ALTIGEN COMMUNICATIONS, INC.

State of Incorporation: Delaware

670 N McCarthy Blvd Suite 200
Milpitas, CA 95035
(408) 597-9000
www.altigen.com

SIC Code: 3661

QUARTERLY REPORT
For the quarterly period ended June 30, 2019
(the "Reporting Period")

The number of shares outstanding of our common stock, par value $0.001 per share ("common stock"), is 22,887,246 shares as of June 30, 2019.

The number of shares outstanding of our common stock was 22,842,246 shares as of September 30, 2018.

Indicate by check mark whether the company is a shell company (as defined in Rule 405 of the Securities Act of 1933 and Rule 12b-2 of the Exchange Act of 1934):

Yes: ☐ No: ☒

Indicate by check mark whether the company's shell status has changed since the previous reporting period:
Yes: ☐ No: ☒

Indicate by check mark whether a change in control of the company has occurred over this reporting period:
Yes: ☐ No: ☒

For more information:
www.OTCQB.com Ticker: ATGN
or
www.altigen.com

ALTIGEN COMMUNICATIONS, INC.
QUARTERLY REPORT
FOR THIRD QUARTER ENDED JUNE 30, 2019

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FORWARD-LOOKING STATEMENTS

Certain statements made in this Quarterly Report are "forward-looking statements" regarding the plans and objectives of management for future operations and market trends and expectations. Such statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. The forward-looking statements included herein are based on current expectations that involve numerous risks and uncertainties. Our plans and objectives are based, in part, on assumptions involving the continued expansion of our business. Assumptions relating to the foregoing involve judgments with respect to, among other things, future economic, competitive and market conditions and future business decisions, all of which are difficult or impossible to predict accurately and many of which are beyond our control. Although we believe that our assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate and, therefore, there can be no assurance that the forward-looking statements included in this report will prove to be accurate. In light of the significant uncertainties inherent in the forward-looking statements included herein, the inclusion of such information should not be regarded as a representation by us or any other person that our objectives and plans will be achieved.

These forward-looking statements rely on assumptions, estimates and predictions that could be inaccurate and that are subject to risks and uncertainties that could cause actual results to differ materially from expected results. We cannot guarantee future results, outcomes, levels of activity, performance, or achievements, and there can be no assurance that our expectations, intentions, anticipations, beliefs, or projections will result or be achieved or accomplished. Forward-looking statements speak only as of the date of this report. Except as required by applicable law, we undertake no obligation to publicly update or revise any forward-looking statements, or to update the reasons actual results could differ significantly from those anticipated in these forward-looking statements, even if new information becomes available in the future.

Item 1. Exact Name of the Issuer and the Address of its Principal Executive Offices.

Exact name of issuer:	Altigen Communications, Inc.
Principal Executive Offices:	670 N McCarthy Blvd Suite 200 Milpitas, CA 95035 Telephone: (408) 597-9000 Facsimile: (408) 597-2020 Website: www.altigen.com
Investor Relations Officer:	Carolyn David, Vice President of Finance 670 N McCarthy Blvd Suite 200 Milpitas, CA 95035 Telephone: (408) 597-9000 Email Address: ir@altigen.com

Item 2. Shares Outstanding.

The following tables set forth the number of shares outstanding for each class of securities authorized as of the dates set forth below:

As of June 30, 2019					
Class	Number of Shares Authorized	Number of Shares Outstanding	Freely Tradable Shares (Public Float) (1)	Total Number of Beneficial Stockholders (2)	Total Number of Stockholders of Record
Common Stock	50,000,000	22,887,246	16,625,048	1,515	80
Preferred Stock	5,000,000	—	—	—	—
As of September 30, 2018					
Class	Number of Shares Authorized	Number of Shares Outstanding	Freely Tradable Shares (Public Float) (1)	Total Number of Beneficial Stockholders (2)	Total Number of Stockholders of Record
Common Stock	50,000,000	22,842,246	16,642,035	1,426	80
Preferred Stock	5,000,000	—	—	—	—
As of September 30, 2017					
Class	Number of Shares Authorized	Number of Shares Outstanding	Freely Tradable Shares (Public Float) (1)	Total Number of Beneficial Stockholders (2)	Total Number of Stockholders of Record
Common Stock	50,000,000	22,798,683	16,641,672	1,407	79
Preferred Stock	5,000,000	—	—	—	—

(1) For purposes of this calculation only, shares of common stock held by each of Altigen's directors and officers on the given date and by each person who Altigen knows beneficially owned 5% or more of the outstanding common stock on that date have been excluded in that such persons may be deemed to be affiliates.

(2) Estimate based on beneficial share range analysis, received from Broadridge Financial Solutions, Inc. There are greater than 100 beneficial shareholders owning at least 100 shares of the Company's common stock.

Item 3. Interim Financial Statements.

ALTIGEN COMMUNICATIONS, INC.
CONSOLIDATED BALANCE SHEETS
(amounts in thousands, except shares and per share amounts)

	June 30, 2019 (Unaudited)	September 30, 2018 (1)
ASSETS		
Current assets:		
Cash, cash equivalents and restricted cash	$ 4,614	$ 3,080
Trade receivables, net	446	531
Other receivables	—	557
Prepaid expenses and other current assets	318	1,065
Total current assets	5,378	5,233
Property and equipment, net	93	78
Capitalized software development costs, net	961	327
Deferred tax assets	8,713	8,713
Long-term deposit	36	11
Total assets	$ 15,181	$ 14,362
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 99	$ 62
Accrued compensation and benefits	177	284
Revolving line of credit	324	719
Accrued expenses	413	822
Deferred revenue, short-term	1,004	1,041
Total current liabilities	2,017	2,928
Deferred revenue, long-term	299	221
Deferred rent, long-term	—	—
Total liabilities	2,316	3,149
Commitments and contingencies (Note 3)		
Stockholders' equity:		
Convertible preferred stock, $0.001 par value; Authorized—5,000,000 shares; Issued and outstanding—none at June 30, 2019 and September 30, 2018	—	—
Common stock, $0.001 par value; Authorized—50,000,000 shares; Issued and outstanding—22,887,246 shares at June 30, 2019 and 22,842,246 shares at September 30, 2018	25	25
Treasury stock at cost—1,918,830 shares at June 30, 2019 and September 30, 2018	(1,565)	(1,565)
Additional paid-in capital	71,882	71,857
Accumulated deficit	(57,477)	(59,104)
Total stockholders' equity	12,865	11,213
Total liabilities and stockholders' equity	$ 15,181	$ 14,362

(1) The information in this column was derived from the Company's audited consolidated financial statements as of and for the year ended September 30, 2018.

The accompanying notes are an integral part of the consolidated financial statements.

ALTIGEN COMMUNICATIONS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited; amounts in thousands, except per share amounts)

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	**2018**	**2019**	**2018**
Net revenue:				
Hosted services	$ 1,591	$ 1,256	$ 4,595	$ 3,612
Service support programs	693	768	2,173	2,427
Software	191	484	857	1,157
Professional services and other	176	45	345	131
Total net revenue	2,651	2,553	7,970	7,327
Cost of revenue:				
Hosted services	487	393	1,400	1,146
Software	27	19	51	34
Professional services and other	1	(1)	4	13
Total cost of revenue	515	411	1,455	1,193
Gross profit	2,136	2,142	6,515	6,134
Operating expenses:				
Research and development	675	733	1,935	2,183
Sales and marketing	523	544	1,563	1,551
General and administrative	367	429	1,411	1,242
Litigation (1)	—	342	13	342
Total operating expenses	1,565	2,048	4,922	5,318
Income from operations	571	94	1,593	816
Interest and other income (expense), net				
Interest and other income, net	48	5	67	14
Interest expense	(5)	(6)	(15)	(14)
Total interest and other income (expense), net	43	(1)	52	—
Income before income taxes	614	93	1,645	816
Provision for income taxes	2	1	18	3
Net income	$ 612	$ 92	$ 1,627	$ 813
Net income per share:				
Basic	$ 0.03	$ 0.00	$ 0.07	$ 0.04
Diluted	$ 0.02	$ 0.00	$ 0.06	$ 0.03
Shares used to compute net income per share:				
Basic	22,887	22,833	22,865	22,812
Diluted	25,876	25,047	25,759	24,731

(1) Refer to Note 3, "Commitments and Contingencies" of the Consolidated Financial Statements and Item 5, "Legal Proceedings" of this Quarterly Report.

The accompanying notes are an integral part of the consolidated financial statements.

ALTIGEN COMMUNICATIONS, INC.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(amounts in thousands, except share data)

	Common Stock					
	Shares	**Amount**	**Treasury Stock**	**Additional Paid-in Capital**	**Accumulated Deficit**	**Total Stockholders' Equity**
Balance at September 30, 2018	22,842,246	$ 25	$ (1,565)	$ 71,857	$ (59,104)	$ 11,213
Net income.....................................	—	—	—	—	1,627	1,627
Common stock issued under stock plans..	45,000	—	—	8	—	8
Stock-based compensation	—	—	—	17	—	17
Balance at June 30, 2019	22,887,246	$ 25	$ (1,565)	$ 71,882	$ (57,477)	$ 12,865

The accompanying notes are an integral part of the consolidated financial statements.

ALTIGEN COMMUNICATIONS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited, amounts in thousands)

	Nine Months Ended June 30, 2019	Nine Months Ended June 30, 2018
CASH, CASH EQUIVALENTS AND RESTRICTED CASH, BEGINNING OF PERIOD	$ 3,080	$ 3,876
OPERATING ACTIVITIES:		
Net income	1,627	813
Adjustments to reconcile net income to net cash from activities:		
Depreciation and amortization	37	32
Amortization of capitalized software	68	4
Stock-based compensation	17	19
Changes in operating assets and liabilities:		
Trade receivables	85	(109)
Prepaid expenses and other current assets	1,304	(88)
Accounts payable	37	16
Accrued expenses	(516)	419
Deferred revenue	(21)	(128)
Deferred rent	62	(25)
Net cash provided by operating activities	2,700	953
INVESTING ACTIVITIES:		
Changes in long-term deposits	(25)	20
Purchases of property and equipment	(52)	(68)
Capitalized software development costs	(702)	(138)
Net cash used in investing activities	(779)	(186)
FINANCING ACTIVITIES:		
Proceeds from issuances of common stock	8	8
Payment to line of credit	(395)	(150)
Net cash used in financing activities	(387)	(142)
Net change in cash, cash equivalents and restricted cash	1,534	625
CASH, CASH EQUIVALENTS AND RESTRICTED CASH, END OF PERIOD	$ 4,614	$ 4,501

The accompanying notes are an integral part of the consolidated financial statements.

ALTIGEN COMMUNICATIONS, INC.
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

ORGANIZATION AND BASIS OF PRESENTATION

Altigen Communications, Inc. ("Altigen," the "Company," "we," "us" or "our") was incorporated in the State of California in May 1994, and reincorporated in the State of Delaware in June 1999. We are a leading Microsoft Cloud Solutions provider of premise and cloud-based IP-PBX and Contact Center solutions. As one of the first companies to offer VoIP solutions, we design, deliver and support Voice over Internet Protocol (VoIP) phone systems and call center solutions that combine high reliability with integrated IP communications applications. Altigen has been deploying systems since 1996. Our unique and feature rich Cloud PBX and Multi-channel Contact Center solutions natively integrate with Skype for Business and Office 365 to deliver business-critical functionalities required by SMBs and enterprises.

During fiscal year 2017, the Company established a Representative Office in Taipei, Taiwan, which serves as our international office for research and development functions.

The accompanying audited consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") for interim financial reporting. The preparation of these consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses, cash flow and related disclosure of contingent assets and liabilities during the reported periods. Key estimates include certain accruals for doubtful accounts reserve, long-lived assets, accounting for income taxes and the fair value of stock options granted and outstanding. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. Actual results could differ from those estimates. To the extent that there are material differences between these estimates and our actual results, our future consolidated financial statements will be affected.

These consolidated financial statements should be read in conjunction with our audited consolidated financial statements for the fiscal year ended September 30, 2018, included in the Company's 2018 Annual Report filed through the OTC Disclosure and News Services on December 31, 2018. The Company's results of operations for any interim period are not necessarily indicative of the results of operations for any other interim period or for a full fiscal year.

CASH, CASH EQUIVALENTS AND RESTRICTED CASH

Cash and cash equivalents consist of cash on hand and highly liquid investments, such as time deposits. We consider all highly liquid investments with original maturities of three months or less to be cash equivalents. Restricted cash represents cash that serves as collateral for our revolving line of credit and is restricted as to withdrawal or use. At June 30, 2019, cash, cash equivalents and restricted cash totaled approximately $4.6 million, as compared to $3.1 million at September 30, 2018. Restricted cash was approximately $800,000 as of June 30, 2019, and is presented as part of our cash, cash equivalents and restricted cash in our consolidated balance sheets.

TRADE ACCOUNTS RECEIVABLE

The Company extends credit to its customers and generally does not require collateral. Management performs ongoing credit evaluations of its customers and establishes an allowance for estimated losses to reduce accounts receivable to the amount management expects to collect. Historically, actual collections have been within management's expectations. Accounts receivable are due under normal trade terms generally requiring payment within 30 days from the invoice date. Customer account balances with invoices dated 60-90 days old are considered delinquent.

The allowance for doubtful accounts reflects management's analysis of receivables and the probability of collecting those accounts. Trade accounts receivable are charged against the allowance when the Company determines that payments will not be received. Any subsequent receipts are credited to the allowance. In the third quarter of fiscal year 2019, the Company's allowance for doubtful accounts was insignificant.

PROPERTY AND EQUIPMENT, NET

Property and equipment are stated at cost, which includes purchase cost, applicable taxes and freight costs, less accumulated depreciation and amortization. We compute depreciation and amortization using the straight-line method over the estimated useful lives of the assets, which is three years except for leasehold improvements. We depreciate leasehold improvements over the shorter of the lease term or the improvement's estimated useful life. For the nine months ended June 30, 2019, depreciation and amortization expense was approximately $37,000. Repairs and maintenance costs for the periods presented were immaterial and were expensed as incurred.

We periodically review our portfolio of equipment for impairment. Based on our impairment assessment, we determined there were no impairment losses for the periods referenced in the table below.

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

	June 30, 2019	September 30, 2018
Furniture and equipment	$ 495	$ 547
Computer software	391	392
Leasehold improvements	52	132
Total	938	1,071
Accumulated depreciation and amortization	(845)	(993)
Property and equipment, net	$ 93	$ 78

SOFTWARE DEVELOPMENT COST

Costs incurred for the development of software to be marketed and sold are expensed as incurred until technological feasibility has been established, at which time such costs are capitalized until the product is available for general release to the public. Capitalized software development costs include purchased materials and services, and payroll and personnel-related costs attributable to programmers, software engineers and quality control. We amortize software development costs using the straight-line method over the product's estimated useful life, generally three years to cost of revenue for software sales.

We capitalize certain costs of software developed for internal use. Capitalized costs include payroll and personnel-related costs for employees who are directly associated with and who devote time to the internal-use software projects, and purchased materials and services consumed in developing or obtaining internal-use software. The cost of internally developed software is amortized on a straight-line basis over its estimated useful life, generally three years to cost of revenue for hosted services.

The following table summarizes capitalized software costs and accumulated amortization as of September 30, 2018 and activities during the nine months ended June 30, 2019 (in thousands):

	Capitalized Software	Accumulated Amortization	Net
Balance at September 30, 2018	$ 333	$ (6)	$ 327
Additions	702	(68)	634
Balance at June 30, 2019	$ 1,035	$ (74)	$ 961

REVENUE RECOGNITION AND COST OF REVENUE

We derive our revenue from the sales of hosted services, service support (known as software assurance programs), software licenses, professional and deployment services. Revenue from sales to end-users and resellers is recognized when delivery has occurred, or services have been rendered, collection of the receivable is reasonably assured, persuasive evidence of an arrangement exists, and the sales price is fixed and determinable. If the Company determines that any one of the four criteria is not met, recognition of revenue is deferred until all the criteria are met.

HOSTED SERVICES

Hosted service revenue is generated from the sale of subscriptions to our software applications and related services. Hosted services consist primarily of our proprietary hosted VoIP Unified Communications system. The cloud-based model focuses on serving the needs of enterprise business that require the highest quality voice and integrated business productivity applications. The hosted offering includes hosted IP PBX service, Session Initiation Protocol (SIP) Trunk service, call center solutions, voice and video calling, conference calling, and a variety of long-distance services. Our solutions are used by businesses and organizations in industries such as financial services, healthcare, retail and business services. Our hosted services are sold through reseller partners and direct arrangements with end-user customers. We recognize hosted service revenue in the period when the services are performed. Our customers will typically enter into a one-year service agreement whereby they are billed for such services on a monthly basis. In accordance with U.S. GAAP, revenue recognition is deferred until such time the customer goes live to ensure the revenue will match the use of services. Such services include recurring fixed plan subscription fees, variable usage-based fees for usage in excess of plan limits and other recurring fees related to our subscriptions. Hosted services revenue accounted for 60% and 58% of our total net revenue for the three and nine months ended June 30, 2019, respectively.

Cost of hosted services consists primarily of costs associated with hosting our service and providing support, costs associated with data center capacity and certain fees paid to various third parties for the use of their technology, services and data.

SERVICE SUPPORT PROGRAMS

Our service support programs, also referred to as "software assurance" are post-contract customer support ("PCS") services and provide our customers with the latest software updates, patches, new releases, and technical support for the applications they are licensed to use. These programs have an annual subscription and are generally structured with a one-year or three-year term. Sales from our service support programs are recorded as deferred revenue and recognized as revenue over the terms of their subscriptions. Subscriptions with expiration dates of less than one year are classified as "deferred revenue, short-term" and greater than one year are classified as "deferred revenue, long-term" in the accompanying consolidated balance sheets. Short-term service support deferred revenue was approximately $1.0 million as of June 30, 2019 and September 30, 2018, respectively. Long-term service support deferred revenue was approximately $237,000 as of June 30, 2019, compared to $221,000 as of September 30, 2018. Service support revenue accounted for 26% and 27% of our total net revenue for the three and nine months ended June 30, 2019, respectively. Our service plan offering remains a key part of our business as we continue to add new service customers.

The estimated cost of providing software assurance is insignificant and the upgrades and enhancements offered at no cost during software assurance arrangements have historically been, and are expected to continue to be, minimal and infrequent. All estimated costs of providing the services, including upgrades and enhancements, are spread over the life of the software assurance contract term.

SOFTWARE REVENUE

Software revenue consists of license revenue that is recognized upon the delivery, usually a download from the Company's website with a specified one-time download key/password that the Company provides to each customer upon sale. Our software revenue consists of direct sales to end-users, resellers and distributors. The software license is sold on a standalone basis with no other services or products bundled in. The Company will only provide such PCS on a rare and limited basis consisting primarily of technical support and bug fixes on installation if the download with the passcode key did not work. The Company does not provide any further PCS after installation in connection with the software license sale. The related cost of software revenue is immaterial.

PROFESSIONAL SERVICES AND OTHER REVENUE

The Company also derives revenue from professional services, which primarily include custom software development to extend system capabilities and enable UC integration with other enterprise applications. Our professional services are sold separately from software services and have standalone value. Revenue from professional services is recognized when the milestones are achieved and accepted by the customer for fixed price contracts. Cost of professional services consists primarily of employee-related costs, including stock-based expenses. Other revenue consists of deployments and training. Revenue from deployments and training is recognized as the services are performed.

CONCENTRATIONS

Our customers are primarily end-users, resellers and distributors. We have distribution agreements with Altisys Communications, Inc. ("Altisys") and Synnex Corporation ("Synnex") in North America. Our agreements with Altisys and Synnex have initial terms of one year. Each of these agreements are renewed automatically for additional one-year terms, provided that each party has the right to terminate the agreement for convenience upon ninety (90) days' written notice prior to the end of the initial term or any subsequent term of the agreement. In addition, our agreements with Altisys and Synnex also provide for termination, with or without cause and without penalty, by either party upon thirty (30) days' written notice to the other party or upon a party's insolvency or bankruptcy.

In North America, we also have a reseller agreement with Fiserv Solutions, Inc. ("Fiserv"). Our agreement with Fiserv has an initial term of ten years ending on August 28, 2019 and shall be renewed automatically for additional five-year terms unless either party provides the other party with ninety (90) days' written notice of termination prior to the end of the initial term, or any subsequent term of the agreement. The agreement can also be terminated for, among other things, material breach or insolvency of either party. Upon termination, Altigen would continue to have support obligations for products that Fiserv distributed subject to Fiserv's obligation to remain current on maintenance fees.

The foregoing statements are subject to, and are qualified in their entirety by reference to, the agreements with Fiserv, Synnex and Altisys described above, which have been filed with the SEC as exhibits to the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2009, Annual Report on Form 10-K for the fiscal year ended September 30, 2003, and Quarterly Report on Form 10-Q for the quarter ended December 31, 2001, respectively.

Altisys, Synnex and Fiserv, collectively represent approximately 31% and 30% of our total net revenue for the three and nine months ended June 30, 2019, respectively, as compared to 34% and 29% for the same periods in fiscal year 2018.

SEGMENT REPORTING

The Company manages its business primarily on a geographic basis. Accordingly, the Company determined its operating segments, which are generally based on the nature and location of its customers, to be North America and Rest of World. The North America segment is comprised of the United States, Canada, Mexico, Central America and the Caribbean. The Rest of World segment is primarily comprised of Europe.

2. REVOLVING LINE OF CREDIT

On September 1, 2018, we amended the credit agreement governing our Revolving Line of Credit Note ("Line of Credit") with our primary financial lender. Under the renewed terms, the Line of Credit was extended for a period of one year and expires on August 31, 2019. The total amount available for the Company to borrow was reduced from $1.0 million to $800,000. The terms of the Line of Credit also require us to maintain restricted cash with our financial institution equal to the aggregate principal amount of $800,000 as collateral. The restricted cash is included in our cash, cash equivalents and restricted cash in our consolidated balance sheets as of June 30, 2019. Under the amended credit agreement, we are not subject to any restrictive financial covenants.

The Line of Credit is available to finance working capital and for general corporate purposes and requires monthly interest payments based on the prevailing 30-day LIBOR rate plus 0.75% (3.152% at June 30, 2019), and the interest rate is reset monthly. For the three and nine months ended June 30, 2019 and 2018, interest expense associated with the Line of Credit was approximately $5,000 and $15,000, respectively, as compared to $5,000 and $14,000, respectively.

As of June 30, 2019, the availability under the Line of Credit was approximately $476,000 and we had outstanding borrowings of $324,000, which is included in current liabilities on the accompanying consolidated balance sheets. The unpaid balance of the Line of Credit may increase or decrease with each payment or new advance. Any outstanding borrowings and accrued interest shall be due and payable in full on August 31, 2019.

3. COMMITMENTS AND CONTINGENCIES

Commitments

In April 2019, the Company entered into a new five-year operating lease for its corporate headquarters located in Milpitas, California. This facility is leased through July 2024 and serves as our principal office space for global sales and marketing, research and development, and general and administration functions. The terms of the lease required a security deposit of approximately $25,000, rent escalations, and one consecutive option to extend the lease term for an additional five-year period. In connection with this lease arrangement, the Company received rent abatement as a lease incentive in the amount of $59,000. Under the terms of the lease agreement, total rent payment is approximately $1.2 million for a period of five years commencing on September 1, 2019.

The Company's operating lease for its corporate headquarters located in San Jose, California expired on May 31, 2019. There were no significant costs incurred with respect to the expiration of this lease.

In December 2017, the Company entered into a three-year operating lease agreement, which expires in December 2020, for approximately 2,284 square feet of office space located in Taipei, Taiwan. The facility serves as our international office for research and development functions. Pursuant to the terms of the lease agreement, total base rent payment is approximately $137,000 over a period of three years with one month rent free at the initial term of the lease. Additionally, under the terms of the lease agreement, the Company is obligated to pay certain customary amounts for its share of operating expenses, and the terms of the lease required a security deposit of approximately $11,000, which is classified as long-term deposit in the Consolidated Balance Sheets.

Future non-cancellable minimum lease payments required under all existing operating leases as of June 30, 2019 are as follows:

Fiscal Year		Future Lease Payments (in thousands)
Remainder of 2019	$	31
2020		285
2021		254
2022		254
2023		261
2024		224
Total	$	1,309

Contingencies

From time to time, we may become subject to other legal proceedings, claims and litigation arising in the ordinary course of business. Litigation can be expensive, lengthy and disruptive to normal business operations. Moreover, the results of complex legal proceedings are difficult to predict. An unfavorable resolution of a particular lawsuit or proceeding could have a material adverse effect on our results of operations, financial position or cash flows. Except as noted below, the Company is not a party to any material legal proceedings nor is the Company aware of any pending or threatened litigation that, in its opinion, would have a material adverse effect on its business or its financial position, results of operations or cash flows should such litigation be resolved unfavorably.

CTI Litigation

On March 30, 2016, CTI Communications, LLC, a former reseller of the Company ("CTI"), filed a complaint against the Company, Affiliated Technology Solutions, LLC, a current reseller of the Company ("ATS"), James Jerome Cruz, a former CTI employee, and Thomas W. Welsh, President of ATS, in the Colorado District Court, Larimer County (the "Court"). The complaint alleged misappropriation of trade secrets, breach of contract, civil conspiracy and tortious interference. On March 17, 2017, CTI filed an amended complaint adding certain members of management and executive officers as additional defendants, including the Company's Chief Executive Officer, Jeremiah J. Fleming, Vice President of Sales, Michael Plumer and Regional Sales Manager, Matthew Nielson. On August 16, 2017, the Court dismissed with prejudice all of CTI's claims against Mr. Fleming. On March 27, 2018, a jury directed a verdict in favor of CTI, and the Court entered a judgment that held all defendants jointly and severally liable and awarded plaintiff approximately $724,000 in compensatory damages, unjust enrichment, punitive damages and pre-judgment interest on compensatory damages. On August 22, 2018, the Court served our financial institution and ordered $729,000 for the judgment and post-judgment interest through April 30, 2018 be sent to a trust account held by plaintiff's counsel until further order. Furthermore, after ruling on October 5, 2018, CTI was entitled to recover attorneys' fees and costs in the sum of $433,000. The Company filed a Motion for Stay of Execution of Judgement with the Court, and on July 25, 2018, the Company and all defendants in the litigation filed a Notice of Appeal in the Colorado Court of Appeals. The appeal process is ongoing. The Company believes it has meritorious defenses to CTI's claims and intends to continue to vigorously defend against the claims asserted. On November 29, 2018, the Company, ATS, Mr. Welsh, and Mr. Cruz entered into a settlement agreement pursuant to which the parties thereto allocated damages among themselves and $557,000 was paid to the Company by such other co-defendants on December 3, 2018. Consequently, the Company recorded litigation expanse in the sum of $604,000, a receivable in the amount of $557,000, and a payable in the amount of $433,000 in the fourth quarter of fiscal 2018 in connection with this matter. Pursuant to the judgement on attorneys' fees and costs, on February 7, 2019, the Court served our financial institution and ordered $445,000 in attorneys' fees and costs plus post-judgment interest on damages through October 23, 2018 be paid to plaintiff's counsel.

Intellitalk Litigation

On February 1, 2019, the Company was served with a cross-complaint filed by Intellitalk, Inc. ("Intellitalk"), an active reseller of the Company. The cross-complaint was filed in the Superior Court of the State of California, County of Riverside on January 15, 2019. The complaint alleges interference with prospective economic advantage and unfair competition. Although the outcome of this matter is not determinable as of the date of this report, we believe Intellitalk's claims are without merit and we intend to vigorously defend against the allegations. The Company has not recorded any liability with respect to this litigation as of June 30, 2019.

4. STOCKHOLDERS' EQUITY AND STOCK-BASED COMPENSATION EXPENSE

Equity Stock Incentive Plans

The Company grants incentive stock options ("ISO"), non-qualified stock options ("NSO") and restricted stock awards to eligible employees, officers, directors and consultants under the 2009 Stock Plan ("2009 Stock Plan"), which is the successor to the 1999 Stock Plan. The 2009 Stock Plan provides for the granting of ISO, NSO, restricted stock awards, restricted stock units, stock appreciation rights, performance units and performance shares for over a period not to exceed ten years and at exercise prices that are not less than 100% of the fair market value of the Company's common stock on the date of grant as determined by the Board of Directors. The exercise price of options granted to a greater than 10% stockholder may not be less than 110% of the fair market value on the date of grant. Stock options issued under the 2009 Stock Plan generally vest 25% at one year from the date of grant and 1/48th monthly thereafter. Options under the 2009 Stock Plan will generally expire ten years after the date of grant. The value of common stock subject to incentive stock options that become exercisable by any one employee in any calendar year may not exceed $100,000. In June 2019, the 2009 Stock Plan expired. The plan will, however, continue to govern the securities previously granted under the plan. The Company intends to adopt a new stock plan in the fourth quarter of fiscal 2019.

The following table summarizes the Company's stock options as of October 1, 2018 and changes during the nine months ended June 30, 2019:

	Number of Shares		Weighted-Average Exercise Price	Weighted Average Remaining Contractual Life (in years)		Aggregate Intrinsic Value (in thousands)
Outstanding at October 1, 2018	4,088,124	$	0.28			
Granted	4,500		0.48			
Exercised	(45,000)		0.16			
Forfeitures and cancellations	(272,989)		0.86			
Outstanding at June 30, 2019	3,774,635	$	0.24	4.83	$	3,053,910
Exercisable at June 30, 2019	3,645,947	$	0.24	4.71	$	2,956,042

Stock-Based Compensation

The Company accounts for stock-based compensation, including grants of stock options, as an operating expense in the consolidated statement of operations. The Company measures stock-based compensation cost at the grant date based on the fair value of the grant. The value of the portion of the grant that is ultimately expected to vest is recognized as expense over the requisite service periods. Stock-based compensation expense was $4,000 and $17,000 for the three and nine months ended June 30, 2019, respectively, compared to $7,000 and $19,000 for the three and nine months ended June 30, 2018, respectively.

5. SHAREHOLDER RIGHTS PLAN

The Company adopted a Preferred Stock Rights Agreement (the "Plan") and declared a dividend distribution of one right for each outstanding share of its common stock. The record date for the distribution was May 7, 2009. The Company designed the plan to protect the long-term value of the Company for its shareholders during any future unsolicited acquisition attempt. The Company did not adopt the Plan in response to any specific attempt to acquire the Company or its securities, and the Company is not aware of any current efforts to do so. These rights will become exercisable only upon the occurrence of certain events specified in the Plan, including the acquisition of 15% of the Company's outstanding shares of common stock by a person or group. Should a person or group acquire 15% or more of the outstanding shares of common stock or announce an unsolicited tender offer, the consummation of which would result in a person or group acquiring 15% or more of the outstanding shares of common stock, stockholders other than the acquiring person may exercise the rights, unless the Board of Directors has approved the transaction in advance. Each right will initially entitle stockholders to purchase one one-thousandths (0.001) of the Company's preferred stock for $4.00 per share. However, the rights are not immediately exercisable and will become exercisable only upon the occurrence of certain events. If a person or group acquires, or announces a tender or exchange offer that would result in the acquisition of, fifteen percent (15%) or more of our common stock while the stockholder rights plan remains in place, then, unless the rights are redeemed by us for $0.001 per right, the rights will become exercisable by all rights holders, except the acquiring person or group, for shares of Altigen or shares of the third party acquirer having a value of twice the right's then-current exercise price. On May 7, 2019, the stockholder rights plan expired.

6. SUBSEQUENT EVENTS

On August 1, 2019, the Company entered into an asset purchase agreement with WorkSpace Communications, LLC ("WorkSpace"), pursuant to which, on such date, the Company acquired all of WorkSpace's rights to its customer relationships for $400,000 in cash plus additional contingent cash consideration of up to $1.2 million subject to the terms on which such customers are transitioned to Altigen. In connection therewith, WorkSpace agreed to provide certain transition services on a monthly basis at the Company's expense until such services are no longer needed by the Company, and the Company hired certain WorkSpace employees.

Item 4. Management's Discussion and Analysis of Plan of Operation.

These statements are based on current expectations and assumptions regarding future events and business performance and involve known and unknown risks, uncertainties and other factors that may cause industry trends or our actual results, level of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by these statements. These unaudited interim consolidated financial statements and notes thereto should be read in conjunction with the audited consolidated financial statements and related notes included in our Annual Report for the fiscal year ended September 30, 2018, filed through the OTC Disclosure and News Services on December 31, 2018. The Company undertakes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

Overview

Altigen Communications, Inc. ("Altigen," the "Company," "we," "us" or "our") was incorporated in the State of California in May 1994, and reincorporated in the State of Delaware in June 1999. We are a leading Microsoft Cloud Solutions provider of premise and cloud-based IP-PBX and Contact Center solutions. As one of the first companies to offer VoIP solutions, we design, deliver and support Voice over Internet Protocol (VoIP) phone systems and call center solutions that combine high reliability with integrated IP communications applications. Altigen has been deploying systems since 1996. Our unique and feature rich Cloud PBX and Multi-channel Contact Center solutions natively integrate with Skype for Business and Office 365 to deliver business-critical functionalities required by SMBs and enterprises.

Altigen's Unified Communications (UC) solutions are designed with an open architecture, built on industry standard communication protocols, and Microsoft Windows-based applications. This adherence to widely used standards allows our solutions to both integrate with and leverage a company's existing technology investment. Altigen's award winning, integrated IP applications suite provides customers with a complete business communications solution. Voicemail, Contact Center, Unified Messaging, Automatic Call Distribution, Call Recording, Call Activity Reporting, and Mobility solutions take advantage of the convergence of voice and data communications to achieve superior business results.

Altigen was formed in 1994 as a California corporation and was reincorporated in the State of Delaware in 1999. Our primary facility housing research and development, sales and marketing, and administrative functions is located in San Jose, California. We also have a Representative Office in Taipei, Taiwan, which serves as our international office for research and development functions. Our fiscal year end is September 30 of each year. The Company's common stock trades on the OTCQB U.S. tier under the symbol "ATGN." Trading in the common shares of the Company commenced on March 16, 2010 and Pink OTC Markets, Inc. provides quotes and other information at www.otcmarkets.com. The Company has not been in bankruptcy, receivership, or any similar proceeding.

We focus our sales efforts on first and second tier hosted voice service providers, medium and enterprise sized businesses, multi-site businesses, corporate branch offices, and call centers. Our first products began shipping in 1996. Our UC solutions are primarily sold to small-to-medium sized businesses, multi-site businesses, corporate branch offices, call centers, credit unions and community banks.

Altigen's software products are available from independent authorized resellers and strategic partners.

Altigen's primary SIC code is 3661 (telephone and telegraph apparatus). Altigen has never been "shell company" as defined under the Securities Act of 1933, as amended.

Critical Accounting Policies and Estimates

Management's discussion and analysis of the Company's financial condition and consolidated results of operations is based upon the Company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States ("U.S. GAAP"). The preparation of these financial statements requires the Company's management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. The Company's estimates are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis for the Company's conclusions. The Company continually evaluates the information used to make these estimates as its business and the economic environment change. The Company's management believes that certain estimates, assumptions and judgments derived from the accounting policies have significant impact on its financial statements, so the Company considers the following be its critical accounting policies.

Revenue Recognition

We derive our revenue from the sales of hosted services, service support (known as software assurance programs), software licenses, professional and deployment services. Revenue from sales to end-users and resellers is recognized when delivery has occurred, or services have been rendered, collection of the receivable is reasonably assured, persuasive evidence of an arrangement exists, and the sales price is fixed and determinable. If the Company determines that any one of the four criteria is not met, recognition of revenue is deferred until all the criteria are met.

Hosted Services Revenue. We generate recurring revenue through our cloud-based products referred to as hosted services sold through reseller partners and direct arrangements with end-user customers. Hosted services revenue is derived from providing our proprietary VoIP UC solutions in a hosted environment, in which customers pay a minimum monthly fee to use a specified number of software licenses, plus SIP services. Customers are billed the greater of their minimum monthly fee or actual usage, and revenue is recognized monthly as the services are performed. In accordance with generally accepted accounting principles, revenue recognition is deferred until such time the customer goes live to ensure the revenue will match the use of services. Cost of hosted services consists primarily of costs associated with hosting our service and providing support, costs associated with data center capacity and certain fees paid to various third parties for the use of their technology, services and data.

Service Support Revenue. Service support, also referred to as software assurance, are post-contract customer support ("PCS") services. We provide software assurance consisting primarily of the latest software updates, patches, new releases and technical support. Such software assurance sales are sold separately from any software licenses. Revenue from service support sales are recognized ratably over the contract term, generally over a period of one year or three years. Sales from our service support programs are recorded as deferred revenue and recognized as revenue over the terms of their subscriptions. Subscriptions with expiration dates of less than one year are classified as "deferred revenue, short-term" and greater than one year are classified as "deferred revenue, long-term" in the accompanying consolidated balance sheets. The estimated cost of providing software assurance during the arrangement is insignificant and the upgrades and enhancements offered at no cost during software assurance arrangements have historically been, and are expected to continue to be, minimal and infrequent. All estimated costs of providing the services, including upgrades and enhancements, are deferred and recognized to costs of revenue over the life of the software assurance contract term.

Software Revenue. Software revenue consists of license revenue that is recognized upon the delivery, usually a download from the Company's website with a specified one-time download key/password that the Company provides to each customer upon sale. Our software revenue consists of direct sales to end-users, resellers and distributors. The software license is sold on a standalone basis with no other services or products bundled in. The Company will only provide such PCS on a rare and limited basis consisting primarily of technical support and bug fixes on installation if the download with the passcode key did not work. The Company does not provide any further PCS after installation in connection with the software license sale. The related cost of software revenue is immaterial.

Professional Services and Other Revenue. The Company also derives revenue from professional services, which primarily include custom software development to extend system capabilities and enable UC integration with other enterprise applications. Our professional services are sold separately from software services and have standalone value. Revenue from professional services is recognized when the milestones are achieved and accepted by the customer for fixed price contracts. Cost of professional services consists primarily of employee-related costs, including stock-based expenses. Other revenue consists of deployments and training. Revenue from deployments and training is recognized as the services are performed.

The following table sets forth percentages of net revenue by product type with respect to such revenue for the periods indicated:

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	**2018**	**2019**	**2018**
Hosted services	60%	49%	58%	49%
Service support programs	26%	30%	27%	33%
Software	7%	19%	11%	16%
Professional services and other	7%	2%	4%	2%
Total	100%	100%	100%	100%

Cash, Cash Equivalents and Restricted Cash

Cash and cash equivalents consist of cash on hand and highly liquid investments, such as time deposits. We consider all highly liquid investments with original maturities of three months or less to be cash equivalents. Restricted cash represents cash that serves as collateral for our revolving line of credit and is restricted as to withdrawal or use. At June 30, 2019, cash, cash equivalents and restricted cash totaled approximately $4.6 million, as compared to $3.1 million at September 30, 2018. Restricted cash was approximately $800,000 as of June 30, 2019, and is presented as part of our cash, cash equivalents and restricted cash in our consolidated balance sheets.

Results of Operations

The following table sets forth consolidated statements of operations data for the periods indicated as a percentage of net revenue.

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	**2018**	**2019**	**2018**
Net revenue:				
Hosted services	60.0 %	49.2 %	57.6 %	49.3 %
Service support programs	26.1	30.1	27.3	33.1
Software	7.2	19.0	10.8	15.8
Professional services and other	6.7	1.7	4.3	1.8
Total net revenue	100.0	100.0	100.0	100.0
Cost of revenue:				
Hosted services	18.4	15.4	17.6	15.6
Software	1.0	0.7	0.6	0.5
Professional services and other	—	—	—	0.2
Total cost of revenue	19.4	16.1	18.2	16.3
Gross profit	80.6	83.9	81.8	83.7
Operating expenses:				
Research and development	25.5	28.7	24.3	29.8
Sales and marketing	19.7	21.3	19.6	21.2
General and administrative	13.8	16.8	17.7	16.9
Litigation (1)	—	13.4	0.2	4.7
Total operating expenses	59.0	80.2	61.8	72.6
Income from operations	21.6	3.7	20.0	11.1
Interest and other income (expense), net				
Interest and other income, net	1.8	0.2	0.8	0.2
Interest expense	(0.2)	(0.2)	(0.2)	(0.2)
Total interest and other income (expense), net	1.6	—	0.6	—
Income before income taxes	23.2	3.7	20.6	11.1
Provision for income taxes	0.1	—	0.2	—
Net income	23.1 %	3.7 %	20.4 %	11.1 %

(1) Refer to Note 3, "Commitments and Contingencies" of the Consolidated Financial Statements and Item 5, "Legal Proceedings" of this Quarterly Report.

The accompanying notes are an integral part of the consolidated financial statements.

Results of Operations — Three and Nine Months Ended June 30, 2019 Compared to Three and Nine Months Ended June 30, 2018

Net Revenue

Net revenue consists of revenue from direct sales to end-users, resellers and distributors.

We categorize our operations into two operating segments - North America and Rest of World. The North America segment is comprised of the United States, Canada, Mexico, Central America and the Caribbean. The Rest of World segment is primarily comprised of Europe.

Net revenue increased 4% to $2.7 million and 9% to $7.9 million for the three and nine months ended June 30, 2019, respectively, compared to $2.6 million and $7.3 million for the same periods in fiscal year 2018. The increase in the third quarter was primarily attributable to a 27%, or $335,000 increase in hosted services revenue, partially offset by a decrease in service support and software revenue. The year-over-year increase was primarily caused by a favorable shift in our product mix resulting in an increase of 27%, or $983,000 in hosted services revenue, an increase of 192%, or $227,000 in professional services, partially offset by a decrease in service support and software revenue.

Cost of Revenue

Cost of hosted services primarily consists of costs associated with hosting our services, personnel costs associated with customer care and related costs of the hosted operation, costs associated with data center capacity purchased from third-party providers and certain fees paid to various third parties for the use of their technology, services and data. Cost of hosted services is expensed as incurred. Cost of revenue also includes amortization of capitalized software development costs, and other allocated overhead expenses.

For the three months ended June 30, 2019, cost of revenue was $515,000, or 19% of net revenue, compared to $411,000, or 16% of net revenue for the same period of fiscal year 2018. For the nine months ended June 30, 2019, cost of revenue was $1.5 million, or 18% of net revenue, compared to $1.2 million, or 16% of net revenue for the same period of fiscal year 2018.

Cost of hosted services was approximately $487,000, or 18% of net revenue and $1.4 million, or 18% of net revenue for the three and nine months ended June 30, 2019, respectively, compared to $393,000, or 15% of net revenue and $1.1 million, or 16% of net revenue for the three and nine months ended June 30, 2018, respectively. The increase was primarily attributable to the positive impact of the hosted revenue growth. Cost of hosted services, both in absolute dollars and as percentage of revenue, may fluctuate in the future periods depending on the growth rate of our hosted service offerings and the associated costs.

Cost of service support consists principally of upgrades, enhancements and technical support. Service support costs are deferred and recognized to costs of revenue over the life of the software assurance contract term. For the three and nine months ended June 30, 2019 and 2018, the related cost of service support was immaterial.

Cost of professional services and other revenue consists primarily of employee-related costs, including stock-based compensation expenses. Costs incurred by the Company in connection with providing such services are charged to expense as incurred. For the three and nine months ended June 30, 2019 and 2018, the related cost of professional services and other revenue was immaterial.

Research and Development (“R&D”) Expenses

R&D expenses consist primarily of salaries, benefits and overhead expenses, non-cash stock-based compensation, consultant fees, and other costs associated with the design, development, enhancements and testing of our products. We expense all R&D expenses as incurred and capitalize certain costs of product development when the projects under development reach technological feasibility for software to be sold, and capitalize certain costs as incurred for internal-use software developed as a service.

For the third quarter of fiscal year 2019, research and development expenses were $675,000, or 26% of net revenue, compared to $733,000, or 29% of net revenue for the third quarter of fiscal year 2018. For the nine months ended June 30, 2019, research and development expenses were $1.9 million, or 24% of net revenue, compared to $2.2 million, or 30% of net revenue for the same period of fiscal year 2018.

Excluding the impact of capitalized development costs, research and development expenses increased 11%, to $909,000 in the third quarter of fiscal 2019, compared with $818,000 for the same period of fiscal year 2018. The increase was predominately driven by an increase of $81,000 in salaries, benefits and overhead expenses due to an increase in headcount. Excluding the impact of capitalized development costs, research and development expenses increased 14%, to $2.6 million for the nine months ended June 30, 2019, compared to $2.3 million in the comparable prior year period. The increase was largely due to increased salaries, benefits and overhead expenses of $341,000, offset by a decrease of $46,000 in consulting fees.

Capitalized development costs were $234,000 and $702,000 for the three and nine months ended June 30, 2019, respectively, compared with $85,000 and $138,000 for the three and nine months ended June 30, 2018, respectively.

We believe our future success relies on our ability to expand the functionality and scalability of our products and services and enhancing their ease of use, as well as our ability to development and introduce new product offerings, related software applications and services for both premise and hosted customers. Over the long term, we expect our R&D expenses to increase in absolute dollars and as percentage of revenue as we expand our international development division, and as we continue to invest in the development of new solutions and expand our product and service offerings. While our main R&D activities for our products and services are conducted in the United States, we also have additional design and development engineering teams located in China and Taiwan.

Sales and Marketing Expenses

Sales and marketing expenses consist primarily of salaries, benefits and overhead expenses, sales commissions, travel, non-cash stock-based compensation expense and costs related to marketing, trade shows and promotional activities.

For the third quarter of fiscal year 2019, sales and marketing expenses were $523,000, or 20% of net revenue, compared to $544,000, or 21% of net revenue for the third quarter of fiscal year 2018. For the nine months ended June 30, 2019, sales and marketing expenses were $1.6 million, or 20% of net revenue, compared to $1.5 million, or 21% of net revenue for the same period of fiscal year 2018.

We plan to continue investing in our domestic marketing activities to help build brand awareness, create sales leads and to drive growth in our sales. To the extent we achieve higher sales levels, we expect sales and marketing expenses to increase in the future periods over the long-term due to increased staffing levels as well as increased commissions expense, although we will continue to maintain a prudent expense philosophy.

General and Administrative Expenses

General and administrative expenses consist of salaries, benefits and overhead expenses, non-cash stock-based compensation expense and related expenses for our executive, finance and administrative personnel, facilities and allowance for doubtful accounts. In addition, general and administrative expenses include legal, accounting services and general corporate expenses.

For the third quarter of fiscal year 2019, general and administrative expenses were $367,000, or 14% of net revenue, compared to $429,000, or 17% of net revenue for the third quarter of fiscal year 2018, representing an increase of $62,000. For the nine months ended June 30, 2019, general and administrative expenses were $1.4 million, or 18% of net revenue, compared to $1.2 million, or 17% of net revenue for the same period of fiscal year 2018. The three-month decrease was primarily driven by reduced salaries, benefits and overhead expenses of $30,000 and reduced legal expenses of approximately $32,000. The nine-month increase of $170,000 was primarily driven by an increase of $65,000 in accounting fees related to section 382 ownership change analysis to determine if the Corporation has any limitation on the utilization of its NOLs, and an increase of $105,000 in legal expenses related to such matters disclosed in Note 3, “Commitments and Contingencies” of the Consolidated Financial Statements and Item 5, “Legal Proceedings” of this quarterly report.

We expect general and administrative expenses will continue at their current rate as management continues to monitor expenses and plans to keep them in line with expected revenue opportunities.

Interest and Other (Expense) Income, Net

Interest Income and Expense

Interest expense consists primarily of interest charged on the outstanding borrowing of our revolving line of credit. Interest income relates to amounts earned on our cash and cash equivalents. The Company recorded $12,000 as interest income and $5,000 as interest expense in the third quarter of fiscal year 2019, compared to $5,000 of interest income and $6,000 of interest expense in the third quarter of fiscal year 2018. For the nine months ended June 30, 2019, the company recorded $31,000 as interest income and $15,000 as interest expense, compared to $14,000 of interest income and $14,000 of interest expense during the same periods in fiscal year 2018.

Other Income

In the third quarter of fiscal year 2019, in connection with the relocation of the Company's headquarters to Milpitas, California, the Company received cash proceeds of $36,000 from the sale of certain office furniture. Such amount is included in other income in the consolidated statements of operations.

Liquidity and Capital Resources

Since inception, we have financed our operations primarily through the sale of equity securities and cash flows from operations. As of June 30, 2019, total cash, cash equivalents and restricted cash represents approximately 86% of total current assets. We believe our cash and cash equivalents, and our ability to access capital through our debt arrangements will satisfy our operations through at least the next 12 months from August 15, 2019, the date our consolidated financial statements were available to be issued.

The following table shows the major components of our consolidated statements of cash flows for the stated periods:

	Nine Months Ended June 30,	
	2019	**2018**
	(amounts in thousand)	
Cash, cash equivalents and restricted cash, beginning of period	$ 3,080	$ 3,876
Cash provided by operating activities	2,700	953
Cash used in investing activities	(779)	(186)
Cash used in financing activities	(387)	(142)
Cash, cash equivalents and restricted cash, end of period	$ 4,614	$ 4,501

Cash Provided by Operating Activities

During the nine months ended June 30, 2019, cash provided by operating activities of $2.7 million was the result of $1.6 million of net income, $122,000 of adjustments for non-cash items and an increase of $951,000 in net changes in operating assets and liabilities. Non-cash items consist of depreciation and amortization and stock-based compensation expenses. Changes in operating assets and liabilities was primarily due to collections of other receivables of $557,000 in connection with the CTI lawsuit. For additional information, refer to Item 5, "Legal Proceedings" of this quarterly report.

During the nine months ended June 30, 2018, cash provided by operating activities of $953,000 was the result of $813,000 of net income, adjustments for non-cash items of $55,000 and an increase in net changes in operating assets and liabilities of $85,000. Non-cash items consist of depreciation and amortization and stock-based compensation expenses.

Cash Used in Investing Activities

Cash flows from investing activities primarily relate to capitalized software costs associated with the development of new products and services and enhancements of existing products and services, as well as, capital expenditures related to technological equipment, software licenses and to a lesser degree, office equipment. Our cash used in investing activities of $779,000 for the nine months ended June 30, 2019 was attributable to changes in long-term deposits of $25,000, capital expenditures of property and equipment totaling $52,000, and capitalized software development costs totaling $702,000. Cash used in investing activities for the nine months ended June 30, 2018 was attributable to changes in long-term deposits and capital expenditures of $48,000 and capitalized software development costs totaling $138,000.

Cash Used in Financing Activities

Our financing activities have consisted primarily of repayments under our revolving line of credits and the net proceeds from the issuance of common stock from employee option exercises. Cash used in financing activities of $387,000 during the nine months ended June 30, 2019 was primarily the result of cash outflow used to pay down the principal balance on our revolving line of credit of $395,000, offset by proceeds of $8,000 from the exercise of stock options. Cash used in financing activities of $142,000 during the nine months ended June 30, 2018 consisted primarily of cash used to pay down the principal balance on our revolving line of credit of $150,000, offset by proceeds of $8,000 from the exercise of stock options.

Based on our recent performance and current expectations, we believe our existing cash and cash equivalents, as well as cash expected to be generated from operating activities will adequately meet our working capital, capital expenditure needs, and other liquidity requirements associated with our existing operations one year from August 15, 2019, the date our consolidated financial statements were available to be issued.

Our cash needs depend on numerous factors, including market acceptance of and demand for our products and services, our ability to develop and introduce new product offerings and enhancements to existing products, the prices at which we can sell our products, the resources we devote to developing, marketing, selling and supporting our products, as well as other factors. If we are unable to raise additional capital or if sales from our new products or enhancements are lower than expected, we will be required to make additional reductions in operating expenses and capital expenditures to ensure that we will have adequate cash reserves to fund operations.

The current bank line of credit with our financial institution extends through August 2019 and permits borrowings up to $800,000. As of June 30, 2019, the Company had not borrowed any funds under the Line of Credit. We expect to generate sufficient cash from operations to pay the Line of Credit due on August 31, 2019, which had outstanding borrowing of $324,000.

Additional financing, if required, may not be available on favorable terms, or at all. To the extent that existing cash and cash equivalents are not sufficient to fund our future operations, we may need to raise additional funds through public or private equity offerings or through additional debt financing. If we cannot raise additional funds on acceptable terms, we may not be able to further develop or enhance our products and services, take advantage of opportunities, or respond to competitive pressures or unanticipated requirements, which could seriously harm our business. Even if additional financing is available, we may be required to obtain the consent of our stockholders, which we may or may not be able to obtain. In addition, the issuance of equity or equity-related securities will dilute the ownership interest of our stockholders and the issuance of debt securities could increase the risk or perceived risk of investing in our securities.

We did not have any material commitments for capital expenditures as of June 30, 2019. We had total outstanding commitments on non-cancelable operating leases of approximately $1.3 million as of June 30, 2019. Lease terms on our existing operating leases generally range from three to five years. The lease for our headquarters located in San Jose, California expired on May 31, 2019. In April 2019, the Company entered into a five-year operating lease for a new corporate headquarters located in Milpitas, California.

Contractual Obligations

The following table presents certain commitments that will require the use of cash in future periods under contractual obligations with minimum firm commitments as of June 30, 2019 (amounts in thousands):

Contractual Obligations	Total	Payments Due in Less Than 1 Year	Payments Due in 1 - 3 Years	Payments Due in 4 - 5 Years	Payments Due in More Than 5 Years
Operating lease obligations [1]	$ 1,309	$ 31	$ 793	$ 485	$ —

(1) Refer to discussion of "*Commitments and Contingencies*" Note 3 to Consolidated Financial Statements.

Effects of Recently Issued Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which is a new standard on revenue recognition. The new standard contains principles that an entity will need to apply to determine the measurement of revenue and timing of when revenue is recognized. The underlying principle is to recognize revenue to depict the transfer of goods or services to customers at an amount that the entity expects to be entitled to in exchange for those goods or services. The standard has a five-step approach which includes identifying the contract or contracts, identifying the performance obligations, determining the transaction price, allocating the transaction price, and recognizing revenue. The standard also significantly expands the quantitative and qualitative disclosure requirements for revenue, which are intended to help users of financial statements understand the nature, amount, timing, and uncertainty of revenue and the related cash flows. ASU 2014-09 is effective for annual periods beginning after December 15, 2019. The Company is currently evaluating this new standard and the impact it will have on its financial statements and processes.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*, which requires lessees to recognize a liability associated with obligations to make payments under the terms of the arrangement in addition to a right-of-use asset representing the lessee's right to use or control the use of the given asset assumed under the lease. The standard will be effective for nonpublic business entities for annual periods beginning after December 15, 2019. Early adoption is permitted. The Company is currently evaluating this new standard and the impact it will have on its financial statements and processes.

Item 5. Legal Proceedings

Litigation

From time to time, we may become subject to other legal proceedings, claims and litigation arising in the ordinary course of business. Litigation can be expensive, lengthy and disruptive to normal business operations. Moreover, the results of complex legal proceedings are difficult to predict. An unfavorable resolution of a particular lawsuit or proceeding could have a material adverse effect on our results of operations, financial position or cash flows. Except as noted below, the Company is not a party to any material legal proceedings nor is the Company aware of any pending or threatened litigation that, in its opinion, would have a material adverse effect on its business or its financial position, results of operations or cash flows should such litigation be resolved unfavorably.

CTI Litigation

On March 30, 2016, CTI Communications, LLC, a former reseller of the Company ("CTI"), filed a complaint against the Company, Affiliated Technology Solutions, LLC, a current reseller of the Company ("ATS"), James Jerome Cruz, a former CTI employee, and Thomas W. Welsh, President of ATS, in the Colorado District Court, Larimer County (the "Court"). The complaint alleged misappropriation of trade secrets, breach of contract, civil conspiracy and tortious interference. On March 17, 2017, CTI filed an amended complaint adding certain members of management and executive officers as additional defendants, including the Company's Chief Executive Officer, Jeremiah J. Fleming, Vice President of Sales, Michael Plumer and Regional Sales Manager, Matthew Nielson. On August 16, 2017, the Court dismissed with prejudice all of CTI's claims against Mr. Fleming. On March 27, 2018, a jury directed a verdict in favor of CTI, and the Court entered a judgment that held all defendants jointly and severally liable and awarded plaintiff approximately $724,000 in compensatory damages, unjust enrichment, punitive damages and pre-judgment interest on compensatory damages. On August 22, 2018, the Court served our financial institution and ordered $729,000 for the judgment and post-judgment interest through April 30, 2018 be sent to a trust account held by plaintiff's counsel until further order. Furthermore, after ruling on October 5, 2018, CTI was entitled to recover attorneys' fees and costs in the sum of $433,000. The Company filed a Motion for Stay of Execution of Judgement with the Court, and on July 25, 2018, the Company and all defendants in the litigation filed a Notice of Appeal in the Colorado Court of Appeals. The appeal process is ongoing. The Company believes it has meritorious defenses to CTI's claims and intends to continue to vigorously defend against the claims asserted. On November 29, 2018, the Company, ATS, Mr. Welsh, and Mr. Cruz entered into a settlement agreement pursuant to which the parties thereto allocated damages among themselves and $557,000 was paid to the Company by such other co-defendants on December 3, 2018. Consequently, the Company recorded litigation expanse in the sum of $604,000, a receivable in the amount of $557,000, and a payable in the amount of $433,000 in the fourth quarter of fiscal 2018 in connection with this matter. Pursuant to the judgement on attorneys' fees and costs, on February 7, 2019, the Court served our financial institution and ordered $445,000 in attorneys' fees and costs plus post-judgment interest on damages through October 23, 2018 be paid to plaintiff's counsel.

Intellitalk Litigation

On February 1, 2019, the Company was served with a cross-complaint filed by Intellitalk, Inc. ("Intellitalk"), an active reseller of the Company. The cross-complaint was filed in the Superior Court of the State of California, County of Riverside on January 15, 2019. The complaint alleges interference with prospective economic advantage and unfair competition. Although the outcome of this matter is not determinable as of the date of this report, we believe Intellitalk's claims are without merit and we intend to vigorously defend against the allegations. The Company has not recorded any liability with respect to this litigation as of June 30, 2019.

Item 6. Defaults upon Senior Securities.

None.

Item 7. Other Information.

None.

Item 8. Exhibits.

The following is a list of all contracts which the Company is a party to, and which currently can reasonably be regarded as material to a security holder of the Company as of the date of this Quarterly Report:

- Lease Agreement for 670 N McCarthy Blvd, Milpitas, California, dated as of April 16, 2019, between McCarthy Center Holding LLC and the Company.
- Amended Line of Credit Agreement, dated as of September 1, 2018, between Wells Fargo Bank and the Company.
- Amended and Restated Certificate of Incorporation of the Company.
- Second Amended and Restated Bylaws of the Company.
- Certificate of Designation of Rights, Preferences and Privileges of Series A Participating Preferred Stock of the Company.
- Preferred Stock Rights Agreement, dated as of April 21, 2009, between the Company and Computershare Trust Company, N.A., including the Certificate of Designation, the form of Rights Certificate and the Summary of Rights attached thereto as Exhibits A, B and C, respectively.
- Executive Employment Agreement by and between Jeremiah J. Fleming and the Company, dated as of December 18, 2007.
- OEM Agreement between Altisys Communications and the Company, dated as of January 18, 1999.
- Distribution Agreement between Synnex Information Technologies, Inc. and the Company, dated as of December 22, 1999.
- Reseller Agreement between Fiserv Solutions, Inc. and the Company, dated as of August 28, 2009.

Copies of these agreements will be available for inspection at the office of the Company located at 670 N McCarthy Blvd Suite 200, Milpitas, California 95035, during ordinary business hours.

Item 9. Certifications.

CERTIFICATION OF CHIEF EXECUTIVE OFFICER

I, Jeremiah J. Fleming, certify that:

1. I have reviewed this quarterly disclosure statement of Altigen Communications, Inc.;

2. Based on my knowledge, this disclosure statement does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this disclosure statement; and

3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.

Date: August 15, 2019

BY: /s/ Jeremiah J. Fleming
Jeremiah J. Fleming
Chairman of the Board, President and Chief Executive Officer

CERTIFICATION OF VICE PRESIDENT OF FINANCE

I, Carolyn David, certify that:

1. I have reviewed this quarterly disclosure statement of Altigen Communications, Inc.;

2. Based on my knowledge, this disclosure statement does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this disclosure statement; and

3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.

Date: August 15, 2019

BY: /s/ Carolyn David
Carolyn David
Vice President of Finance