separately, the SSP is determined using information that may include market conditions and other observable inputs.

The Company's products are generally sold with a limited right of return and the Company may provide other credits or incentives, which are accounted for as variable consideration when estimating the amount of revenue to recognize.

Disaggregated Revenue

The Company's revenue includes amounts earned through sales to dealers and distributors located outside of the United States. There was no single foreign country that accounted for more than 10% of total revenue for the three months ended March 31, 2019 and 2018. The following table sets forth revenue from the United States, Canada and all other international dealers and distributors combined (in thousands):

	Three Months Ended	
	March 31,	
	2019	2018
Revenue-United States	\$ 41,003	\$ 40,964
Revenue-Canada	5,171	5,264
Revenue-all other international sources	14,251	12,921
Total revenue	\$ 60,425	\$ 59,149
International revenue (excluding Canada) as a percent of total revenue	24 %	22 %

Contract Balances

As of March 31, 2019 and December 31, 2018, accounts receivable, net of allowance for doubtful accounts, were \$30.3 million and \$33.0 million, respectively.

The Company extends credit to some of its dealers and distributors, which consist primarily of small, local businesses. Issuance of credit is based on ongoing credit evaluations by the Company of dealers' and distributors' financial condition and generally requires no collateral. Trade accounts receivable are recorded at the invoiced amount and do not generally bear interest. The Company maintains an allowance for doubtful accounts to reserve for potential uncollectible receivables. The allowance is based upon the creditworthiness of the Company's dealers

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and distributors, the dealers' and distributors' historical payment experience, the age of the receivables and current market and economic conditions. Provisions for potentially uncollectible receivables are recorded in sales and marketing expenses. The Company writes off accounts receivable balances to the allowance for doubtful accounts when it becomes likely that they will not be collected.

The following table presents the changes in the allowance for doubtful accounts (in thousands):

	<u>Allowance</u>
Balance at December 31, 2018	\$ 1,529
Provision	8
Write-offs	(291)
Balance at March 31, 2019	<u>\$ 1,246</u>

Payment terms and conditions vary by contract type, although terms generally include a requirement of payment within 30 days. In instances where the timing of revenue recognition differs from the timing of invoicing, the Company has determined the contracts generally do not include a significant financing component. The primary purpose of invoicing terms is to provide customers with simplified and predictable ways of purchasing products and services, not to receive financing from customers, such as invoicing at the beginning of a subscription term with revenue recognized ratably over the contract period.

Deferred revenue is comprised mainly of unearned revenue related to subscription services as well as revenue deferred on the sale of solution products for software updates and technical support. The following table presents the changes in deferred revenue for the three months ended March 31, 2019 (in thousands):

	<u>Deferred Revenue</u>
Balance at December 31, 2018	\$ 8,699
Deferred revenue	4,593
Recognition of deferred revenue	(4,548)
Balance at March 31, 2019	<u>\$ 8,744</u>

Revenue allocated to remaining performance obligations represent contracted revenue that has not yet been recognized ("contracted not recognized"), which includes unearned revenue and amounts that will be invoiced and recognized as revenue in future periods. Contracted but not recognized revenue was \$9.8 million as of March 31, 2019, of which the Company expects to recognize approximately 44% of the revenue over the next 12 months and the remainder over a period of three to four years.

Assets Recognized from the Costs to Obtain a Contract with a Customer

The Company has elected to immediately expense contract acquisition costs that would be amortized in one year or less. The Company recognizes an asset for the incremental costs of obtaining a contract with a customer if the benefit of those costs is expected to be longer than one year; these incremental costs were immaterial during both periods presented.

9. Equity Compensation

Stock Options

In 2003, the Board of Directors adopted the 2003 Equity Incentive Plan (the “2003 Plan”), which provided for the granting of nonqualified and incentive stock options, stock appreciation rights, stock awards, restricted stock units and restricted stock awards. Under the 2003 Plan, the Company was able to grant nonqualified and incentive stock options to directors, employees and non-employees providing services to the Company. On June 11, 2013, the Company’s Board of Directors adopted the 2013 Stock Option and Incentive Plan (the “2013 Plan”), which was subsequently approved by the Company’s stockholders. The 2013 Plan became effective as of the closing of the Company’s initial public offering. To the extent that any awards outstanding under the 2003 Plan are forfeited or lapse unexercised after August 1, 2013, the shares of common stock subject to such awards will become available for issuance under the 2013 Plan. The 2013 Plan provides for annual increases in the number of reserved shares of 5% of the outstanding number of shares of the Company’s Common Stock as of the preceding December 31. On January 1, 2019, the number of reserved shares was increased by 1,325,845 in accordance with the provisions of the 2013 Plan.

A summary of stock option activity for the three months ended March 31, 2019 is presented below:

	Shares Subject to Options Outstanding	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)
Balance at December 31, 2018	1,081,212	12.98	
Exercised	(32,010)	9.70	
Expired	(2,626)	16.96	
Forfeited	(1,336)	7.28	
Balance at March 31, 2019	<u>1,045,240</u>	13.08	
Exercisable options at March 31, 2019	1,010,354	13.21	4.4
Vested and expected to vest at March 31, 2019	1,045,240	13.08	4.4

The following table summarizes information about stock options outstanding and exercisable at March 31, 2019:

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Weighted Average Exercise Price	Number of Underlying Shares	Weighted- Average Remaining Contractual Life (in years)	Number of Underlying Shares	Weighted- Average Remaining Contractual Life (in years)
\$ 4.89 - 7.49	6.22	269,614	2.4	267,480	2.3
\$ 8.16 - 12.93	10.57	274,926	4.9	242,174	4.8
\$ 12.98 - 19.56	15.60	270,481	5.6	270,481	5.6
\$ 20.91 - 22.92	21.16	230,219	4.8	230,219	4.8
		<u>1,045,240</u>		<u>1,010,354</u>	

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For the stock option awards vested during the three months ended March 31, 2019, the total fair value was \$0.1 million. The following table summarizes the aggregate intrinsic-value of options exercised, exercisable and vested and expected to vest (in thousands):

	For the Three Months Ended and as of March 31,	
	2019	2018
Options Exercised	\$ 269	\$ 2,765
Options Exercisable	4,757	15,335
Options Vested and Expected to Vest	5,026	17,203

Restricted stock units

A summary of restricted stock unit activity for the three months ended March 31, 2019 is presented below:

	Number of Shares	Weighted Average Grant Date Fair Value
Non-vested balance at December 31, 2018	824,365	\$ 19.77
Awarded	808,520	17.69
Vested	(314,606)	19.07
Forfeited	(9,002)	19.39
Non-vested balance at March 31, 2019	<u>1,309,277</u>	18.66

During the three months ended March 31, 2019, 314,606 restricted stock units vested of which 103,094 shares were withheld for tax purposes resulting in the issuance of 211,512 shares of common stock.

Company Matching Contribution to the 401(k) Plan

The Company offers a 401(k) Plan and in November 2016, the Company's Board of Directors authorized a matching contribution by the Company starting in 2017 and amended effective in 2019. Current matching contributions are as follows: the Company will match 100% of the first 1% of salary contributed by a participant, and 70% of the next 5% of salary contributed by a participant, for a maximum matching contribution of 4.5% of the salary of a participant up to the limit on contributions imposed by the Internal Revenue Service ("IRS"). Currently, the Company funds its match in contribution with shares of Control4's common stock. During the three months ended March 31, 2019, the Company contributed 34,854 shares of stock to employees under this plan and recorded \$0.6 million of expenses associated with this contribution.

Stock-based compensation expense

Total stock-based compensation expense has been classified as follows in the accompanying condensed consolidated statements of operations (in thousands):

	Three Months Ended March 31,	
	2019	2018
Cost of revenue	\$ 78	\$ 68
Research and development	1,287	1,084
Sales and marketing	870	959
General and administrative	1,294	1,224
Total stock-based compensation expense	<u>\$ 3,529</u>	<u>\$ 3,335</u>

At March 31, 2019, there was \$0.6 million of total unrecognized compensation cost related to non-vested stock option awards that will be recognized over a weighted-average period of 0.3 years. At March 31, 2019, there was \$18.0 million of total unrecognized compensation cost related to non-vested restricted stock units that will be recognized over a weighted-average period of 2.3 years if all vesting conditions are met.

10. Share Repurchases

During the three months ended March 31, 2019, the Company repurchased 139,782 shares for \$2.5 million compared to 300,000 shares for \$7.4 million in the same period in 2018.

In October 2018, the Company's Board of Directors authorized the expansion of the repurchase program providing approval for the Company to repurchase an additional \$20 million in Control4 common stock from time to time on the open market until December 31, 2019. As a result, the Company has \$13.6 million remaining under the share repurchase program.

11. Income Taxes

Income tax benefit was \$0.8 million for the three months ended March 31, 2019, compared to \$0.1 million for the three months ended March 31, 2018, or approximately 28% and 14% of income (loss) before income taxes, respectively. The effective tax rate for the three months ended March 31, 2019 differs from the U.S. federal statutory rate of 21% primarily due to the limitations on tax deductions allowable for executive compensation and global intangible low-taxed income, or GILTI, state income taxes, and foreign income taxes; offset by tax deductions resulting from stock-based compensation.

As of December 31, 2018, the Company's NOL carryforward amounts for U.S. federal income and state tax purposes were \$57.1 million and \$61.1 million, respectively. The federal and state NOL carryforwards will expire between 2020 and 2037 if not utilized. In addition to the NOL carryforwards, as of December 31, 2018, the Company had U.S. federal and state research and development credit carryforwards of \$6.4 million and \$2.8 million, respectively, which will expire between 2019 and 2034.

The Company files income tax returns in the United States, including various state and local jurisdictions. The Company's subsidiaries file income tax returns in Australia, China, Germany, India, New Zealand, Serbia, Switzerland, and the United Kingdom. The Company is subject to federal income tax as well as income tax of multiple state and foreign jurisdictions. The Company is no longer subject to income tax examinations for the following jurisdictions and years: federal, for years before 2015; state and local, for years before 2014; or foreign, for years before 2013. However, federal net operating loss and credit carryforwards from all years are subject to examination and adjustments for at least three years following the year in which the attributes are used.

12. Retirement Benefits

As part of the acquisition of NEEO, the Company assumed a defined benefit plan covering all employees in Switzerland. GAAP requires recognition of the funded status, or difference between the fair value of plan assets and the projected benefit obligations of the pension plan on the balance sheet, by recording a corresponding expense in net loss. If the projected benefit obligation exceeds the fair value of plan assets, then that difference or unfunded status represents the pension liability.

The Company records a net periodic pension cost in the condensed consolidated statements of comprehensive income (loss). The liabilities and annual income or expense of the pension plan is determined using methodologies that involve several actuarial assumptions, the most significant of which are the discount rate and the long-term rate of asset return, based on the market-related value of assets. The expected long-term rate of return on plan assets during the year is 1.5%. Future benefits, to the extent that they are based on compensation, include salary increases consistent with past experiences and estimates of future increases in the Swiss labor market. The fair value of plan assets is determined based on prevailing market prices.

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The components of net periodic pension cost and other amounts recognized in other comprehensive loss before taxes are as follows (in thousands):

	Three Months Ended	
	March 31,	
	2019	
Service Cost	\$	50
Interest Cost		2
Expected Return on Plan Assets		(2)
Amortization of initial net obligation (asset)		7
Amortization of net (gain) loss		2
Net periodic benefit cost		59

The components of net periodic benefit cost other than the service cost component are included in the line item “other income (expense), net” in the condensed consolidated statement of operations.

The Company contributed \$172,000 to the pension plan during the three months ended March 31, 2019. The Company expects to contribute approximately \$60,000 to the pension plan during the remainder of 2019.

13. Related Party Transactions

As part of the acquisition of NEEQ, the Company assumed a \$0.2 million obligation due to one of the former owners of NEEQ, who is now a current employee, that is outstanding as of March 31, 2019.

14. Commitments and Contingencies

Purchase Commitments

The Company had non-cancellable purchase commitments for the purchase of inventory, which extend through March 2020 totaling approximately \$61.3 million as of March 31, 2019.

Indemnification of Directors and Officers

The Company has agreed to indemnify its officers and directors for certain events or occurrences while the officer or director is or was serving at the Company’s request in such capacity. The maximum amount of potential future indemnification is unlimited; however, the Company has a directors’ and officers’ insurance policy that provides corporate reimbursement coverage that limits its exposure and enables it to recover a portion of any future amounts paid. The Company has no liabilities recorded for these agreements as of March 31, 2019, as there were no outstanding claims.

Legal Matters

From time to time, the Company may become involved in legal proceedings arising in the ordinary course of business. The Company is not presently a party to any legal proceedings, that if determined adversely to Control4, the Company believes would individually or in the aggregate have a material adverse effect on the business, results of operations, financial condition or cash flows.

15. Subsequent Events

On May 8, 2019, the Company entered into an Agreement and Plan of Merger (the “Merger Agreement”) with Wirepath Home Systems, LLC, a North Carolina limited liability company (“Parent”), and Copper Merger Sub Inc., a Delaware corporation and wholly-owned subsidiary of Parent, to be acquired for an aggregate value of approximately \$680 million (the “Merger”). Under the terms of the Merger Agreement, Company stockholders will receive \$23.91 per share in cash upon the closing of the Merger. The Merger is subject to approval by the Company’s stockholders, the expiration or termination of the applicable waiting period under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended, the decisions, orders, consents or expiration of any waiting periods required to consummate the Merger under the foreign investment, monopolization and anti-competition laws and regulations of certain foreign jurisdictions, the accuracy of the representations and warranties and compliance with the covenants contained in the Merger Agreement, subject to qualifications, and other customary closing conditions. The Merger is currently expected to close in the second half of 2019.

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis is intended to provide greater details of our results of operations and financial condition and should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2018, which was filed with the U.S. Securities and Exchange Commission (the "SEC") on February 11, 2019, and our condensed consolidated financial statements and the notes thereto included elsewhere in this document, as well as other documents we file with the SEC from time to time. Certain statements in this Quarterly Report constitute forward-looking statements and as such, involve risks and uncertainties, as well as assumptions that, if they never materialize or prove incorrect, could cause our results to differ materially from those expressed or implied by such forward-looking statements. Such forward-looking statements include any expectation of earnings, revenues or other financial items including without limitation statements about the anticipated effect of any acquisitions on our business or financial performance; any statements of the plans, strategies and objectives of management for future operations or growth; factors that may affect our operating results; statements related to future capital expenditures; statements related to future economic conditions or performance; statements as to industry trends or market opportunities and other matters that do not relate strictly to historical facts or statements of assumptions underlying any of the foregoing. These statements are often identified by the use of words such as "anticipate," "believe," "continue," "could," "estimate," "expect," "intend," "may" or "will," and similar expressions or variations. Such forward-looking statements are subject to risks, uncertainties and other factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those discussed in the section titled "Risk Factors" included in Item 1A of Part II of this Quarterly Report, and the risks discussed in our other SEC filings.

We urge you to consider these factors carefully in evaluating the forward-looking statements contained in this Quarterly Report and not give undue reliance to these forward-looking statements. These statements are based on the beliefs and assumptions of our management based on information currently available to management. The forward-looking statements included in this Quarterly Report are made only as of the date of this Quarterly Report. All subsequent written or oral forward-looking statements attributable to our company or persons acting on our behalf are expressly qualified in their entirety by these cautionary statements. We do not undertake, and specifically disclaim, any obligation to update any forward-looking statements to reflect the occurrence of events or circumstances after the date of such statements, except as required by law.

Our Management's Discussion and Analysis of Financial Condition and Results of Operations (the "MD&A") is provided in addition to the accompanying condensed consolidated financial statements and notes to assist readers in understanding our operations, financial condition and cash flows. Our MD&A is organized as follows:

- *Overview.* Discussion of our business and overall analysis of financial and other highlights affecting our business in order to provide context for the remainder of the MD&A.
- *Factors and Trends Affecting our Performance.* A summary of certain market factors and trends that we believe are important to our business that we must successfully address in order to continue to grow our business.
- *Key Operating and Financial Metrics.* Key operating and financial metrics that we use to evaluate and manage our business.
- *Results of Operations.* An analysis of our financial results comparing 2019 to 2018.
- *Liquidity and Capital Resources.* An analysis of changes in our balance sheets and cash flows, and discussion of our financial condition and potential sources of liquidity.
- *Non-GAAP Financial Measures.* A reconciliation of certain non-GAAP financial measures used by management to understand and evaluate our operating performance and trends, to prepare and approve our annual budget, and to develop short- and long-term operational plans.

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- *Contractual Obligations and Off-Balance Sheet Arrangements.* An overview of our contractual obligations, contingent liabilities, commitments and off-balance sheet arrangements outstanding as of March 31, 2019, including an expected payment schedule.
- *Critical Accounting Estimates.* Accounting estimates that we believe are most important to understanding the assumptions and judgments incorporated in our reported financial results and forecasts.

Overview

We are a leading provider of professionally-installed smart home and business solutions that are designed to personalize and enhance how consumers engage with an ever-changing connected world. Our entertainment, smart lighting, comfort and convenience, safety and security, and networking solutions unlock the potential of connected devices, making entertainment systems easier to use and more accessible, homes and businesses more comfortable and energy efficient, and individuals more connected and secure. Our premium smart home and small business solutions provide consumers with the ability to integrate audio, video, lighting, temperature, security, communications, network management and other functionalities into a unified automation solution, customized to match their lifestyles and business needs. Our advanced software, delivered through our controller and user-interface products together with various cloud services, power this customized experience, enabling cohesive interoperability with thousands of connected Control4 and third-party devices.

Consumers purchase our smart solutions from our worldwide network of certified independent dealers, distributors, and retailers. These dealers, distributors and retailers design and install customized solutions to fit the specific needs of each consumer, whether it is a one-room home theater set-up or a whole-home automation system that features the integration of audio, video, lighting, temperature, security, network management, and communications devices. Our products are installed in both new and existing residences, multi-dwelling units and small commercial facilities. We refer to revenue from sales of our products through these dealers, distributors and retailers as our Core revenue (“Core revenue”). In addition, a portion of our revenue is attributable to sales in the hospitality industry, primarily related to products installed in hotels, which is excluded from our calculation of Core revenue as well as certain specialty display products and associated installation sales in Australia. Our revenue from sales to hotels is generally project-based and has been significant in some periods and insignificant in other periods. In the future, we expect revenue from hospitality to continue to be project-based and uneven from period to period. During the three months ended March 31, 2019, over 4,590 active direct dealers were authorized to sell and install the full Control4 line of products in the United States, Australia, Canada, the United Kingdom, and 63 other countries, and 31 distributors were authorized to cover an additional 42 countries where we do not have direct dealer relationships. These distributors sell our solutions through dealers and provide warehousing, training, technical support, and billing for dealers in each of those countries. We have approximately 870 additional active dealers and 8 distributors that are currently authorized to sell only our Pakedge and Triad product lines.

We derive the majority of our revenue from the sale of products that contain our proprietary software, which functions as the operating system of the home or business and other related ancillary products used in automation projects. We also generate revenue from the sale of annual subscriptions to our 4Sight subscription service. Our 4Sight services give homeowners the ability to, among other things, (1) remotely monitor and control their smart home solutions from their mobile devices; (2) communicate through our audio/video application, Intercom Anywhere; and (3) enable voice recognition services.

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We were founded in 2003 and began shipping our products and generating revenue in 2005. Our revenue growth rates for the last five complete calendar years are shown in the following table (dollars in millions):

	For the Years Ended December 31,				
	2018	2017	2016	2015	2014
		* As adjusted	* As adjusted		
Core revenue	\$ 267.7	\$ 238.8	\$ 203.2	\$ 160.7	\$ 144.7
Core revenue growth over prior year	12 %	18 %	26 %	11 %	14 %
Other revenue	\$ 4.8	\$ 5.4	\$ 4.9	\$ 2.5	\$ 4.1
Other revenue changes over prior year	(11)%	10 %	96 %	(39)%	95 %
Total revenue	\$ 272.5	\$ 244.2	\$ 208.1	\$ 163.2	\$ 148.8
Total revenue growth over prior year	12 %	17 %	28 %	10 %	16 %

*The revenue growth rate data for the years ended December 31, 2017 and 2016 reflects the adoption of ASC 606. The revenue growth rate data for the years ended December 31, 2015, 2014 and 2013 does not reflect the adoption of ASC 606.

Over the past five years, we have experienced double-digit annual growth in Core revenue. Our Core revenue growth during that period has been the result of a combination of the net addition of new independent dealers and distributors to our sales channels, an increase in the number of projects performed by our existing network of independent dealers and distributors, and the addition of new products developed internally and acquired through business combinations. We believe our ability to grow our core sales channel has been enhanced through product innovation, expansion of our product offerings and helping our independent dealers and distributors grow their business. Some recent developments that we believe may enhance our offerings and help drive growth include, but are not limited to, the following:

- Opened an additional fulfillment center in Hebron, Kentucky, in an effort to better support our dealers with faster shipping on all products and to provide additional redundancy if there is an interruption of service experienced by one of our other fulfillment facilities;
- Expanded our KNX, a popular standard for lighting and HVAC control in global markets including Australia, China, Germany, Singapore, and the United Kingdom, solution to natively support over 300 KNX products including new keypads, lighting, HVAC, and shades. This support for KNX enables interoperability with the entire Control4 ecosystem, including support for Amazon Alexa voice control, where available, and nearly 13,000 other connected products;
- Released OS 2.10.4, featuring expanded music streaming service integration with Amazon Music and Deezer HiFi as well as added hands-on personalization choices for homeowners with our “When >> Then” automation;
- Released Intercom Anywhere, a modern video doorbell enabling homeowners to see and communicate with visitors at the front door, whether they are home or away, in addition to allowing the homeowner to see who is at the door prior to answering; and
- Unveiled over 200 Control4 Certified Showrooms built by Control4 authorized dealers at their locations across the United States, Australia, Canada, China, and the United Kingdom, revolutionizing how people learn about, experience, and interact with Control4 smart home solutions. The Control4 Certified Showroom program is designed to direct homeowners, architects, and designers in the market for smart home solutions to a location where they can experience Control4 solutions in a showroom environment.

While our historical revenue growth has been primarily organic, we have completed several acquisitions that we believe enhance our product offerings and position us for continued growth in the future. Recent acquisitions that have impacted our growth include the acquisition of Pakedge in 2016 and Triad in 2017. More recently, we have acquired NEEO in 2019, which will enhance our user interface product offerings and impact our growth in the

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future. Moreover, in the first quarter of 2019, we transitioned from a two-tier distribution model to a direct-to-dealer model in Ireland, New Zealand, and Switzerland, which we believe will position us for continued growth in those countries.

Historically, we have experienced seasonal variations in our revenue as a result of holiday-related factors that are common in our industry. Our revenue is generally highest in the fourth quarter due to consumers' desires to complete their home installations prior to the holiday season. We generally see decreased sales in the first quarter due to seasonal purchase tendencies of consumers as well as the impact of winter weather on new construction and travel in certain geographies. In addition, our year-over-year revenue growth on a quarterly basis is not always linear for a variety of reasons including: the timing of new product releases, the use of marketing programs to accelerate intra-quarter sales of certain products or product families, the impact of foreign currency fluctuations, and the impact of general regional economic conditions on consumer buying decisions and harsh weather that delayed or canceled building projects. We generally expect these seasonal and other trends to continue in the future, which may cause quarterly fluctuations in our results of operations and certain financial metrics.

Factors and Trends Affecting Our Performance

A number of industry trends have facilitated our growth over the past several years, including the proliferation of connected devices and the constant growth of network-enabled homes and businesses. From smartphones to smart watches to smart cars, technology is transforming nearly every aspect of our lives, streamlining daily routines and providing quick, easy access to the capabilities and content we want most. Not only are new technologies providing convenience on-the-go, but they are becoming increasingly accessible and interconnected. Voice services are a recent example of an emerging technology in our connected world, and our integration with Amazon Alexa helps keep us at the forefront of our industry in our adoption of voice-activated solutions. We remain committed to embracing emerging technologies through our open platform and broad ecosystem.

Our open platform makes it easy for a broad community of original equipment manufacturer partners to participate in our smart home ecosystem, which includes over 13,500 drivers and approximately 7,500 Simple Device Discovery Protocol ("SDDP") enabled products. SDDP is a software solution that we make available to manufacturers of network aware devices, which allows them to be immediately recognized by a Control4 system, allowing our integration to be completed quickly and seamlessly. We believe that companies are increasingly recognizing the value of including SDDP with their new releases to simplify integration of their products into Control4 installations. Our broad ecosystem, which includes audio, video, lighting, temperature, network, security and communication device categories, gives consumers flexibility to integrate nearly any connectable device into their smart home. In addition, our partners are constantly contributing new device integrations. As such, our dynamic ecosystem remains current with the latest product innovations and allows our smart home platform to grow alongside emerging technologies to meet our consumers' changing needs and preferences. We believe that our open platform and the resulting ecosystem is a key competitive advantage that will continue to facilitate our growth.

Our products leverage both wired and wireless technologies and are designed to be installed in both new construction and existing homes. We expect that future increases in both new home construction and existing home renovations will have a positive impact on our revenue. In new home construction, we continue to engage builders to introduce entry- to mid-level Control4 systems as a standard feature in new home projects, and we believe that the release of our new CA-1 controller, which is offered at the lowest price point of any Control4 controller, will help with adoption of our solutions in these types of projects. We further believe home automation is increasingly becoming a higher priority for home buyers, and this is one of the reasons for our investment in national and regional builder programs.

We believe that the growth of our business and our future success are dependent upon many factors, including the rates at which consumers adopt our products and services, our commitment to growing the awareness of our brands, our ability to optimize and expand our dealer and distributor network, our ability to expand internationally, our ability to meet competitive challenges, and our ability to respond to worldwide economic events. While each of these areas presents significant opportunities for us, they also pose important challenges that we must successfully address to sustain or expand the growth of our business and improve our results of operations. These challenges include:

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- ***Increasing Adoption Rates of Our Products and Services.*** We are focused on increasing adoption rates of our products and services through enhancements to our software platform and product offerings. We intend to accomplish these enhancements through both continued investments in research and development activities and acquisitions of complementary businesses and technologies.
- ***Growing Our Leadership Position in the Industry.*** We are committed to growing awareness of the Control4, Pakedge, and Triad brands among our dealers, distributors and partners. We believe that our investments in creating brand awareness in the industry have contributed to dealer recruitment, product adoption, and revenue growth. We are proud of the many awards we received from various industry groups and dealer consortiums, formally recognizing our commitment to excellence. For example, Control4 was named the top home automation provider in seven of the 2018 CE Pro Brand Analysis categories. Notably, Control4 was named the Brand Leader in Whole-House Automation for the fourth consecutive year, and Pakedge was named the Brand Leader for Home Networks for the sixth year in a row. Furthermore, in 2019, Control4 received a record 10 CE Pro Quest for Quality awards, the highest number of awards given to a single manufacturer, including Platinum for Best Technical Support, Best Lead Generation, and Best Sales & Marketing Assistance.
- ***Accelerating and Enhancing Consumer Lead Generation.*** We remain focused on generating and pursuing leads received from our marketing efforts. We are continuing to invest in new online tools and inside sales representatives to qualify inbound inquiries and direct them to qualified independent dealers. To date, our enhanced lead generation strategies continue to increase consultations, bids and project installations. Through the continual optimization of our marketing efforts and investment, we believe we can improve lead conversion rates and increase the amount of revenue per lead.
- ***Optimizing and Expanding Our North America Dealer Network.*** We intend to continue to optimize the performance of and expand our network of dealers in North America to ensure that we have geographic coverage and technical expertise to address our existing markets and new markets into which we plan to expand. We continue to work with all appropriately qualified dealers to explore our home control, networking, and audio solutions, and we continue to cross-train and cross-certify dealers in accordance with our existing standards of technical proficiency and business practices.
- ***Expanding our International Dealer and Distributor Network.*** We believe that our future growth will depend in part on our ability to expand our dealer and distributor network outside of North America, to adapt our products and services to foreign markets, and to increase awareness of our brands internationally. We continue to add field sales and service personnel to assist in the optimization of our international channels. We have adopted a direct-to-dealer model in specific international regions, namely in Australia, China, Germany, Ireland, New Zealand, Switzerland, and the United Kingdom, and we will continue to evaluate opportunities in other countries.
- ***Managing Competition.*** The market for home automation is fragmented, highly competitive and continually evolving. In addition to competing with traditional players in the luxury segment of the home automation market, including Crestron, Elan, and Savant, a number of large technology companies such as Amazon, Apple, Google, and Samsung offer device control capabilities within some of their products, applications and services, and are engaged in ongoing efforts to address the broader home automation market. In addition, managed service companies such as ADT, Alarm.com, Comcast, and Vivint, have broadened their service offerings to include control of devices such as door locks, lights, and cameras. Our ability to compete in the growing home automation market over the next several years will be a key factor in our ability to continue to grow our business and meet or exceed our future expectations.

Key Operating and Financial Metrics

We use the following key operating and financial metrics to evaluate and manage our business.

North America Direct Dealers⁽¹⁾

	Three Months Ended March 31,	
	2019	2018
Authorized dealers at the beginning of the period	3,402	3,174
Additions	94	83
Terminations	(33)	(42)
Authorized dealers at the end of the period	3,463	3,215
Number of active dealers ⁽²⁾	3,305	3,108
Active dealers as a % of authorized dealers ⁽²⁾	95 %	97 %

International Direct Dealers⁽¹⁾

	Three Months Ended March 31,	
	2019	2018
Authorized dealers at the beginning of the period	1,479	1,315
Additions ⁽³⁾	183	52
Terminations	(25)	(9)
Authorized dealers at the end of the period	1,637	1,358
Number of active dealers ⁽²⁾	1,290	1,195
Active dealers as a % of authorized dealers ⁽²⁾	79 %	88 %

	Three Months Ended March 31,	
	2019	2018
Number of controllers sold	23,517	23,413
Core revenue growth	3 %	18 %
International core revenue as a percentage of total revenue	23 %	22 %

- (1) These dealer figures only include dealers authorized to sell and install the full Control4 line of products and exclude the approximately 870 dealers that are currently authorized to sell only the Pakedge and Triad line of products.
- (2) An “active dealer” is an authorized dealer that has placed an order with us in the trailing 12-month period.
- (3) The figures for the three months ended March 31, 2019 include 133 dealers that were acquired as part of the direct-to-dealer transitions in Ireland, New Zealand, and Switzerland.

Number of North America and Direct International Dealers

Because our dealers promote, sell, install and support our products, a broader dealer network allows us to reach more potential consumers across more geographic regions. We expect our dealer network to continue to grow, both in North America and internationally. While we have historically focused on dealers affiliated with CEDIA, our sales team focus includes adding new dealers outside of CEDIA, including non-traditional A/V dealers, electrical contractors, and security system installers.

Strengthening our worldwide dealer channel through business and installation tools, education programs, and new dealer recruitment also remains an ongoing priority. Our goal is to continuously increase our dealers’ productivity and growth. Enabling our dealers to increase productivity will ultimately drive our revenue growth.

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In conjunction with the broad availability of our newest generation products and software, we periodically review each of our current dealers with regard to their ability to successfully market, sell and install our current solutions. Part of developing a productive, capable dealer network, requires us to regularly review individual dealer performance and as necessary, terminate dealer licenses where volume, technical training and performance requirements are not fulfilled. We view this as a healthy part of growing our dealer channel worldwide.

As a result of our traditional efforts to expand our channel, the number of active international dealers for our full Control4 line of products increased 8% from March 31, 2018 to March 31, 2019, and we saw an increase of 6% in the number of active North American direct dealers during the same period.

Number of Controllers Sold

Our controllers contain our proprietary software and provide consumers with the essential technology to enable home control, automation and personalization. The number of controllers we sell in a given period provides us with an indication of consumer adoption of our technology, though a variety of other factors may also impact controller sales variability from period to period. Our sales of controllers also create significant opportunity to sell our other products and services. Once a consumer has deployed our controller, we believe that the consumer is more likely to remain committed to our technology platform and purchase more of our products, applications and services in the future.

In February 2018, we released our CA-1 controller, which is designed for entry-level projects for homeowners interested in lighting, temperature control, and security. Our Entertainment and Audio (“EA”) and Controller and Automation (“CA”) controllers, together, better address a broad range of solutions from simple single room projects to large, elegant whole-home deployments. Our EA-1 and CA-1 controllers broaden the addressable market for our solutions by providing single-room and lower cost solutions which typically involve more narrowly defined use cases with fewer connected devices. During the three months ended March 31, 2019, 25% of the Control4 automation projects our dealers sold were single-room or low-cost projects consisting only of a controller or controller paired with a remote.

During the three months ended March 31, 2019, we sold 23,517 controllers compared to 23,413 controllers sold in the same period in 2018.

Core Revenue Growth

The majority of our revenue comes from sales of our products through our distribution channels comprised of independent dealers in the United States and Canada, and independent dealers and distributors located throughout the rest of the world. We refer to revenue attributable to sales through dealers located in the United States and Canada as “North America Core revenue,” and revenue attributable to sales through dealers and distributors located throughout the rest of the world as “International Core revenue.” Core revenue does not include revenue from sales to hotels or certain specialty display products and associated installation sales in Australia.

International Revenue as a Percentage of Total Revenue

We believe that the international market represents a large and underpenetrated opportunity for us. We have established or acquired sales support offices in the United Kingdom, Australia, New Zealand, Germany, China, and India. We have formed relationships with independent international dealers and distributors, and we have expanded foreign language support for our solutions. We track international revenue as a percentage of total revenue as a key measure of our success in expanding our business internationally.

[Table of Contents](#)**Results of Operations***Revenue*

The following is a breakdown of our revenue between North America and International Core revenue and other revenue:

	Three Months Ended March 31,	
	2019	2018
	(in thousands)	
North America Core Revenue	\$ 46,199	\$ 45,701
International Core Revenue	14,145	12,790
Other Revenue	81	658
Total Revenue	<u>\$ 60,425</u>	<u>\$ 59,149</u>
North America Core Revenue as a % of Total Revenue	76 %	77 %
International Core Revenue as a % of Total Revenue	23 %	22 %

North America Core revenue increased \$0.5 million, or 1% for the three months ended March 31, 2019, compared to the same period in 2018. International Core revenue increased \$1.4 million, or 11%, in the three months ended March 31, 2019, compared to the same period in 2018.

Revenue growth in both North America and internationally is driven by a variety of factors. We continue to see growth from net new dealer additions as well as growth from existing dealers driven by an increase in the number of projects that are being performed and increased revenue per project, which is a derivative of our new product innovation and our acquisition strategy. However, we believe macro-economic factors are creating headwinds for many businesses, including ours, which has contributed to a deceleration in our growth rate starting in the third quarter of 2018 and influence our perspective on near-term opportunities and our current year guidance.

Our international sales model includes both direct-to-dealer and distribution channels. In targeted international regions and countries, we generally invest in some combination of local technical support, training personnel and facilities, warehousing and fulfillment, and sales support personnel. We have made these types of investments in the regions serviced by our offices in the United Kingdom, Germany, Australia, New Zealand, China, and India and these are markets where we see our greatest opportunity for international growth and expansion.

The following table further breaks out our International Core revenue and illustrates the relative revenue growth we are experiencing in the regions serviced by our offices in the United Kingdom, Germany, Australia, New Zealand, China, and India compared to other international regions. The revenue figures for the three months ended March 31, 2018 have been adjusted in the following table to include New Zealand as a Targeted International Region for comparability to the three months ended March 31, 2019.

	Three Months Ended March 31,	
	2019	2018
	(in thousands)	
Targeted International Regions ⁽¹⁾	\$ 12,172	\$ 11,055
Other International Regions	1,973	1,735
Total International Core Revenue	<u>\$ 14,145</u>	<u>\$ 12,790</u>

(1) Serviced by our offices in the Australia, China, Germany, India, New Zealand and the United Kingdom.

International Core revenue in the targeted international regions grew 10% during the three months ended March 31, 2019, compared to the same period in 2018, while International Core revenue in the other international regions increased 14% during the three months ended March 31, 2019, compared to the same period in 2018.

Improvements in channel mix, with more revenue being generated from sales to dealers instead of distributors, in our targeted international regions have generally contributed to an increase in revenue for the three

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months ended March 31, 2019 compared to the same period in 2018. A higher percentage of sales were made direct-to-dealer in our other international regions during the three months ended March 31, 2019 compared to the same period in 2018. Revenue in our other international regions was negatively impacted by ownership changes and unfavorable geopolitical conditions during 2018.

We continue to make investments internationally to improve our dealers' ability to sell and install our products and believe that these investments will enable us to grow our key international markets. Notwithstanding the foregoing, we sell broadly throughout the world and we believe that regional, adverse international economic conditions may create challenges and slow growth in certain geographies in the future.

Gross Margin

As a percentage of revenue, our gross margin has been, and will continue to be, affected by a variety of factors. Our gross margin is relatively consistent across our products. Our gross margin on third-party products that we sell through our online distribution platform is higher than our gross margin on our other product sales because we only recognize our net profit on these sales as revenue. While software licensing and subscription revenue is not material for all periods presented, our gross margin is higher on software licensing and subscription revenue than it is on product sales. Our gross margin is also higher on our sales made directly through dealers than it is on our sales made through distributors. Gross margin may be negatively affected by price competition in our target markets, associated promotional or volume incentive rebates offered to our independent dealers and distributors, as well as import and export tariffs.

Gross margin for the three months ended March 31, 2019 and 2018 was as follows (in thousands, except percentages):

	Three Months Ended March 31,	
	2019	2018
Gross margin	\$ 29,283	\$ 30,739
Percentage of revenue	48.5 %	52.0 %

As a percentage of revenue, our gross margin was 48.5% for the three months ended March 31, 2019, compared to 52.0% for the same period in 2018. The decrease in gross margin was primarily due to unfavorable fluctuations in exchange rates in markets where we sell our products in the local currency, higher programmatic price reductions, higher fixed overhead costs and product mix; offset by lower volume incentive rebates and an increase in 4Sight subscriptions due to enabling end customers with the ability to self-renew their subscriptions online.

Our sales in Europe, Australia, New Zealand and Canada are generally priced in the pound sterling, Swiss franc, or the euro, the Australian dollar, the New Zealand dollar, and the Canadian dollar, respectively, while our cost of goods sold is denominated in the U.S. dollar. The changing value of the pound sterling, the euro, and the Australian, New Zealand and Canadian dollars relative to the U.S. dollar will continue to contribute to variability in our gross margin for sales in Europe, Australia, New Zealand and Canada.

The impact of distribution and other overhead expenses as a percentage of revenue on our gross margin percentage varies depending on total revenue and overhead spending in a given period.

Beginning in the second quarter of 2018, we began making incremental investments in our global fulfillment centers to accommodate growth and improve delivery times to our dealers, which put downward pressure on our gross margin but should enable us to continue to scale and improve gross margins in future years.

In 2018, the U.S. government announced new tariff rules on goods imported from China. The first of these new tariffs went into effect on July 6 and August 23, 2018 for certain classes of imported goods, while further tariffs are currently under consideration. To date, we have absorbed the impact of the new tariffs. We will continue to monitor developments and changes to import tariffs so that we can plan and address these developments and changes, as well as explore all options to reduce the impact of any further rule changes.

[Table of Contents](#)*Research and Development Expenses*

Research and development expenses consist primarily of compensation for our engineers and product managers, including non-cash stock compensation expense. Research and development expenses also include prototyping and field-testing expenses incurred in the development of our products. We also include fees paid to agencies to obtain regulatory certifications. Finally, research and development expenses include ongoing, periodic amortization of acquired intangible assets.

Research and development expenses for the three months ended March 31, 2019 and 2018 were as follows (in thousands, except percentages):

	Three Months Ended March 31,	
	2019	2018
Research and development	\$ 11,817	\$ 10,940
Percentage of revenue	20 %	18 %

Research and development expenses increased \$0.9 million, or 8%, in the three months ended March 31, 2019, compared to the same period in 2018. The increase in absolute dollars primarily relates to costs associated with personnel, including non-cash stock compensation expense, as well as product development, tooling, and costs associated with NEEO.

Our research and development expenses both as a percentage of revenue and in absolute dollars fluctuate depending on our investments in the development of new solutions. For example, the timing of new hardware and software releases and the expense associated with prototyping, beta testing and compliance and regulatory fees can have an impact on total research and development expenses from period to period.

We expect research and development expenses to increase year over year in absolute dollars, as we continue to invest in new product development to drive future revenue growth, but to remain flat.

Sales and Marketing Expenses

Sales and marketing expenses consist primarily of compensation and related travel expenses for our sales, technical support and marketing personnel, including non-cash stock compensation expense. Sales and marketing expenses also include expenses associated with trade shows, marketing events, advertising and other marketing-related programs. We also include the amortization of certain intangible assets such as those related to our dealer network as well as those related to trademarks/trade names.

Sales and marketing expenses for the three months ended March 31, 2019 and 2018 were as follows (in thousands, except percentages):

	Three Months Ended March 31,	
	2019	2018
Sales and marketing	\$ 13,342	\$ 12,535
Percentage of revenue	22 %	21 %

Sales and marketing expenses increased \$0.8 million, or 6%, in the three months ended March 31, 2019, compared to the same period in 2018. The increase in absolute dollars primarily relates to increased personnel costs, which can be attributed to expanding our support for our growing channel including additional staffing to support marketing and sales services provided on behalf of our dealers, as well as credit card processing fees associated with revenue growth and discretionary marketing costs.

We expect our sales and marketing expenses to increase year over year in absolute dollars as we work to grow our global sales channels, but to decrease slightly as a percent of revenue in future periods.

[Table of Contents](#)*General and Administrative Expenses*

General and administrative expenses consist primarily of compensation for our employees in our executive administration, finance, information systems, human resource and legal departments, including non-cash stock-based compensation expense. Also included in general and administrative expenses are outside legal fees, audit fees, facilities expenses and insurance costs. Finally, during a period with an acquisition, we also include acquisition-related costs in general and administrative expenses.

General and administrative expenses for the three months ended March 31, 2019 and 2018 were as follows (in thousands, except percentages):

	Three Months Ended March 31,	
	2019	2018
General and administrative	\$ 7,117	\$ 6,293
Percentage of revenue	12 %	11 %

General and administrative expenses increased \$0.8 million, or 13%, and in the three months ended March 31, 2019, compared to the same period in 2018. The increase in absolute dollars primarily relates to personnel costs, including non-cash stock compensation expense, as well as professional fees, including costs associated with the integration of NEEO, and facilities costs with our various offices throughout the world, including three new offices in New Zealand and Switzerland as a result of the direct-to-dealer transition in New Zealand and the NEEO acquisition.

We expect our general and administrative expenses to increase year over year in absolute dollars as a result of growth in the business, increasing facilities costs associated with our various offices throughout the world, incremental professional fees related to the integration of business combinations, and increases in administrative expenses and fees that typically occur over time.

Income Tax Benefit

Income tax benefit for the three months ended March 31, 2019 and 2018 was as follows (in thousands, except percentages):

	Three Months Ended March 31,	
	2019	2018
Income tax benefit	\$ (766)	\$ (116)
Percentage of revenue	1 %	0 %

We recognized income tax benefit of \$0.8 million, or approximately 28% of loss before income taxes, for the three months ended March 31, 2019, compared to income tax benefit of \$0.1 million, or approximately 14% of income before income taxes, for the three months ended March 31, 2018. The effective tax rate differs from the U.S. federal statutory rate of 21% primarily due to the limitations on tax deductions allowable for executive compensation and global intangible low-taxed income, or GILTI, state income taxes, and foreign income taxes, offset by tax deductions resulting from stock-based compensation.

Liquidity and Capital Resources*Primary Sources of Liquidity*

As of March 31, 2019, we had \$72.0 million in unrestricted cash and cash equivalents and net marketable securities, a decrease of \$21.3 million from December 31, 2018. The overall change in cash and cash equivalents and net marketable securities was primarily due to the following:

- We acquired NEEO for \$14.5 million in consideration, less the non-cash settlement of receivables outstanding as of December 31, 2018 of \$1.7 million, acquired cash of approximately \$0.4 million and

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a holdback of approximately \$1.3 million, resulting in net cash paid of approximately \$11.1 million. The remaining \$1.3 million holdback will be held for up to 18 months from the acquisition date to cover any of the sellers' post-closing obligations, including without limitation any indemnification obligations that may arise;

- In February 2018, our Board of Directors authorized the expansion of the repurchase program providing approval to repurchase up to \$20 million in Control4 common stock from time to time on the open market; and in October 2018, the Board of Directors amended this amount by an additional \$20 million and extended the repurchase period to December 31, 2019. For the three months ended March 31, 2019, we have repurchased a total of 139,782 shares for approximately \$2.5 million;
- We made \$1.8 million in payments for withholding taxes in lieu of issuing an additional 103,094 shares related to the net share settlement of restricted stock units that lapsed during the period;
- We used cash from operations of \$4.7 million during the period;
- We made capital purchases of approximately \$1.2 million; and
- We received \$0.3 million in proceeds from the exercise of options for common stock.

We invest in highly-rated securities, and our investment policy generally limits the amount of credit exposure to any one issuer. Our investment policy requires investments to be investment grade, with the primary objective of minimizing the potential risk of principal loss. The maturities of our long-term investments range from one to two years, with the average maturity of our investment portfolio less than one year. Cash equivalents and marketable securities are comprised of money market and other funds, highly liquid debt instruments of the U.S. government and its agencies, debt instruments issued by municipalities in the United States, corporate securities, and asset-backed securities.

The following table shows selected financial information as of March 31, 2019 and December 31, 2018 (in thousands):

	March 31, 2019	December 31, 2018
Cash and cash equivalents	\$ 19,828	\$ 40,395
Investments, net ⁽¹⁾	52,154	52,932
Accounts receivable, net	30,316	33,016
Inventories	45,867	42,684
Working capital	114,951	134,386

⁽¹⁾ Includes accrued investment balances not included in the investments line items on the consolidated balance sheet.

We closely monitor accounts receivable and inventory because of their significant impact on cash and working capital. Our accounts receivable balance at March 31, 2019 has decreased by \$2.7 million, or 8%, since December 31, 2018 due to collection efforts made during the first quarter of 2019 as well as lower sales in the first quarter compared to the preceding fourth quarter reflecting the typical seasonality of our business. Furthermore, inventory has increased by \$3.2 million from December 31, 2018 to March 31, 2019. The increase in inventory was due primarily to the addition of our new fulfillment center, purchases of certain product components in advance of anticipated price increases as a result of quantity shortages worldwide, and acquired inventory from NEEO as well as acquired inventory from the distributors in Ireland, New Zealand, and Switzerland as a result of the direct-to-dealer transition in these countries.

We have an asset-based, revolving credit facility of \$40.0 million and at March 31, 2019 we had no outstanding borrowings under the credit facility.

We believe that our existing cash and cash equivalents, as well as our borrowing capacity on our revolving credit facility, will be sufficient to fund our operations for at least the next 12 months.

[Table of Contents](#)*Cash Flow Analysis*

A summary of our cash flows for the three months ended March 31, 2019 and 2018 is set forth below (in thousands):

	Three Months Ended	
	March 31,	
	2019	2018
Unrestricted and restricted cash and cash equivalents at the beginning of the period	\$ 40,654	\$ 30,034
Net cash provided by (used in) operating activities	(4,707)	469
Net cash used in investing activities	(11,838)	(1,193)
Net cash used in financing activities	(4,059)	(9,086)
Effect of exchange rate changes on cash and cash equivalents	42	48
Net change in cash and cash equivalents	(20,562)	(9,762)
Unrestricted and restricted cash and cash equivalents at the end of the period	\$ 20,092	\$ 20,272

Operating Activities

Cash provided by operating activities is net income adjusted for certain non-cash items and changes in certain assets and liabilities.

The decrease in cash provided by (used in) operating activities of \$5.2 million during the three months ended March 31, 2019 compared to the same period in 2018 is due to the differences in working capital account changes such as accounts receivable, inventory, accounts payable, and accrued liabilities partially offset by net income after adjusting for the non-cash effects of the amortization of intangible assets and tax benefits recorded in 2018 from business acquisitions.

Investing Activities

Cash used in investing activities primarily consist of purchases, maturities, and sales of marketable securities, business acquisitions, net of cash acquired, and purchases of property and equipment.

Cash used in investing activities increased to \$11.8 million in 2019 from \$1.2 million in 2018. The year-over-year increase in cash used in investing activities is due to cash used for business acquisitions in 2019.

Financing Activities

Financing cash flows consist primarily of the repurchase of common stock on the open market, proceeds from the exercise of options to acquire common stock, and tax payments related to the net share settlement of restricted stock units.

During the three months ended March 31, 2019, we repurchased 139,782 shares of our stock in the open market for \$2.5 million compared to 300,000 shares for \$7.4 million in the same period in 2018.

During the three months ended March 31, 2019 and 2018, we received proceeds of \$0.3 million and \$2.1 million, respectively, from the exercise of options to purchase common stock.

During the three months ended March 31, 2019 and 2018, we made withholding tax payments of \$1.8 million and \$3.6 million, respectively, related to the net share settlement of restricted stock units that lapsed during the period.

Non-GAAP Financial Measures

In addition to our GAAP operating results, we use certain non-GAAP financial measures to understand and evaluate our operating performance and trends, to prepare and approve our annual budget, and to develop short- and long-term operational plans. These measures, which we refer to as our non-GAAP financial measures, are not prepared in accordance with generally accepted accounting principles in the United States. Non-GAAP gross margin, non-GAAP income from operations, and non-GAAP net income exclude non-cash expenses related to stock-based compensation, amortization of intangible assets, acquisition-related costs, as well as expenses related to executive severance and litigation settlements.

Management believes that it is useful to exclude stock-based compensation expense because the amount of such expense in any specific period may not directly correlate to the underlying performance of our business operations.

We have recently completed acquisitions which resulted in operating expenses that would not have otherwise been incurred. Management has provided supplementary non-GAAP financial measures, which exclude acquisition-related expense items, to allow more accurate comparisons of the financial results to historical operations, forward-looking guidance and the financial results of less acquisitive peer companies. Management considers these types of costs and adjustments to be largely unpredictable and dependent on a significant number of factors that are outside of our control. Furthermore, we do not consider these acquisition-related costs and adjustments to be related to the organic continuing operations of the acquired businesses and are generally not relevant to assessing or estimating the long-term performance of the acquired assets. In addition, the size, complexity and/or volume of past acquisitions, which often drives the magnitude of acquisition-related costs, may not be indicative of the size, complexity and/or volume of future acquisitions. By excluding acquisition-related costs and adjustments from our non-GAAP measures, management is better able to evaluate our ability to utilize its existing assets and estimate the long-term value that acquired assets will generate for us. We believe that providing a supplemental non-GAAP measure which excludes these items allows management and investors to consider the ongoing operations of the business both with, and without, such expenses.

These acquisition-related costs are included in the following categories: (i) professional service fees, recorded in operating expenses, which include third-party costs related to transactions, and legal and other professional service fees associated with diligence, entity formation and corporate structuring, disputes and regulatory matters related to transactions; (ii) transition and integration costs, recorded in operating expenses, which include retention payments, transitional employee costs, earn-out payments treated as compensation expense, as well as the costs of integration-related services provided by third parties; and (iii) acquisition-related adjustments, which include adjustments to acquisition-related items such as being required to record inventory at its fair value, resulting in a step-up in the inventory value, and having to reverse part of our valuation allowance in order to offset the deferred tax liability that was recorded based on differences between the book and tax basis of assets acquired and liabilities assumed. The step-up in inventory is recorded through cost of goods sold when the inventory is sold, resulting in a negative impact to our gross margin. Although these expenses are not recurring with respect to past acquisitions, we will generally incur these types of expenses in connection with any future acquisitions.

We exclude the amortization of acquired intangible assets from non-GAAP measures. These amounts are inconsistent in amount and frequency and are significantly impacted by the timing and size of acquisitions. Providing a supplemental measure that excludes these charges allows management and investors to evaluate results “as-if” the acquired intangible assets had been developed internally rather than acquired. Although we exclude amortization of acquired intangible assets from non-GAAP measures, we believe that it is important for investors to understand that such intangible assets contribute to revenue generation. Amortization of intangible assets that relate to past acquisitions will recur in future periods until such intangible assets have been fully amortized. Future acquisitions may result in the amortization of additional intangible assets.

Furthermore, we believe it is useful to exclude expenses related to litigation settlements and executive severance because of the variable and unpredictable nature of these expenses which are not indicative of past or future operating performance. We believe that past and future periods are more comparable if we exclude these expenses.

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We believe these adjustments provide useful comparative information to investors. Non-GAAP results are presented for supplemental informational purposes only for understanding our operating results. The non-GAAP results should not be considered a substitute for financial information presented in accordance with generally accepted accounting principles and may be different from non-GAAP measures used by other companies. Our non-GAAP financial measures may not provide information that is directly comparable to that provided by other companies in our industry, as other companies in our industry may calculate non-GAAP financial results differently, particularly related to non-recurring, unusual items. We urge our investors to review the reconciliation of our non-GAAP financial measures to the comparable GAAP financial measures included below, and not to rely on any single financial measure to evaluate our business.

	Three Months Ended March 31,	
	2019	2018
(in thousands, except percentages and per share data)		
Reconciliation of Gross Margin to Non-GAAP Gross Margin:		
Gross margin	\$ 29,283	\$ 30,739
Stock-based compensation expense in cost of revenue	78	68
Amortization of intangible assets in cost of revenue	864	921
Non-GAAP gross margin	<u>\$ 30,225</u>	<u>\$ 31,728</u>
Revenue	\$ 60,425	\$ 59,149
Gross margin percentage	48.5 %	52.0 %
Non-GAAP gross margin percentage	50.0 %	53.6 %
Reconciliation of Income (Loss) from Operations to Non-GAAP		
Income (Loss) from Operations:		
Income (loss) from operations	\$ (2,993)	\$ 971
Stock-based compensation expense	3,529	3,335
Amortization of intangible assets	1,620	1,446
Acquisition-related costs	459	16
Non-GAAP income (loss) from operations	<u>\$ 2,615</u>	<u>\$ 5,768</u>
Revenue	\$ 60,425	\$ 59,149
Operating margin percentage	(5.0)%	1.6 %
Non-GAAP operating margin percentage	4.3 %	9.8 %
Reconciliation of Net Income (Loss) to Non-GAAP Net Income:		
Net income (loss)	\$ (1,970)	\$ 966
Stock-based compensation expense	3,529	3,335
Amortization of intangible assets	1,620	1,446
Acquisition-related costs	459	16
Non-GAAP net income (loss)	<u>\$ 3,638</u>	<u>\$ 5,763</u>
Non-GAAP net income (loss) per common share:		
Basic	\$ 0.14	\$ 0.22
Diluted	\$ 0.13	\$ 0.21
Weighted-average number of shares:		
Basic	26,563	25,904
Diluted	27,133	27,526

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Off-Balance Sheet Arrangements

We have no material off-balance sheet arrangements.

Contractual Obligations

We enter into long-term contractual obligations in the normal course of business, primarily purchase commitments and non-cancellable operating leases.

Our contractual cash obligations as of March 31, 2019 are as follows:

	Total	1 year	2 - 3 years	3 - 5 years	More than 5 years
			(in thousands)		
Operating lease obligations	13,864	5,140	6,730	1,384	610
Purchase commitments	61,349	61,349	—	—	—
Total contractual obligations	<u>\$75,213</u>	<u>\$66,489</u>	<u>\$ 6,730</u>	<u>\$ 1,384</u>	<u>\$ 610</u>

Critical Accounting Policies and Estimates

Our unaudited condensed consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles, or GAAP. The preparation of these condensed consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, expenses, and related disclosures. These estimates and assumptions are often based on judgments that we believe to be reasonable under the circumstances at the time made, but all such estimates and assumptions are inherently uncertain and unpredictable. Actual results may differ from those estimates and assumptions, and it is possible that other professionals, applying their own judgment to the same facts and circumstances, could develop and support alternative estimates and assumptions that would result in material changes to our operating results and financial condition. We evaluate our estimates and assumptions on an ongoing basis. Our estimates are based on historical experience and various other assumptions that we believe to be reasonable under the circumstances. Our actual results could differ from these estimates.

Our critical accounting policies and estimates are detailed in Management’s Discussion and Analysis of Financial Condition and Results of Operations contained in the Annual Report on Form 10-K as filed with the SEC on February 11, 2019. None of our critical accounting policies and estimates have changed significantly since that filing.

Recently Issued and Adopted Accounting Pronouncements

For information with respect to recent accounting pronouncements and the impact of these pronouncements on our condensed consolidated financial statements, see Note 1 “Description of Business and Summary of Significant Accounting Policies — Recent Accounting Pronouncements” in the notes to condensed consolidated financial statements (unaudited).

ITEM 3. Quantitative and Qualitative Disclosures about Market Risk

Our market risk disclosures are detailed in Quantitative and Qualitative Disclosures about Market Risk contained in the Annual Report on Form 10-K as filed with the SEC on February 11, 2019. Other than our interest rate risk described below, our market risk has not changed significantly since that filing.

Interest Rate Risk

Changes in interest rates could affect the interest earned on our cash, cash equivalents and investments as well as the fair value of our investments. Our investment policy and strategy are focused on preservation of capital and supporting our liquidity requirements. A portion of our cash is managed by external managers within the guidelines of our investment policy.

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Our exposure to changes in interest rates relates primarily to our investment portfolio. We invest in highly-rated securities, and our investment policy generally limits the amount of credit exposure to any one issuer. The policy requires investments to be investment grade, with the primary objective of minimizing the potential risk of principal loss.

We performed a sensitivity analysis on the value of our investment portfolio assuming a hypothetical change in rates of 100 basis points. Based on investment positions as of March 31, 2019, a hypothetical 100 basis point increase in interest rates across all maturities would result in a \$0.2 million incremental decline in the fair market value of the portfolio. Such losses would only be realized if we sold the investments prior to maturity.

ITEM 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended as of the end of the period covered by this Form 10-Q. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that as of such date, our disclosure controls and procedures were effective.

Changes in Internal Control over Financial Reporting

Except as set forth below, during the three months ended March 31, 2019, we did not make any material changes in our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

The Company implemented a new lease accounting system and process in response to the adoption of ASU 2016-02, “*Leases (Topic 842)*,” effective January 1, 2019. These implementations resulted in a material change in a component of our internal control over financial reporting. The operating effectiveness of these changes will be evaluated as part of our annual assessment of the effectiveness of internal control over financial reporting.

Inherent Limitations of Internal Controls

Our management, including our Chief Executive Officer and Chief Financial Officer, do not expect that our disclosure controls and procedures or our internal controls will prevent all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of a simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

PART II — OTHER INFORMATION

ITEM 1. Legal Proceedings

From time to time, we may become involved in legal proceedings arising in the ordinary course of our business. We are not presently a party to any legal proceedings, that if determined adversely to us, we believe would individually or in the aggregate have a material adverse effect on our business, results of operations, financial condition or cash flows.

ITEM 1A. Risk Factors

A description of certain risks and uncertainties associated with our business is set forth below. You should carefully consider such risks and uncertainties, together with the other information contained in this report, and in our other public filings. Factors that could cause our business, financial condition or operating results to differ materially from the plans, projections and other forward-looking statements included in the section titled “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and elsewhere in this report and in our other public filings include, but are not limited to, the following risks and uncertainties, which could cause substantial harm to our business, financial condition or operating results and the market price of our stock to decline, perhaps significantly.

Risks Related to Our Business and Industry

The announcement and pendency of our agreement to merge with SnapAV could adversely affect our business.

On May 8, 2019, we announced that we had entered into the Merger Agreement, the effect of which will be to combine the Company and SnapAV. Uncertainty about the effect of the proposed transaction on our customers, employees, dealers, partners, end users, and other parties may adversely affect our business. Our employees may experience uncertainty about their roles or seniority following the transaction. There can be no assurance that our employees, including key personnel, can be retained to the same extent that we have previously been able to attract and retain employees. Any loss or distraction of such employees could adversely affect our business and operations. In addition, we have diverted, and will continue to divert, significant management resources toward the completion of the transaction, which could adversely affect our business and operations. Parties with which we do business may experience uncertainty associated with the transaction and related transactions, including with respect to current or future business relationships with us. Uncertainty may cause clients to refrain from doing business with us, which could adversely affect our business, results of operations and financial condition.

The failure to complete the merger with SnapAV could adversely affect our business.

Completion of the merger with SnapAV is subject to several conditions beyond our control that may prevent, delay, or otherwise adversely affect its completion. The consummation of the transaction is conditioned on receipt of certain regulatory approvals, including expiration or termination of the waiting period under the Hart-Scott-Rodino Antitrust Improvements Act of 1976; the decisions, orders, consents or expiration of any waiting periods required to consummate the Merger under the foreign investment, monopolization and anti-competition laws and regulations of certain foreign jurisdictions, the accuracy of the representations and warranties and compliance with the covenants contained in the Merger Agreement, subject to qualifications; and other customary conditions. Many of the conditions to consummation of the transaction are not within our control or the control of Parent and none of us can predict when or if these conditions will be satisfied. If any of these conditions are not satisfied or waived, it is possible that the transaction will not be consummated in the expected time frame or that the Merger Agreement may be terminated. If the proposed sale or a similar transaction is not completed, the share price of our common stock could drop to the extent that the current market price of our common stock reflects an assumption that a transaction will be completed. Further, a failed transaction may result in negative publicity and a negative impression of us in the investment community. Finally, any disruption to our business resulting from the announcement and pendency of the transaction and from intensifying competition from our competitors, including any adverse changes in our relationships with our dealers, employees, partners, end users, and other parties, could continue or accelerate in the event of a failed transaction. There can be no assurance that our business, these

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relationships or our financial condition will not be adversely affected, as compared to the condition prior to the announcement of the transaction, if the transaction is not consummated.

While the Merger is pending, we are subject to business uncertainties and contractual restrictions that could harm our operations and the future of our business or result in a loss of employees.

The Merger Agreement includes restrictions on the conduct of our business prior to the completion of the transaction, generally requiring us to conduct our businesses in the ordinary course, consistent with past practice, and subjecting us to a variety of specified limitations unless we obtain Parent's prior written consent. We may find that these and other contractual arrangements in the Merger Agreement may delay, prevent or limit us from responding effectively to competitive pressures, industry developments and future business opportunities that may arise during such period, even if our management and board of directors think that they may be advisable. The pendency of the transaction may also divert management's attention and our resources from ongoing business and operations. Our dealers, employees, partners and other parties may have uncertainties about the effects of the transaction. In connection with the pending transaction, it is possible that some dealers, partners, end users, and other persons with whom we have a business relationship may delay or defer certain business decisions or might decide to seek to terminate, change or renegotiate their relationship with us as a result of the transaction. Similarly, current and prospective employees may experience uncertainty about their future roles with us following completion of the transaction, which may harm our ability to attract and retain key employees. If any of these effects were to occur, it could materially and adversely impact our revenue, earnings and cash flows and other business results and financial condition, as well as the market price of our common stock and our perceived acquisition value, regardless of whether the transaction is completed. In addition, whether or not the transaction is completed, while it is pending we will continue to incur costs, fees, expenses and charges related to the proposed transaction, which may materially and adversely affect our business results and financial condition.

The markets in which we participate are highly competitive and many companies, including large technology companies, retailers, broadband and security service providers, as well as other managed service providers, are actively targeting the home automation market. Our failure to differentiate ourselves and compete successfully against these companies would make it difficult for us to add and retain consumers, and our sales and profitability could be adversely affected.

The market for home automation is fragmented, highly competitive and continually evolving. A number of technology companies, including industry leaders such as Amazon, Apple, Google, Honeywell, Lutron and Samsung, offer device control capabilities in some of their products, applications and services and are engaged in ongoing development efforts to address even broader segments of the home automation market. These large technology companies already have broad consumer awareness and sell a variety of devices for the home, and consumers may choose their offerings instead of ours, even if we offer broader interoperability or superior products and services. Additionally, these and other companies may further expand into our industry by developing additional solutions or by acquiring other providers. Similarly, many managed service providers, such as cable TV, telephone and security companies, are offering services that provide device control capability within the home for an additional monthly service fee. For example, Comcast's Xfinity service offers residential security, energy and automation services, and Vivint and ADT have made significant efforts to market smart home services that incorporate these companies' traditional security offerings. These managed service providers have the advantage of leveraging their existing consumer base, network of installation and support technicians and name recognition to gain traction in the home automation market. In addition, consumers may prefer the monthly service fee model offered by some of these managed service providers, which allows them to get certain control and automation services with little to no upfront cost as compared to a model with a higher upfront cost but little to no monthly service fees.

We expect competition from these large technology companies, retailers and managed service providers to increase in the future. This increased competition could result in pricing pressure, reduced sales, lower margins or the failure of our solutions to achieve or maintain broad market acceptance. To remain competitive and to maintain our position as a leading provider of professionally installed automation and control solutions for the connected home, we will need to invest continuously in product development, marketing, dealer and distributor service and support, and product delivery infrastructure. We may not have sufficient resources to continue to make the investments in all of the areas needed to maintain our competitive position. In addition, many of our competitors have longer operating histories, greater name recognition, larger consumer bases and significantly greater financial,

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technical, sales, marketing and other resources than us, which may provide them with an advantage in developing, marketing or servicing new solutions. Increased competition could reduce our market share, revenue and operating margins, increase our operating costs, harm our competitive position or otherwise harm our business and results of operations.

Consumers may choose to adopt point products that provide control of discrete home functionality or do-it-yourself (“DIY”) home automation solutions rather than adopt our unified, professionally-installed home automation solution. If we are unable to increase market acceptance of the benefits of our unified solution, our revenue may not continue to grow, or it may decline.

Many vendors have emerged, and may continue to emerge, to provide point products with advanced functionality for use in the home, such as thermostats, lighting, doorbells or alarm system that can be controlled by an application on a smartphone or control panel. We expect an increasing number of consumer electronic and consumer appliance products to be network-aware and connected—each very likely to have its own smart device (phone or tablet) application. Consumers may be attracted to the relatively low costs and ease of installation of these point products and the ability to expand their home control solution over time with minimal upfront costs, despite the disadvantages of this approach such as requiring multiple interfaces and an inability to conveniently interoperate. While we have built our solution to be flexible and support many third-party point products, the adoption of these products may reduce the revenue we receive for each installation. It is therefore important that we provide attractive top-quality products in many areas, such as networking, lighting, audio, video, thermostats and security, and establish broad market awareness and acceptance of these solutions as well as the advantages of integrating them in a unified solution. If a significant number of consumers in our target market choose to rely solely on the functionality included in point products or DIY solutions rather than acquiring our unified automation solution, then our business, financial condition and results of operations will be harmed, and we may not be able to achieve sustained growth or our business may decline.

Providers of luxury integrated installations with long operating histories, established markets, broad user bases and proven consumer acceptance, may be successful in expanding their offerings in the home automation market, or otherwise compete against our solutions, which may reduce our market share and harm our growth and future prospects.

Many companies with which we directly compete have been operating in this industry for many years, and as a result, have established significant name recognition in the home automation industry. For example, Crestron, a provider of luxury integrated installations, has been in business for over 45 years and has become an established presence in the home and commercial automation industry.

New entrants may be successful in penetrating the home automation market, which may reduce our market share and harm our growth and future prospects.

Given the growth potential of the market, we expect there may be many new entrants in the future. To the extent these providers are able to develop more affordable or attractive products or otherwise compete with our business, our growth may be constrained and our business could suffer.

We have incurred operating losses in the past, may incur operating losses in the future, and may not achieve or maintain profitability.

We began our operations in 2003. For most of our history, we have experienced net losses and negative cash flows from operations. As of March 31, 2019, we had an accumulated deficit of \$30.4 million. We expect our operating expenses to increase in the future as we expand our operations. If our revenue does not continue to grow to offset any increased expenses, we will not continue to be profitable. After achieving profitability in 2013 and 2014 of \$3.5 million and \$8.2 million respectively, we sustained a net loss of \$1.7 million in 2015. Our net income for the years ended December 31, 2016, 2017 and 2018 was \$12.3 million, \$15.5 million, and \$43.8 million, respectively, and consequently we released our U.S. federal and state deferred tax asset valuation allowance in 2018. However, we may incur significant losses in the future for a number of reasons, including without limitation the other risks and uncertainties described herein. Additionally, we may encounter unforeseen operating or legal expenses, difficulties, complications, delays in manufacturing and selling our products and other unknown factors that may result in losses

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in future periods. If these losses exceed our expectations or our revenue growth expectations are not met in future periods, our profitability will be harmed and we may need to establish a valuation allowance for our U.S. federal and state deferred taxes assets again in the future and our stock price may fall.

Our quarterly results of operations have fluctuated and may continue to fluctuate. As a result, we may fail to meet or exceed the expectations of investors or securities analysts, which could cause our stock price to decline.

Our quarterly revenue and results of operations have fluctuated and may continue to fluctuate as a result of a variety of factors, many of which are outside of our control. In the past when our quarterly revenue or results of operations have fallen below the consensus expectations of securities analysts, the price of our common stock has declined. If our quarterly revenue or results of operations fall below the consensus expectations of investors or securities analysts in the future, the price of our common stock could decline again, perhaps substantially. Fluctuations in our results of operations may be due to a number of factors, including but not limited to:

- Demand for and market acceptance of our solutions;
- Our ability to continue to develop and maintain relationships with productive independent dealers and distributors and incentivize them to continue to market, sell, install and support our solutions;
- The ability of our contract manufacturers to continue to manufacture high-quality products, and to supply sufficient products to meet our demands;
- The timing and success of acquisitions, new product introductions or upgrades by us or by our competitors;
- The strength of regional, national and global economies;
- Our ability to develop products and programs that sell successfully into hospitality projects and new home developments;
- The strength of the U.S. dollar relative to other currencies and the impact this has on dealer and distributor margins and their ability to competitively sell our products to consumers;
- The impact of harsh seasonal weather, natural disasters or manmade problems such as terrorism;
- Changes in our business and pricing policies, or those of our competitors;
- Competition, including entry into the industry by new competitors and new offerings by existing competitors;
- The impact of seasonality on our business;
- A systemic impairment or failure of one or more of our products that erodes dealer and/or end-user confidence;
- Changes in applicable tax and tariff rates;
- Political or regulatory changes in the markets in which we operate;
- The cost and availability of component parts used in our products;
- Aggressive business tactics by our competitors, including: selling at a discount, offering products on a bundled basis at no charge, extensive marketing efforts, and providing financing incentives;

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- The amount and timing of expenditures, including those related to expanding our operations, increasing research and development, introducing new solutions or costs related to disputes and litigation; and
- Temporary discounts or permanent changes in the price or payment terms for our solutions.

Due to the foregoing factors and the other risks discussed herein, you should not rely on quarter-to-quarter comparisons of our results of operations as an indication of our future performance, nor should you consider any revenue growth or results of operations in any quarter to be indicative of our future performance.

If we are unable to develop new solutions, sell our solutions into new markets, or further penetrate our existing markets, our revenue may not grow as expected or it may decline.

Our ability to increase sales will depend in large part on our ability to enhance and improve our solutions, to introduce new solutions in a timely manner, to sell into new markets, and to further penetrate our existing markets. The success of any enhancement or new product or solution depends on several factors, including the timely completion, introduction and market acceptance of enhanced or new solutions, the ability to attract, retain and effectively train product development, sales and marketing personnel (among others), the ability to develop relationships with independent dealers and distributors and the effectiveness of our marketing programs. Any new product or solution we develop or acquire may not be introduced in a timely or cost-effective manner, and may not achieve the broad market acceptance necessary to generate significant revenue. Any new markets into which we attempt to sell our solutions, including new vertical markets and new countries or regions, may not be receptive. Our ability to further penetrate our existing markets depends on the quality of our solutions and our ability to design our solutions to meet consumer demand. Moreover, we are frequently required to enhance and update our solutions as a result of changing standards and technological developments, which makes it difficult to recover the cost of development and forces us to continually qualify new solutions with our consumers. If we are unable to successfully develop or acquire new solutions, enhance our existing solutions to meet consumer requirements in a timely manner, sell solutions into new markets, or sell our solutions to additional consumers in our existing markets, our revenue may not grow as expected or it may decline.

We rely on our independent dealers and distributors to sell our solutions, and if our dealers and distributors fail to perform, our ability to sell and distribute our products and services will be limited, and our results of operations may be harmed.

Substantially all of our revenue is generated through the sales of our solutions by our authorized dealers and distributors. Our dealers and distributors are independent businesses that voluntarily sell our products as well as the products of other companies to consumers. We provide our dealers and distributors with specific training programs to assist them in selling, installing and servicing our products, and we also provide our dealer-network with leads to potential customers which we generate through our internal marketing efforts, but we cannot assure that these steps will be effective. We have observed, and expect to continue to observe, high volatility in the monthly, quarterly and annual sales performance of individual dealers and distributors. Although we can make estimated forecasts of cumulative sales of large numbers of dealers and distributors, we cannot assure their accuracy collectively or individually. Accordingly, we may not be able to reduce or slow our spending quickly enough if our actual sales fall short of our expectations. As a result, we expect that our revenues, results of operations and cash flows may fluctuate significantly on a quarterly basis. We believe that period-to-period comparisons of our revenues, results of operations and cash flows should not be relied upon as an indication of future performance.

Our independent dealers and distributors may be unsuccessful in marketing, selling, installing and supporting our products and services. If we are unable to provide high-quality products in a timely manner at competitive prices and to develop and maintain effective sales incentive programs for our dealers and distributors, we may not be able to incentivize them to sell our products to consumers. Our dealers and distributors may also market, sell and support products and services that are competitive with ours, and may devote more resources to the marketing, sales, and support of such competitive products. Our dealers and distributors may have incentives to promote our competitors' products to the detriment of our own or may cease selling our products altogether. Our agreements with our dealers and distributors may generally be terminated for any reason by either party with

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advance notice. We cannot assure that we will retain these dealers and distributors, or that we will be able to secure additional or replacement dealers and distributors.

In addition, while we take certain steps to protect ourselves from liability for the actions of our dealers and distributors, such as including contractual provisions limiting our liability with both consumers and dealer/distributors, consumers may seek to recover amounts from us for any damages caused by independent dealers in connection with system installations, or the failure of a system to perform properly due to an incorrect installation by a dealer, and, in the event of litigation with respect to these matters, we cannot guarantee that our contractual protections will be enforced. Furthermore, dealers and distributors may initiate claims against us related to any failure or perceived failure to operate our business in accordance with our contracts and the law. In addition, our independent dealers and distributors may use our name and our brand in ways we do not authorize, and any such improper use may harm our reputation or expose us to liability for their actions.

If we fail to effectively manage our existing sales channels then our results of operations may be harmed.

Our success depends, in part, on our ability to develop and expand our global network of independent dealers and distributors.

As of March 31, 2019, we have over 5,460 active direct dealers and 39 distributors authorized to sell, install and support our solutions. We rely on our independent dealers and distributors to provide consumers with a successful Control4 home automation experience. In some cases, dealers may choose not to offer our solution and instead offer a product from one of our competitors or, in other cases, the dealer may simply discontinue its operations. In order to continue our growth and expand our business, it is important that we continue to add new dealers and distributors and ensure that our existing relationships remain productive. We must also work to expand our network of dealers and distributors to ensure that we have sufficient geographic coverage and technical expertise to address new markets and technologies. While it is difficult to estimate the total number of available dealers in our markets, there are a finite number of dealers that are able to perform the types of technical installations required for home automation systems. In the event that we saturate the available dealer pool, or if market or other forces cause the available pool of dealers to decline, it may be increasingly difficult to grow our business. As consumers' home automation options grow, it is important that we enhance our dealer footprint by broadening the expertise of our dealers, working with larger and more sophisticated dealers and distributors and expanding our line of consumer products that our dealers and distributors offer. If we are unable to expand our network of independent dealers and distributors, or maintain productive relationships with our existing dealers and distributors, our business could be harmed.

Since we rely on third-party dealers and distributors to sell and install our solutions, we do not have a direct sales pipeline, which makes it difficult for us to accurately forecast future sales and correctly predict manufacturing requirements.

We depend on our independent dealer and distributor network to sell and install our solution. As a result, we do not directly develop or control our sales pipeline, making it difficult for us to accurately predict future sales. In addition, because the production of certain of our products requires long lead times, we enter into agreements for the manufacture and purchase of certain of our products well in advance of the time in which those products will be sold. These contracts are based on our best estimates of our near-term product needs. If we underestimate consumer demand, we may forego revenue opportunities, lose market share and damage our relationships. Conversely, if we overestimate consumer demand, we may purchase more inventory than we are able to sell at any given time, or at all. If we fail to accurately estimate demand for our products, we could have excess or obsolete inventory, resulting in a decline in the value of our inventory, which would increase our costs of revenues and reduce our liquidity. Our failure to accurately manage inventory relative to demand would adversely affect our results of operations.

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We have relatively limited visibility regarding the consumers that ultimately purchase our products, and we often rely on information from third-party dealers and distributors to help us manage our business. If we are unable to obtain timely or accurate information, our ability to quickly react to market changes and effectively manage our business may be harmed.

We sell our solutions through independent dealers and distributors. These dealers and distributors work with consumers to design, install, update and maintain their home automation installations. While we are able to track orders from dealers and distributors and have access to certain information about the configurations of the Control4 systems they install that we receive through our controllers, we also rely on these dealers and distributors to provide us with information about consumer behavior, product and system feedback, consumer demographics, buying patterns and information about our competitors. We use this channel sell-through data, along with other metrics, to assess consumer demand for our solutions, develop new products, adjust pricing and make other strategic business decisions. Our channel sell-through data is subject to limitations due to collection methods and the third-party nature of the data and thus may not be complete or accurate. In addition, from time to time we collect information directly from consumers through surveys that we conduct and other methods, but the consumers who chose to participate self-select and vary by geographic region and from period to period, which may impact the usefulness of the results. If we do not receive consumer information on a timely or accurate basis, or if we do not properly interpret this information, our ability to quickly react to market changes and effectively manage our business may be harmed.

We have entered into several strategic arrangements and intend to pursue additional strategic opportunities in the future. If the intended benefits from our strategic relationships are not realized, our results of operations may be harmed.

We are working to develop relationships with strategic partners in order to increase awareness of our solutions and to attempt to reach markets that we cannot currently address cost-effectively. If these relationships do not develop in the manner we intend, our future growth could be impacted. Any loss of a major partner or distribution channel or other channel disruption could harm our results of operations and make us more dependent on alternate channels, damage our reputation, increase pricing and promotional pressures from other partners and distribution channels, increase our marketing costs, or harm buying and inventory patterns, payment terms or other contractual terms.

If we do not maintain the compatibility of our solutions with third-party products and applications that our consumers use, demand for our solutions could decline.

Our solutions are designed to interoperate with a wide range of other third-party products, including products in the areas of audio, video, lighting, temperature, and security, and we benefit from our relationships with partners that allow our system to provide integrated and extensible control of approximately 13,500 third-party devices and services. If we do not support the continued integration of our solutions with third-party products and applications, including new and additional products, demand for our solutions could decline and we could lose sales. In addition, companies that provide certain point solutions have eliminated or restricted, and may in the future, eliminate or restrict, our ability to integrate with, control and otherwise be compatible with these products. As a result, we may not be successful in making our solutions compatible with these third-party products and applications or lose functionality in existing systems to the extent that they depend on the ability to integrate with third-party products, which could reduce demand for our solutions. In addition, if prospective consumers require customized features or functions that we do not offer, then the market for our solutions may be harmed.

If we are unable to adapt to technological change and implement technological and aesthetic enhancements to our products, this could impair our ability to remain competitive.

The market for home automation and control solutions is characterized by rapid technological change, frequent introductions of new products and evolving industry standards. However, product development often requires significant lead-time and upfront investment and our ability to attract new consumers and increase revenue from existing consumers will depend in significant part on our ability to accurately anticipate changes in industry standards and to continue to appropriately fund development or acquisition efforts to enhance existing solutions or introduce new solutions in a timely basis to keep pace with technological developments. This is true of all our

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products but is particularly important with respect to our user interface and other direct consumer interface products. Similarly, if any of our competitors implement new technologies before we are able to implement them, those competitors may be able to provide more effective products than ours, possibly at lower prices, which could impact sales and decrease our market share. Any delay or failure in the introduction of new or enhanced solutions could harm our business, results of operations and financial condition.

If we are unable to design products that scale for use in larger projects, this could impair our ability to remain competitive.

As the market for automation, control, and networking matures, the complexity of projects pursued by our consumers is increasing. If we are not able to design products that work in such larger and more complex projects, our reputation may suffer, we may lose business opportunities, and projects may fail.

We currently rely on contract manufacturers to manufacture our products and on component vendors to supply parts used in our products. Any disruption in our supply chain, or our failure to successfully manage our relationships with our contract manufacturers or component vendors could harm our business.

Our reliance on contract manufacturers reduces our control over the assembly process, exposing us to risks, including reduced control over quality assurance, production costs and product supply. We rely on a limited number of contract manufacturers to manufacture most of our products and components, and in many cases one of these manufacturers is our only source for a particular product or product family. We also do business with a number of component vendors, and the parts they supply may not perform as expected. Most of our contract manufacturers and component vendors are located outside of the United States, and all of them may be subject to political, economic, social, regulatory and legal uncertainties that may harm our relationships with them. If we fail to manage our relationships with our contract manufacturers, component vendors or shipping partners effectively, or if our contract manufacturers, component vendors or shipping partners experience delays, disruptions, capacity constraints or quality control problems in their operations, our ability to ship products may be impaired and our competitive position and reputation could be harmed. In addition, any adverse change in our contract manufacturers', component vendors' or shipping partners' financial or business condition could disrupt our ability to supply quality products to our dealers and distributors. If we are required to change contract manufacturers, component vendors, or shipping partners we may lose revenue, incur increased costs or damage our relationships, or we might be unable to find a new contract manufacturer or component vendor on acceptable terms, or at all. In addition, qualifying a new contract manufacturer or component vendor could be an expensive and lengthy process. If we experience increased demand that our contract manufacturers or component vendors are unable to fulfill, or if they are unable to provide us with adequate supplies of high-quality products for any reason, we could experience a delay in our order fulfillment, and our business, results of operations and financial condition would be harmed.

Changes in import/export regulatory regimes and duties could negatively impact our business.

In 2018, the United States implemented a number of new tariffs on the importation of materials, which prompted some affected nations to respond with new tariffs on U.S. exports. Of particular note, the United States recently imposed and proposed tariffs on a number of goods from China. In turn, China has responded by imposing reciprocal tariffs on U.S. exports to China, and both countries have indicated that there could be continued escalation of protectionist policies. We continue to evaluate the impact of these tariffs and policies on our supply chain and to consider appropriate responses in our sourcing of products and components while exploring certain government affairs initiatives to help shape future policies. Increased import taxes or duties could negatively impact our cost structures in future periods and make it prudent for us to move certain manufacturing to alternative geographies. If the United States, or other countries in which we do significant business, were to withdraw from or materially modify certain international trade agreements, further change tariff or tax provisions related to the global manufacturing and sales of our products, or otherwise alter regulations impacting our existing business, or if these changes negatively affect us disproportionately as compared to our competitors, our financial condition and results of operations could be adversely affected. In addition, if any of our products are found to have been misclassified under various tariff codes, we could be subject to higher duties and/or fines.

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Growth of our business may depend on market awareness and a strong brand, and any failure to develop, broaden, protect and enhance market awareness of our products could hurt our ability to retain or attract consumers.

Because of the competitive nature of the home automation market, we believe that building and maintaining market awareness, brand recognition and goodwill may be material to our success. This will depend largely on our ability to continue to provide high-quality solutions, and we may not be able to do so effectively. We may choose to engage in a broader marketing campaigns to further promote our brand, but this effort may not be successful. Our efforts in developing our brand may be affected by the marketing efforts of our competitors, negative publicity and social media commentary, and our reliance on our independent dealers, distributors and strategic partners to install our products and promote our brand effectively. If we are unable to cost-effectively maintain and increase positive awareness of our brand, our business, results of operations and financial condition could be harmed.

We operate in the emerging and evolving home automation market, which may develop more slowly or differently than we expect. If the home automation market does not grow as we expect, or if we cannot expand our solutions to meet the demands of this market, our revenue may decline, fail to grow or fail to grow at an accelerated rate, and we may incur operating losses.

The market for home automation and control solutions is evolving, and it is uncertain whether our solutions will achieve and sustain high levels of demand and market acceptance. Some consumers may be reluctant or unwilling to use our solutions for a number of reasons, including satisfaction with other solutions, concerns about cost, and lack of awareness of our solutions. Unified home automation solutions such as ours have traditionally been luxury purchases for the high end of the residential market, and while our solutions target the high end of the market, we also have solutions that target middle- and entry-level home owners, including our EA-1 that is designed to control smaller, single room projects with an entertainment component and the CA-1 controller for smaller projects that only include lighting, comfort, and/or security. Our ability to expand the sales of our solutions to a broader consumer base depends on several factors, including market awareness of our solutions, the timely completion, introduction and market acceptance of our solutions, the ability to attract, retain and effectively train sales and marketing personnel, the effectiveness of our marketing programs, the ability to develop effective relationships with independent dealers and distributors, homebuilders, and other strategic partners, the cost and functionality of our solutions and the success of our competitors. If we are unsuccessful in developing and marketing our home automation solutions to consumers, or if these consumers do not perceive or value the benefits of our solutions, the market for our solutions might not continue to develop or might develop more slowly than we expect, either of which would harm our revenue and growth prospects.

Our consumers may experience service failures or interruptions due to defects in the software, products, infrastructure, third-party components or processes that comprise our solutions, or due to errors in product installation or servicing by our independent dealers, any of which could harm our business.

Our solutions may contain undetected defects in the software, products, infrastructure, third-party components or processes. If these defects lead to service failures, we could be subject to liability for such failures and we could experience harm to our branded reputation. Such defects could also result in a loss of, or delay in, market acceptance of our solutions, which could harm our business, results of operations and financial condition.

In addition to failures due to product defects, because our solutions are installed by independent dealers, if they do not install or maintain our solutions correctly or if the underlying network or infrastructure in a home or business is not sufficiently robust, our solutions may not function properly. If the improper installation or maintenance of our solutions leads to service failures of a product or solution, we could experience harm to our branded reputation, claims by our consumers, dealers, distributors, strategic partners or developers and we may incur increased expense during the period required to address the cause of the problem, which could harm our business, results of operations and financial condition.

Any defect in, or disruption to, our solutions could cause consumers to remove their products, not to purchase additional products from us, prevent other potential consumers from purchasing our solutions, or harm our reputation. The nature of the solutions we provide, including our interface with home security solutions, may expose

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us to greater risks of liability for system failure or even installation errors by our independent dealers than may be inherent in other businesses. Substantially all of our dealer agreements contain provisions limiting our liability to dealers and our consumers in an attempt to reduce this risk. However, in the event of litigation with respect to these matters, we cannot be sure that these limitations will be enforced, and defending a lawsuit, regardless of its merit, could be costly, divert management's attention, affect our ability to obtain or maintain liability insurance on acceptable terms and could harm our business. In addition, there can be no assurance that we are adequately insured for these risks. Certain of our insurance policies and the laws of some jurisdictions may limit or prohibit insurance coverage for punitive or certain other types of damages or liability arising from gross negligence. Although we currently maintain some warranty reserves, we cannot be sure that these warranty reserves will be sufficient to cover future liabilities. Furthermore, we may be required to indemnify our dealers, distributors and other partners against certain liabilities they may incur as a result of defects of our products or third-party intellectual property claims related to our products or other materials we provide to them.

Our networking solutions business may be harmed if users perceive our solution as the cause of a slow or unreliable network connection, or in the event of a high-profile network failure, even though certain technical problems experienced by users may not be caused by our products.

Our networking solutions have been deployed in many different locations and user environments and are capable of providing connectivity to many different types of Wi-Fi-enabled devices operating a variety of applications. The ability of our products to operate effectively can be negatively impacted by many different elements unrelated to our products. For example, a user's experience may suffer from an incorrect setting in a Wi-Fi device. Although certain technical problems experienced by users may not be caused by our products, users often may perceive the underlying cause to be a result of poor performance of the wireless network. This perception, even if incorrect, could harm our business and reputation. Similarly, a high-profile network failure may be caused by improper operation of the network or failure of a network component that we did not supply, but users and other service providers may perceive that our products were implicated, which, even if incorrect, could harm our business, operating results and financial condition.

Failure to maintain the security of our information and technology networks, including information relating to our dealers, distributors, partners, consumers and employees, could adversely affect our business. Furthermore, without limiting the preceding sentence, if security breaches in connection with the delivery of our products and services allow unauthorized third parties to obtain control of or otherwise access consumers' networks or appliances, our reputation, business, results of operations and financial condition could be harmed.

The legal, regulatory and contractual environment surrounding information security, privacy and fraud is constantly evolving and companies that collect and retain information are under increasing attack by cyber-criminals around the world. We are dependent on information technology networks and systems, including the Internet, to process, transmit and store electronic information and, in the normal course of our business, we collect and retain certain information, including financial information and personally identifiable information, from and pertaining to our dealers, distributors, partners, consumers and employees. The protection of dealer, distributor, partner, consumer and employee data is important to us, and we devote significant resources to addressing security vulnerabilities in our products and information technology systems, including encrypting some data repositories and engaging security experts to conduct penetration testing to help us uncover vulnerabilities in our systems. However, the policies and security measures that we put in place could prove to be inadequate and cannot guarantee security, and our information technology infrastructure may be vulnerable to criminal cyber-attacks or data security incidents due to employee or dealer negligence, error, malfeasance, or other vulnerabilities. Cyber security attacks are increasingly sophisticated, change frequently, and often go undetected until after an attack has been launched. We may fail to identify these new and complex methods of attack or fail to invest sufficient resources in security measures. We have and will continue to experience cyber-attacks, and we cannot be certain that advances in cyber-capabilities or other developments will not permit compromise or breach the technology protecting the networks that access our products and services and repositories where we store this information.

We have acquired a number of companies over the years and may continue to do so in the future. While we make significant efforts to address any information technology security issues with respect to our acquisitions, we may still inherit such risks when we integrate the acquired products and systems.

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In addition, consumers can use our tools for authorized, remote access to their automation systems, and certain of our employees and independent dealers can be provided authorized access to monitor and update certain of our products and services remotely. Security breaches by third parties or by, or originating from, one or more of our dealers, distributors or employees, that allow unauthorized access or control of our consumers' appliances through our products or to obtain, collect, use or disclose any personal data of consumers, could harm our reputation, business, results of operations and financial condition. Furthermore, although we do not recommend or approve of port forwarding for remote access to our solutions, certain of our dealers have in the past and may in the future enable port forwarding, which could create security vulnerabilities in their customers' home networks.

It is difficult to determine what harm may result from any specific interruption or security breach. Any failure or perceived failure to maintain performance, reliability, security and availability of systems or the actual or potential theft, loss, fraudulent use or misuse of our products or associated confidential information, including personally identifiable data of a dealer, distributor, partner, consumer, and employee, could result in:

- harm to our reputation or brand, which could lead some consumers to stop using certain of our products or services, reduce or delay future purchases of our products or services, use competing products or services, or materially and adversely affect the overall market perception of the security and reliability of our services and home automation products generally;
- individual and/or class action lawsuits, which could result in financial judgments against us and that would cause us to incur legal fees and costs;
- legal or regulatory enforcement action, which could result in fines and/or penalties and which would cause us to incur legal fees and costs; and/or
- additional costs associated with responding to the interruption or security breach, such as investigative and remediation costs, the costs of providing individuals and/or data owners with notice of the breach, legal fees, the costs of any additional fraud detection activities, or the costs of prolonged system disruptions or shutdowns.

Any of these actions could materially adversely impact our business and results of operations.

Because we store, process, and use data, some of which contains personal information, we are subject to complex and evolving federal, state, and foreign laws and regulations regarding privacy, data protection, and other matters. Many of these laws and regulations are subject to change and uncertain interpretation, and could result in investigations, claims, changes to our business practices, increased cost of operations, and declines in user growth, retention, or engagement, any of which could seriously harm our business.

We are subject to a variety of laws and regulations that involve matters central to our business, including privacy, rights of publicity, data protection, content, intellectual property, distribution, electronic contracts and other communications, competition, protection of minors, consumer protection, taxation, and online-payment services. Because we store, process, and use data, some of which contains personal information, we are subject to complex and evolving federal, state, and foreign laws and regulations regarding privacy, data protection, and other matters. Both in the United States and abroad, these laws and regulations constantly evolve and are subject to significant change. In addition, in the United States each state has a separate statutory approach to privacy regulation, and recently states such as California have been very active in pursuing new regulations that are typically more restrictive than other jurisdictions. The application and interpretation of these laws and regulations are often uncertain, particularly in the new and rapidly evolving industry in which we operate. Continually implementing up-to-date data security tools and procedures and maintaining privacy standards that comply with ever-changing privacy regulations in multiple jurisdictions is challenging. For example, the General Data Protection Regulation (GDPR) in the European Union, which went into effect on May 25, 2018, has not yet been fully interpreted by legal and regulatory bodies, and while we have invested significant resources in compliance efforts, there is no guarantee that our efforts to date will be found to be adequate.

In addition, there are restrictions on cross-border transfers of personal data. For example, jurisdictions such as the European Union and Switzerland do not view the privacy protections of U.S. law to be independently sufficient to

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receive personal data from their jurisdictions. However, the United States and the European nations adopted a safe-harbor framework called the Privacy Shield, whereby U.S. companies doing business in Europe can lawfully transfer personal data to the United States, provided that such U.S. companies self-certify under this framework. We have submitted our self-certification application pursuant to the Privacy Shield, and as part of this self-certification, we have committed to abide by the Privacy Shield principles with respect to any personal information transferred. However, the Privacy Shield is subject to an annual review by the European Commission, and on July 5, 2018 members of the European Parliament passed a nonbinding resolution calling for the Privacy Shield to be suspended at the European Commission's next review which occurred in September 2018. Thus far the Privacy Shield has not been suspended, but if it is suspended in the future, we will need to find other ways to lawfully transfer personal data that is required for our business and operations from the EU and Switzerland to the U.S., and there is no guarantee that we will be able to adequately implement such alternative compliance methodologies, such as implementing binding corporate rules, before the suspension goes into effect.

We publicly post our privacy policies and practices concerning our processing, use and disclosure of personal information. Our privacy policy and other statements we publish provide promises and assurances about privacy and security that could subject us to potential regulatory action or other liabilities if: (a) such statements are found to be deceptive or misrepresentative of our practices, (b) we fail to take adequate measures to ensure that we adhere to applicable regulations, or (c) our third-party data processors fail to adequately protect personal information that they process on our behalf.

We encounter seasonality in sales, which could harm the amount, timing and predictability of our revenue and cause our stock price to fluctuate.

We have little recurring revenue or backlog, and our revenue is generated from orders of our solutions from new and existing consumers, each of which may cause our quarterly results to fluctuate. In addition, we may experience seasonality in the sales of our solutions. Historically, our revenue is generally highest in the fourth quarter and lowest in the first quarter. Seasonal variations in our sales may lead to significant fluctuations in our cash flows and results of operations on a quarterly basis and this may cause our stock price to fluctuate.

We may not generate significant revenue as a result of our current research and development efforts.

We have made and expect to continue to make significant investments in research and development and related product opportunities. During the three months ended March 31, 2019, we spent \$11.8 million on research and development expenses. High levels of expenditures for research and development could harm our results of operations, especially if not offset by corresponding future revenue increases. We believe that we must continue to dedicate a significant amount of resources to our research and development efforts to maintain our competitive position. However, it is difficult to estimate when, if ever, we will generate significant revenue as a result of these investments.

Our strategy includes pursuing acquisitions and our potential inability to identify good opportunities and to successfully integrate newly-acquired technologies, assets, businesses, or personnel may harm our financial results.

We believe part of our growth will be driven by acquisitions of other companies or their technologies, assets and businesses, but we may not be able to acquire the targeted technologies, assets and businesses we identify as desirable for a price we consider to be reasonable or at all. Recent acquisitions include Pakedge in January 2016, Triad in February 2017, ihiji in December 2017, and NEEO in January 2019. These acquisitions and any future acquisitions we evaluate and complete will give rise to risks, including:

- Incurring higher than anticipated capital expenditures and operating expenses;
- Failing to assimilate the operations and personnel, or failing to retain the key personnel of the acquired company or business;
- Failing to integrate the acquired technologies, or incurring significant expense to integrate acquired technologies into our solutions;

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- Disrupting our ongoing business;
- Dissipating or diverting our management resources;
- Failing to maintain uniform standards, controls and policies;
- Incurring significant accounting charges;
- Impairing relationships with employees, dealers, distributors, partners or consumers;
- Finding that the acquired technology, assets or business does not further our business strategy, that we overpaid for the technology, assets or business, or that we may be required to write off acquired assets or investments partially or entirely;
- Failing to realize the expected synergies of the transaction;
- Being exposed to unforeseen liabilities and contingencies that were not identified and mitigated during diligence conducted prior to acquiring the company, including but not limited to the risk that the products or services of the acquired company violate third-party intellectual property rights or regulatory standards or contain other vulnerabilities; and
- Being unable to generate sufficient revenue from acquisitions to offset the associated acquisition costs.

Fully integrating acquired technology, asset, business, or personnel into our operations may take a significant amount of time and resources. We may not be successful in overcoming these risks or any other problems encountered with such acquisitions. To the extent we do not successfully avoid or overcome the risks or problems related to any such acquisitions, our results of operations and financial condition could be harmed. Acquisitions also could impact our financial position and capital needs, or could cause fluctuations in our quarterly and annual results of operations.

Acquisitions could include significant goodwill and intangible assets. The amortization of such intangible assets would reduce our profitability and there may be future impairment charges that would reduce our stated earnings. We may incur significant costs in our efforts to engage in strategic transactions and these expenditures may not result in successful acquisitions.

Future acquisitions of technologies, assets or businesses, that are paid for partially or entirely through the issuance of stock or stock rights, could dilute the ownership of our existing stockholders.

We expect that the consideration we might pay for any future acquisitions of technologies, assets or businesses could include stock, rights to purchase stock, cash or some combination of the foregoing. If we issue stock or rights to purchase stock in connection with such future acquisitions, net income (loss) per share and then-existing holders of our common stock may experience dilution.

We may pursue business opportunities that diverge from our current business model, which may cause our business to suffer.

We may pursue business opportunities that diverge from our current business model, including expanding our solutions into lines of business with which we have no experience, investing in new and unproven technologies, and expanding our existing sales channels or adding new sales channels, including through acquisitions such as our recent acquisition of Triad and its speaker lines. We can offer no assurance that any such new business opportunities will prove to be successful. Among other negative effects, our pursuit of such business opportunities could reduce operating margins and require more working capital, or materially and adversely affect our business, financial condition, results of operations and cash flows.

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Our gross margins can vary significantly depending on multiple factors, which can result in fluctuations in our results of operations.

Our gross margins are likely to vary due to consumer demand, product mix, new product introductions, unit volumes, commodity and supply chain costs, regulatory changes including changes to import/export duties, product delivery costs, geographic sales mix, excess and obsolete inventory and the complexity and functionality of new product innovations. In particular, if we are not able to introduce new solutions in a timely manner at the cost we expect, or if consumer demand for our solutions is less than we anticipate, or if there are product pricing, marketing and other initiatives by our competitors to which we need to react that lower our margins, then our overall gross margin will be less than we project. The impact of these factors on gross margins can create unanticipated fluctuations in our results of operations, which may cause volatility in our stock price.

If we are unable to substantially utilize our net operating loss or tax credit carryforwards, our financial results will be harmed.

As of December 31, 2018, our net operating loss (“NOL”) carryforward amounts for U.S. federal income and state tax purposes were \$57.1 million and \$61.1 million, respectively. In addition to the NOL carryforwards, as of December 31, 2018, we had U.S. federal and state tax credit carryforwards of \$6.4 million and \$2.8 million, respectively. While we have generated profits at times in the past, there is no assurance that we will be able to generate sufficient taxable income to utilize our NOLs or tax credits before they expire.

If we are unable to manage our business growth and diverse and complex operations, our reputation in the market and our ability to generate revenue from new or existing consumers may be harmed.

Because our operations are geographically diverse and complex, our personnel resources and infrastructure could become strained and our reputation in the market and our ability to successfully implement our business plan may be harmed. The growth in the size, complexity and diverse nature of our business and the expansion of our product lines and consumer base, including through acquisitions, have placed increased demands on our management and operations, and further growth, if any, may place additional strains on our resources in the future. Our ability to effectively compete and to manage our plan to continue to expand our headcount and operations may depend on, among other things:

- Maintaining institutional knowledge by retaining and expanding the core competencies critical to our operations in our senior management and key personnel;
- Increasing the productivity of our existing employees and attracting new talent;
- Maintaining existing productive relationships and developing new productive relationships with independent contract manufacturers, dealers and distributors;
- Improving our operational, financial and management controls; and
- Improving our information reporting systems and procedures.

If we do not manage the size, complexity and diverse nature of our business effectively, we could experience delayed product releases and longer response times by our dealers in assisting our consumers in implementing our solutions, and could lack adequate resources to support our consumers on an ongoing basis, any of which could harm our reputation in the market, our ability to successfully implement our business plan and our ability to generate revenue from new or existing consumers.

If we fail to retain our key employees and attract talented new personnel as needed, our business would be harmed and we might not be able to implement our business plan successfully.

Given the complex nature of the technology on which our business is based and the speed with which such technology advances, our future success is dependent, in large part, upon our ability to attract and retain highly qualified executive, managerial, engineering, and sales and marketing personnel. Competition for talented personnel

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is intense, and we cannot be certain that we can retain our executive, managerial, engineering, and sales and marketing personnel, or that we can attract, assimilate or retain such personnel in the future. Our inability to attract and retain such personnel could harm our business, results of operations and financial condition.

Downturns in general economic and market conditions, including but not limited to downturns in housing markets and reductions in consumer spending, may reduce demand for our solutions, which could harm our revenue, results of operations, financial condition and cash flows.

Our revenue, results of operations and cash flows depend on the overall demand for our solutions and the willingness of our dealer-channel to invest in marketing our solutions, both of which can be significantly reduced in economic environments characterized by market and interest rate volatility, decreased consumer confidence, high unemployment, declines in residential remodeling and housing starts, fluctuating exchange rates, and diminished growth expectations in the U.S. economy and abroad. During periods of weak or unstable economic and market conditions, providers of products and services that represent discretionary purchases, such as our home automation products, are disproportionately affected. In addition, during these periods, the number of independent dealers and distributors may decline as the prospects for home building and home renovation projects diminish, which may have a corresponding impact on our growth prospects. Furthermore, during challenging economic times consumers may face issues in gaining timely access to sufficient credit, which could impair their ability to make timely payments. There is also an increased risk during these periods that an increased percentage of our dealers will file for bankruptcy protection, which may harm our reputation, revenue, profitability and results of operations. We cannot predict the timing, strength or duration of any economic slowdown, instability or recovery, generally or within any particular geography or industry. Any downturns in the general economic conditions of the geographies and industries in which we operate, or any other factors negatively impacting housing markets or consumer spending, could materially and adversely impact our revenue, results of operations, financial condition and cash flows.

If our estimates or judgments relating to our critical accounting policies are based on assumptions that change or prove to be incorrect, our results of operations could fall below expectations of securities analysts and investors, resulting in a decline in our stock price.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in our consolidated financial statements and accompanying notes. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, as provided in “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” the results of which form the basis for making judgments about the carrying values of assets, liabilities and equity, and the amount of revenue and expenses that are not readily apparent from other sources. Significant assumptions and estimates used in preparing our consolidated financial statements include, or may in the future include, those related to revenue recognition, allowance for doubtful accounts, inventories, product warranties, income taxes and stock-based compensation expense. Our results of operations may be harmed if our assumptions change or if actual circumstances differ from those in our assumptions, which could cause our results of operations to fall below the expectations of securities analysts and investors, resulting in a decline in our stock price.

Changes in existing financial accounting standards or practices, or taxation rules or practices, may harm our results of operations.

Changes in existing accounting or taxation rules or practices, new accounting pronouncements or taxation rules, or varying interpretations of current accounting pronouncements or taxation practice could harm our results of operations or the manner in which we conduct our business. For example, on December 22, 2017, “H.R.1”, known as the “Tax Cuts and Jobs Act”, (the “Tax Act”) was signed into U.S. law, which among other changes reduced the corporate income tax rate to 21%, creates a territorial tax system (with a one-time mandatory tax on previously deferred foreign earnings), and requires companies to pay minimum taxes on foreign earnings and subjects certain payments from U.S. corporations to foreign related parties to additional taxes. While the Tax Act will result in a lower domestic income tax rate once we fully utilize our net operating losses and other accumulated tax credits, in 2018 we were subject to the one-time mandatory tax on previously deferred foreign earnings, which resulted in increased utilization of our net operating loss carryover to eliminate any cash federal income taxes. In addition, the Tax Act is subject to further interpretation from the U.S. federal and state governments and regulatory organizations,

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such as the Treasury Department and/or Internal Revenue Service (the “IRS”) and this could change our U.S. tax liabilities based on updated guidance and interpretations. The guidance and notices may have a material impact on us. In addition, the IRS has already issued and stated that it intends to continue to issue notices of intent to amend certain regulations and also institute new regulations with respect to the Tax Act. These proposed regulations either clarify certain tax positions or provide new regulations. We have not taken these notices into account as they are yet to be become final regulations and may or may not have a material impact on us. Also, because there may be additional state income tax implications, we will continue to monitor changes in state and local tax laws to determine if state and local taxing authorities intend to conform or deviate from changes to U.S. federal tax legislation as a result of the Tax Act.

We also earn a portion of our operating income from outside the United States. The Tax Act significantly impacts how U.S. multinational corporations are taxed on foreign earnings. Numerous countries are evaluating their existing tax laws in response to the changes in U.S. tax laws. Although we cannot predict whether or in what form any legislation based on such proposals may be adopted by the countries in which we do business, future tax reform based on such proposals may increase the amount of taxes we pay and adversely affect our operating results and cash flows. We will continue to monitor the impact of this and further changes to applicable tax laws to our overall business strategy.

Mergers or other strategic transactions involving our competitors could weaken our competitive position, which could harm our results of operations.

Our industry is highly fragmented, and we believe it is likely that some of our existing competitors will consolidate or be acquired. In addition, some of our competitors may enter into new alliances with each other or may establish or strengthen cooperative relationships with systems integrators, third-party consulting firms or other parties. For example, Amazon acquired Ring, a manufacturer of video doorbells; Google acquired Nest Labs, a manufacturer of thermostats and smoke detectors; Nest Labs acquired Dropcam, a home-monitoring camera company; and Samsung Electronics acquired SmartThings and Harman International Industries. Transactions such as these, as well as any additional consolidations, acquisitions, alliances or cooperative relationships, or new product introductions by companies in our industry, could lead to pricing pressure, reduce our market share or result in a competitor with greater financial, technical, marketing, service and other resources than ours, all of which could harm our business, results of operations and financial condition.

Failure to achieve and maintain effective internal control over financial reporting could result in our failure to accurately report our financial results. Any inability to report and file our financial results accurately and timely could harm our business and adversely impact investor confidence in our company and, as a result, the value of our common stock.

Effective internal controls are necessary for us to produce reliable financial reports and are important to helping prevent financial fraud. If we cannot provide reliable financial reports or prevent fraud, our business and results of operations could be harmed, investors could lose confidence in our reported financial information, and the trading price of our stock could drop significantly. We are required to perform system and process evaluation and testing of our internal control over financial reporting to allow management to report on the effectiveness of our internal control over financial reporting, as required by Section 404 of the Sarbanes-Oxley Act, or Section 404. This assessment includes disclosure of any material weaknesses identified by our management in our internal control over financial reporting. During the evaluation and testing process, if we identify one or more material weaknesses in our internal control over financial reporting, we will be unable to assert that our internal controls are effective. We may not be able to remediate any future material weaknesses, or to complete our evaluation, testing and any required remediation in a timely fashion. If we are unable to assert that our internal control over financial reporting is effective, or if our auditors are unable to express an opinion on the effectiveness of our internal controls when they are required to issue such opinion, investors could lose confidence in the accuracy and completeness of our financial reports, which could harm our stock price.

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Our failure to raise additional capital or generate cash flows necessary to expand our operations, invest in new technologies and otherwise respond to business opportunities or unforeseen circumstances in the future could reduce our ability to compete successfully and harm our results of operations.

While we believe that our existing cash and cash equivalents will be sufficient to meet our anticipated cash requirements for at least the next 12 months, at some point we may need to raise additional funds, and we may not be able to obtain additional debt or equity financing on favorable terms, if at all. If we raise additional equity financing, our security holders may experience significant dilution of their ownership interests and the value of shares of our common stock could decline. If we engage in debt financing, we may be required to accept terms that restrict our ability to incur additional indebtedness, force us to maintain specified liquidity or other ratios or restrict our ability to pay dividends or make acquisitions. If we need additional capital and cannot raise it on acceptable terms, if at all, we may not be able to, among other things:

- Develop and enhance our solutions;
- Continue to expand our research and development, sales and marketing organizations;
- Hire, train and retain employees;
- Respond to competitive pressures or unanticipated working capital requirements; or
- Pursue acquisition opportunities.

Our inability to do any of the foregoing could reduce our ability to compete successfully and harm our results of operations.

We may be subject to additional tax liabilities, which would harm our results of operations.

We are subject to income, sales, use, value added, tariffs and other taxes in the United States and other countries in which we conduct business, which laws and rates vary greatly by jurisdiction. Certain jurisdictions in which we do not collect sales, use, value added, tariffs or other taxes on our sales may assert that such taxes are applicable, which could result in tax assessments, penalties and interest, and we may be required to collect such taxes in the future. Significant judgment is required in determining our worldwide provision for income taxes and evaluating our uncertain tax positions. These determinations are highly complex and require detailed analysis of the available information and applicable statutes and regulatory materials. In the ordinary course of our business, there are many transactions and calculations where the ultimate tax determination is uncertain. Although we believe our tax estimates are reasonable, the final determination of tax audits and any related litigation could be different from our historical tax practices, provisions and accruals. If we receive an adverse ruling as a result of an audit, or we unilaterally determine that we have misinterpreted provisions of the tax regulations to which we are subject, our tax provision, results of operations or cash flows could be harmed. In addition, liabilities associated with taxes are often subject to an extended or indefinite statute of limitations period. Therefore, we may be subject to additional tax liability (including penalties and interest) for any particular year for extended periods of time depending on the specific statute of limitations in the relevant jurisdiction.

Our business is subject to the risks of earthquakes, hurricanes, fire, power outages, floods and other catastrophic events, and to interruption by man-made problems such as terrorism.

A significant natural disaster, such as an earthquake, hurricane, fire or a flood, or a significant power outage could harm our business, results of operations and financial condition. Natural disasters could affect our manufacturing vendors' or logistics providers' ability to perform services such as manufacturing products or assisting with shipments on a timely basis. Our three largest contract manufacturers have manufacturing facilities located in China and Korea. In the event our manufacturing vendors' information technology systems or manufacturing or logistics abilities are hindered by any of the events discussed above, shipments could be delayed or cancelled, resulting in missing financial targets, such as revenue and shipment targets, for a particular quarter. Further, if a natural disaster occurs in a region from which we derive a significant portion of our revenue, such as metropolitan areas in North America, consumers in those regions may delay or forego purchases of our solutions

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from dealers and distributors, which may harm our results of operations for a particular period. In addition, acts of terrorism, including cyber terrorism or crime, acts of war, financial crises, trade friction or geopolitical and social turmoil in those parts of the world that serve as markets for our solutions, such as Europe, Asia, Australia or elsewhere, could cause disruptions in our business or the business of our manufacturers, logistics providers, dealers, distributors, consumers or the economy as a whole. These uncertainties may cause our consumers to reduce discretionary spending on their home and make it difficult for us to accurately plan future business activities. Given our typical concentration of sales at the end of each month and quarter, any disruption in the business of our manufacturers, logistics providers, dealers, distributors and consumers that impacts sales at the end of our quarter could have a greater impact on our quarterly results. All of the aforementioned risks may be augmented if the disaster recovery plans for us and our suppliers prove to be inadequate. To the extent that any of the above results in delays or cancellations of orders, or delays in, or cancellations of the manufacture, deployment or shipment of our products, our business, financial condition and results of operations would be harmed.

Failure to comply with laws and regulations could harm our business.

Our business is subject to regulation by various federal, state, local and foreign governmental agencies, including agencies responsible for monitoring and enforcing employment and labor laws, workplace safety, product safety, environmental laws, consumer privacy and protection laws, anti-bribery laws, import/export controls, federal securities laws and tax laws and regulations. Furthermore, existing regulations are subject to change, and such changes may require among other things, additional testing, development, and certification. As we continue to develop new products, acquire companies with new product lines and expand our geographical footprint to market and sell products directly in new jurisdictions, we may become subject to additional rules and regulations, and these regulatory requirements may be different from or more stringent than those in the United States and Europe. While we have obtained these certifications for many of our products currently sold in expanded jurisdictions, we continue to work towards full and continued compliance for all of our products sold. Delays in meeting, or failure to meet, these certification standards may cause us to miss market opportunities and may hinder us from entering and selling our products in those markets. Noncompliance with applicable regulations or requirements could subject us to investigations, sanctions, enjoinders of future shipments, mandatory product recalls, seizures, enforcement actions, disgorgement of profits, fines, damages, civil and criminal penalties or injunctions. If any governmental sanctions are imposed, or if we do not prevail in any possible civil or criminal litigation, our business, results of operations and financial condition could be materially harmed. In addition, responding to any action will likely result in a significant diversion of management's attention and resources and an increase in professional fees. Enforcement actions and sanctions could further harm our business, results of operations and financial condition.

Governmental regulations affecting the import or export of our products could harm our revenues.

The United States and various foreign governments have imposed controls, export license requirements and restrictions on the import or export of some technologies, especially encryption technology, and may impose additional or broader controls, export license requirements and restrictions on the import or export of some technologies in the future. In addition, from time to time, governmental agencies have proposed additional regulation of encryption technology, such as requiring the escrow and governmental recovery of private encryption keys. Although we do not believe that any of our products currently require an export license, if our products or components of our products become subject to governmental regulation of encryption technology or other governmental regulation of imports or exports, we may be required to obtain import or export approval for such products, which could increase our costs and harm our international and domestic sales. In addition, failure to comply with such regulations could result in penalties, costs and restrictions on export privileges, which would harm our results of operations.

Regulations related to "conflict minerals" may force us to incur additional expenses, may result in damage to our business reputation and may adversely impact our ability to conduct our business.

Pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), we are required to adhere to certain reporting and other requirements regarding the use of certain minerals and derivative metals (referred to as "conflict minerals," regardless of their actual country of origin) in our products. Some of these metals are commonly used in electronic equipment and devices, including our products. These requirements require that we investigate, disclose and report whether or not any such metals in our products

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originated from the Democratic Republic of Congo or adjoining countries. We do not directly source any of our own raw conflict minerals, rather we have a complex supply chain, with numerous suppliers for the components and parts used in each of our products. As a result, we incur costs to comply with the diligence and disclosure requirements of Dodd-Frank Act. In addition, because our supply chain is so complex, we may not be able to sufficiently verify the origin of all relevant metals used in our products through the due diligence procedures that we implement. We may incur reputational damage if we determine that any of our products contain minerals or derivative metals that are not conflict free or if we are unable to sufficiently verify the source for all conflict minerals used in our products through the procedures we may implement. Furthermore, key components and parts that can be shown to be “conflict free” may not be available to us in sufficient quantity, or at all, or may only be available at significantly higher cost to us. If we are not able to meet customer requirements, customers may choose to disqualify us as a supplier. Any of these outcomes could adversely affect our business, financial condition or operating results.

Health care reform could increase our cost of labor

In March 2010, the Patient Protection and Affordable Care Act (the “ACA”) was signed into U.S. law. The ACA is comprehensive U.S. health care legislation that includes provisions that subject us to potential penalties unless we offer certain employees minimum essential health care coverage that is affordable and provides minimum value. In order to comply with the employer mandate provision of the ACA that became effective January 1, 2015, we offer health care coverage to all applicable employees eligible for coverage under the ACA. Designating employees as eligible is complex, and is subject to challenge by employees and the Internal Revenue Service. While we believe we have properly identified eligible employees, a later determination that we failed to offer the required health coverage to eligible employees could result in penalties that may harm our business or reputation. We cannot be certain that compliant insurance coverage will remain available to us on reasonable terms, and we could face additional risks arising from future changes to the ACA or other legislation or executive orders that repeal and replace in whole or in part the ACA.

Government regulations of wireless networking in the United States or internationally may result in unanticipated costs and failure to comply with such laws and regulations could harm our business.

Our wireless communication and networking products operate through the transmission of radio signals and radio emissions are subject to regulation in the United States and in other countries in which we do business. In the United States, various federal agencies, including the Federal Communications Commission (“FCC”), and various state agencies have promulgated regulations that concern the use of radio/electromagnetic emissions standards. Member countries of the European Union have enacted similar standards concerning electrical safety and electromagnetic compatibility and emissions. As these regulations and standards evolve, and if new regulations or standards are implemented, we will be required to modify our products or develop and support new versions of our products, and our compliance with these regulations and standards may become more burdensome. The failure of our products to comply, or delays in compliance, with the various existing and evolving industry regulations and standards could prevent or delay introduction of our products, which could harm our business. Our inability to alter our products to address these requirements and any regulatory changes may have a material adverse effect on our business, operating results and financial condition. In addition, dealer and end-user uncertainty regarding future policies may also affect demand for wireless networking products, including our products.

Risks Related to Our International Operations

In recent years, a significant amount of our revenue has come from sales outside of the United States, and we are therefore subject to a number of risks associated with international sales and operations.

We have a limited history of marketing, selling, and supporting our products and services internationally. However, international revenue (excluding Canada) accounted for 24% of our total revenue for the three months ended March 31, 2019, and that percentage may grow in the future. As a result, we must hire and train experienced personnel to staff and manage our foreign operations. To the extent that we experience difficulties in recruiting, training, managing, and retaining international dealers, distributors, and international staff, and specifically staff related to sales management and sales personnel, we may experience difficulties in productivity in foreign markets.

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If we are not able to increase the sales of our solutions to consumers located outside of North America, our results of operations or revenue growth may be harmed. In addition, in connection with our expansion into foreign markets, we are a receiver of currencies other than the U.S. dollar. Accordingly, changes in exchange rates, and in particular a strengthening of the U.S. dollar, will negatively affect our net sales as expressed in U.S. dollars. There is also a risk that we will have to adjust local currency product pricing due to competitive pressures when there has been significant volatility in foreign currency exchange rates.

Conducting and launching operations on an international scale requires close coordination of activities across multiple jurisdictions and time zones and consumes significant management resources. Our limited experience in operating our business in certain countries outside of the United States increases the risk that our current and any future international expansion efforts will not be successful. Conducting international operations subjects us to risks that, generally, we do not face in the United States, including:

- Fluctuations in currency exchange rates;
- Unexpected changes in foreign regulatory requirements;
- Longer accounts receivable payment cycles and difficulties in collecting accounts receivable;
- Difficulties in managing and staffing international operations, including differences in labor laws, which may result in higher personnel-related liabilities and expenses;
- Potentially adverse tax consequences, including the complexities of foreign value added tax systems and restrictions on the repatriation of earnings;
- Localization of our solutions and other materials, including translation into foreign languages and associated expenses;
- Localization of applicable agreements under applicable foreign law and differing legal standards and risks;
- The burdens of complying with a wide variety of foreign laws and different legal standards, including laws and regulations related to import/export, privacy, the transfer of personal information across borders, and data security and limitations on liability;
- Increased financial accounting and reporting burdens and complexities;
- Political, social and economic instability abroad, terrorist attacks and security concerns in general, including crime and cyber security; and
- Reduced or varied protection for intellectual property rights in some countries.

The impact of any one of these could harm our international business and, consequently, our results of operations generally. Additionally, operating in international markets also requires significant management attention and financial resources. We cannot be certain that the investment and additional resources required in establishing, acquiring or integrating operations and personnel in other countries will produce desired levels of revenue or profitability.

We conduct a significant amount of business in the European Union, including through our office located in England, and our operations may be affected by the results of the referendum vote by the United Kingdom to leave the European Union.

On June 23, 2016, the citizens of the United Kingdom approved a referendum to leave the European Union (“Brexit”), which led to significant political, economic and legal uncertainty. On March 29, 2017, the United Kingdom provided its official notice to the European Council that it intends to leave the European Union, triggering

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the two-year transitional period, which was set to expire on March 29, 2019, but was extended until October 31, 2019, in order to give Britain and the European Union more time to negotiate a mutually agreeable exit framework. There is still considerable uncertainty about how the new relationship will be implemented. Given the lack of comparable precedent, it is unclear how Brexit will affect economic conditions in the United Kingdom, the European Union, or globally, and Control4 specifically. Because we have sales throughout the European Union and offices in England and Germany, it is possible that Brexit could disrupt our current business structure in the European Union and may require us to restructure some or all of our operations in this region. In addition, the resulting fluctuation in currencies and market conditions may adversely affect our business, results of operations and financial condition.

Due to the global nature of our business, we could be harmed by violations of the U.S. Foreign Corrupt Practices Act, the U.K. Bribery Act or similar anti-corruption laws in other jurisdictions in which we operate, or various international trade and export laws.

The global nature of our business creates various domestic and local regulatory challenges. The U.S. Foreign Corrupt Practices Act (the “FCPA”), the U.K. Bribery Act 2010 (the “U.K. Bribery Act”), and similar anti-corruption laws in other jurisdictions generally prohibit companies and their intermediaries from making improper payments to government officials for the purpose of obtaining or retaining business. In addition, U.S.-based companies are required to maintain records that accurately and fairly represent their transactions and have an adequate system of internal accounting controls. We operate in areas of the world that experience corruption by government officials to some degree and, in certain circumstances, compliance with anti-corruption laws may conflict with local customs and practices. Although we periodically train our employees and agents about these anti-corruption laws, we cannot assure that our training is effective in reducing the risks attendant to such anti-corruption laws. Our global operations require us to import from and export to several countries, which geographically stretches our compliance obligations. In addition, changes in such laws could result in increased regulatory requirements and compliance costs, which could harm our business, financial condition and results of operations. Our employees or other agents may engage in prohibited conduct and render us responsible under the FCPA, the U.K. Bribery Act or similar anti-corruption laws. If we are found to be in violation of the FCPA, the U.K. Bribery Act or other anti-corruption laws (either due to acts or inadvertence of our employees, or due to the acts or inadvertence of other parties), we could suffer criminal or civil penalties or other sanctions, which could harm our business.

Risks Related to Our Intellectual Property

If we fail to protect our intellectual property and proprietary rights adequately, our business could be harmed.

We believe that proprietary technology is essential to establishing and maintaining our leadership position. We seek to protect our intellectual property through trade secrets, confidentiality, non-compete, non-solicitation and nondisclosure agreements, and by registering numerous patents, trademarks, copyrights, and/or domain names in various jurisdictions, as well as using other measures, some of which afford only limited protection. We also rely on patent, trademark, trade secret and copyright laws to protect our intellectual property. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy aspects of our technology or to obtain and use information that we regard as proprietary. Our means of protecting our proprietary rights may not be adequate or our competitors may independently develop similar or superior technology, or design around our intellectual property. In addition, the laws of some foreign countries do not protect our proprietary rights to as great an extent as the laws of the United States. Intellectual property protections may also be unavailable, limited or difficult to obtain and enforce in some countries, which could make it easier for competitors to capture market share. Our failure or inability to adequately protect our intellectual property and proprietary rights could harm our business, financial condition and results of operations.

To prevent substantial unauthorized use of our intellectual property rights, it may be necessary to prosecute actions for infringement and/or misappropriation of our proprietary rights against third parties. Any such action could result in significant costs and diversion of our resources and management’s attention, and we cannot assure that we will be successful in such action. Furthermore, many of our current and potential competitors have the ability to dedicate substantially greater resources to enforce their intellectual property rights than we do. Accordingly, despite our efforts, we may not be able to prevent third parties from infringing upon or misappropriating our intellectual property.

An assertion by a third party that we are infringing its intellectual property could subject us to costly and time-consuming litigation and lead to expensive licenses or significant liabilities in the event of an adverse judgment.

The industries in which we compete are characterized by the existence of a large number of patents, copyrights, trademarks and trade secrets, and by frequent litigation based on allegations of infringement or other violations of intellectual property rights. We have been subject to patent litigation in the past and we may be subject to similar litigation in the future. Given that our solution integrates with almost all network aware products, the risk that our solution may be subject to these allegations is exacerbated. As we seek to extend our solutions, we could be constrained by the intellectual property rights of others, including patent holding companies.

We are defendants in legal proceedings related to intellectual property rights from time to time, and in the past, we have entered into settlement agreements relating to contractual claims and alleged patent infringements, which have included future royalty payments on certain products, the payment of a lump sum amount for alleged past damages, and/or the payment of a fixed amount in exchange for a covenant not to sue.

We might not prevail in any current or future intellectual property infringement litigation given the complex legal and technical issues and inherent uncertainties in such litigation. Defending such claims, regardless of their merit, could be time-consuming and distracting to management, result in costly litigation or settlement, cause development delays or require us to enter into royalty or licensing agreements. In addition, we currently have a limited portfolio of issued patents compared to our larger competitors, and therefore may not be able to effectively utilize our intellectual property portfolio to assert defenses or counterclaims, or negotiate cross-licenses in response to patent infringement claims or litigation brought against us by third parties. Further, litigation may involve patent holding companies or other adverse patent owners who have no relevant products or revenues and against which our potential patents provide no deterrence, and many other potential litigants have the capability to dedicate substantially greater resources to enforce their intellectual property rights and to defend claims that may be brought against them. If our solutions exceed the scope of in-bound licenses or violate any third-party proprietary rights, we could be required to withdraw those solutions from the market, re-develop those solutions or seek to obtain licenses from third parties, which might not be available on reasonable terms or at all. Any efforts to re-develop our solutions, obtain licenses from third parties on favorable terms or license a substitute technology might not be successful and, in any case, might substantially increase our costs and harm our business, financial condition and results of operations. If we were compelled to withdraw any of our solutions from the market, our business, financial condition and results of operations could be harmed.

We are generally obligated to indemnify our independent dealers, distributors and partners for certain expenses and liabilities resulting from intellectual property infringement claims regarding our products, which could force us to incur substantial costs.

We have agreed to indemnify our independent dealers, distributors and other partners for certain intellectual property infringement claims regarding our products and other materials we provide to them. As a result, in the case of infringement claims against these dealers, distributors and partners, we could be required to indemnify them for losses resulting from such claims. We expect that some of our dealers, distributors and partners may seek indemnification from us in connection with infringement claims brought against them. We evaluate each such request on a case-by-case basis and we may not succeed in refuting any such claim we believe to be unjustified. If a dealer, distributor or partner elects to invest resources in enforcing a claim for indemnification against us that we believe is unjustified, we could incur significant costs disputing it. If we do not succeed in disputing it, we could face substantial liability.

The use of open source software in our solutions may expose us to additional risks and harm our intellectual property.

Some of our solutions use or incorporate software that is subject to one or more open source licenses. Open source software is typically freely accessible, usable and modifiable. Certain open source software licenses require a user who intends to distribute the open source software as a component of the user's software to disclose publicly part or all of the source code to the user's software. In addition, certain open source software licenses require the

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user of such software to make any derivative works of the open source code available to others on potentially unfavorable terms or at no cost.

The terms of many open source licenses to which we are subject have not been interpreted by U.S. or foreign courts, and accordingly there is a risk that those licenses could be construed in a manner that imposes unanticipated conditions or restrictions on our ability to commercialize our solutions. In that event, we could be required to seek licenses from third parties in order to continue offering our solutions, to re-develop our solutions, to discontinue sales of our solutions or to release our proprietary software code under the terms of an open source license, any of which could harm our business. Further, given the nature of open source software, it may be more likely that third parties might assert copyright and other intellectual property infringement claims against us based on our use of these open source software programs. Litigation could be costly for us to defend, have a negative effect on our operating results and financial condition, or require us to devote additional research and development resources to change our solutions.

We monitor the use of all open source software in our products, solutions, processes and technology, and seek to ensure that no open source software is used in such a way as to require us to disclose the source code to the related product or solution when we do not wish to do so. Despite these precautions, if a third-party software provider has incorporated certain types of open source software into software we license from such third-party provider for our solutions without our knowledge or if we have otherwise incorporated unfavorable open source software into our solutions, we could, under certain circumstances, be required to disclose the related source code to our solutions. This could harm our intellectual property position and our business, results of operations and financial condition.

We rely on the availability of third-party licenses. If these licenses are available to us only on less favorable terms or not at all in the future, our business and results of operations may be harmed.

We have incorporated third-party licensed technology into our products. It may be necessary in the future to renew licenses relating to various aspects of these products or to seek additional licenses for existing or new products. The necessary licenses may not be available on acceptable terms, or at all. The inability to obtain certain licenses or other rights, or to obtain those licenses or rights on favorable terms, or the need to engage in litigation regarding these matters, could result in our inability to include certain features in our products or delays in product releases until such time, if ever, as equivalent technology could be identified, licensed or developed and integrated into our products, which may have a material adverse effect on our business, results of operations and financial condition. Moreover, the inclusion in our products of intellectual property licensed from third parties on a nonexclusive basis could limit our ability to protect our proprietary rights in our products.

Risks Related to Owning Our Common Stock

Our share price may be volatile, which may result in securities class action litigation against us.

The market price of our common stock has been and again could be subject to wide fluctuations in response to many risk factors listed in this section and other factors beyond our control, including but not limited to:

- Actual or anticipated fluctuations in our financial condition and results of operations;
- Overall conditions in our industry and market;
- Addition or loss of independent dealers, distributors or consumers;
- Changes in laws or regulations applicable to our solutions;
- Actual or anticipated changes in our growth rate relative to our competitors;
- Announcements by us, our competitors or strategic buyers of significant acquisitions, strategic partnerships, joint ventures or capital commitments;

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- Additions or departures of key personnel;
- Competition from existing products or new products that may emerge;
- Issuance of new or updated research or reports by securities analysts, activist investors and those who short our stock;
- Fluctuations in the valuation of companies perceived by investors to be comparable to us;
- Disputes or other developments related to proprietary rights, including patents, litigation matters and our ability to obtain intellectual property protection for our technologies;
- Actual or threatened litigation or adverse regulatory action against us;
- Trading of our common stock by us or our stockholders, or issuance of new shares;
- Share price and volume fluctuations attributable to inconsistent trading volume levels of our shares; and
- General economic, geopolitical and market conditions.

Furthermore, the stock markets have experienced extreme price and volume fluctuations that have affected and continue to affect the market prices of equity securities of many companies. These fluctuations often have been unrelated or disproportionate to the operating performance of those companies. These broad market and industry fluctuations, as well as general economic, geopolitical and market conditions such as recessions, interest rate changes or international currency and capital markets fluctuation, may harm the market price of our common stock. In the past, companies that have experienced volatility in the market price of their stock have been subject to securities class action litigation. We may be the target of this type of litigation in the future. Securities litigation against us could result in substantial costs and divert our management's attention from other business concerns, which could harm our business.

If securities or industry analysts do not publish research or reports about our business, or publish negative reports about our business, our share price and trading volume could decline.

The trading market for our common stock depends in part on the research and reports that securities or industry analysts publish about our business. We do not have any control over these analysts, activist investors, or those who short our stock. If one or more of the foregoing analysts who cover us, activist investors, or those who short our stock downgrade our shares, change their opinion of our shares, or publish negative or false reports for their own purposes, our share price will likely decline. If one or more of these analysts cease coverage of our company or fail to regularly publish research or reports on us, we could lose visibility in the financial markets, which could cause our stock price or trading volume to decline.

The concentration of ownership of our capital stock limits your ability to influence corporate matters.

As of March 31, 2019, our directors, executive officers and holders of more than 5% of our common stock, together with their affiliates, beneficially own, in the aggregate, 25% of our outstanding common stock. As a result, these stockholders, acting together, may have the ability to significantly influence the outcome of matters submitted to our stockholders for approval, including the election of directors and any merger, consolidation or sale of all or substantially all of our assets. In addition, these stockholders, acting together, control or significantly influence most matters related to the management and affairs of our company. Accordingly, this concentration of ownership and managerial authority might harm the market price of our common stock by:

- Delaying, deferring or preventing a change in corporate control;

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- Impeding a merger, consolidation, takeover or other business combination involving us; or
- Discouraging a potential acquirer from making a tender offer or otherwise attempting to obtain control of us.

Anti-takeover provisions in our charter documents and under Delaware law could make an acquisition of us, which may be beneficial to our stockholders, more difficult and may prevent attempts by our stockholders to replace or remove our current management and limit the market price of our common stock.

Provisions in our amended and restated certificate of incorporation and amended and restated bylaws may have the effect of delaying or preventing a change of control or changes in our management. Our amended and restated certificate of incorporation and amended and restated bylaws include provisions that:

- Authorize our board of directors to issue, without further action by the stockholders, up to 25,000,000 shares of undesignated preferred stock;
- Require that any action to be taken by our stockholders be effected at a duly called annual or special meeting and not by written consent;
- Specify that special meetings of our stockholders can be called only by our board of directors, the Chairman of the Board, the Chief Executive Officer or the President;
- Establish an advance notice procedure for stockholder approvals to be brought before an annual meeting of our stockholders, including proposed nominations of persons for election to our board of directors;
- Provide that directors may be removed only for cause;
- Provide that vacancies on our board of directors may be filled only by a majority of directors then in office, even though less than a quorum;
- Establish that our board of directors is divided into three classes—Class I, Class II and Class III—with each class serving staggered terms; and
- Require a super-majority of votes to amend certain of the above-mentioned provisions.

These provisions, alone or together, could delay or prevent hostile takeovers and changes in control. These provisions may also frustrate or prevent any attempts by our stockholders to replace or remove our current management by making it more difficult for stockholders to replace members of our board of directors, which is responsible for appointing the members of our management.

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

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

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds***Unregistered Sales of Equity Securities***

During the quarter ended March 31, 2019, we did not issue or sell any shares of our common stock or other equity securities pursuant to unregistered transactions in reliance upon an exemption from the registration requirements of the Securities Act of 1933, as amended.

Share Repurchases

In February 2018, the Company's Board of Directors authorized the repurchase of up to \$20.0 million in Control4 common stock from time to time on the open market. In October 2018, the Company's Board of Directors authorized the expansion of the repurchase program providing approval for the Company to repurchase an additional \$20 million in Control4 common stock from time to time on the open market until December 31, 2019.

During the three months ended March 31, 2019, the Company repurchased 139,782 shares for \$2.5 million. The Company has \$13.6 million remaining under the share repurchase program as of March 31, 2019.

Period	Total Number of Shares Purchased	Average Price Paid Per Share⁽¹⁾	Total Number of Shares Purchased as Part of Publicly Announced Plan	Dollar Value of Shares that May Yet Be Purchased Under the Plan (in thousands)
February 1 - February 28, 2019	139,782	\$ 18.04	139,782	
	<u>139,782</u>		<u>139,782</u>	<u>\$ 13,606</u>

⁽¹⁾ These amounts include fees and commissions associated with the share repurchase

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ITEM 6. Exhibits

The exhibits listed below are filed or incorporated by reference as part of this Quarterly Report on Form 10-Q.

Exhibit Number	Description of Exhibits	Incorporated by Reference from Form	Incorporated by Reference from Exhibit Number	Date Filed
2.1	Agreement and Plan of Merger by and among Wirepath Home Systems, LLC, Copper Manager Sub, Inc., and Control4 Corporation.	8-K	2.1	May 9, 2019
3.1	Amended and Restated Certificate of Incorporation.	10-Q	3.1	August 30, 2013
3.2	Amended and Restated Bylaws.	S-1	3.4	July 1, 2013
4.1	Form of Common Stock certificate of the Registrant.	S-1/A	4.1	July 18, 2013
21.1	List of Subsidiaries of the Registrant	Filed herewith		
31.1	Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act.	Filed herewith		
31.2	Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act.	Filed herewith		
32.1*	Certification of the Chief Executive Officer and the Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act.	Furnished herewith		
101.INS	XBRL Instance Document	Filed herewith		
101.SCH	XBRL Taxonomy Extension Schema Document	Filed herewith		
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document	Filed herewith		
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document	Filed herewith		
101.LAB	XBRL Taxonomy Extension Label Linkbase Document	Filed herewith		
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document	Filed herewith		

* The certifications furnished in Exhibit 32.1 hereto are deemed to accompany this Quarterly Report on Form 10-Q and will not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, except to the extent that the Registrant specifically incorporates it by reference.

Subsidiaries of Control4 Corporation

Control4 EMEA Ltd (United Kingdom)

Control4 Germany GmbH (Subsidiary of Control4 EMEA Ltd)

Control4 Europe doo Belgrade (Subsidiary of Control4 EMEA Ltd)

NEEO AG (Switzerland)

Control4 HK Limited (Hong Kong)

Control4 India Private Limited (India)

Control4 Smart Control Technology Shanghai Co., Ltd. (PR China)

Control4 Australia Pty Ltd (Australia)

Nexus Technologies Holdings Pty Ltd (Subsidiary of Control4 Australia Pty Ltd)

Control4 APAC Pty Ltd (Subsidiary of Nexus Technologies Holdings Pty Ltd)

Control4 New Zealand Pty Limited (Subsidiary of Control4 Australia Pty Ltd)



**CERTIFICATION PURSUANT TO RULE 13a-14(a) OR 15d-14(a) OF
THE SECURITIES EXCHANGE ACT OF 1934,
AS ADOPTED PURSUANT TO SECTION 302 OF
THE SARBANES-OXLEY ACT OF 2002**

I, Martin Plaehn, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Control4 Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 10, 2019

By: /s/ Martin Plaehn
Martin Plaehn
President and Chief Executive Officer
(Principal Executive Officer)

**CERTIFICATION PURSUANT TO RULE 13a-14(a) OR 15d-14(a) OF
THE SECURITIES EXCHANGE ACT OF 1934,
AS ADOPTED PURSUANT TO SECTION 302 OF
THE SARBANES-OXLEY ACT OF 2002**

I, Mark Novakovich, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Control4 Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 10, 2019

By: /s/ Mark Novakovich
Mark Novakovich
Chief Financial Officer
(Principal Financial and Accounting Officer)

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER
PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report on Form 10-Q of Control4 Corporation for the quarterly period ended March 31, 2019 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), Martin Plaehn, as Chief Executive Officer of Control4 Corporation, hereby certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of his knowledge, the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, and the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of Control4 Corporation.

Date: May 10, 2019

By: /s/ Martin Plaehn

Martin Plaehn
President and Chief Executive Officer
(Principal Executive Officer)

In connection with the Quarterly Report on Form 10-Q of Control4 Corporation for the quarterly period ended March 31, 2019 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), Mark Novakovich, as Chief Financial Officer of Control4 Corporation, hereby certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of his knowledge, the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, and the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of Control4 Corporation.

Date: May 10, 2019

By: /s/ Mark Novakovich

Mark Novakovich
Chief Financial Officer
(Principal Financial and Accounting Officer)
