

CONTROL4 CORP  
Form 10-Q  
August 05, 2016  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

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FORM 10-Q

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(Mark one)

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

For the quarterly period ended June 30, 2016

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)

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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 84020  
(Address of principal executive offices) (Zip Code)

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

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(do not check if a smaller reporting company)

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

On July 29, 2016, 23,300,047 shares of the registrant's Common Stock, \$0.0001 par value, were outstanding.

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## PART I — Financial Information

## ITEM 1. Condensed Consolidated Financial Statements

## CONTROL4 CORPORATION

## CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except share data)

	June 30, 2016 (unaudited)	December 31, 2015
Assets		
Current assets:		
Cash and cash equivalents	\$ 22,807	\$ 29,530
Restricted cash	268	296
Short-term investments	20,780	37,761
Accounts receivable, net	22,982	21,322
Inventories	32,775	19,855
Prepaid expenses and other current assets	3,395	3,842
Total current assets	103,007	112,606
Property and equipment, net	6,564	6,584
Long-term investments	5,010	13,716
Intangible assets, net	25,633	4,547
Goodwill	16,615	2,760
Other assets	2,097	1,650
Total assets	\$ 158,926	\$ 141,863
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	\$ 19,484	\$ 17,588

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Accrued liabilities	7,733	5,880
Deferred revenue	1,303	1,099
Current portion of notes payable	441	727
Total current liabilities	28,961	25,294
Revolving credit line	5,000	—
Notes payable	85	186
Other long-term liabilities	805	938
Total liabilities	34,851	26,418
Commitments and contingencies (Note 11)	—	—
Stockholders' equity:		
Common stock, \$0.0001 par value; 500,000,000 shares authorized; 24,753,839 and 24,590,768 shares issued; 23,171,713 and 23,436,288 shares outstanding at June 30, 2016 and December 31, 2015, respectively	2	2
Treasury stock, at cost; 1,582,126 and 1,154,480 shares at June 30, 2016 and December 31, 2015, respectively	(12,262)	(9,020)
Additional paid-in capital	225,396	220,782
Accumulated deficit	(88,417)	(95,580)
Accumulated other comprehensive loss	(644)	(739)
Total stockholders' equity	124,075	115,445
Total liabilities and stockholders' equity	\$ 158,926	\$ 141,863

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

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## CONTROL4 CORPORATION

## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
	(unaudited)		(unaudited)	
Revenue	\$ 53,215	\$ 44,641	\$ 96,250	\$ 76,724
Cost of revenue	27,188	22,312	49,737	38,784
Gross margin	26,027	22,329	46,513	37,940
Operating expenses:				
Research and development	9,039	8,122	17,518	16,117
Sales and marketing	11,114	7,812	21,249	15,179
General and administrative	5,059	4,288	9,872	8,909
Litigation settlement	—	—	400	—
Total operating expenses	25,212	20,222	49,039	40,205
Income (loss) from operations	815	2,107	(2,526)	(2,265)
Other income (expense), net:				
Interest, net	—	42	5	63
Other income (expense), net:	(122)	70	(217)	(340)
Total other income (expense), net	(122)	112	(212)	(277)
Income (loss) before income taxes	693	2,219	(2,738)	(2,542)
Income tax expense (benefit)	169	178	(9,901)	(352)
Net income (loss)	\$ 524	\$ 2,041	\$ 7,163	\$ (2,190)
Net income (loss) per common share:				
Basic	\$ 0.02	\$ 0.08	\$ 0.31	\$ (0.09)
Diluted	\$ 0.02	\$ 0.08	\$ 0.30	\$ (0.09)
Weighted-average number of shares:				
Basic	23,162	24,309	23,248	24,326
Diluted	23,930	25,296	23,958	24,326

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





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## CONTROL4 CORPORATION

## CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(in thousands)

	Three Months		Six Months Ended	
	Ended June 30, 2016 (unaudited)	2015	June 30, 2016 (unaudited)	2015
Net income (loss)	\$ 524	\$ 2,041	\$ 7,163	\$ (2,190)
Other comprehensive income (loss):				
Foreign currency translation adjustment, net of tax	(366)	41	25	(246)
Net unrealized gains (losses) on available-for-sale investments, net of tax	(4)	(12)	70	28
Total other comprehensive income (loss)	(370)	29	95	(218)
Comprehensive income (loss)	\$ 154	\$ 2,070	\$ 7,258	\$ (2,408)

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

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## CONTROL4 CORPORATION

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

	Six Months Ended	
	June 30,	2015
	2016	(unaudited)
Operating activities		
Net income (loss)	\$ 7,163	\$ (2,190)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation expense	1,573	1,321
Amortization of intangible assets	2,172	728
Provision for doubtful accounts	167	172
Investment premium amortization	216	—
Stock-based compensation	3,950	3,528
Tax benefit from business acquisition	(9,708)	—
Changes in assets and liabilities:		
Accounts receivable	(1,600)	(1,458)
Inventories	(6,940)	(1,912)
Prepaid expenses and other current assets	1,513	(421)
Other assets	(347)	(116)
Accounts payable	1,752	(1,818)
Accrued liabilities	514	(256)
Deferred revenue	212	190
Other long-term liabilities	(462)	(369)
Net cash provided by (used in) operating activities	175	(2,601)
Investing activities		
Purchases of available-for-sale investments	(1,996)	(36,272)
Proceeds from maturities of available-for-sale investments	27,208	39,079
Purchases of property and equipment	(1,171)	(1,927)
Business acquisitions, net of cash acquired	(32,891)	(8,380)
Net cash used in investing activities	(8,850)	(7,500)
Financing activities		
Proceeds from exercise of options for common stock	711	710
Repurchase of common stock	(3,242)	(2,148)
Repayment of notes payable	(387)	(506)

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Proceeds from revolving credit facility	5,000	—
Payment of debt issuance costs	(89)	—
Net cash provided by (used in) financing activities	1,993	(1,944)
Effect of exchange rate changes on cash and cash equivalents	(41)	38
Net decrease in cash and cash equivalents	(6,723)	(12,007)
Cash and cash equivalents at beginning of period	29,530	29,187
Cash and cash equivalents at end of period	\$ 22,807	\$ 17,180
Supplemental disclosure of cash flow information		
Cash paid for interest	\$ 104	\$ 65
Cash paid for taxes	622	121
Supplemental schedule of non-cash investing and financing activities		
Net unrealized losses on available-for-sale investments	70	28

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

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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 personalized, smart home solutions that are designed to enhance the daily lives of our customers. The Company’s solutions unlock the potential of connected devices throughout a home or business, making entertainment systems easier to use and more accessible, spaces more comfortable and energy efficient, and individuals more secure. The Company was incorporated in the state of Delaware on March 27, 2003.

Unaudited Interim Financial Statements

The accompanying condensed consolidated balance sheets, condensed consolidated statements of operations, condensed consolidated statements of comprehensive income (loss), and condensed consolidated statements of cash flows are unaudited. These unaudited interim condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) on the same basis as the audited consolidated financial statements 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 and six months ended June 30, 2016 are not necessarily indicative of the results that may be expected for the year ending December 31, 2016, or any other future interim or annual period.

These unaudited interim 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 Securities and Exchange Commission (the “SEC”) on February 16, 2016. The December 31, 2015 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 United States dollars, except for sales to dealers and distributors located in the United Kingdom, Canada, Australia, and the European Union, which are generally denominated in pounds sterling, Canadian dollars, Australian dollars, and the euro, respectively. There were no individual account balances greater than 10% of total accounts receivable as of June 30, 2016 and December 31, 2015.

No dealer or distributor accounted for more than 10% of total revenue for the three and six months ended June 30, 2016 and 2015.

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The Company relies on a limited number of suppliers for its contract manufacturing. A significant disruption in the operations 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.

## Geographic Information

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 and six months ended June 30, 2016 and 2015. The following table sets forth revenue from U.S., Canadian and all other international dealers and distributors combined (in thousands):

	Three Months Ended		Six Months Ended	
	June 30, 2016	2015	June 30, 2016	2015
Revenue-United States	\$ 37,461	\$ 30,054	\$ 68,836	\$ 51,271
Revenue-Canada	4,164	4,122	7,109	7,208
Revenue-all other international sources	11,590	10,465	20,305	18,245
Total revenue	\$ 53,215	\$ 44,641	\$ 96,250	\$ 76,724
International revenue (excluding Canada) as a percent of total revenue	22	% 23	% 21	% 24

## Use of Accounting Estimates

The preparation of financial statements in conformity with 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 years, with the exception of networking products that have a limited product warranty of three years. 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 number of installed systems, 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 (in thousands):

	Warranty Liability
Balance at December 31, 2015	\$ 1,415
Warranty costs accrued	902
Warranty claims	(562)
Balance at June 30, 2016	\$ 1,755



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## Net Income (Loss) Per 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 per share. Potentially dilutive common shares result from the assumed exercise of outstanding stock options and settlement of restricted stock units.

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		Six Months Ended	
	June 30,	2015	June 30,	2015
	2016		2016	2015
Numerator:				
Net income (loss)	\$ 524	\$ 2,041	\$ 7,163	\$ (2,190)
Denominator:				
Weighted average common stock outstanding for basic net income (loss) per common share	23,162	24,309	23,248	24,326
Effect of dilutive securities—stock options and restricted stock units	768	987	710	—
Weighted average common shares and dilutive securities outstanding	23,930	25,296	23,958	24,326

In a net loss position, diluted net loss per share is computed using only the weighted-average number of common shares outstanding during the period, as any additional common shares would be anti-dilutive as they would decrease the loss per share. 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 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	Six Months
Months	Ended

	Ended			
	June 30,		June 30,	
	2016	2015	2016	2015
Options to purchase common stock	2,553	2,417	2,624	4,817
Restricted stock units	2	-	35	-
Total	2,555	2,417	2,659	4,817

#### Recent Accounting Pronouncements

In March 2016, the FASB issued ASU 2016-09, “Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting.” The amendments in this update simplify several aspects of the accounting for employee share-based payment transactions, including the accounting for income taxes, forfeitures and statutory tax withholding requirements, as well as classification in the statement of cash flows. ASU 2016-09 will be effective for the Company in fiscal year 2017, but early adoption is permitted. Any adjustments resulting from the adoption of this standard will be reflected as of the beginning of the fiscal year of adoption. The Company is currently evaluating the impact of this update on the consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, “Leases (Topic 842),” which supersedes the guidance in ASC 840, “Leases.” The purpose of the new standard is to improve transparency and comparability related to the accounting and reporting of leasing arrangements. The guidance will require balance sheet recognition for assets and liabilities associated with rights and obligations created by leases with terms greater than twelve months. The guidance is effective for fiscal years beginning after December 15, 2018, including interim periods within those years. Modified retrospective application is required. Early adoption is permitted. The Company is evaluating the impact of adopting this guidance.

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In July 2015, the FASB issued ASU 2015-11, “Inventory (Subtopic 330) – Simplifying the Measurement of Inventory.” This update requires that inventory within the scope of the guidance be measured at the lower of cost and net realizable value. Inventory measured using last-in, first-out (LIFO) and the retail inventory method (RIM) are not impacted by the new guidance. The guidance is effective in fiscal years beginning after December 15, 2016, including interim periods within those years. Prospective application is required. Early adoption is permitted as of the beginning of an interim or annual reporting period. The Company is evaluating the impact of adopting this guidance.

In May 2014, the FASB issued ASU 2014-09, “Revenue from Contracts with Customers (Topic 606),” which amends the guidance in ASC 605, “Revenue Recognition.” The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In August 2015, the FASB issued ASU 2015-14, deferring the effective date of this standard for one year, and is now effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. The deferred standard allows early adoption of the standard on the original effective date of December 15, 2016. The Company is still evaluating the impact of adopting this guidance, as well as whether the Company will apply the amendments retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of applying this update at the date of initial application.

## 2. Balance Sheet Components

Inventories consisted of the following (in thousands):

	June 30, 2016	December 31, 2015
Finished goods	\$ 29,731	\$ 16,982
Component parts	2,785	2,575
Work-in-process	259	298
	\$ 32,775	\$ 19,855

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

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	June 30, 2016	December 31, 2015
Computer equipment and software	\$ 5,254	\$ 4,799
Manufacturing tooling and test equipment	4,678	4,267
Lab and warehouse equipment	3,673	3,376
Leasehold improvements	2,946	2,949
Furniture and fixtures	2,879	2,881
Marketing equipment	748	752
	20,178	19,024
Less: accumulated depreciation	(13,614)	(12,440)
	\$ 6,564	\$ 6,584

Other assets consisted of the following (in thousands):

	June 30, 2016	December 31, 2015
Deposits	\$ 664	\$ 933
Prepaid licensing	594	664
Deferred tax asset	817	—
Other	22	53
	\$ 2,097	\$ 1,650

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Accrued liabilities consisted of the following (in thousands):

	June 30, 2016	December 31, 2015
Sales returns and warranty accruals	\$ 3,125	\$ 2,508
Compensation accruals	3,121	2,331
Other accrued liabilities	1,487	1,041
	\$ 7,733	\$ 5,880

### 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.

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 and six months ended June 30, 2016 and 2015, 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 June 30, 2016 and December 31, 2015 (in thousands):

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	June 30, 2016						
	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value	Cash and Cash Equivalents	Short-term Investments	Long-term Investments
Cash	\$ 11,653	\$ —	\$ —	\$ 11,653	\$ 11,653	\$ —	\$ —
Level 1:							
Money market funds	10,156	—	—	10,156	10,156	—	—
U.S. government notes	999	1	—	1,000	—	1,000	—
Subtotal	11,155	1	—	11,156	10,156	1,000	—
Level 2:							
Asset-backed securities	5,007	3	—	5,010	—	—	5,010
Corporate bonds	17,777	5	—	17,782	—	17,782	—
Commercial paper	1,995	—	—	1,995	998	997	—
U.S. agency securities	1,001	—	—	1,001	—	1,001	—
Subtotal	25,780	8	—	25,788	998	19,780	5,010
Total	\$ 48,588	\$ 9	\$ —	\$ 48,597	\$ 22,807	\$ 20,780	\$ 5,010

	December 31, 2015						
	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value	Cash and Cash Equivalents	Short-term Investments	Long-term Investments
Cash	\$ 7,593	\$ —	\$ —	\$ 7,593	\$ 7,593	\$ —	\$ —
Level 1:							
Money market funds	21,937	—	—	21,937	21,937	—	—
U.S. government notes	998	—	(2)	996	—	—	996
Subtotal	22,935	—	(2)	22,933	21,937	—	996
Level 2:							
Asset-backed securities	6,739	—	(9)	6,730	—	—	6,730
Corporate bonds	39,195	2	(51)	39,146	—	33,156	5,990

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Commercial paper	1,100	—	—	1,100	—	1,100	—
U.S. agency securities	3,506	—	(1)	3,505	—	3,505	—
Subtotal	50,540	2	(61)	50,481	—	37,761	12,720
Total	\$ 81,068	\$ 2	\$ (63)	\$ 81,007	\$ 29,530	\$ 37,761	\$ 13,716

As of June 30, 2016, 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 and six months ended June 30, 2016 and 2015, the Company did not recognize any significant impairment charges. The Company typically invests in highly-rated securities, and its investment policy generally limits the amount of credit exposure to any one issuer. The policy requires investments generally 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.



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## Fair Value of Other Financial Instruments

The carrying amounts reported in the accompanying consolidated financial statements for cash and cash equivalents, restricted cash, accounts payable and accrued liabilities approximate their fair value because of the short term nature of the accounts. The fair value of the notes payable and the revolving credit facility approximates the carrying value based on the variable nature of interest rates and current market rates available to the Company (see Note 6). As a result, the balance of the notes payable and revolving credit facility is categorized within the Level 2 fair value hierarchy.

## Derivative Financial Instruments

The Company has foreign currency exposure related to the operations in the United Kingdom, Canada, Australia, 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 Statements of Operations as Other income (expense), net.

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 June 30, 2016.

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

	Income Statement Location	Three Months		Six Months	
		Ended June 30, 2016	2015	Ended June 30, 2016	2015
Foreign exchange contracts	Other income (expense), net	\$ 359	\$ (100)	\$ 43	\$ (100)

## 4. Acquisitions

#### Australia Expansion

On April 1, 2016, the Company began working directly with home automation integrators in Australia in order to capitalize on the growth of the smart home category in that country. As part of the shift from its distribution model in Australia, Control4 Corporation, through its wholly owned subsidiary, Control4 Australia Holdings Pty., Ltd, acquired customer lists and inventory from the Company's Australian distributor for \$0.7 million. Total consideration transferred for this acquisition was allocated to tangible and identifiable intangible assets acquired and liabilities assumed.

The Company determined this acquisition was not a significant acquisition under Rule 3-05 of Regulation S-X.

#### Acquisition of Pakedge Device and Software Inc.

On January 29, 2016, the Company entered into a Stock Purchase Agreement (the "Purchase Agreement") with Pakedge Device and Software Inc. ("Pakedge"). In accordance with the terms and conditions of the Purchase Agreement, Control4 agreed to acquire all of the outstanding shares of common stock of Pakedge for a price of \$32.0 million. After customary working capital adjustments, the total purchase price was \$33.0 million, which included cash acquired of \$0.8 million. In accordance with the Purchase Agreement, \$5.0 million was deposited in escrow, and 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.

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Total consideration transferred for the Pakedge acquisition was allocated to tangible and identifiable intangible assets acquired and liabilities assumed, including an allocation of \$0.3 million to a contingent liability for potential costs associated with regulatory compliance issues, based on their fair values at the acquisition date as set forth below. Management estimated the fair values of tangible and intangible assets and liabilities in accordance with the applicable accounting guidance for business combinations. The preliminary amount of consideration transferred is subject to potential adjustments in the event that the preliminary estimates of inventory, warranty reserves, sales return liability, contingent liability, 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). Due to new information obtained related to the net working capital adjustments, valuation of inventory, and tax liabilities, based on facts that existed at the acquisition date, the Company recorded measurement period adjustments to inventory, goodwill and deferred tax liability. The net change to goodwill was an increase of \$16,000. Had these adjustments been recorded as of the acquisition date, the Company's deferred tax benefit would have decreased \$0.1 million for the three months ended March 31, 2016.

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

	Pakedge Acquisition
Cash	\$ 843
Accounts receivable	460
Inventory	5,674
Other assets acquired	1,139
Intangible assets	23,156
Goodwill	13,535
Total assets acquired	44,807
Deferred tax liability	9,708
Warranty liability	391
Other liabilities assumed	1,688
Total net assets acquired	\$ 33,020

## Identifiable Intangible Assets

The Company acquired intangible assets that consisted of customer relationships, trademarks/trade names, developed technology and non-compete agreements, which had estimated fair values of \$8.8 million, \$4.4 million, \$9.7 million and \$0.3 million, respectively. The intangible assets were measured at fair value reflecting the highest and best use of nonfinancial assets in combination with other assets and liabilities using an income approach that discounts expected future cash flows to present value. The estimated net cash flows were discounted using discount rates between 15%

and 17%, based on the estimated internal rate of return for the acquisition and represent the rates that market participants might use to value the intangible assets based on the risk profile of the asset. The projected cash flows were determined using key assumptions such as: estimates of revenues and operating profits; capital expense investments; and the life of the product. The Company will amortize the intangible assets on a straight-line basis over their estimated useful lives of 8 years for the customer relationships, 12 years for the trademark/trade name, 5 years for the developed technology, and 2 years for non-compete agreements. The amortization of these intangible assets is not deductible for income tax purposes.

#### Goodwill

Goodwill of \$13.5 million represents the excess of consideration transferred over the fair value of assets acquired and liabilities assumed and is attributable to Pakedge's assembled workforce, strategic positioning value and the projected profits from new products and dealers. This goodwill is not deductible for income tax purposes.

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## Other

From the date of acquisition through June 30, 2016, the Company recorded revenue and net losses associated with Pakedge of approximately \$9.0 million and \$0.5 million, respectively. Additionally, the Company incurred approximately \$2.1 million in total acquisition-related costs accounted for in the accompanying condensed consolidated statements of operations as cost of revenue and general and administrative expenses for the six months ended June 30, 2016 related solely to the Pakedge acquisition. Of this amount, approximately \$1.5 million is related to the step-up in inventory recorded to cost of revenue as the acquired inventory was sold.

## Pro Forma Information

The unaudited pro forma information for the three and six months ended June 30, 2016 and 2015 presented below includes the effects of the Pakedge acquisition as if it had been consummated as of January 1, 2015, 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, depreciation expense, interest expense and estimated tax benefits. These adjustments are based upon information and assumptions available to us at the time of filing this Quarterly Report on Form 10-Q. The income tax benefit related to the reduction in the Company's valuation allowance as a result of the acquisition is excluded from the pro forma information as it is non-recurring. The unaudited pro forma information does not reflect any operating efficiency or potential cost savings that could result from the consolidation of Pakedge. Accordingly, the unaudited pro forma information is presented for informational purposes only and is not necessarily indicative of what the actual results of the combined company would have been if the acquisition had occurred at the beginning of the period presented, nor is it indicative of the future results of operations.

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2016	2015	2016	2015
Revenue	\$ 53,215	\$ 49,357	\$ 97,434	\$ 85,553
Income (loss) from operations	803	1,253	(4,279)	(3,983)
Net income (loss)	\$ 675	\$ 1,543	(4,300)	(3,220)
Net income (loss) per common share:				
Basic	\$ 0.03	\$ 0.07	(0.18)	(0.13)
Diluted	\$ 0.03	\$ 0.07	(0.18)	(0.13)

Acquisition of Nexus Technologies Pty Ltd.

On January 30, 2015, the Company, through its wholly owned subsidiary, Control4 Australia Pty., Ltd (“Control4 Australia”), completed the acquisition of Nexus Technologies Pty Ltd. (“Nexus”), an Australia-based provider of audio/video distribution products (under the brand of Leaf), pursuant to a Share Sale Agreement dated January 30, 2015, by and among Control4 Australia and all of the shareholders of Nexus, under which Control4 Australia purchased all of the issued and outstanding shares of Nexus from its shareholders, and Nexus became a wholly owned subsidiary of Control4 Australia. The total consideration transferred was \$8.5 million in cash. Of the cash consideration, \$0.8 million of cash was deposited in escrow as partial security for the indemnification obligations of the Nexus shareholders pursuant to the Share Sale Agreement, which was released to the Nexus shareholders on December 18, 2015. The Company incurred \$0.9 million in acquisition-related expenses accounted for in the accompanying condensed consolidated statements of operations as general and administrative expenses and cost of revenue for the six months ended June 30, 2015. Of this amount, approximately \$0.3 million is related to the step-up in inventory recorded to cost of revenue as the acquired inventory was sold.

The Company determined the Nexus acquisition was not a significant acquisition under Rule 3-05 of Regulation S-X.

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## 5. Goodwill and Intangible Assets

## Goodwill

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

	Amount
Balance at December 31, 2015	\$ 2,760
Current period acquisitions	13,814
Foreign currency translation adjustment	41
Balance at June 30, 2016	\$ 16,615

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

## Amortizable Intangible Assets

The Company's intangible assets and related accumulated amortization consisted of the following as of June 30, 2016 and December 31, 2015 (in thousands):

	June 30, 2016		
	Gross Carrying Amount	Accumulated Amortization	Net
Developed technology	\$ 16,668	\$ (4,123)	\$ 12,545
Customer relationships	9,208	(571)	8,637
Trademark/trade name	4,410	(153)	4,257
Non-competition agreements	295	(101)	194
Total intangible assets	\$ 30,581	\$ (4,948)	\$ 25,633

	December 31, 2015		
	Gross Carrying	Accumulated	Net
	Amount	Amortization	
Developed technology	\$ 6,907	\$ (2,643)	\$ 4,264
Customer relationships	342	(66)	276
Non-competition agreements	53	(46)	7
Total intangible assets	\$ 7,302	\$ (2,755)	\$ 4,547

The weighted average amortization period for acquired technology, customer relationships, trademarks/trade names and non-competition agreements is 4.9 years, 7.9 years, 12.0 years, and 2.0 years, respectively; and 6.8 years for all amortizable intangible assets in total.

The Company recorded amortization expense during the respective periods for these intangible assets as follows (in thousands):

	Three Months		Six Months	
	Ended	Ended	Ended	Ended
	June 30,	June 30,	June 30,	June 30,
	2016	2015	2016	2015
Amortization of intangible assets	\$ 1,238	\$ 403	\$ 2,172	\$ 728



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Amortization of finite lived intangible assets as of June 30, 2016 for the next five years is as follows (in thousands):

	Amount
2016	\$ 2,416
2017	4,712
2018	4,508
2019	4,348
2020	3,484
Thereafter	6,165
	\$ 25,633

## 6. Long-Term Obligations

### Loan and Security Agreement

On January 29, 2016, Control4 entered into the Second Loan Modification Agreement (the “2016 Loan Amendment”) with Silicon Valley Bank, a California corporation (“SVB”), which amends that certain Amended and Restated Loan and Security Agreement dated as of June 17, 2013, between Control4 and SVB (the “2013 Loan Agreement”).

In the 2016 Loan Amendment, Control4 established a revolving credit facility of \$30.0 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 28, 2018. Advances made pursuant to the New Credit Facility are either: (i) Prime Rate Advances, which bear interest at the Prime Rate plus a Prime Rate Margin of either 0% or 0.25%, depending on Control4’s leverage ratio for the subject quarter, or (ii) LIBOR Rate Advances, which bear interest at the LIBOR Rate plus a LIBOR Rate Margin of either 2.50% or 2.75%, depending on Control4’s leverage ratio for the subject quarter. As of June 30, 2016, the interest rate on the revolving credit facility equaled the prime rate of 3.50%, and Control4 had outstanding borrowings of \$5.0 million under the revolving credit facility.

The 2016 Loan Amendment did not amend the term borrowing provisions of the 2013 Loan Agreement. Term borrowings are payable in 42 equal monthly payments of principal plus interest and bear interest at prime plus 0.50%,

which was 4.00% as of June 30, 2016.

The 2016 Loan Amendment contains various restrictive and financial covenants and the Company was in compliance with each of these covenants as of June 30, 2016.

## 7. Income Taxes

In order to determine the quarterly provision for income taxes, the Company considers the estimated annual effective tax rate, which is based on expected annual taxable income and statutory tax rates in the various jurisdictions in which the Company operates. Certain significant or unusual items are separately recognized in the quarter during which they occur and can be a source of variability in the effective tax rates from quarter to quarter.

Income tax expense was \$0.2 million and \$0.2 million for the three months ended June 30, 2016 and 2015, respectively, or approximately 24% and 8% of income (loss) before income taxes, respectively. Income tax benefit was \$9.9 million and \$0.4 million for the six months ended June 30, 2016 and 2015, respectively, or approximately 362% and 14% of income (loss) before income taxes, respectively. The effective tax rate for the three and six months ended June 30, 2016 differs from the U.S. federal statutory rate of 34% primarily due to the domestic valuation allowance offsetting most of the statutory rate, offset by the partial reversal of the Company's valuation allowance due to the deferred tax liability that was recorded as part of the Pakedge acquisition, primarily due the differences between the book and tax basis of the acquired intangible assets. The rate is further increased by foreign income taxes, minimum state income taxes or taxes in states for which net operating loss carryforwards are not

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available, the U.S. federal alternative minimum tax and the impact of incentive stock options as well as other permanent differences. As of December 31, 2015, the Company's net operating loss ("NOL") carryforward amounts for U.S. federal income and state tax purposes were \$78.1 million and \$75.9 million, respectively. The NOL carryforwards will expire between 2019 and 2035. In addition to the NOL carryforwards, as of December 31, 2015, the Company had U.S. federal and state research and development credit carryforwards of \$6.7 million and \$2.8 million, respectively, which will expire between 2017 and 2034.

Significant judgment is required in determining the Company's provision for income taxes, recording valuation allowances against deferred tax assets and evaluating the Company's uncertain tax positions. In evaluating the ability to recover its deferred tax assets, in full or in part, the Company considers all available positive and negative evidence, including past operating results, forecast of future market growth, forecasted earnings, future taxable income and prudent and feasible tax planning strategies. Due to historical net losses incurred and the uncertainty of realizing the deferred tax assets, for all the periods presented, the Company has a full valuation allowance against domestic deferred tax assets. To the extent that the Company generates positive income and expects, with reasonable certainty, to continue to generate positive domestic income, the Company may release all or a portion of the valuation allowance in a future period. This release would result in the recognition of certain deferred tax assets, resulting in a decrease to income tax expense for the period such release is made. In addition, the effective tax rate in subsequent periods would increase, and more closely approximate the federal statutory rate of 34%, after giving consideration to state income taxes, foreign income taxes and the effect of exercising incentive stock options.

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 the United Kingdom, Australia, China, Germany, India and Serbia. The Company is subject to examination in the United States, the United Kingdom, Australia, Hong Kong, China, Germany, India and Serbia as well as various state jurisdictions. As of June 30, 2016, the Company was not under examination by any tax authorities. Tax years beginning in 2012 are subject to examination by tax authorities in the United States and in some states tax years as early as 2011 are subject to examination by tax authorities, although net operating loss and credit carryforwards from all years are subject to examinations and adjustments for at least three years following the year in which the attributes are used. Tax years beginning in 2011 are subject to examination by the taxing authorities in Australia and Hong Kong. Tax years beginning in 2012 are subject to examination by the taxing authorities in China and India. Tax years beginning in 2013 are subject to examination by the taxing authorities in the United Kingdom. Tax years beginning in 2015 are subject to examination by the taxing authorities in Germany. Tax years beginning in 2016 are subject to examination by the taxing authorities in Serbia.

## 8. 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 and restricted stock.

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 subsequent to 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. There was no annual increase to the Company's reserved shares in 2016.

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A summary of stock option activity for the six months ended June 30, 2016 is presented below:

	Shares Subject to Options Outstanding	Weighted Average Grant Date Fair Value	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)
Balance at December 31, 2015	4,572,672		\$ 10.72	
Granted	50,000	4.63	8.16	
Exercised	(163,071)		4.36	
Expired	(49,001)		13.38	
Forfeited	(42,701)		16.02	
Balance at June 30, 2016	4,367,899		10.85	
Exercisable options at June 30, 2016	3,317,629		9.54	5.2
Vested and expected to vest at June 30, 2016	3,316,345		10.79	5.8

The following table summarizes information about stock options outstanding and exercisable at June 30, 2016:

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)	
\$ 2.34 - 3.59	2.78	206,448	0.6	206,448	0.6	
\$ 4.78 - 7.28	5.90	1,499,698	4.3	1,477,314	4.2	
\$ 7.49 - 11.28	9.69	1,109,401	6.1	836,360	5.5	
\$ 11.72 - 17.66	14.75	867,106	8.4	382,475	8.3	
\$ 19.56 - 22.92	21.04	685,246	7.4	415,032	7.2	
		4,367,899		3,317,629		

For the stock option awards vested during the three and six months ended June 30, 2016, the total fair value was \$1.4 million and \$2.9 million, respectively. The following table summarizes the aggregate intrinsic-value of options exercised, exercisable and vested and expected to vest (in thousands):

	For the Six Months Ended and as of June 30,	
	2016	2015
Options Exercised	\$ 585	\$ 1,039
Options Exercisable	4,553	6,991
Options Vested and Expected to Vest	4,574	7,266

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The fair value of each option award was estimated on the date of grant using the Black-Scholes option-pricing model with the following assumptions:

	Three Months Ended		Six Months Ended	
	June 30, 2016	2015	June 30, 2016	2015
Expected volatility	62 %	53 %	62 %	53 - 55 %
Expected dividends	0 %	0 %	0 %	0 %
Expected terms (in years)	6.1	5.3 - 6.1	6.1	5.3 - 6.1
Risk-free rate	1.1 %	1.5 - 1.8 %	1.1 %	1.3 - 1.8 %

## Restricted stock units

A summary of restricted stock unit activity for the six months ended June 30, 2016 is presented below:

	Number of Shares	Weighted Average Grant Date Fair Value
Non-vested balance at December 31, 2015	425,000	\$ 8.18
Awarded	1,139,846	7.37
Forfeited	(50,000)	7.32
Non-vested balance at June 30, 2016	1,514,846	7.60

There were no restricted stock units that vested during the six months ended June 30, 2016.

## 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		Six Months Ended	
	Ended		June 30,	
	June 30,	2015	2016	2015
Cost of revenue	\$ 47	\$ 39	\$ 90	\$ 86
Research and development	890	667	1,704	1,439
Sales and marketing	600	387	1,109	841
General and administrative	590	586	1,047	1,162
Total stock-based compensation expense	\$ 2,127	\$ 1,679	\$ 3,950	\$ 3,528

At June 30, 2016, there was \$8.9 million of total unrecognized compensation cost related to non-vested stock option awards that will be recognized over a weighted-average period of 2.1 years. At June 30, 2016, there was \$9.7 million of total unrecognized compensation cost related to non-vested restricted stock units that will be recognized over a weighted-average period of 2.6 years.



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9. Share Repurchases

In May 2015, the Company's Board of Directors authorized the repurchase of up to \$20 million in Control4 common stock from time to time on the open market. In February 2016, the Board of Directors authorized an extension to this repurchase program from its original end-date of May 13, 2016 to June 30, 2017, unless terminated earlier. During the three and six months ended June 30, 2016, the Company repurchased 193,831 and 427,646 shares for \$1.5 million and \$3.2 million, respectively. These share repurchases are classified as treasury stock in the accompanying Condensed Consolidated Balance Sheets as a reduction of Stockholders' Equity. As of June 30, 2016, the Company has \$7.7 million remaining to repurchase shares of common stock under this share repurchase program.

10. Related Party Transactions

A member of the Company's Board of Directors is also an officer of a company that has a product line the Company began selling in its online store in November 2015. For the three and six months ended June 30, 2016, Control4 recognized revenue from sales of this product line of \$34,000 and \$63,000, net of cost of revenue, consistent with the Company's accounting policy on sales of third-party products sold through the Company's online ordering system. As of June 30, 2016, the Company had accounts payable due to this related party of \$19,000.

The Company has a royalty agreement with a company that has a director who is also a member of the Company's Board of Directors. For the three and six months ended June 30, 2016, the Company had incurred royalty expenses of \$0.1 million and \$0.2 million and had accounts payable due to this related party of \$0.1 million.

11. Commitments and Contingencies

Operating Leases

The Company leases office and warehouse space under operating leases that expire between 2017 and 2021. The terms of the leases include periods of free rent, options for the Company to extend the leases (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 and has accrued for rental expense recorded but not paid.

Rental expense was approximately \$0.6 million and \$0.5 million for the three months ended June 30, 2016 and 2015, respectively, and \$1.2 million and \$0.9 million for the six months ended June 30, 2016 and 2015, respectively.

Future minimum rental payments required under non-cancelable operating leases with initial or remaining terms in excess of one year consist of the following as of June 30, 2016 (in thousands):

2016	\$ 1,520
2017	3,121
2018	2,086
2019	594
2020	191
Thereafter	32
	\$ 7,544

#### Purchase Commitments

The Company had non-cancellable purchase commitments for the purchase of inventory, which extend through February 2017 totaling approximately \$33.5 million at June 30, 2016.

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Indemnification

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 is unable to reasonably estimate the maximum amount that could be payable under these arrangements since these obligations are not capped but are conditional to the unique facts and circumstances involved. Accordingly, the Company has no liabilities recorded for these agreements as of June 30, 2016, as there were no outstanding claims.

Legal Matters

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.

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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, 2015, which was filed with the U.S. Securities and Exchange Commission (the "SEC") on February 16, 2016, 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 accretive effect of any acquisitions; 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 adding employees; 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," "exp," "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 on Form 10-Q, 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 on Form 10-Q 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 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 2016 to 2015.
- **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 June 30, 2016, including 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

Control4 is a leading provider of smart home and business solutions that are designed to personalize and enhance how you 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 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 products, cloud services and user-interface products 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, regional and national retailers and distributors. These dealers, retailers and distributors 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 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, retailers and distributors 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. 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 attributable to large projects and will continue to be uneven from period to period. During the six months ended June 30, 2016, over 3,700 active direct dealers were authorized to sell and install the full Control4 line of products in the United States, Canada, the United Kingdom and 50 other countries, and we partnered with 27 distributors to cover an additional 40 countries where we do not have direct dealer relationships. These distributors sell our solutions through dealers and provide warehousing, training, technical support, billing and service for dealers in each of those countries. We also have an additional 1,100 dealers and 17 distributors that are currently authorized to sell our Pakedge line of products only.

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. We also generate revenue from the sale of annual subscriptions to our 4Sight subscription service, which allows consumers to remotely access, backup, and control their smart home solutions from their mobile devices, as well as receive e-mail and “push notification” alerts regarding activities in their home. 4Sight also allows dealers to perform remote diagnostic and programming 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,				
	2015	2014	2013	2012	2011
Core revenue	\$ 160.7	\$ 144.7	\$ 126.4	\$ 105.6	\$ 88.3
Core revenue growth over prior year	11 %	14 %	20 %	20 %	25 %
Other revenue	\$ 2.5	\$ 4.1	\$ 2.1	\$ 3.9	\$ 5.1
Other revenue changes over prior year	-39 %	95 %	-46 %	-24 %	28 %
Total revenue	\$ 163.2	\$ 148.8	\$ 128.5	\$ 109.5	\$ 93.4
Total revenue growth over prior year	10 %	16 %	17 %	17 %	25 %

Over the past five years, we have experienced double-digit annual Core revenue growth. Our Core revenue growth during that period has been the result of a combination of both the net addition of new independent dealers and distributors to our sales channels, an increase in revenue from our existing network of independent dealers and distributors, and new products both 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 and gross margins by providing enhanced dealer installation and marketing tools. In terms of organic growth, we recently:

- Rolled out a new line of entertainment and automation controllers, the EA Series, featuring high-resolution audio, high-performance automation, and our broad interoperability, in January 2016. With three separate models, the Control4 EA Series is designed and priced to deliver exceptional automation power, reliability, and high-impact entertainment experiences for projects ranging from a single-room to an entire home or estate;
- Announced and began selling a new line of intelligent Square Wireless Lighting products, expanding custom and retrofit lighting opportunities for our dealers in Europe and Asia;
- Announced a new agreement with GreenSky to offer end-user financing to our U.S. dealer network of over 2,700 businesses; and
- Released Control4 OS 2.8, providing an enhanced user experience for our security and media solutions, including native streaming of Pandora, Deezer and TIDAL music services and iOS compatibility with the Apple Watch.

While our historical revenue growth has been primarily organic, we have completed several acquisitions since our IPO that we believe enhanced our product offerings and positioned us for continued growth in the future. Recent acquisitions of technology and distribution-related business are as follows:

- In April 2016, we transitioned from a two-tier distribution model to direct-to-dealer in Australia, and as part of this process, acquired customer lists and inventory of the former distributor;
- In January 2016, we acquired Pakedge, a developer and manufacturer of networking products, power distribution and management solutions, as well as cloud network-managed services for both wireless and wired networking solutions in the connected home and business. Pakedge's portfolio includes the Connect+ Platform, with wired products such as switches and routers, wireless products such as access points, as well as power management and cloud based network management technologies. Pakedge brings to Control4 deep networking expertise, innovative technologies, and a sophisticated suite of newly refreshed networking products and rich software capability; and





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In January 2015, we acquired Nexus, a developer and manufacturer of the Leaf brand of custom audio/video distribution and switching systems. We previously sold certain Leaf products under our Control4 brand and through our online ordering platform. After this acquisition, we began offering a complete line of video distribution solutions under the Control4 brand to Control4 customers worldwide, we gained market share in the growing audio and video (A/V) category, and we leveraged Nexus's valuable engineering expertise to develop new and innovative A/V solutions.

We plan to continue to identify, acquire and integrate strategic technologies, assets and businesses that we believe will enhance the overall strength of our business, allow us to streamline sales, technical support and training, and enhance our dealers' ability to grow their businesses.

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 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. Voice services is a recent example of emerging technology in our connected world. We remain committed to embracing these emerging technologies through our open platform and broad ecosystem.

Our open platform makes it easy for a broad community of original equipment manufacturer (OEM) partners to participate in our smart home ecosystem, which currently includes over 9,700 drivers and more than 1,500 SDDP-enabled products. Our broad ecosystem, which includes audio, video, lighting, temperature, network, security and communication device categories, gives consumers flexibility to integrate nearly any connectable device they have 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, our builder programs continue to gain traction. We continue to engage builders to introduce entry- to mid-level Control4 systems as a standard feature in new home projects. We 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 ability to strengthen and expand our dealer and distributor network, our ability to expand internationally, and our ability to meet competitive challenges. While each of these areas presents significant opportunities for us, they also pose important challenges that we must successfully address in order 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, such as Pakedge and Nexus.
- Increasing Our Brand Awareness. We are committed to growing awareness of the Control4 and Pakedge brands among our dealers, distributors and end consumers. We believe that our investments in creating brand awareness have contributed to our revenue growth and increasing adoption of our smart home solutions. We are proud of the numerous awards we received from various industry groups and dealer consortiums, formally recognizing our commitment to excellence. In June 2016, Control4 was named as the top Whole-Home Automation brand, and Pakedge was named the top networking brand, by the “2016 CE Pro 100 Brand Analysis” report. This is the second year in a row that Control4 was recognized as the top Whole-Home Automation brand, and the fourth year in a row that Pakedge has been named the top brand for home networking. In addition, Control4 solutions were recognized as the top brand in the categories of whole-house Audio/Video, access control, and HVAC/thermostats; and among the leading brands in the categories of lighting control, remote controls, and communications (phones/intercoms). Also, in May 2016, the ProSource Buying Group named Control4 the 2016 Custom Integration Vendor of the Year. In September 2015, Control4 was named the “2015 Custom Integration Vendor of the Year” by the Home Technology Specialists of America (HTSA) Buying Group. Continuing to enhance our brand is a meaningful factor in our plans for the future.
- Accelerating and Enhancing Lead Generation. We determined that there is an opportunity for us to play a more active role in generating and following up on leads received from our marketing efforts. Therefore, we created a small team of inside sales representatives to qualify inbound inquiries and direct them to qualified independent dealers. Our enhanced lead generation strategies have increased consultations, bids and project installations, as well as increased the number of leads we are able to pass on to our dealers.
- 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. In addition, through our acquisition of Pakedge, we increased the size of our total independent dealer network from over 3,700 active dealers to over 4,800 dealers. We intend to encourage all appropriately qualified dealers to explore both home control and networking product lines, and we plan 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 our brand awareness internationally. We continue to add field sales and service personnel to assist in the optimization of our international channels. We have transitioned to a dealer-direct model in specific international regions, namely in the United Kingdom, China, India, Germany and Australia, 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 Savant, Crestron and Elan, a number of large technology companies such as Apple, Google, Amazon and Samsung offer device control capabilities among some of their own products, applications and services, and are engaged in ongoing development efforts to address the broader home automation market. In addition, managed service companies such as Alarm.com, Comcast Xfinity 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.

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· Impact of the United Kingdom’s Vote to Leave the European Union. On June 23, 2016, the United Kingdom (“UK”) voted to leave (“Brexit”) the European Union (“EU”) raising concerns of a potential slowdown in the UK’s economy specifically and the EU in general. We have engaged with our dealers in the UK to assess their perception of how the Brexit vote might impact their business in the near and long-term. Their responses are varied and reflect the uncertainty that currently exists in the market. We will continue to monitor the risks and uncertainties throughout what is expected to be a lengthy process. The Brexit vote had the immediate impact of devaluing the pound sterling relative to the euro and the U.S. dollar. We generally sell our products and incur expense in local currencies including the pound sterling and the euro, but incur exchange rate gains and losses for U.S. dollar denominated assets and liabilities including intercompany and third-party accounts receivables and payables. We enter into forward contracts to help offset our exposure to movements in foreign currency exchange rates relative to these types of U.S. dollar denominated balances. When consolidating the revenue and expenses of our foreign subsidiaries, we translate local currencies to the U.S. dollar using average exchange rates during the period, resulting in either higher or lower net income depending on changes in the relative value of foreign currencies to the U.S. dollar. We do not believe that Brexit will have a material impact on our net income as generated by our subsidiary in the UK in the short-term.

### Acquisition of Pakedge

In January 2016, we acquired Pakedge, a developer and manufacturer of networking products, power distribution and management solutions, as well as cloud network-managed services for both wireless and wired networking solutions in the connected home and business. Like Control4, Pakedge conducts its business through a broad channel of approximately 1,700 independent dealers, of which, only one-third were certified dealers of the entire Control4 product line. We expect to grow Pakedge product sales through our network of more than 3,700 active Control4 dealers, and expand our combined business through the additional 1,100 Pakedge dealers. From the date of acquisition in January 2016 through July 2016, over 800 new Control4 dealers have started purchasing and begun selling Pakedge networking products, generating revenue of approximately \$2.6 million.

We will continue to support the Pakedge product line for all Pakedge dealers, whether or not they become Control4 certified. We intend to grow both the Pakedge product business and the Control4 product business through our combined dealer channel of over 4,800 total active dealers. We encourage all appropriately qualified dealers to explore both product lines, and we plan to actively cross-train and cross-certify dealers in accordance with our existing standards of technical proficiency and business practices. We believe Pakedge provides a significant boost to our development capabilities, our solution portfolio, and business flexibility moving forward. For 2016, we believe Pakedge will be accretive to our growth rate and gross margin, while contributing positively to our net income for the year; however, no assurance of such accretive effect can be given.

### 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 June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Authorized dealers at the beginning of the period	2,818	2,672	2,787	2,676
Additions	84	90	183	174
Terminations	(37)	(58)	(105)	(146)
Authorized dealers at the end of the period	2,865	2,704	2,865	2,704
Number of active dealers(2)	2,820	2,667	2,820	2,667
% of active dealers(2)	98 %	99 %	98 %	99 %

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## International Direct Dealers(1)

	Three Months		Six Months	
	Ended		Ended	
	June 30,		June 30,	
	2016	2015	2016	2015
Authorized dealers at the beginning of the period	933	836	901	787
Additions(3)	143	53	187	117
Terminations	(45)	(11)	(57)	(26)
Authorized dealers at the end of the period(3)	1,031	878	1,031	878
Number of active dealers(2)	972	754	972	754
% of active dealers(2)	94	% 86	% 94	% 86

	Three Months		Six Months	
	Ended		Ended	
	June 30,		June 30,	
	2016	2015	2016	2015
Number of controllers sold	24,520	20,908	48,653	34,839
Core revenue growth	18	% 23	% 24	% 13
International core revenue as a percentage of total revenue	21	% 22	% 20	% 22

- (1) These dealer figures only include dealers authorized to sell and install the full Control4 line of products and exclude the dealers that are currently authorized to sell only the Pakedge line of products, which as of June 30, 2016 totals approximately 1,100.
- (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 and six months ended June 30, 2016, include 100 dealers that were acquired as part of the direct-to-dealer transition in Australia.

## 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 the Custom Electronics Design and Installation Association (“CEDIA”), we believe there is an opportunity to broaden relationships with dealers outside of CEDIA, including non-traditional A/V dealers, electrical contractors, and security system installers.

We continue to invest in tools and technologies to help our dealers be more successful and increase the year-over-year sales of our products. Our goal is to continuously increase our dealers' productivity and capacity to grow. Enabling our dealers to increase productivity will ultimately drive our revenue growth.

As part of our normal process for developing a productive, capable dealer network, we regularly review individual dealer performance and as necessary, terminate dealer agreements where volume, technical training and performance requirements are not being fulfilled. As a result, there are times when the number of dealer terminations exceed the number of new dealer additions in North America. We view this as a healthy part of growing our customer install direct dealer channel worldwide. We continue to add new dealers, expanding both our North America and international direct dealer networks.

As a result of our traditional efforts to expand our channel, the number of active international dealers increased 29% between the six months ended June 30, 2016 and 2015, and we saw an increase of 6% in the number of active North American direct dealers during the same periods. Generally, the growth percentage internationally is higher because our presence in these markets is less mature and our base of dealers is much lower than the North American market. Much of this growth in our international dealer network is attributed to new dealer additions in China, India, Germany and Australia. In April 2016, we started selling direct-to-dealers in the Australian market. We plan to continue to monitor other markets that are currently served by a single distributor and, when we feel that

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those markets aren't growing to their potential, establish direct relationships with selected dealers in these regions, which we expect would further increase our number of direct international dealers.

We continue to support and grow the unique Pakedge dealers that only purchase networking solutions, of which there were approximately 1,100 as of June 30, 2016.

While we believe that we will continue to have significant international opportunities, it is difficult to anticipate the exact timing and amount of growth, particularly in new and emerging markets. Such challenges may cause our growth rate to be slower than anticipated, offsetting our efforts to expand into these emerging geographies. Divergent regional and local economic and political trends in Latin America, particularly relating to new home construction and strengthening of the U.S. dollar versus certain local currencies, and the recent vote in the UK to exit the European Union, are examples of challenges we must address in order to continue our international expansion. In response to a weakening Canadian dollar, starting in February 2016, we announced to our dealer network in Canada that we now offer the ability to order and pay for products in Canadian dollars versus U.S. dollars. We believe this offering will help to strengthen our long-term results in Canada while eliminating the margin and quoting uncertainty associated with volatility of foreign exchange rates for our dealers. While revenue in Canada during the three and six months ended June 30, 2016 is relatively flat year-over-year, we saw an increase of 41% in revenue in the three months ended June 30, 2016, compared to the same period ended March 31, 2016.

## 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 January 2016, we introduced a new line of entertainment and automation controllers, the EA Series. With three separate models, our EA Series is designed and priced for projects ranging from a single-room to an entire home or estate. As a result of the launch, we saw a significant increase in controller sales in the first quarter, both year-over-year and quarter-over-quarter. Although end customer adoption, sell-through, and overall revenue growth for the new controllers is strong, the increase in the first quarter was due in part to initial purchases by dealers for their showrooms.

During the three and six months ended June 30, 2016, we sold 24,520 and 48,653 controllers, respectively, compared to 20,908 and 34,839 controllers sold in the same period in 2015, respectively. Controller sales for the three and six



months ended June 30, 2016 increased 17% and 40% compared to the same periods in 2015.

#### 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.

#### 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, Germany, China, India, and Serbia. 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.

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## 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		Six Months Ended	
	June 30, 2016	2015	June 30, 2016	2015
	(in thousands)			
North America Core Revenue	\$ 40,846	\$ 34,280	\$ 74,785	\$ 58,670
International Core Revenue	11,013	9,792	19,470	17,167
Other Revenue	1,356	569	1,995	887
Total Revenue	\$ 53,215	\$ 44,641	\$ 96,250	\$ 76,724
North America Core Revenue as a % of Total Revenue	77	% 77	78	% 76
International Core Revenue as a % of Total Revenue	21	% 22	20	% 22

North America Core revenue increased \$6.6 million, or 19%, and \$16.1 million, or 27%, respectively, in the three and six months ended June 30, 2016, respectively, compared to the same period in 2015. International Core revenue increased \$1.2 million, or 12%, and \$2.3 million, or 13%, respectively, in the three and six months ended June 30, 2016, respectively.

The direct sale and fulfillment of networking products is new to our business as of January 29, 2016, when we acquired Pakedge. We generated revenue from the sale of our networking products of \$5.9 million and \$9.0 million during the three months ended June 30, 2016 and the period from January 29, 2016 to June 30, 2016, respectively, with no similar revenue in 2015. Approximately 87% of these sales are included in North America Core revenue.

Growth in North America excluding Pakedge was 5% and 14% for the three and six months ended June 30, 2016, respectively, compared to the same periods in 2015, and was driven in large part by the release of several new products including our EA Series controllers.

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, we believe that adverse international macro-economic conditions will continue to challenge and slow growth in certain geographies, including Canada and Latin America.

### 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 and associated promotional or volume incentive rebates offered to our independent dealers and distributors.

In addition, in conjunction with our acquisition of Pakedge and Nexus as well as the direct-to-dealer transition in Australia, we were required to record acquired inventory at fair value, as determined under ASC 805, Business Combinations, resulting in a step-up in the inventory value. Such step-up is recorded through cost of goods sold when the specific inventory is sold, resulting in a negative impact to our gross margin. Also, cost of goods sold includes ongoing, periodic amortization of the acquired technology.

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Gross margin for the three and six months ended June 30, 2016 and 2015 was as follows (in thousands, except percentages):

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2016	2015	2016	2015
Gross margin	\$ 26,027	\$ 22,329	\$ 46,513	\$ 37,940
Percentage of revenue	49 %	50 %	48 %	49 %

As a percentage of revenue, our gross margin decreased to 49% and 48%, respectively, in the three and six months ended June 30, 2016, from 50% and 49%, respectively, during the same period in 2015. The decrease in gross margin was due primarily to amortization of the technology acquired from Pakedge and Nexus, the step-up in basis of purchased inventory, and decreases in the selling price of our products in certain foreign markets due to the strengthening of the U.S. dollar relative to certain international currencies. These factors were offset by component and other product cost reductions as well as product mix and associated pricing.

The negative effect on gross margin percentage resulting from the step-up in purchased inventory carrying value was limited to the first and second quarters of 2015 as it relates to Nexus and is expected to have an impact on the first, second and third quarters of 2016 as it relates to Pakedge and the Australia direct-to-dealer transition, while the amortization of the acquired technology is expected to occur over the expected life of the acquired technology.

The introduction of new products, including the introduction of the EA Series of controllers in the first quarter of 2016, generally has a negative impact on gross margins as we offer discounted pricing to our dealers for demo units placed in their showrooms.

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

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

## 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.

Research and development expenses for the three and six months ended June 30, 2016 and 2015 were as follows (in thousands, except percentages):

	Three Months		Six Months Ended	
	Ended June 30, 2016	2015	June 30, 2016	2015
Research and development	\$ 9,039	\$ 8,122	\$ 17,518	\$ 16,117
Percentage of revenue	17 %	18 %	18 %	21 %

Research and development expenses increased \$0.9 million, or 11%, and \$1.4 million, or 9%, respectively, in the three and six months ended June 30, 2016, respectively, compared to the same periods in 2015. The net increase for the three and six-month period included approximately \$1.0 million and \$1.7 million, respectively, in expenses associated with our new networking products, offset by lower overall spending for our ongoing product development activities.

We expect our research and development expenses related to organic growth to remain relatively flat in absolute dollars for the foreseeable future as we continue to invest in the development of new solutions; however,

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we expect those expenses to fluctuate as a percentage of our revenue in future periods based on fluctuations in our revenue and the timing of those expenses.

## Sales and Marketing Expenses

Sales and marketing expenses consist primarily of compensation and related travel expenses for our sales 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 and six months ended June 30, 2016 and 2015 were as follows (in thousands, except percentages):

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2016	2015	2016	2015
Sales and marketing	\$ 11,114	\$ 7,812	\$ 21,249	\$ 15,179
Percentage of revenue	21 %	17 %	22 %	20 %

Sales and marketing expenses increased \$3.3 million, or 42%, and \$6.1 million, or 40%, respectively, in the three and six months ended June 30, 2016, respectively, compared to the same periods in 2015. The increase in absolute dollars for sales and marketing expenses for the three and six-month periods included \$1.3 million and \$2.4 million, respectively, in sales and marketing expenses associated with our new networking products as well as amortization of intangible assets related to the Pakedge acquisition. In addition, we increased our general marketing expenses \$0.8 million and \$1.5 million, respectively, to increase lead generation, transition to a direct-to-dealer model in Australia and Germany, grow our dealer and distributor networks throughout the world and deliver tools to the sales channel to support local marketing and sales lead generation.

We intend to continue to supplement our more traditional marketing programs with similar lead generation programs, including social media and pay-per-click advertising. In addition, we expect our sales and marketing expenses related to organic growth to increase slightly in absolute dollars as we continue to invest in marketing, including our consumer marketing, to increase awareness of our products and brand.

## 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. 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 and six months ended June 30, 2016 and 2015 were as follows (in thousands, except percentages):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
General and administrative	\$ 5,059	\$ 4,288	\$ 9,872	\$ 8,909
Percentage of revenue	10 %	10 %	10 %	12 %

General and administrative expenses increased \$0.8 million, or 18%, and \$1.0 million, or 11% in the three and six months ended June 30, 2016, respectively, compared to the same periods in 2015. The increase in absolute dollars is primarily due to increased personnel costs and other administrative costs associated with running our business, including \$0.3 million and \$0.5 million, respectively, in transition costs associated with the Pakedge integration for the three and six-month periods.

During the second quarter of 2016, we finalized a plan to restructure certain operations relating to the original Pakedge business. As a result, we anticipate paying approximately \$0.3 million in employee termination

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related expenses and during the three months ended June 30, 2016, recorded approximately \$0.2 million of these expenses as retention services were provided. In addition, we anticipate vacating one of our facilities in the San Francisco, California Bay Area. We are in the process of marketing the space and anticipate that we will record an estimated loss of approximately \$0.4 million associated with the sublease when we vacate the premises in August 2016.

We expect our general and administrative expenses related to organic growth to increase slightly in absolute dollars as a result of growth in the business. However, we also expect our general and administrative expenses to fluctuate as a percentage of our revenue in future periods based on fluctuations in our revenue and the timing of those expenses.

## Litigation Settlement Expenses

During the six months ended June 30, 2016, we recorded expenses of \$0.4 million to resolve certain legal matters.

## Other Income (Expense)

Other income (expense) consists primarily of foreign currency transaction gains (losses) and net interest income (expense). Other income (expense) for the three and six months ended June 30, 2016 and 2015 was as follows (in thousands, except percentages):

	Three Months		Six Months Ended	
	Ended June 30, 2016	2015	June 30, 2016	2015
Other income (expense)	\$ (122)	\$ 112	\$ (212)	\$ (277)
Percentage of revenue	0 %	0 %	0 %	0 %

In the second quarter of 2016, we recorded other expense of \$0.1 million compared to other income of \$0.1 million in the second quarter of 2015. Other expense decreased \$0.1 million in the six months ended June 30, 2016, compared to the same period in 2015. Other expense varies primarily as a result of net foreign currency gains (losses) generated on our U.S. dollar obligations that are carried in local currency by our foreign subsidiaries. This is due to the U.S. dollar fluctuating in value against the pound sterling, euro, and Australian dollar during the periods, causing those U.S. dollar obligations, primarily intercompany payable to the U.S. entity, to increase (decrease) in local currency resulting



in increased expense (income).

Beginning in the second quarter of 2015, we began entering 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 our subsidiaries in the United Kingdom and Australia. We settle our foreign exchange contracts on the last day of every month and enter into a new forward contract effective on the first day of the next month. Changes in the fair value (i.e. gains or losses) of these derivative instruments are recorded as other income (expense), net.

#### Income Tax Expense (Benefit)

Income tax expense (benefit) for the three and six months ended June 30, 2016 and 2015 was as follows (in thousands, except percentages):

	Three Months		Six Months Ended	
	Ended June 30,		June 30,	
	2016	2015	2016	2015
Income tax expense (benefit)	\$ 169	\$ 178	\$ (9,901)	\$ (352)
Percentage of revenue	0 %	0 %	10 %	0 %

We recognized an income tax expense of \$0.2 million and income tax benefit of \$9.9 million, or approximately 24% and 362% of income (loss) before taxes, respectively, for the three and six months ended June

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30, 2016. The effective tax rate differs from the U.S. federal statutory rate of 34% primarily due to the domestic valuation allowance offsetting most of the statutory rate, partial reversal of the valuation allowance due to the deferred tax liability that was recorded as part of the Pakedge acquisition, state income taxes, foreign income taxes, U.S. federal alternative minimum tax and incentive stock options. Cash payments for taxes of \$0.6 million for the six months ended June 30, 2016, are primarily related to provisional tax payments paid in Australia and state taxes paid in the U.S.

Significant judgment is required in determining our provision for income taxes and evaluating our uncertain tax positions. In evaluating our ability to recover our deferred tax assets, in full or in part, we consider all available positive and negative evidence, including our past operating results, our forecast of future market growth, forecasted earnings, future taxable income and prudent and feasible tax planning strategies. Due to historical net losses incurred and the uncertainty of realizing the deferred tax assets, for all the periods presented, we have a full valuation allowance against our domestic deferred tax assets. To the extent that we generate positive domestic income and expect, with reasonable certainty, to continue to generate positive income, we may release all or a portion of our valuation allowance in a future period. This release would result in the recognition of certain deferred tax assets and a decrease to income tax expense for the period such release is made.

## Liquidity and Capital Resources

### Primary Sources of Liquidity

As of June 30, 2016, we had \$48.8 million in unrestricted cash and cash equivalents and net marketable securities, a decrease of \$32.2 million from December 31, 2015. The overall decrease in cash and cash equivalents and net marketable securities was impacted by the following:

- We purchased Pakedge for \$33.0 million in cash, net of cash acquired of \$0.8 million, resulting in net cash paid of \$32.2 million. In addition, we incurred approximately \$2.3 million in acquisition-related expenses.
- We established a \$30.0 million credit line to fund strategic growth and borrowed \$5.0 million during the six months ended June 30, 2016 to help fund the Pakedge acquisition.
- In May 2015, our Board of Directors authorized the repurchase of up to \$20 million in Control4 common stock from time to time on the open market. For the six months ended June 30, 2016, we repurchased 427,646 shares for \$3.2 million.

Our inventory increased by \$12.9 million during the six months ended June 30, 2016, including a \$5.1 million increase in networking product line inventory due to the acquisition of Pakedge. In addition, we invested an additional \$6.5 million in inventory to support other growth initiatives including the rollout of our new EA Series of controllers and the transition to direct-to-dealer fulfillment in Australia.

We typically 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 generally 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 U.S., corporate securities, and asset-backed securities.

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The following table shows selected financial information and statistics as of June 30, 2016 and December 31, 2015 (in thousands):

	June 30, 2016	December 31, 2015
Cash and cash equivalents	\$ 22,807	\$ 29,530
Investments, net	25,973	51,477
Accounts receivable, net	22,982	21,322
Inventories	32,775	19,855
Working capital	74,046	87,312

We closely monitor accounts receivable and inventory because of their significant impact on cash and working capital. Our accounts receivable balance at June 30, 2016 has increased by \$1.7 million, or 8% since December 31, 2015, due to growth in revenue during that time period. Furthermore, inventory has increased by \$12.9 million from December 31, 2015 to June 30, 2016. As explained above, the increase in inventory was due primarily to the acquisition of Pakedge, buildup of inventory to support direct-to-dealer fulfillment in Australia and new product introductions including the EA Series controllers.

We have an asset-based, revolving credit facility of \$30.0 million and at June 30, 2016 we had outstanding borrowings of \$5.0 million under the New Credit Facility. Our loan agreements contain various restrictive and financial covenants and we were in compliance with each of these covenants as of June 30, 2016. Subsequent to June 30, 2016, we used cash flows from operations to repay \$3.5 million of the balance outstanding under the revolving 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. From time to time, we may explore additional financing sources to develop or enhance our product solutions, to fund expansion of our business, to respond to competitive pressures, or to acquire or invest in complementary products, businesses or technologies. We cannot give assurance that any additional financing will be available to us on acceptable terms, if at all. If we raise additional funds through the issuance of equity or convertible debt or other equity-linked securities, our existing stockholders could suffer significant dilution, and any new equity securities we issue could have rights, preferences and privileges senior to those of holders of our common stock.

## Cash Flow Analysis

A summary of our cash flows for the six months ended June 30, 2016 and 2015 is set forth below (in thousands):

	Six Months Ended	
	June 30,	
	2016	2015
Cash and cash equivalents at the beginning of the period	\$ 29,530	\$ 29,187
Net cash provided by (used in) operating activities	175	(2,601)
Net cash used in investing activities	(8,850)	(7,500)
Net cash provided by (used in) financing activities	1,993	(1,944)
Effect of exchange rate changes on cash and cash equivalents	(41)	38
Net change in cash and cash equivalents	(6,723)	(12,007)
Cash and cash equivalents at the end of the period	\$ 22,807	\$ 17,180

### Operating Activities

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

The increase in cash provided by operating activities of \$2.8 million during the six months ended June 30, 2016 compared to the same period in 2015 is due primarily to net income, as adjusted for certain non-cash operating expenses for the period, and changes in working capital which included an increase in inventory as described above.

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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 \$8.9 million in 2016 from \$7.5 million in 2015. The year-over-year increase is primarily due to the difference in cash used for business acquisitions, offset by the difference in available-for-sale investment activity. The change in the investment activity was a direct result of the Pakedge acquisition as we used the proceeds from the maturity of available-for-sale investments toward the purchase price, rather than reinvesting those funds.

Financing Activities

Financing cash flows consist primarily of the repurchase of Control4 stock in the open market, repayment of long-term debt, borrowing against our revolving credit facility, and proceeds from the exercise of options to acquire common stock.

During the six months ended June 30, 2016, we repurchased 427,646 shares of our stock in the open market for \$3.2 million compared to 227,275 shares for \$2.1 million in the six months ended June 30, 2015.

Net repayments on our term loan agreements were \$0.4 million and \$0.5 million during the six months ended June 30, 2016 and 2015, respectively.

During the six months ended June 30, 2016, we borrowed \$5.0 million from our revolving credit facility and paid \$0.1 million in financing fees related to the 2016 Loan Amendment.

During the six months ended June 30, 2016 and 2015, we received proceeds of \$0.7 million and \$0.7 million, respectively, from the exercise of options to purchase common stock.

## 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 resulting from acquisitions, 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 a great extent, to be 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

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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 the acquisition, and legal and other professional service fees associated with diligence, entity formation and corporate structuring, disputes and regulatory matters related to acquired entities; (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 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 those expenses.

Management provides a non-GAAP measure representing the fair market value of our available-for-sale investments. We account for purchases and sales of investments on a trade-date basis. This is a non-GAAP measure representing the fair market value of our available-for-sale investments on a settlement date basis because from time to time, the investment trade date and the investment settlement date will cross a reporting period. We believe presentation of our investments on a settlement date basis is relevant to readers of our financial statements.

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.

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	Three Months Ended		Six Months Ended	
	June 30,	2015	June 30,	2015
	2016		2016	
	(in thousands, except percentages and per share data)			
<b>Reconciliation of Gross Margin to Non-GAAP Gross Margin:</b>				
Gross margin	\$ 26,027	\$ 22,329	\$ 46,513	\$ 37,940
Stock-based compensation expense in cost of revenue	47	39	90	86
Amortization of intangible assets in cost of revenue	817	379	1,466	684
Acquisition-related costs in cost of revenue	988	—	1,640	294
Non-GAAP gross margin	\$ 27,879	\$ 22,747	\$ 49,709	\$ 39,004
Revenue	\$ 53,215	\$ 44,641	\$ 96,250	\$ 76,724
Gross margin percentage	48.9 %	50.0 %	48.3 %	49.4 %
Non-GAAP gross margin percentage	52.4 %	51.0 %	51.6 %	50.8 %
<b>Reconciliation of Income (Loss) from Operations to Non-GAAP Income (Loss) from Operations:</b>				
Income (loss) from operations	\$ 815	\$ 2,107	\$ (2,526)	\$ (2,265)
Stock-based compensation expense	2,127	1,679	3,950	3,528
Amortization of intangible assets	1,238	403	2,172	728
Acquisition-related costs	1,338	—	2,320	886
Litigation settlements	—	—	400	—
Executive severance	157	—	157	—
Non-GAAP income (loss) from operations	\$ 5,675	\$ 4,189	\$ 6,473	\$ 2,877
Revenue	\$ 53,215	\$ 44,641	\$ 96,250	\$ 76,724
Operating margin percentage	1.5 %	4.7 %	(2.6) %	(3.0) %
Non-GAAP operating margin percentage	10.7 %	9.4 %	6.7 %	3.7 %
<b>Reconciliation of Net Income (Loss) to Non-GAAP Net Income (Loss):</b>				
Net income (loss)	\$ 524	\$ 2,041	\$ 7,163	\$ (2,190)
Stock-based compensation expense	2,127	1,679	3,950	3,528
Amortization of intangible assets	1,238	403	2,172	728
Acquisition-related costs	1,454	—	(7,388)	886
Litigation settlements	—	—	400	—
Executive severance	157	—	157	—
Non-GAAP net income (loss) (1)	\$ 5,500	\$ 4,123	\$ 6,454	\$ 2,952
Non-GAAP net income (loss) (1) per common share:				
Basic	\$ 0.24	\$ 0.17	\$ 0.28	\$ 0.12
Diluted	\$ 0.23	\$ 0.16	\$ 0.27	\$ 0.12
Weighted-average number of shares:				
Basic	23,162	24,309	23,248	24,326
Diluted	23,930	25,296	23,958	25,474
<b>Reconciliation of Investments to Investments, net:</b>				
Short-term investments	\$ 20,780	\$ 46,118	\$ 20,780	\$ 46,118
Long-term investments	5,010	19,838	5,010	19,838
Accrued investments	183	(703)	183	(703)

Investments, net	\$ 25,973	\$ 65,253	\$ 25,973	\$ 65,253
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(1) Excludes the calculated effect of non-GAAP adjustments on income tax expense (benefit) of \$55,629 and (\$190,000) for the three and six months ended June 30, 2016, respectively.

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## Off-Balance Sheet Arrangements

During the periods presented, we did not engage in any off-balance sheet activities. We do not have any off-balance interest in variable interest entities, which include special purpose entities and other structured finance entities.

## Contractual Obligations

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

Our contractual cash obligations at June 30, 2016 are as follows:

	Total	Less than 1 year	1 - 3 years	3 - 5 years	More than 5 years
	(in thousands)				
Long-term debt obligations, including interest (1)	\$ 624	\$ 524	\$ 100	\$ —	\$ —
Revolving credit facility	5,000	—	5,000	—	—
Operating lease obligations	7,542	3,080	4,052	410	—
Purchase commitments	33,501	33,501	—	—	—
Total contractual obligations	\$ 46,667	\$ 37,105	\$ 9,152	\$ 410	\$ —

(1) Interest was calculated on outstanding borrowings at the date indicated in the table above and assumes the rate remains constant during the following years. The New Credit Facility has a variable rate of interest of prime or LIBOR plus 2.50%, as selected by us. The variable rate was 3.50% at June 30, 2016. Term borrowings are payable in equal monthly payments of principal plus interest and bear interest at prime plus 0.50%, which was 4.00% at June 30, 2016.

## 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 16, 2016. None of our critical accounting policies and estimates have changed significantly since that filing. The acquisition of Pakedge did not significantly impact our critical accounting policies and estimates because their accounting policies and procedures were aligned with ours. However, the acquisition did result in an increase to our warranty reserves since Pakedge currently offers a product warranty of three years compared to the warranty of two years historically offered by Control4.

#### 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).

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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 16, 2016. Other than our interest rate risk and uncertainty associated with the UK's recent vote to exit the European Union described below, our market risk has not changed significantly since that filing.

Interest Rate Risk

Changes in U.S. 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.

Our exposure to changes in interest rates relates primarily to our investment portfolio. We typically invest in highly-rated securities, and our investment policy generally limits the amount of credit exposure to any one issuer. The policy requires investments generally 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 June 30, 2016, a hypothetical 100 basis point increase in interest rates across all maturities would result in a \$0.1 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.

European Market Risk

On June 23, 2016, the United Kingdom ("UK") voted to leave ("Brexit") the European Union ("EU") raising concerns of a potential slowdown in the UK's economy specifically and the EU in general. We have engaged with our dealers in the UK to assess their perception of how the Brexit vote might impact their business in the near and long-term. Their responses are varied and reflect the uncertainty that currently exists in the market. We will continue to monitor the risks and uncertainties throughout what is expected to be a lengthy process.

The Brexit vote had the immediate impact of devaluing the pound sterling relative to the euro and the U.S. dollar. We generally sell our products and incur expense in local currencies including the pound sterling and the euro, but incur exchange rate gains and losses for U.S. dollar denominated assets and liabilities including intercompany and third-party accounts receivables and payables. We enter into forward contracts to help offset our exposure to movements in foreign currency exchange rates relative to these types of U.S. dollar denominated balances. When consolidating the revenue and expenses of our foreign subsidiaries, we translate local currencies to the U.S. dollar using average exchange rates during the period, resulting in either higher or lower net income depending on changes in the relative value of foreign currencies to the U.S. dollar. We do not believe that Brexit will have a material impact on our net income as generated by our subsidiary in the UK in the short-term.

#### 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 (the “Exchange Act”)), 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.

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Changes in Internal Control over Financial Reporting

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



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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

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 June 30, 2016, we had an accumulated deficit of \$88.4 million. We expect our operating expenses to increase in the future as we expand our operations. Furthermore, as a public company, we incur additional legal, accounting and other expenses that we did not incur as a private company. If our revenue does not grow to offset any increased expenses, we will not 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 after the first six months of 2016 is \$7.2 million, but 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 in future periods. If these losses exceed our expectations or our revenue growth expectations are not met in future periods, our financial performance will be harmed.

The markets in which we participate are highly competitive and many companies, including large technology companies, retailers, broadband and security service providers, and other managed service providers, are actively targeting the home automation market. Our failure to differentiate ourselves and compete successfully with 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 among some of their own products, applications and services and are engaged in ongoing development efforts to address 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 superior products and services. Additionally, these and other companies may further expand into our industry by developing their own 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 has recently made a significant effort to market its smart home services. 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

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fee with little to no upfront cost offered by some of these managed service providers over a larger upfront cost with 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 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, most of our competitors have longer operating histories, greater name recognition, larger consumer bases and significantly greater financial, 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 rather than adopting our unified 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 a thermostat or alarm system that can be controlled by an application on a smartphone. We expect more and more 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 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. While we have built our solution to be flexible and support 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 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 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 mainstream 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 40 years and has become an established presence in the home automation industry. Another provider of luxury integrated installations is Savant Systems. Given the strong growth potential of the market, we expect there to 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 solutions across any of our target demographics, our growth may be constrained and our business could suffer.

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

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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.

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 these dealers and distributors fail to provide 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.

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;
- 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;

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- 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;
- 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;
- 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
- 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.

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, 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.

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

As of June 30, 2016, we have developed a global network of over 3,700 active direct dealers and 27 distributors authorized to sell, install and support our complete solution set. In addition, we have over 1,100 dealers and 17 distributors authorized to sell only our Pakedge branded networking 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 most of our existing



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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 mainstream consumer products that our dealers and distributors offer. If we are unable to expand our network of independent dealers and distributors, or maintain the relationships with our existing dealers and distributors, including dealers and distributors we added as a result of our acquisition of Pakedge, our business could be harmed.

We rely on our independent dealers and distributors to sell our solution, 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 solution 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, 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 may not be meaningful and 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 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 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. For example, in February 2015, we announced that we were transitioning from a single distributor to a direct-to-dealer sales model in Germany, and in February 2016, we announced a similar transition in Australia. While we believe that these actions will ultimately have a positive impact on sales and profitability in those regions, they may also create disruption in the established channels and our sales and results of operations may be impacted in connection with this or any similar change in our sales process in the future.

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 still 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, or if our dealers or distributors are unsuccessful in fulfilling the orders for our products, then our results of operations may be harmed.

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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 in the process of growing our 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 music, video, lighting, temperature and security, and we benefit from our relationships with partners that allow our system to provide integrated and extensible control of over 9,700 third party devices and services. If we do not support the continued integration of our solutions with third-party products and applications, including through the provision of application programming interfaces, proxies and drivers that enable data to be transferred readily between our solutions and third-party products and applications, demand for our solutions could decline and we could lose sales. We will also be required to make our solutions compatible with new or additional third-party products and applications that are introduced into the markets that we serve. 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.

Our inability to adapt to technological change and implement technological and aesthetic enhancements to our products 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 enhance existing solutions or introduce new solutions in a timely basis to keep pace with technological developments. This is true of all of our products, but is particularly important with respect to our user

interface and other products that our consumers interface with directly. 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.

We currently rely on contract manufacturers to manufacture our products and on component vendors to supply parts used in our products. The majority of our components are supplied by a single source. 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 substantially all of our products. We also do business with a number of component vendors, and the parts they supply may not perform as expected. For certain of our products and components, we rely on a sole-source manufacturer or supplier. For the six months ended June 30, 2016, three contract manufacturers, Sanmina, RCS and iLife, manufactured approximately 60% of our inventory purchases.

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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 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.

Growth of our business will depend on market awareness and a strong brand, and any failure to develop, maintain, protect and enhance our brand would hurt our ability to retain or attract consumers.

Because of the early stage of development of the mainstream home automation market, we believe that building and maintaining market awareness, brand recognition and goodwill is critical 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. While 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 mainstream 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 additional operating losses.

The market for home automation and control solutions is developing, and it is uncertain whether, how rapidly or how consistently this market will develop, and even if it does develop, 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 traditional solutions, concerns for additional costs 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 controller which we released in January 2016 that is designed to control smaller, single room projects. Our ability to expand the sales of our solutions to a broader consumer base, including adoption of our EA-1 controller by entry-level consumers, 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 ability to develop relationships with independent dealers and distributors, the effectiveness of our marketing programs, the costs of our solutions and the success of our competitors. If we are unsuccessful in developing and marketing our home automation solutions to mainstream 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, infrastructure, third-party components or processes that comprise our existing or new 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, infrastructure, third-party components or processes. If these defects lead to service failures after introduction of or an upgrade to a product or solution by an

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independent dealer, we could be subject to liability for such failures and we could experience harm to our branded reputation and our business could suffer. We may find defects in new or upgraded solutions, resulting in 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 or lost revenue during the period required to address the cause of the problem, each of 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 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 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 states 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.

Our recently acquired 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 such 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, 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



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information technology systems. However, the security measures that we put in place 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.

In addition, consumers can use our tools to access their automation systems remotely, and certain of our employees and independent dealers can access and update certain of our products and services through the Internet. Security breaches by third parties or by, or originating from, one or more of our dealers, distributors or employees, that allow unauthorized third parties to obtain control of our consumers' appliances through our products or to obtain, collect, use or disclose any the 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 a consumer's home network. If a security breach occurs, our reputation, business, results of operations and financial condition could be harmed. In addition, even the perception that there is a security risk associated with home automation devices generally, or that we or our dealers, distributors or employees have improperly used our technology or mishandled personal information, could have a negative effect on our business. This negative perception may be increased in the event of a security breach or cyber-attack impacting one of our competitors or their products and services.

Additionally, we design and sell solutions that allow our customers to wirelessly access sensitive data on their network and to remotely manage and operate devices and applications that contain, transmit and store a variety of information. We use data encryption and other security measures to protect our internal systems and data, and we include various security mechanisms in our products and services, but these security measures cannot provide absolute protection against breaches and attacks.

Though it is difficult to determine what harm may directly 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.

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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. For the six months ended June 30, 2016, we spent \$17.5 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 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. For example, we acquired Nexus in January 2015 and Pakedge in January 2016. These acquisitions and any future acquisitions we 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;
- 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 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; and
- Being unable to generate sufficient revenue from acquisitions to offset the associated acquisition costs.

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Fully integrating an acquired technology, asset, business, or personnel into our operations may take a significant amount of time. 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, 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 Pakedge and its networking technologies. 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.

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, 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 carryforwards, our financial results will be harmed.

As of December 31, 2015, our net operating loss (“NOL”) carryforward amounts for U.S. federal income and state tax purposes were \$78.1 million and \$75.9 million, respectively. In addition to the NOL carryforwards, as of December 31, 2015, we had U.S. federal and state research and development credit carryforwards of \$6.7 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 before they expire.

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If we are unable to manage our 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 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;
- Attracting, training, motivating and retaining our employees, particularly our technical employees, senior management and key personnel;
- 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, 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 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, 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



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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.

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, beginning in 2014, Google Inc. acquired Nest Labs, a manufacturer of thermostats and smoke detectors;

Nest Labs acquired Dropcam, a home-monitoring camera company; Apple Inc. introduced HomeKit, a framework for communicating with and controlling connected devices in a user's home; and Samsung Electronics Co., Ltd. acquired home automation startup, SmartThings. 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.

We are an "emerging growth company," and any decision on our part to comply with certain reduced disclosure requirements applicable to emerging growth companies could make our common stock less attractive to investors.

We are an "emerging growth company," as defined in the Jumpstart Our Business Startups Act of 2012 (the "JOBS Act"), and we may take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not "emerging growth companies," including not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements, and exemptions from the requirements of holding an annual non-binding advisory vote on executive compensation and nonbinding stockholder approval of any golden parachute payments not previously approved. If we choose not to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act, our auditors will not be required to

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opine on the effectiveness of our internal control over financial reporting. As a result, investors may become less comfortable with the effectiveness of our internal controls and the risk that material weaknesses or other deficiencies in our internal controls go undetected may increase. If we choose to provide reduced disclosures in our periodic reports and proxy statements while we are an emerging growth company, investors would have access to less information and analysis about our executive compensation, which may make it difficult for investors to evaluate our executive compensation practices. We cannot predict if investors will find our common stock less attractive because we may rely on these exemptions and provide reduced disclosure. If some investors find our common stock less attractive as a result, there may be a less active trading market for our common stock and our stock price may be harmed. We will remain an “emerging growth company” for up to five years following our initial public offering or such earlier time that we are no longer an emerging growth company. We will remain an emerging growth company until the earliest to occur of: the last day of the fiscal year in which we have more than \$1.0 billion in annual revenue; the date we qualify as a “large accelerated filer,” with at least \$700 million of equity securities held by non-affiliates determined as of the last business day of the previous second fiscal quarter; the issuance, in any three-year period, by us of more than \$1.0 billion in non-convertible debt securities; or the last day of the fiscal year ending after the fifth anniversary of our initial public offering.

In addition, Section 107 of the JOBS Act provides that an emerging growth company can take advantage of the extended transition period provided in Section 7(a)(2)(B) of the Securities Act of 1933, as amended (the “Securities Act”), for complying with new or revised accounting standards. In other words, an emerging growth company can delay the adoption of certain accounting standards until those standards would otherwise apply to private companies. However, we have chosen to “opt out” of such extended transition period, and as a result, we will comply with new or revised accounting standards on the relevant dates on which adoption of such standards is required for non-emerging growth companies. Section 107 of the JOBS Act provides that our decision to opt out of the extended transition period for complying with new or revised accounting standards is irrevocable.

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. However, our auditors will not be required to formally opine on the effectiveness of our internal control over financial reporting pursuant to Section 404 until we are no longer an “emerging growth company” as defined in the JOBS Act, and we continue to take advantage of the exemptions available to us through the JOBS Act. Our auditors will be required to formally opine on the effectiveness of our internal controls no later than our Form 10-K for the fiscal year ended December 31, 2018.

Our compliance with Section 404 may require us to continue to incur substantial expense and expend significant management efforts. 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. 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. 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.

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. 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 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 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, 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, 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. Sanmina and LiteOn, two of our contract manufacturers that manufactured 60% of our inventory purchases for the six months ended June 30, 2016, have manufacturing facilities located in China. 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

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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 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, could cause disruptions in our business or the business of our manufacturers, logistics providers, dealers, distributors, consumers or the economy as a whole. 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.

Global or regional economic, political and social conditions could harm our business and results of operations.

External factors such as potential crime, terrorist attacks, 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 or elsewhere, could harm our business and results of operations. 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. More generally, these geopolitical, social and economic conditions could result in increased volatility in worldwide financial markets and economies that could harm our sales. We are not insured for losses or interruptions caused by terrorist acts or acts of war. The occurrence of any of these events or circumstances could harm our business and results of operations.

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. As we continue to develop new products, acquire companies with new product lines and expand our geographical footprint to market and sell products 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 these new jurisdictions, we continue to work towards full 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.

In addition, we have in the past relied on adherence to the U.S. Department of Commerce’s Safe Harbor Privacy Principles and compliance with the U.S.-EU and U.S.-Swiss Safe Harbor Frameworks as agreed to and set forth by the U.S. Department of Commerce, and the European Union and Switzerland, which established a means for legitimating the transfer of personally identifiable information (“PII”), by U.S. companies doing business in Europe from the European Economic Area to the U.S. As a result of the October 6, 2015 European Union Court of Justice (“ECJ”), opinion in Case C-362/14 (Schrems v. Data Protection Commissioner) that the U.S.-EU Safe Harbor Framework, the U.S. – EU Safe Harbor Framework is no longer deemed to be an adequate method of compliance with restrictions set forth in the Data Protection Directive (and member states’ implementations thereof) regarding the transfer of data outside of the European Economic Area. On July 12, 2016 the European Commission formally adopted the new EU – U.S. Privacy Shield announced on February 2, 2016. It is anticipated that U.S. companies will be able to begin to self-certify with the U.S. Department of Commerce beginning August 1, 2016. We continue to explore options to legitimize certain data transfers from the European Economic Area, including without limitation meeting the requirement of self-certification pursuant to the this new Privacy Shield, adopting



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model contractual clauses with certain suppliers, and looking for suppliers that house data in the European Economic Area. We may be unsuccessful in establishing legitimate means of transferring certain data from the European Economic Area, and we are at risk of enforcement actions taken by an EU data protection authority until such point in time that we ensure that all data transfers to us from the European Economic Area are legitimized. We may find it necessary to establish additional systems to maintain EU-origin data in the European Economic Area, which may involve substantial expense and distraction from other aspects of our business. We publicly post our privacy policies and practices concerning our processing, use and disclosure of PII. Our publication of our privacy policy and other statements we publish that provide promises and assurances about privacy and security can subject us to potential state, federal or other regulatory action if they are found to be deceptive or misrepresentative of our practices.

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

The U.S. 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 and our revenue. 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.

New 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 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 an extremely complex supply chain, with numerous suppliers, many of whom may not be obligated to investigate their own supply chains, for the components and parts used in each of our products. As a result, we may incur significant costs to comply with the diligence and disclosure requirements, including costs related to determining the source of any of the relevant metals used in our products and other potential changes to products or sources of supply as a consequence of such verification activities. Because these regulations are new, we and the companies comprising our supply chain each have a limited history of investigating, disclosing and reporting use of these minerals, and there is a limited history of regulatory guidance regarding compliance with these requirements. 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, which may harm our business reputation. 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

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value. Recent changes, especially the employer mandate and employer penalties that became effective January 1, 2015, may increase our labor costs significantly in future years. In order to comply with the employer mandate provision of the ACA, 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.

We incur increased costs and demands upon management as a result of complying with the laws and regulations affecting public companies, which could harm our results of operations and our ability to attract and retain qualified executives and board members.

As a public company, we have incurred and will continue to incur significant legal, accounting and other expenses that we did not incur as a private company, including costs associated with public company reporting and corporate governance requirements. These requirements include compliance with Section 404 and other provisions of the Sarbanes-Oxley Act of 2002, the Dodd-Frank Act, as well as rules implemented by the Securities and Exchange Commission (“SEC”), The NASDAQ Stock Market LLC, and other applicable securities or exchange-related rules and regulations. In addition, our management team has also had to adapt to the requirements of being a public company. Complying with these rules and regulations substantially increases our legal and financial compliance costs and makes some activities more difficult, time consuming or costly. These compliance requirements and costs will increase once we are no longer an “emerging growth company,” as defined in the JOBS Act.

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, installing and supporting our products and services internationally. However, international revenue (excluding Canada) accounted for 21% of our total revenue for the six months ended June 30, 2016, and we expect that percentage to 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 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 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 Europe Union, including through our office located in England, and our operations may be affected by the results of the recent referendum vote by the United Kingdom to leave the European Union.

On June 23, 2016, a majority of voters in the United Kingdom approved a referendum to leave the European Union (“Brexit Vote”), which immediately led to significant market volatility around the world, as well as political, economic and legal uncertainty. It is expected that the United Kingdom’s exit from the European Union will take place within two years after the United Kingdom formally notifies the European Council of its intention to

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withdraw. During this time negotiations will take place to unravel all of the existing legal, political and financial frameworks and obligations, and put new structures in place. At this stage, it is uncertain what the results of these negotiations will be and how the Brexit Vote will affect economic conditions in the United Kingdom, the European Union, or globally. Because Control4 has sales throughout the European Union and offices in England and Germany, it is possible that the Brexit Vote may require us to restructure some or all of our operations, and depending on what is negotiated, could impair our ability to transact business in other countries in the European Union. In addition, the 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 others), 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.



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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 (a summary of current litigation and outstanding claims that if determined adversely to us, we believe would have a material adverse effect on our business, results of operations, financial condition or cash flows, if any, is set forth below in Part I Item 3, Legal Proceedings), 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 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, and expect to continue to agree, to indemnify our independent dealers, distributors and other partners for certain intellectual property infringement claims regarding our products. 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 or to refund amounts they have paid to us. 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, 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

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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 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 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;

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- Announcements by us or our competitors of significant acquisitions, strategic partnerships, joint ventures or capital commitments;
- 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;
- Sales of our common stock by us or our stockholders;
- 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 June 30, 2016, our directors, executive officers and holders of more than 5% of our common stock, together with their affiliates, beneficially own, in the aggregate, 57% of our outstanding common stock. As a result, these stockholders, acting together, would 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, would have the ability to

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control the management and affairs of our company. Accordingly, this concentration of ownership might harm the market price of our common stock by:

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



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

## Unregistered Sales of Equity Securities

During the quarter ended June 30, 2016, 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 May 2015, the Company's Board of Directors authorized the repurchase of up to \$20 million in Control4 common stock from time to time on the open market. In February 2016, the Board of Directors authorized an extension to this repurchase program from its original end-date of May 13, 2016 to June 30, 2017, unless terminated earlier. Any shares repurchased will be in compliance with applicable legal requirements, at prices determined to be attractive and in the best interests of both the company and its stockholders. During the three months ended June 30, 2016, we repurchased 193,831 shares of outstanding common stock under the share repurchase program, as set forth in the table below:

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)
May 1 - 31, 2016	193,831	\$ 7.77	193,831	
	193,831	—	193,831	\$ 7,738

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

## ITEM 4. Mine Safety Disclosures

None.



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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
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
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		Filed herewith		

XBRL Taxonomy Extension Presentation  
Linkbase Document

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\*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.

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SIGNATURES

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

Date: August 5, 2016

CONTROL4 CORPORATION

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