CLEARONE COMMUNICATIONS INC
Form 10-Q
February 11, 2008

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

x Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended December 31, 2007

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: 000-17219

CLEARONE COMMUNICATIONS, INC.
(Exact name of registrant as specified in its charter)

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

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

Indicate by check whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and larger accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Larger Accelerated Filer ¨ Accelerated Filer ¨ Non-Accelerated Filer x

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

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date. There were 10,723,447 shares of the Company's Common Stock, par value $0.001, outstanding on February 8, 2008.

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REPORT ON FORM 10-Q
FOR THE QUARTER ENDED DECEMBER 31, 2007

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DISCLOSURE REGARDING FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. These statements reflect our views with respect to future events based upon information available to us at this time. These forward-looking statements are subject to uncertainties and other factors that could cause actual results to differ materially from these statements. Forward-looking statements are typically identified by the use of the words "believe," "may," "could," "will," "should," "expect," "anticipate," "estimate," "project," "propose," "plan," "intend," and sim expressions; however, not all forward-looking statements contain these words. Examples of forward-looking statements are statements that describe the proposed development, manufacturing, and sale of our products; statements that describe our results of operations, pricing trends, the markets for our products, our anticipated capital expenditures, our cost reduction and operational restructuring initiatives, and regulatory developments; statements with regard to the nature and extent of competition we may face in the future; statements with respect to the sources of and need for future financing; and statements with respect to future strategic plans, goals, and objectives. Forward-looking statements are contained in this report in Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations," Item 3, "Quantitative and Qualitative Disclosures About Market Risk," and Item 4, "Controls and Procedures" included in this Quarterly Report on Form 10-Q. The forward-looking statements are based on present circumstances and on our predictions respecting events that have not occurred, that may not occur, or that may occur with different consequences and timing than those now assumed or anticipated. Actual events or results may differ materially from those discussed in the forward-looking statements as a result of various factors, including the risk factors discussed in this report under Part II – Other Information, Item 1A, "Risk Factors" and the application of "Critical Accounting Policies" as discussed in Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations." These cautionary statements are intended to be applicable to all related forward-looking statements wherever they appear in this report. The cautionary statements contained or referred to in this report should also be considered in connection with any subsequent written or oral forward-looking statements that may be issued by us or persons acting on our behalf. Any forward-looking statements are made only as of the date of this report and ClearOne assumes no obligation to update forward-looking statements to reflect subsequent events, changes in circumstances, or changes in estimates.

PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

CLEARONE COMMUNICATIONS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands of dollars, except per share amounts)

	(unaudited) December 31, 2007	(audited) June 30, 2007
ASSETS		
Current assets:		
Cash and cash equivalents	$ 3,014	$ 2,782
Marketable securities	19,676	19,871
Accounts receivable, net of allowance for doubtful accounts of $60 and $54, respectively	7,790	8,025
Deposit, Bond for Preliminary Injunction	908	0
Note Receivable	126	163
Inventories, net	6,792	7,263
Deferred income taxes	124	0
Prepaid expenses	512	213
Total current assets	38,942	38,317
Property and equipment, net	2,651	2,694
Note Receiveable - long-term	0	43
Other assets	9	9
Total assets	$ 41,602	$ 41,063
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 1,294	$ 1,745
Accrued taxes	0	660
Accrued liabilities	3,047	1,874
Deferred product revenue	4,980	4,872
Total current liabilities	9,321	9,151
Deferred rent	777	855
Deferred income taxes, net	124	0
Other long-term liabilities	1,084	619
Total liabilities	11,306	10,625
Shareholders' equity:		
Common stock, par value $0.001, 50,000,000 shares authorized,		
	11	11

10,771,165 and 10,861,920 shares issued and outstanding, respectively				
Additional paid-in capital		46,877		47,582
Accumulated deficit		(16,592)		(17,155)
Total shareholders' equity		30,296		30,438
Total liabilities and shareholders' equity	$	41,602	$	41,063

See accompanying notes to condensed consolidated financial statements

CLEARONE COMMUNICATIONS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)
(in thousands of dollars, except per share amounts)

	Three Months Ended		Six Months Ended	
	December 31, 2007	December 31, 2006	December 31, 2007	December 31, 2006
Product Revenue:	$ 10,787	$ 10,107	$ 20,229	$ 19,518
Cost of goods sold:				
Total cost of goods sold	4,414	4,860	8,714	9,176
Gross profit	6,373	5,247	11,515	10,342
Operating expenses:				
Sales and marketing	1,578	1,789	3,180	3,707
General and administrative	1,198	688	4,093	1,497
Research and product development	1,678	1,855	3,433	3,934
Total operating expenses	4,454	4,332	10,706	9,138
Operating income	1,919	915	809	1,204
Other income, net:				
Interest income	296	283	610	590
Other, net	15	37	43	62
Total other income, net	311	320	653	652
Income (loss) from continuing operations before income taxes	2,230	1,235	1,462	1,856
(Provision) benefit from income taxes	(449)	(155)	(620)	(136)
Income from continuing operations	1,781	1,080	842	1,720
Discontinued operations:				
Income from discontinued operations	-	20	-	75
Gain on disposal of discontinued operations	1	(13)	25	(10)
Income tax provision	-	(3)	(9)	(24)
Income from discontinued operations	1	4	16	41
Net income	$ 1,782	$ 1,084	$ 858	$ 1,761

See accompanying notes to condensed consolidated financial statements

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CLEARONE COMMUNICATIONS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME (CONTINUED)
(Unaudited)
(in thousands of dollars, except per share amounts)

	Three Months Ended		Six Months Ended	
	December 31, 2007	December 31, 2006	December 31, 2007	December 31, 2006
Basic earnings per common share from continuing operations	$ 0.16	$ 0.09	$ 0.08	$ 0.14
Diluted earnings per common share from continuing operations	$ 0.16	$ 0.09	$ 0.08	$ 0.14
Basic earnings per common share from discontinued operations	$ 0.00	$ 0.00	$ 0.00	$ 0.00
Diluted earnings per common share from discontinued operations	$ 0.00	$ 0.00	$ 0.00	$ 0.00
Basic earnings per common share	$ 0.16	$ 0.09	$ 0.08	$ 0.15
Diluted earnings per common share	$ 0.16	$ 0.09	$ 0.08	$ 0.15
Basic weighted average shares	10,840,193	11,922,641	10,900,725	12,053,745
Diluted weighted average shares	10,941,491	11,957,706	11,012,239	12,100,794

See accompanying notes to condensed consolidated financial statements

CLEARONE COMMUNICATIONS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(in thousands of dollars, except per share amounts)

	Six Months Ended	
	December 31, 2007	December 31, 2006
Cash flows from operating activities:		
Net income from continuing operations	$ 842	$ 1,720
Adjustments to reconcile net income from continuing operations		
to net cash provided by (used in) operations:		
Depreciation and amortization expense	384	479
Stock-based compensation	372	453
Write-off of inventory	406	281
(Gain) loss on disposal of assets and fixed assets write-offs	4	-
Provision for doubtful accounts	6	-
Changes in operating assets and liabilities:		
Accounts receivable	61	102
Deposit - Bond	(908)	-
Note receivable - Ken-A-Vision	80	(282)
Inventories	65	424
Prepaid expenses and other asssets	(299)	(74)
Accounts payable	(282)	(514)
Accrued liabilities	1,173	(400)
Income taxes	(490)	215
Deferred product revenue	108	(1,160)
Net cash provided by continuing operating activities	1,522	1,244
Net cash provided by discontinued operating activities	-	47
Net cash provided by operating activities	1,522	1,291
Cash flows from investing activities:		
Purchase of property and equipment	(423)	(616)
Proceeds from the sale of property and equipment	-	55
Purchase of marketable securities	(6,874)	(6,900)
Sale of marketable securities	7,069	10,950
Net cash provided by (used in) continuing investing activities	(228)	3,489

Net cash provided by discontinued investing activities		16		559
Net cash provided by (used in) investing activities		(212)		4,048
Cash flows from financing activities:				
Proceeds from common stock		519		6
Purchase and retirement of stock		(1,664)		(4,745)
Tax benefit attributable to exercise of stock options		67		-
Net cash used in financing activities		(1,078)		(4,739)
Net increase in cash and cash equivalents		232		600
Cash and cash equivalents at the beginning of the period		2,782		1,240
Cash and cash equivalents at the end of the period	$	3,014	$	1,840

See accompanying notes to condensed consolidated financial statements

CLEARONE COMMUNICATIONS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)
(Unaudited)
(in thousands of dollars, except per share amounts)

	Six Months Ended	
	December 31, 2007	December 31, 2006
Supplemental disclosure of cash flow information:		
Cash paid for interest	$ 2	$ 1
Cash paid (received) for income taxes	$ 1,054	$ (55)
Supplemental disclosure of non-cash financing activities:		
Exchanged accounts receivable from a vendor with accounts payable to same vendor	$ 168	$ -
Increase in accumulated deficit and income tax liability as a result of the adoption of FIN48 (see note 5)	$ 295	$ -
Lease incentive for Edgewater leasehold improvements	$ -	$ 1,088

See accompanying notes to condensed consolidated financial statements

CLEARONE COMMUNICATIONS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(in thousands of dollars, except per share amounts)

1. Basis of Presentation

The accompanying condensed consolidated financial statements, consisting of the condensed consolidated balance sheets as of December 31, 2007 and June 30, 2007, the condensed consolidated statements of income for the three months and six months ended December 31, 2007 and 2006, and the condensed consolidated statements of cash flows for the six months ended December 31, 2007 and 2006, have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q. Accordingly, certain information and footnote disclosures normally included in complete financial statements have been condensed or omitted. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended June 30, 2007.

In management's opinion, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. The results of operations for interim periods are not necessarily indicative of the results of operations to be expected for the entire year or for any future period.

2. Inventory

Inventories, net of reserves, consisted of the following as of December 31, 2007 and June 30, 2007 (in thousands):

	December 31, 2007	June 30, 2007
Raw materials	$ 296	$ 453
Finished goods	4,637	4,695
Consigned inventory	1,859	2,115
Total inventory	$ 6,792	$ 7,263

Consigned inventory represents inventory at distributors and other customers where revenue recognition criteria have not been achieved.

3. Share-Based Payment

The Company's share-based compensation primarily consists of the following plans:

On December 31, 2007, the Company had two share-based compensation plans, one which was replaced on November 20, 2007, and one which became active on the same date. The plans are described below.

The Company's 1998 Incentive Plan (the "1998 Plan") had shares of common stock available for issuance to employees and directors. Provisions of the 1998 Plan included the granting of stock options. Provisions of the 1998 Plan include the granting of incentive and non-qualified stock options. Through December 1999, 1,066,000 options were granted that would cliff vest after 9.8 years; however, such vesting was accelerated for 637,089 of these options upon meeting certain earnings per share goals through the fiscal year ended June 30, 2003. Subsequent to December 1999 and through June 2002, 1,248,250 options were granted that would cliff vest after 6.0 years; however, such vesting was

accelerated for 300,494 of these options upon meeting certain earnings per share goals through the fiscal year ended June 30, 2005. As of December 31, 2007, 20,000 and 150,250 of these options that cliff vest after 9.8 and 6.0 years, respectively, remain outstanding.

The Company also has a 2007 Equity Incentive Plan (the "2007 Plan"). Provisions of the 2007 Plan include the granting of up to 1,000,000 incentive and non-qualified stock options, stock appreciation rights, restricted stock and restricted stock units. Options may be granted to employees, officers, non-employee directors and other service providers and may be granted upon such terms as the Compensation Committee of the Board of Directors, in their sole discretion, determine, or in the absence of a Compensation Committee, a properly constituted Compensation Committee or the Board itself.

Of the options granted subsequent to June 2002, all vesting schedules are based on 3 or 4-year vesting schedules, with either one-third or one-fourth vesting on the first anniversary and the remaining options vesting ratably over the remainder of the vesting term. Generally, directors and officers have 3-year vesting schedules and all other employees have 4-year vesting schedules. Additionally, in the event of a change in control or the occurrence of a corporate transaction, the Company's Board of Directors have the authority to elect that all unvested options shall vest and become exercisable immediately prior to the event or closing of the transaction. All options outstanding as of December 31, 2007 had contractual lives of ten years. Under the 1998 Plan, 2,500,000 shares were authorized for grant. As of December 31, 2007, there were 1,363,983 options outstanding under the 1998 Plan, which includes the cliff vesting and 3 or 4-year vesting options discussed above. As of December 31, 2007, no options had been granted under the 2007 Plan.

The Company also has an Employee Stock Purchase Plan ("ESPP"). Employees can purchase common stock through payroll deductions of up to 10 percent of their base pay. Amounts deducted and accumulated by the employees are used to purchase shares of common stock on or about the first day of each month. The Company contributes to the account of the employee one share of common stock for every nine shares purchased by the employee under the ESPP.

Effective July 1, 2005, the Company adopted SFAS No. 123R, "Share-Based Payment." The Company adopted the fair value recognition provisions of SFAS No. 123R using the modified prospective transition method. Under this transition method, stock-based compensation cost recognized beginning July 1, 2005 includes the straight-line compensation cost for (a) all share-based payments granted prior to July 1, 2005, but not yet vested, based on the grant date fair values used in the pro-forma disclosures under the original SFAS No. 123 and (b) all share-based payments granted on or after July 1, 2005, in accordance with the provisions of SFAS No. 123R.

The Company uses judgment in determining the fair value of the share-based payments on the date of grant using an option-pricing model with assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to, the risk-free interest rate of the awards, the expected life of the awards, the expected volatility over the term of the awards, the expected dividends of the awards, and an estimate of the amount of awards that are expected to be forfeited. The Company uses the Black-Scholes option pricing model to determine the fair value of share-based payments granted under SFAS No. 123R and the original SFAS No. 123.

4. Discontinued Operations

During the first fiscal quarter of 2007, the Company completed the sales of its document and educational camera product line to Ken-A-Vision Manufacturing. Additionally, during fiscal 2005, the Company sold its Canadian audiovisual integration services, OM Video, to 6351352 Canada Inc, a Canada corporation (the "OM Purchaser"). Accordingly, the results of operations and the financial position have been reclassified in the accompanying condensed consolidated financial statements as discontinued operations.

	Three Months Ended		Six Months Ended	
	December 31, 2007	December 31, 2006	December 31, 2007	December 31, 2006
Income from discontinued operations:				
Ken-A-Vision	$ -	$ 20	$ -	$ 75
Gain (loss) on disposal of discontinued operations:				

Ken-A-Vision		0		(13)		0		(10)
OM Video		1		0		25		0
Total gain (loss) on disposal of discontinued operations		1		(13)		25		(10)
Income tax benefit (provision):								
Ken-A-Vision		0		(3)		0		(24)
OM Video		0		0		(9)		0
Total income tax benefit (provision)		0		(3)		(9)		(24)
Total income (loss) from discontinued operations, net of income taxes:								
Ken-A-Vision	$	0	$	4	$	0	$	41
OM Video		1		-		16		-
Total income (loss) from discontinued operations, net of income taxes	$	1	$	4	$	16	$	41

OM Video

On March 4, 2005, the Company sold all of the issued and outstanding stock of its Canadian subsidiary, ClearOne Communications of Canada, Inc. (“ClearOne Canada”) to 6351352 Canada Inc., a Canada corporation. ClearOne Canada owned all the issued and outstanding stock of Stechyson Electronics, Ltd., which conducts business under the name OM Video. The Company agreed to sell the stock of ClearOne Canada for $200 in cash; a $1.3 note receivable over a 15-month period, with interest accruing on the unpaid balance at the rate of 5.3 percent per year; and contingent consideration ranging from 3.0 percent to 4.0 percent of related gross revenues over a five-year period. In June 2005, the Company was advised that the OM Purchaser had settled an action brought by the former employer of certain of OM Purchaser’s owners and employees alleging violation of non-competition agreements. The settlement reportedly involved a cash payment and an agreement not to sell certain products for a period of one year. Based on an analysis of the facts and circumstances that existed at the end of fiscal 2005, and considering the guidance from Topic 5U of the SEC Rules and Regulations, “Gain Recognition on the Sale of a Business or Operating Assets to a Highly Leveraged Entity,” the gain is being recognized as cash is collected (as collection was not reasonably assured). Through December 31, 2005, all required payments had been made however, 6351352 Canada Inc. failed to make any subsequent, required payments under the note receivable until June 30, 2006, when we received a payment of $50. The Company reevaluated its options and concluded that its best course of action was to enforce its security and appoint a receiver over the assets of OM Video. As of December 31, 2007, the amount of the promissory note and contingent earn-out provision was approximately $659 which is net of $633 collected through receivership.

5. Income Taxes

In July 2006, the FASB issued Interpretation No. 48 (“FIN 48”), Accounting for Uncertainty in Income Taxes, which clarifies the accounting for uncertainty in income taxes recognized in the financial statements in accordance with FASB Statement No. 109, Accounting for Income Taxes. Under FIN 48, tax positions shall initially be recognized in the financial statements when it is more likely than not the position will be sustained upon examination by the tax authorities. Such tax positions shall initially and subsequently be measured as the largest amount of tax benefit that is greater than 50% likely of being realized upon ultimate settlement with the tax authority assuming full knowledge of the position and all relevant facts.

We adopted the provisions of FIN 48 on July 1, 2007. Upon adoption, we recognized a FIN 48 liability of $755 for permanent tax items. Included in the $755 liability was approximately $78 in interest and penalties related to unrecognized tax benefits. We also recognized $159 of temporary FIN 48 liability. After taking our SFAS 5 “Accounting for Contingencies” contingent liability balance of $618 from June 30, 2007 we posted a cumulative-effect adjustment of approximately $295, increasing our liability for unrecognized tax benefits and reducing the July 1, 2007 balance of retained earnings. The total liability for unrecognized tax benefits at July 1, 2007, including temporary tax differences, was approximately $914.

During our first and second fiscal quarters of 2008, we recorded approximately $45 and $125, respectively, related to unrecognized tax benefits that would favorably impact our effective tax rate if recognized. The total outstanding balance for liabilities related to unrecognized tax benefits at December 31, 2007 was $1,084 of which $99 was associated with interest and penalties. We account for interest expense and penalties for unrecognized tax benefits as part of our income tax provision.

We are subject to income taxes in both the United States and in certain non-U.S. jurisdictions. We estimate our current tax position together with our future tax consequences attributable to temporary differences resulting from differing treatment of items, such as deferred revenue, depreciation, and other reserves for tax and accounting purposes. These temporary differences result in deferred tax assets and liabilities. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income, prior year carryback, or future reversals of existing taxable temporary differences. To the extent we believe that recovery is not more likely than not, we establish a valuation allowance against these deferred tax assets. Significant management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities, and any valuation allowance recorded against our deferred tax assets. To the extent we establish a valuation allowance in a period, we must include and expense the allowance within the tax provision in the consolidated statement of operations. The reversal of a previously established valuation allowance results in a benefit for income taxes. As of December 31, 2007 we continued to be fully reserved against our net deferred tax assets which total to approximately $4.7 million.

6. Contingent Liability

In accordance with Statement of Financial Accounting Standards No. 5, Accounting for Contingencies, the Company accrued $1.8 million in its fiscal 2008 first quarter and an additional $115 in its fiscal 2008 second quarter, representing the probable amount that as of the date of the financial statements could be reasonably estimated of its liability, through trial, associated with the advancement of funds related to indemnification agreements with two former officers. As disclosed in July 2007, the Company was informed that two of its former officers have been indicted by the United States Attorney's Office for the District of Utah. The Company has been advised that the trial date has been moved to April 21, 2008. The Company is cooperating fully with the U.S. Attorney's office in this matter and has been advised that it is neither a target nor a subject of the investigation or indictment.

7. Bond for Preliminary Injunction

As explained in Part II. Legal Proceedings, and in reference to the case of ClearOne Communications, Inc. v. Andrew Chiang, et al, a preliminary injunction order was granted to ClearOne on October 30, 2007. In conjunction with the United States District Court's grant of ClearOne's motion for a preliminary injunction, the Courtissued an order establishing the amount for the bond to be posted by ClearOne. The bond was set in the amount of $907,909, placed with the clerk of the Court on November 6, 2007 and recorded as a deposit in the current assets section of the Company's balance sheet.

8. Recent Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board ("FASB") issued the Statement of Financial Accounting Standards ("SFAS") No. 157 "Fair Value Measurements." This statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value. SFAS 157 expands the disclosures about the use of fair value to measure assets and liabilities in interim and annual periods subsequent to initial recognition. The disclosures focus on the inputs used to measure fair value, the recurring fair value measurements using significant unobservable inputs and the effect of the measurement on earnings (or changes in net assets) for the period. The guidance in SFAS 157 also applies for derivatives and other financial instruments measured at fair value under Statement 133 "Accounting for Derivative Instruments and Hedging Activities" at initial recognition and in all subsequent periods. SFAS 157 is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. We are currently reviewing the requirements of SFAS 157, and at this point in time, have not determined what impact, if any, SFAS 157 will have on our results of operations and financial position.

In February 2007, the FASB issued SFAS 159 "The Fair Value Option for Financial Assets and Financial Liabilities." This statement permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This statement requires a business entity to report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. An entity may decide whether to elect the fair value option for each eligible item on its election date, subject to certain requirements described in the statement. SFAS 159 is effective for fiscal years beginning after November 15, 2007. We are currently reviewing the requirements of this statement and, at this point in time, have not determined the impact, if any, that this statement may have on our results of operations and financial position.

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

The following discussion should be read in conjunction with our unaudited condensed consolidated financial statements and related notes to condensed consolidated financial statements included in this Form 10-Q and our audited consolidated financial statements included in our Annual Report on Form 10-K for the year ended June 30, 2007 filed with the SEC and management's discussion and analysis contained therein. This discussion contains forward-looking statements based on current expectations that involve risks and uncertainties, such as our plans, objectives, expectations, and intentions, as set forth under "Disclosure Regarding Forward-Looking Statements." Our actual results and the timing of events could differ materially from those anticipated in these forward-looking statements as a result of various factors, including those set forth in the following discussion and under the caption "Risk Factors" in Part II, Item 1A, as well as other information found in the documents we file from time to time with the SEC. Unless otherwise indicated, all references to a year reflect our fiscal year that ends on June 30.

BUSINESS OVERVIEW

We are an audio conferencing products company. We develop, manufacture, market, and service a comprehensive line of high-quality audio conferencing products, which range from personal conferencing products to tabletop conferencing phones to premium and professionally installed audio systems. We also manufacture and sell conferencing furniture. We have a strong history of product innovation and plan to continue to apply our expertise in audio engineering to develop and introduce innovative new products and enhance our existing products. We believe the performance and reliability of our high-quality audio products create a natural communications environment, which saves organizations of all sizes time and money by enabling more effective and efficient communication.

Our products are used by organizations of all sizes to accomplish effective group communication. Our end-users range from some of the world's largest and most prestigious companies and institutions to small and medium-sized businesses, educational institutions, and government organizations as well as individual consumers. We sell our products to these end-users primarily through a network of independent distributors who in turn sell our products to dealers, systems integrators, and value-added resellers. The Company also sells products on a limited basis directly to dealers, systems integrators, value-added resellers, and end-users.

CRITICAL ACCOUNTING POLICIES

Our discussion and analysis of our results of operations and financial condition are based upon our condensed consolidated financial statements, which have been prepared in conformity with U.S. generally accepted accounting principles. We review the accounting policies used in reporting our financial results on a regular basis. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. We evaluate our assumptions and estimates on an ongoing basis and may employ outside experts to assist in our evaluations. We believe that the estimates we use are reasonable; however, actual results could differ from those estimates. We believe the following critical accounting policies affect our more significant assumptions and estimates that we used to prepare our condensed consolidated financial statements.

Revenue and Associated Allowances for Revenue Adjustments and Doubtful Accounts

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

We provide a right of return on product sales to distributors. Revenue from product sales to distributors is not recognized until the return privilege has expired, which approximates when product is sold-through to customers of the Company's distributors (dealers, system integrators, value-added resellers, and end-users) rather than when the product is initially shipped to a distributor. We evaluate, at each quarter-end, the inventory in the channel through information provided by certain of our distributors. The level of inventory in the channel will fluctuate up or down, each quarter, based upon our distributors' individual operations. Accordingly, each quarter-end revenue deferral is calculated and recorded based upon the underlying, estimated channel inventory at quarter-end. Although certain distributors provide certain channel inventory amounts, we make judgments and estimates with regard to the amount of inventory in the entire channel, for all customers and for all channel inventory items, and the appropriate revenue and cost of goods sold associated with those channel products. Although these assumptions and judgments regarding total channel inventory revenue and cost of goods sold could differ from actual amounts, we believe that our calculations are indicative of actual levels of inventory in the distribution channel. As of December 31, 2007, the Company deferred $5.0 million in revenue and $1.9 million in cost of goods sold related to products sold where return rights had not lapsed. The amounts of deferred cost of goods sold were included in consigned inventory. The following table details the amount of deferred revenue and cost of goods sold at each period end for the 21-month period ended December 31, 2007 (in thousands).

	Deferred Revenue	Deferred Cost of Goods Sold	Deferred Gross Profit
December 31, 2007	$ 4,980	$ 1,859	$ 3,121
September 30, 2007	5,875	2,149	3,726
June 30, 2007	4,872	2,115	2,757
March 31, 2007	5,111	2,265	2,846
December 31, 2006	4,711	2,166	2,545
September 30, 2006	5,249	2,541	2,708
June 30, 2006	5,871	2,817	3,054
March 31, 2006	5,355	2,443	2,912

We offer rebates and market development funds to certain of our distributors and direct dealers/resellers based upon volume of product purchased by them. We record rebates as a reduction of revenue in accordance with Emerging Issues Task Force ("EITF") Issue No. 00-22, "Accounting for Points and Certain Other Time-Based or Volume-Based Sales Incentive Offers, and Offers for Free Products or Services to Be Delivered in the Future." Beginning January 1, 2002, we adopted EITF Issue No. 01-9, "Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products)." We continue to record rebates as a reduction of revenue in the period revenue is recognized.

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

Purchased Intangibles

We assess the impairment of intangibles annually or whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Some factors we consider important which could trigger an impairment review include the following:

- Significant underperformance relative to projected future operating results;
- Significant changes in the manner of our use of the acquired assets or the strategy for our overall business; and
- Significant negative industry or economic trends.

If we determine that the carrying value of intangibles may not be recoverable based upon the existence of one or more of the above indicators of impairment, we would typically measure any impairment based on a projected discounted cash flow method using a discount rate determined by us to be commensurate with the risk inherent in our current business model. We evaluate intangibles for impairment at least annually.

We plan to conduct our annual impairment tests in the fourth quarter of every fiscal year, unless impairment indicators exist sooner. Screening for and assessing whether impairment indicators exist or if events or changes in circumstances have occurred, including market conditions, operating fundamentals, competition, and general economic conditions, requires significant judgment. Additionally, changes in the high-technology industry occur frequently and quickly. Therefore, there can be no assurance that a charge to operations will not occur as a result of future purchased intangible impairment tests.

Impairment of Long-Lived Asset

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

Accounting for Income Taxes

We are subject to income taxes in both the United States and in certain non-U.S. jurisdictions. We estimate our current tax position together with our future tax consequences attributable to temporary differences resulting from differing treatment of items, such as deferred revenue, depreciation, and other reserves for tax and accounting purposes. These temporary differences result in deferred tax assets and liabilities. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income, prior year carryback, or future reversals of existing taxable temporary differences. To the extent we believe that recovery is not more likely than not, we establish a valuation allowance against these deferred tax assets. Significant management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities, and any valuation allowance recorded against our deferred tax assets. To the extent we establish a valuation allowance in a period, we must include an expense for the allowance within the tax provision in the condensed consolidated statement of operations. The reversal of a previously established valuation allowance results in a benefit for income taxes. As of December 31, 2007, we continued to be fully reserved against our net deferred tax assets which total to approximately $4.6 million.

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

We account for our inventory on a first-in, first-out (“FIFO”) basis, and make appropriate adjustments on a quarterly basis to write down the value of inventory to the lower-of-cost or market.

In order to determine what, if any, inventory needs to be written down, we perform a quarterly analysis of obsolete and slow-moving inventory. In general, we write down our excess and obsolete inventory by an amount that is equal to the difference between the cost of the inventory and its estimated market value if market value is less than cost, based upon assumptions about future product life-cycles, product demand, or market conditions. Those items that are found to have a supply in excess of our estimated demand are considered to be slow-moving or obsolete and the appropriate reserve is made to write down the value of that inventory to its realizable value. These charges are recorded in cost of goods sold. At the point of the loss recognition, a new, lower-cost basis for that inventory is established and subsequent changes in facts and circumstances do not result in the restoration or increase in that newly established cost basis. If there were to be a sudden and significant decrease in demand for our products, or if there were a higher incidence of inventory obsolescence because of rapidly changing technology and customer

requirements, we could be required to increase our inventory allowances, and our gross profit could be adversely affected.

Share-Based Payment

Prior to June 30, 2005 and as permitted under the original SFAS No. 123, we accounted for our share-based payments following the recognition and measurement principles of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," as interpreted. Accordingly, no share-based compensation expense had been reflected in our statements of operations for unmodified option grants since (1) the exercise price equaled the market value of the underlying common stock on the grant date and (2) the related number of shares to be granted upon exercise of the stock option was fixed on the grant date.

In December 2004, the FASB issued SFAS No. 123R, "Share-Based Payment." SFAS No. 123R is a revision of SFAS No. 123. SFAS No. 123R establishes standards for the accounting for transactions in which an entity exchanges its equity instruments for goods or services. Primarily, SFAS No. 123R focuses on accounting for transactions in which an entity obtains employee services in share-based payment transactions. It also addresses transactions in which an entity incurs liabilities in exchange for goods or services that are based on the fair value of the entity's equity instruments or that may be settled by the issuance of those equity instruments.

Under SFAS No. 123R, we measure the cost of employee services received in exchange for an award of equity instruments based on the grant date fair value of the award (with limited exceptions). That cost will be recognized over the period during which an employee is required to provide service in exchange for the awards – the requisite service period (usually the vesting period). No compensation cost is recognized for equity instruments for which employees do not render the requisite service. Therefore, if an employee does not ultimately render the requisite service, the costs associated with the unvested options will not be recognized, cumulatively.

Effective July 1, 2005, we adopted SFAS No. 123R and its fair value recognition provisions using the modified prospective transition method. Under this transition method, stock-based compensation cost recognized after July 1, 2005 includes the straight-line basis compensation cost for (a) all share-based payments granted prior to July 1, 2005, but not yet vested, based on the grant date fair values used for the pro-forma disclosures under the original SFAS No. 123 and (b) all share-based payments granted or modified on or after July 1, 2005, in accordance with the provisions of SFAS No. 123R.

Under SFAS No. 123R, we recognize compensation cost net of an anticipated forfeiture rate and recognize the associated compensation cost for those awards expected to vest on a straight-line basis over the requisite service period. We use judgment in determining the fair value of the share-based payments on the date of grant using an option-pricing model with assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to, the expected life of the awards, the expected volatility over the term of the awards, the expected dividends of the awards, the risk-free interest rate of the awards, and an estimate of the amount of awards that are expected to be forfeited. If assumptions change in the application of SFAS No. 123R in future periods, the stock-based compensation cost ultimately recorded under SFAS No. 123R may differ significantly from what was recorded in the current period.

SEASONALITY

Our audio conferencing products revenue has historically been strongest during our second and fourth quarters. There can be no assurance that any historic sales patterns will continue and, as a result, sales for any prior quarter are not necessarily indicative of the sales to be expected in any future quarter.

ANALYSIS OF RESULTS OF OPERATIONS

Results of Operations for the three months or the second fiscal quarter (“2Q”) and six months or the first half of the fiscal year (“1H”) ended December 31, 2007 and 2006
The following table sets forth certain items from our unaudited condensed consolidated statements of operations (in thousands) for the three and six months ended December 31, 2007 and 2006, together with the percentage of total revenue which each such item represents:

CLEARONE COMMUNICATIONS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
(in thousands of dollars, except per share amounts)

	Three Months Ended				Six Months Ended			
	December 31, 2007		December 31, 2006		December 31, 2007		December 31, 2006	
		% of Revenue		% of Revenue		% of Revenue		% of Revenue
Product Revenue:	$ 10,787	100.0%	$ 10,107	100.0%	$ 20,229	100.0%	$ 19,518	100.0%
Cost of goods sold:								
Total cost of goods sold	4,414	40.9%	4,860	48.1%	8,714	43.1%	9,176	47.0%
Gross profit	6,373	59.1%	5,247	51.9%	11,515	56.9%	10,342	53.0%
Operating expenses:								
Marketing and selling	1,578	14.6%	1,789	17.7%	3,180	15.7%	3,707	19.0%
General and administrative	1,198	11.1%	688	6.8%	4,093	20.2%	1,497	7.7%
Research and product development	1,678	15.6%	1,855	18.4%	3,433	17.0%	3,934	20.2%
Total operating expenses	4,454	41.3%	4,332	42.9%	10,706	52.9%	9,138	46.8%
Operating income	1,919	17.8%	915	9.1%	809	4.0%	1,204	6.2%
Other income, net:								
Interest income	296	2.7%	283	2.8%	610	3.0%	590	3.0%
Other, net	15	0.1%	37	0.4%	43	0.2%	62	0.3%
Total other income (expense), net	311	2.9%	320	3.2%	653	3.2%	652	3.3%
Income (loss) from continuing operations before income taxes	2,230	20.7%	1,235	12.2%	1,462	7.2%	1,856	9.5%
(Provision) benefit from income taxes	-449	-4.2%	-155	-1.5%	-620	-3.1%	-136	-0.7%
Income (loss) from continuing operations	1,781	16.5%	1,080	10.7%	842	4.2%	1,720	8.8%

Income from discontinued operations		1	0.0%		4	0.0%		16	0.1%	41	0.2%
Net income (loss)	$	1,782	16.5%	$	1,084	10.7%	$	858	4.2%	$ 1,761	9.0%

Revenue

Revenue for 2Q 2008increased by 7%, or approximately $680,000compared to 2Q 2007. The 2Q 2008 increase was due primarily to growth in the Company's professional audio and partially due to growth in its tabletop conferencing products. The Company's professional audio and tabletop conferencing products collectively increased approximately $985,000 over 2Q 2007. The Company also expended about $95,000 less in marketing related programs (e.g. marketing development funds, rebates, etc.) in 2Q 2008 than in 2Q 2007. The 2Q 2008 increases were offset by an approximate $400,000 decline in the Company's premium, personal and conferencing furniture lines over the same period of 2007.

1H 2008revenue increased by 4%, or approximately $715,000compared to 1H 2007. The 1H 2008 revenue increase was led by growth in professional audio products sales which increased $1.2 million over 1H 2007. The Company also expended $200,000 less in marketing related programs (e.g. marketing development funds, rebates, etc.) in 1H2008 compared to 1H2007. These increases were offset by reduced premium, tabletop, personal, conferencing furniture and other product sales which together declined about $650,000 in 1H2008.

We evaluate, at each quarter-end, the inventory in the channel through information provided by certain of our distributors. The level of inventory in the channel will fluctuate up or down, each quarter, based upon our distributors' individual operations. Accordingly, each quarter-end revenue deferral is calculated and recorded based upon the underlying, estimated channel inventory at quarter-end. During 2Q 2008 and 2007, the net change in deferred revenue based on the net movement of inventory in the channel was a net recognition of $895,000 and $538,000 in revenue, respectively. In 1H 2008 and 2007, the net change in deferred revenue based on the net movement of inventory in the channel was a deferral of ($108,000) and recognition of $1.2 million in revenue, respectively.

Total revenues from sales outside of the United States accounted for 29% and 27% of total revenue for the three and six months ended December 31, 2007, respectively and 31% and 29% of total revenue for the three and six months ended December 31, 2006, respectively.

Costs of Goods Sold and Gross Profit

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

The Company's gross profit margin (GPM), gross profit as a percentage of sales, was 59% and 52% in 2Q 2008 and 2Q 2007, respectively. The 2Q 2008 GPM improvement was due largely to the favorable 2Q 2008 sales mix as the Company's highest margin professional audio conferencing products represented a larger portion of total revenue than in 2Q 2007. Additionally, 2Q 2008 GPM was positively impacted by lower inventory obsolescence reserve requirements and lower unfavorable manufacturing variances than in 2Q 2007.

GPM for 1H 2008 and 1H 2007 was 57% and 53%, respectively. The 1H 2008 GPM improvement was also due to the favorable sales mix as the Company's highest margin professional audio conferencing products represented a larger portion of total revenue than in 1H 2007. The 1H 2008 GPM improvements were partially offset by the 1Q 2008 increase in the Company's reserve for inventory obsolescence required to account for the increase in slow-moving inventory in addition to the 1Q 2008 unfavorable manufacturing variances.

Operating Expenses

2Q 2008 operating expenses were $4.5 million, an increase of about $120,000, or 3%, from $4.3 million for 2Q 2007. 1H 2008 operating expenses were $10.7 million, an increase of $1.6 million, or 17%, from $9.1 million for 1H 2007. The following is a more detailed discussion of expenses related to sales and marketing, general and administrative, and research and product development.

Sales and marketing expenses. Sales and Marketing (S&M) expenses include selling, customer service, and marketing expenses such as employee-related costs, allocations of overhead expenses, trade shows, and other advertising and selling expenses. 2Q 2008 S&M expenses decreased $200,000, or 12%, to $1.6 million compared to 2Q2007 S&M expenses of $1.8 million. As a percentage of revenues, 2Q 2008 and 2007 S&M expenses were 15% and 18%, respectively. The lower 2Q 2008 percentage can be attributed to the 7% higher revenues over 2Q 2007 in addition to lower S&M expenses primarily related to significantly lower payroll and related expenses of $400,000

associated with lower S&M headcount partially offset by an increase in advertising and related expenses to promote the Company’s differentiated value in targeted publications and trade shows. 1H 2008 S&M expenses decreased about $525,000, or 14%, to $3.2 million compared to 1H 2007 expenses of $3.7 million. As a percentage of revenues, 1H 2008 and 2007 marketing and selling expenses were 16% and 19%, respectively. The lower 1H 2008 percentage can be attributed the 4% higher revenues over 1H 2007 in addition to significantly lower payroll and related expenses and lower travel expenses, partially offset by an increase in advertising and related expenses.

General and administrative expenses. General and administrative (G&A) expenses include employee-related costs, professional service fees, allocations of overhead expenses, litigation costs, including costs associated with the SEC investigation and subsequent litigation, and corporate administrative costs, including finance and human resources. 2Q 2008 G&A expenses increased $510,000, or 74%, to $1.2 million compared to 2Q 2007 expenses of $688,000. 2Q 2008 and 2007 G&A expenses were 11% and 7% of sales, respectively. The 2Q 2008 increase was primarily due to higher legal fees of $465,000; $115,000 of which was related to increasing the Company's contingent liability reserve associated with the advancement of funds related to indemnification agreements with two former officers. The remaining $350,000 in 2Q 2008 legal fees were primarily related to the Company's lawsuit filed against WideBand et al. for, among other things, theft of intellectual property, more thoroughly described in Part II of this Form 10-Q.

1H 2008 G&A expenses increased $2.6 million, or 174%, to $4.1 million compared to 1H 2007 expenses of $1.5 million. 1H 2008 and 2007 G&A expenses were 20% and 8% of sales, respectively. The $2.6 million increase in 1H 2008 was primarily due to estimating and establishing a $1.8 million accrual for a contingent liability in 1Q 2008, which was subsequently increased by $115,000 in 2Q 2008. In accordance with Statement of Financial Accounting Standards No. 5, Accounting for Contingencies, the Company has accrued a total of $1.9 million in 1H 2008, the balance of which was $1.1 million at December 31, 2007, representing the probable amount that as of the date of the financial statements could be reasonably estimated of its liability, through trial, associated with the advancement of funds related to indemnification agreements with two former officers (please refer to "Legal Proceedings" in Part II of this Form 10-Q for additional information). Also, during 1H 2008 the Company incurred about $690,000 in legal fees, primarily related to its lawsuit against WideBand, et al. The Company also paid Edward D. Bagley, the Company's former director and Chairman the sum of $200,000 in 1Q 2008 upon his resignation and in consideration for his service as a director of the Company since 1994.

Research and product development expenses. Research and product development (R&D) expenses include research and development, product management, and engineering services, and test and application expenses, including employee-related costs, outside services, expensed materials, depreciation, and an allocation of overhead expenses. 2Q 2008 R&D expenses decreased to $1.7 million from $1.9 million in 2Q 2007. As a percentage of revenues, 2Q 2008 and 2007 R&D expenses were 16% and 18%, respectively. The 2Q 2008 decrease was due primarily to lower payroll and related expenses in addition to slightly lower R&D project expenses. 1H 2008 R&D expenses decreased $500,000, or 13%, to $3.4 million compared with 1H 2007 expenses of $3.9 million. The 1H 2008 decrease in R&D expenses was due primarily lower R&D project expenses as compared to 1H 2007 when the Company was heavily involved in working towards launching its next generation of professional product, Converge Pro.

Operating income. 2Q 2008 operating income increased to $1.9 million from $915,000 in 2Q 2007. The 2Q 2008 operating profit increase of $1.0 million was due mainly to the $1.1 million increase in gross profit. 1H 2008 and 2007 operating income was $809,000 and $1.2 million, respectively. The 1H 2008 operating income decrease of approximately $400,000 was due mainly to the $1.9 million contingent liability charged to general & administrative expenses associated with the advancement of funds under the indemnification agreements with two former officers, partially offset by the 1H 2008 $1.2 million gross profit increase.

Other income, net. Other income (expense), net, includes interest income, interest expense, capital gains, gain (loss) on the disposal of assets, and currency gain (loss). 2Q 2008 other income was $311,000 or slightly lower than other income of $320,000 in 2Q 2007. Other income in 1H 2008 and 2007 was about even at approximately $650,000 in each respective period.

Income from continuing operations before income taxes. 2Q 2008 income from continuing operations was $1.8 million, an increase of $700,000 from $1.1 million in 2Q 2007. As a percentage of revenues, 2Q 2008 and 2007 income from continuing operations was 16.5% and 10.7%, respectively. 1H 2008 income from continuing operations

was $842,000 compared to $1.7 million in 1H 2007. As a percentage of revenues, 1H 2008 and 2007 income from continuing operations was 4.2% and 8.8%, respectively. The lower income from continuing operations in 1H 2008 was due to $1.9 million contingent liability charged to general & administrative expenses associated with the advancement of funds under indemnification agreements with two former officers.

Income (loss) from discontinued operations, net of tax.   During 2Q 2008 and 2007 we recorded income from discontinued operations, net of tax of $1,000 and $4,000, respectively. The 2Q 2008 income was exclusively related to funds received through the receivership of OM Video. The 2Q 2007 income of $4,000 was related to income from the discontinued operations of the document and educational camera product line. For 1H 2008 and 2007 income from discontinued operations, net of tax was $16,000 and $41,000, respectively.

Net income and earnings per share. 2Q 2008 net income was $1.8 million, an increase of $700,000 from $1.1 million in 2Q 2007. As a percentage of revenues, 2Q 2008 and 2007 net income was 16.5% and 10.7%, respectively. The 2Q 2008 increase was due to the 7% increase in revenue, augmented by the 21% increase in gross margins. 1H 2008 net income was $858,000 compared to $1.8 million in 1H 2007. As a percentage of revenues, 1H 2008 and 2007 net income was 4.2% and 9.0%, respectively. The $900,000 1H 2008 decrease was due largely to the establishment of a $1.9 million accrual for the contingent liability representing the probable amount that as of the date of the financial statements could be reasonably estimated of the Company's liability, through trial, associated with the advancement of funds related to indemnification agreements with two former officers. The income tax provision rates in 2Q and 1H 2008 were 20.1% and 42.4%, respectively, compared to 12.6% and 7.3% in 2Q and 1H 2007, respectively. The increase in the 2008 tax rates were due largely to the Company's adoption of FIN 48 Accounting for Uncertainty in Income Taxes in addition to recognition of tax on the undistributed earnings of the Company's foreign subsidiaries.

Diluted 2Q 2008 earnings per share (EPS) were 80% higher than in 2Q 2007. Diluted 1H 2008 (EPS) were 46% lower than in 1H 2007. The significant 2Q 2008 EPS improvement was due to the $700,000 increase in net income augmented by approximately 1 million fewer diluted shares outstanding due to the Company's December 2006 tender offer and open market share repurchases. The 46% decrease 1H 2008 decrease in EPS over the same period of the prior year was due primarily to the Company's 1H 2008 establishment of a $1.9 million accrual for a contingent liability previously discussed partially offset by the approximate 1 million lower diluted shares in 1H2008 from 1H 2007.

2Q and 1H 2008 diluted weighted shares outstanding were 10,941,491 and 11,012,239, respectively. 2Q and 1H 2007 diluted weighted shares outstanding were 11,957,706 and 12,100,794, respectively.

LIQUIDITY AND CAPITAL RESOURCES

As of December 31, 2007, our cash and cash equivalents were approximately $3.0 million and our marketable securities were approximately $19.7 million, which represented a slight overall increase of approximately $37,000 in our balances from June 30, 2007 which had cash and cash equivalents of approximately $2.8 million and marketable securities of approximately $19.9 million.

Net cash provided by operating activities was $1.5 million for the six months ended December 31, 2007, an increase of $230,000 from the net cash provided by operating activities of $1.3 million for the six months ended December 31, 2006. The year-over-year increase can be attributed to the cash provided by changes in working capital of about $1.3 million, partially offset by the decrease in net income from continuing operations of $878,000 and lower depreciation and stock-based compensation which collectively decreased $176,000 from 1H2006.

Net cash flows (used in) investing activities were ($212,000) for the six months ended December 31, 2007, a decrease of $4.3 million from the net cash flows provided by investing activities of $4.1 million for the six months ended December 31, 2006. The change was primarily attributable to the sale of $4.0 million in marketable securities in 1H 2007 used to fund a December 2006 repurchase of tendered shares of common stock in addition to the 1H 2007 $559,000 net cash provided by discontinued investing operations related to the sale of the Company's educational camera product line partially offset by $193,000 lower 1H 2008 property and equipment purchases.

Net cash (used in) financing activities for the six months ended December 31, 2007 totaled ($1.1 million) which was approximately $3.7 million less than the ($4.7 million) (used in) financing activities during 1H 2007. The 1H 2008 decrease was primarily related to the Company's 1H 2007 repurchase of 1.1 million shares of common stock in December 2006.

Additionally in 1H 2008, we paid approximately $1.1 million in income taxes and reduced our July 1, 2007 balance of retained earnings by $295 upon our adoption of FASB issued Interpretation No. 48 ("FIN 48"), Accounting for Uncertainty in Income Taxes as discussed in note 5. During 1H 2007 we recorded $1.1 million in non-cash financing activities related to leasehold improvements to our new headquarters, the majority of which was paid as an incentive by the lessor as part of the lease agreement. These improvements are being accounted for in accordance with FASB Technical Bulletin No. 88-1, Issues Relating to Accounting for Leases, which states among other things that landlord incentives which fund leasehold improvements should be recorded as deferred rent and amortized as reductions to lease expense over the term of the lease.

Management believes that future income from operations and effective management of working capital will provide the liquidity needed to finance growth plans. In addition to capital expenditures, the Company plans to use cash during the remainder of fiscal 2008 for selective infusions of technological, marketing or product manufacturing rights to broaden the Company's product offerings; for continued share repurchases; and if available for a reasonable price, acquisitions that may strategically fit the Company's business and are accretive to performance.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our exposure to market risk has not changed materially since June 30, 2007.

Item 4. CONTROLS AND PROCEDURES

We maintain disclosure controls and procedures designed to ensure that information required to be disclosed in our reports filed under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), is recorded, processed, summarized, and reported within the required time periods and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Principal Financial Officer, as

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

As required by Rule 13a-15 under the Exchange Act, we have completed an evaluation, under the supervision and with the participation of our management, including the Chief Executive Officer and the Chief Financial Officer, of the effectiveness and the design and operation of our disclosure controls and procedures as of December 31, 2007. Based upon this evaluation, our management, including the Chief Executive Officer and the Chief Financial Officer, has concluded that our disclosure controls and procedures were effective as of December 31, 2007.

There were no changes in the Company's internal controls over financial reporting that occurred during the quarter ended December 31, 2007, that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

PART II - OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS

Legal Proceedings. In addition to the legal proceedings described below, we are also involved from time to time in various claims and other legal proceedings which arise in the normal course of business. Such matters are subject to many uncertainties and outcomes that are not predictable. However, based on the information available to us as of February 8, 2008 and after discussions with legal counsel, we do not believe any such other proceedings will have a material, adverse effect on our business, results of operations, financial position, or liquidity, except as described below.

Theft of Intellectual Property and Copyright Complaints. In January 2007, the Company filed a lawsuit in the Third Judicial District Court, Salt Lake County, State of Utah against WideBand Solutions, Inc. and two of its principals, one former employee named Dr. Jun Yang, and one previously affiliated with an entity which sold certain assets to the Company (the "Intellectual Property Case"). ClearOne also brought claims against Biamp Systems Corporation, Inc. The matter was subsequently removed to federal court, the United States District Court, District of Utah, Central Division. The case is styled ClearOne Communications, Inc. v. Jun Yang, et. al. Civil No. 2:07-co-37 TC. The Complaint brings claims against different combinations of the defendants for, among other things, misappropriation of certain trade secrets, breach of contract, conversion, unjust enrichment and intentional interference with business and contractual relations, primarily in relation to certain algorithms and computer code. The relief being sought by the Company includes an order enjoining the defendants from further use of the Company's trade secrets and an award consisting of, among other things, compensation and damages related to the unjust enrichment of the defendants. The Court subsequently granted leave to add a third WideBand principal as a defendant to the case. In August 2007, the Company filed a motion for a preliminary injunction in the Intellectual Property Case, in the United States District Court, District of Utah, seeking to enjoin Wideband Solutions, Inc. from licensing certain technology the Company believes constitutes its intellectual property and trade secrets to Harman Music Group, Inc. On September 13, 2007, the court in the Intellectual Property Case granted ClearOne leave to add Harman and a former ClearOne employee working for Harman as defendants in that case. For procedural reasons, these claims against Harman and the Harman employee were refiled in Utah state court, the Third Judicial District Court for Salt Lake County, on September 18, 2007 (the "Harman Case"). Like the Intellectual Property Case, the Harman Case also brings claims related to the theft and misuse of ClearOne's confidential and trade secret information. On October 30, 2007, the Chief Judge of the United States District Court in the Intellectual Property Case, the Honorable Tena Campbell, issued a Memorandum Decision and Order (the "Injunction Order"). The Injunction Order "GRANTS ClearOne's motion for a Preliminary Injunction," and orders that "Dr. Yang, as well as his agents, servants, officers, employees, entities and those acting under his direction and control, are hereby enjoined from working on or delivering any computer code – either source code or object code – to Harman until the completion of the trial." In reaching its decision, the Court found that Dr. Yang was subject to a valid and enforceable Confidentiality, Non-Competition, and Invention Assignment Agreement (the "NDA"), and that ClearOne had demonstrated "a substantial likelihood that ClearOne will succeed on its claims that Dr. Yang violated the NDA" and derived the code that WideBand was attempting to license to Harman from code

belonging to ClearOne. The Injunction Order is Docket Entry 572. On November 5, 2007, the Honorable Tena Campbell issued an order establishing the amount for the bond to be posted by ClearOne in conjunction with the Court's grant of ClearOne's motion for a preliminary injunction. The bond was set in the amount of $907,909. In accordance with the order, the Company placed the bond with the clerk of the Court on November 6, 2007. On October 29, 2007, the Company filed a second action against WideBand and the same three principals named as defendants in the Intellectual Property Case, this time alleging copyright infringement, vicarious copyright infringement, and contributory copyright infringement (the "Copyright Case"). The claims in the Copyright Case arise out of a copyright issued to the Company for the same intellectual property, including the algorithms and computer code that is the subject of the claims in the Intellectual Property Case. The relief being sought by the Company includes an order enjoining the defendants from further use of the Company's copyrighted material, and an award consisting of, among other things, compensation and damages related to the copyright infringement. These litigations are subject to all of the risks and uncertainties of litigation and there can be no assurance as to the probable result of the litigations.

Former Officer Indemnification. In July 2007, the Company was advised that the United States Attorney's Office for the District of Utah indicted two former officers of the Company. The Company has been advised that a trial date has been set for April 21, 2008. The Company is cooperating fully with the U.S. Attorney's office in this matter and has been advised that it is neither a target nor a subject of the investigation or indictment. By virtue of certain provisions of the Company's Articles of Incorporation, Bylaws and indemnification agreements with these former officers, the Company has a direct financial obligation to advance funds related to the indemnification agreements with each former officer for any liability and for all reasonable attorney's fees and costs incurred in defending against the charges brought by the United States Attorney. In accordance with Statement of Financial Accounting Standards No. 5, Accounting for Contingencies, ClearOne has accrued a total of $1.9 million in the first half of its fiscal 2008, representing the probable amount that as of the date of the financial statements could be reasonably estimated of its liability, through trial, associated with the advancement of funds related to the indemnification agreements. The $1.9 million accrual is management's best estimate of the Company's liability as of the date of the issuance of its financial statements. In accordance with SFAS 5, the Company will adjust its contingent liability, as necessary, to reflect the probable amount of its liability that can be reasonably estimated. The Company's actual liability may be higher or lower than management's estimate upon final resolution of the matter.

Item 1A. RISK FACTORS

Investors should carefully consider the risks described below. The risks described below are not the only ones we face, and there are risks that we are not presently aware of or that we currently believe are immaterial that may also impair our business operations. Any of these risks could harm our business. The trading price of our common stock could decline significantly due to any of these risks and investors may lose all or part of their investment. In assessing these risks, investors should also refer to the other information contained or incorporated by reference in this Quarterly Report on Form 10-Q, including our December 31, 2007 unaudited condensed consolidated financial statements and related notes.

Risks Relating to Our Business

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

As described in more detail in the section entitled "Competition," in our Annual Report on Form 10-K for the year ended June 30, 2007, the markets for our products and services are characterized by intense competition and pricing pressures and rapid technological change. We compete with businesses having substantially greater financial, research and development, manufacturing, marketing, and other resources. If we are not able to continually design, manufacture, and successfully introduce new or enhanced products or services that are comparable or superior to those provided by our competitors and at comparable or better prices, we could experience pricing pressures and reduced sales, gross profit, profits, and market share, each of which could have a materially adverse effect on our business.

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

Orders from our distributors and other distribution participants are based on demand from end-users. Prospective end-user demand is difficult to measure. This means that our revenues in any fiscal quarter could be adversely impacted by low end-user demand, which could in turn negatively affect orders we receive from distributors, dealers, systems integrators and value-added resellers. Our expectations for both short- and long-term future net revenues are based on our own estimates of future demand.

Revenues for any particular time period are difficult to predict with any degree of certainty. We usually ship products within a short time after we receive an order; so consequently, unshipped backlog has not been a good indicator of

future revenues. We believe that the current level of backlog will fluctuate dependent in part on our ability to forecast revenue mix and plan our manufacturing accordingly. A significant portion of our orders are received in the last month of the quarter. We budget the amount of our expenses based on our revenue estimates. If our estimates of sales are not accurate and we experience unforeseen variability in our revenues and operating results, we may be unable to adjust our expense levels accordingly and our gross profit and results of operations will be adversely affected. Higher inventory levels or stock shortages may also result from difficulties in estimating customer demand.

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

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

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

We have, in the past, and may again experience, technical difficulties and delays with the development and introduction of new products. Many of the products we develop contain sophisticated and complicated circuitry, software and components, and utilize manufacturing techniques involving new technologies. Potential difficulties in the development process that could be experienced by us include difficulty in:

- meeting required specifications and regulatory standards;
- meeting market expectations for performance;
- hiring and keeping a sufficient number of skilled developers;
- obtaining prototype products at anticipated cost levels;
- having the ability to identify problems or product defects in the development cycle; and
- achieving necessary manufacturing efficiencies.

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

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

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

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

Reporting of channel inventory by certain distributors.

We defer recognition of revenue from product sales to distributors until the return privilege has expired, which approximates when product is sold-through to customers of our distributors. We evaluate, at each quarter-end, the inventory in the channel through information provided by certain of our distributors. We use this information along

with our judgment and estimates to determine the amount of inventory in the entire channel, for all customers and for all inventory items, and the appropriate revenue and cost of goods sold associated with those channel products. We cannot guarantee that the third party data, as reported, or that our assumptions and judgments regarding total channel inventory revenue and cost of goods sold, will be accurate. We periodically audit a limited number of distributors.

We depend on an outsourced manufacturing strategy.

In August 2005, we entered into a manufacturing agreement with a manufacturing services provider, to manufacturer substantially all the products that were previously manufactured at our Salt Lake City, Utah manufacturing facility. Subsequently, we entered into agreements with offshore manufacturers who also manufacture several of our product lines. If these manufacturers experience difficulties in obtaining sufficient supplies of components, component prices significantly exceed anticipated costs, an interruption in their operations, or otherwise suffer capacity constraints, we would experience a delay in shipping these products which would have a negative impact on our revenues. Should there be any disruption in services due to natural disaster, economic or political difficulties, quarantines, transportation restrictions, acts of terror, or other restrictions associated with infectious diseases, or other similar events, or any other reason, such disruption would have a material adverse effect on our business. Operating in the international environment exposes us to certain inherent risks, including unexpected changes in regulatory requirements and tariffs, and potentially adverse tax consequences, which could materially affect our results of operations. Currently, we have no second source of manufacturing for some of our products.

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

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

We rely on our suppliers to provide us with materials that are compliant with environmental laws and regulations such as Restrictions on Hazardous Substances (RoHS) rules in Europe, and WEEE directives, among others. We also rely on our contract manufacturer's whose processes must be maintained in accordance with such regulations. We work with our suppliers and contract manufacturers for ongoing compliance with regulations and attempt to identify possible discrepancies as quickly as possible; however, one or more of our products could be in violation of a regulation due to a supplier and/or contract manufacturer making a non-compliant material or process change which could result in a material adverse effect on our operating results.

We depend on an outsourced fulfillment strategy.

In January 2008, we commenced the use of a third party supply chain management ("SCM") firm who manages the receiving, storing, picking, packing, shipping and inventory management of the majority of the Company's products. If the SCM firm experiences difficulties and/or interruptions in their operations preventing them from adequately fulfilling the Company's products, we would experience a delay in shipping product to our customers which would negatively impact on our revenues. Should there be any disruption in the SCM's services due to natural disaster, economic or political difficulties, quarantines, transportation restrictions, acts of terror or other similar events, such disruption would have a material adverse effect on our business. Currently, we have no second source of fulfillment of the majority of our products.

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

Our industry is subject to rapid and frequent technological innovations that could render existing technologies in our products obsolete and thereby decrease market demand for such products. If any of our products become slow-moving or obsolete and the recorded value of our inventory is greater than its market value, we will be required to write down

the value of our inventory to its fair market value, which would adversely affect our results of operations. In limited circumstances, we are required to purchase components that our outsourced manufacturers use to produce and assemble our products. Should technological innovations render these components obsolete, we will be required to write down the value of this inventory, which could adversely affect our results of operations.

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

We currently rely primarily on a combination of trade secrets, copyrights, trademarks, patents, patents pending, and nondisclosure agreements to establish and protect our proprietary/intellectual property rights in our products. No assurances can be given that others will not independently develop similar technologies, or duplicate or design around aspects of our technology. In addition, we cannot assure that any patent or registered trademark owned by us will not be invalidated, circumvented or challenged, or that the rights granted thereunder will provide competitive advantages to us. Litigation may be necessary to enforce our intellectual property rights. We believe our products and other proprietary rights do not infringe upon any proprietary rights of third parties; however, we cannot assure that third parties will not assert infringement claims in the future. Our industry is characterized by vigorous protection of intellectual property rights. Such claims and the resulting litigation are expensive and could divert management's attention, regardless of their merit. In the event of a claim, we might be required to license third-party technology or redesign our products, which may not be possible or economically feasible.

We currently hold a number of patents. To the extent that we have patentable technology for which we have not filed patent applications, others may be able to use such technology or even gain priority over us by patenting such technology themselves.

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

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

- unexpected changes in, or the imposition of, additional legislative or regulatory requirements;
- unique environmental regulations;
- fluctuating exchange rates;
- tariffs and other barriers;
- difficulties in staffing and managing foreign sales operations;
- import and export restrictions;
- greater difficulties in accounts receivable collection and longer payment cycles;
- potentially adverse tax consequences;
- potential hostilities and changes in diplomatic and trade relationships; and
- disruption in services due to natural disaster, economic or political difficulties, quarantines, transportation, or other restrictions associated with infectious diseases.

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

Wedepend on our ability to hire and retain qualified key and highly-skilled employees to manage, research and develop, market, and service new and existing products. Competition for such key and highly-skilled employeesis intense, and we may not be successful in attracting or retaining such personnel. To succeed, we must hire and retain employees who are highly skilled in the rapidly changing communications and Internet technologies. Individuals who have the skills and can perform the services we need to provide our products and services are in great demand. Because the competition for qualified employees in our industry is intense, hiring and retaining employees with the

skills we need is both time-consuming and expensive. We might not be able to hire enough skilled employees or retain the employees we do hire. In addition, provisions of the Sarbanes-Oxley Act of 2002 and related rules of the SEC impose heightened personal liability on some of our key employees. The threat of such liability could make it more difficult to identify, hire and retain qualified key and highly-skilled employees. We have relied on our ability to grant stock options as a means of recruiting and retaining key employees. Recent accounting regulations requiring the expensing of stock options will impair our future ability to provide these incentives without incurring associated compensation costs. Our inability to hire and retain employees with the skills we seek could hinder our ability to sell our existing products, systems, or services or to develop new products, systems, or services with a consequent adverse effect on our business, results of operations, financial position, or liquidity.

Our reliance on third-party technology or license agreements.

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

We may have difficulty in collecting outstanding receivables.

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

Interruptions to our business could adversely affect our operations.

As with any company, our operations are at risk of being interrupted by earthquake, fire, flood, and other natural and human-caused disasters, including disease and terrorist attacks. Our operations are also at risk of power loss, telecommunications failure, and other infrastructure and technology based problems. To help guard against such risks, we carry business interruption loss insurance to help compensate us for losses that may occur.

Risks Relating to Our Company

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

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

- statements or changes in opinions, ratings, or earnings estimates made by brokerage firms or industry analysts relating to the market in which we do business or relating to us specifically;
- disparity between our reported results and the projections of analysts;
- the shift in sales mix of products that we currently sell to a sales mix of lower-gross profit product offerings;
- the level and mix of inventory levels held by our distributors;
- the announcement of new products or product enhancements by us or our competitors;
- technological innovations by us or our competitors;
- success in meeting targeted availability dates for new or redesigned products;
- the ability to profitably and efficiently manage our supplies of products and key components;
- the ability to maintain profitable relationships with our customers;
- the ability to maintain an appropriate cost structure;
- quarterly variations in our results of operations;
- general consumer confidence or general market conditions or market conditions specific to technology industries;
- domestic and international economic conditions;
- the adoption of the new accounting standard, SFAS No. 123R, “Share-Based Payments,” which requires us to record compensation expense for certain options issued before July 1, 2005 and for all options issued or modified after June 30, 2005;
- our ability to report financial information in a timely manner; and
- the markets in which our stock is traded.

We have previously identified material weaknesses in our internal controls.

In our Form 10-K for the fiscal year ending June 30, 2006, we reported and identified a material weakness in our internal controls. Although we believe we have remedied this weakness through the commitment of considerable resources, we are always at risk that any future failure of our own internal controls or the internal control at any of our outsourced manufacturers or partners could result in additional reported material weaknesses. Any future failures of our internal controls could have a material impact on our market capitalization, results of operations, or financial position, or have other adverse consequences.

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

Items 2(a) and (b) are not applicable

(c) Stock Repurchases

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1)	Maximum Number (or Approximate Dollar Value) of Shares that May by Purchased Under the Plans or Programs (1)
October 1, 2007- October 31, 2007	85,555	$6.74	85,555	$2,482,511
November 1, 2007 – November 30, 2007	56,969	$5.70	56,969	$2,158,034
December 1, 2007 – December 31, 2007	37,999	$5.19	37,999	$1,960,962
Total	180,523		180,523	

(1) On August 30, 2007, the Company announced that its Board of Directors had approved a stock buy-back program to purchase up $3,625,000 of the Company’s common stock over the next 12 months in open market and private block transactions. All repurchased shares will be immediately retired. The stock buy-back program will expire in August 30, 2008.

Item 3. DEFAULTS UPON SENIOR SECURITIES

Not Applicable.

Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

On November 20, 2007 at the annual meeting, shareholders of the Company approved the following matters submitted to them for consideration:

Elected the following as directors of the Company:

	FOR	WITHHELD
Brad R. Baldwin	8,819,091	1,163,033
Zeynep “Zee” Hakimoglu	8,899,674	1,082,450

Larry R. Hendricks	8,820,363	1,161,761
Scott M. Huntsman	8,820,241	1,161,883

Approved the ClearOne Communications, Inc. 2007 Equity Incentive Plan as follows:

FOR	AGAINST	ABSTAIN	BROKER NON-VOTES
3,020,748	1,792,560	981,418	4,187,398

Item 5. OTHER INFORMATION

Not Applicable.

Item 6. EXHIBITS

Exhibit No.	SEC Ref. No.	Title of Document	Location
31.1	31	Section 302 Certification of Chief Executive Officer	This filing
31.2	31	Section 302 Certification of Chief Financial Officer	This filing
32.1	32	Section 906 Certification of Chief Executive Officer	This filing
32.2	32	Section 906 Certification of Chief Financial Officer	This filing

SIGNATURES

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

CLEARONE COMMUNICATIONS, INC.

February 11, 2008 By: /s/ Zeynep Hakimoglu
Zeynep Hakimoglu
President and Chief Executive Officer
(Principal Executive Officer)

February 11, 2008 By: /s/ Greg A. LeClaire
Greg A. LeClaire
Chief Financial Officer
(Principal Financial and Accounting Officer)

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