

CUI Global, Inc.
Form 10-Q
November 07, 2018

Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2018

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 0-29923

CUI Global, Inc.

(Exact name of registrant as specified in its charter)

Colorado 84-1463284
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

20050 SW 112th Avenue

Tualatin, Oregon 97062

(Address of principal executive offices and zip code)

(503) 612-2300

(Registrant's telephone number, including area code)

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

YES NO

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files).

YES NO

Table of Contents

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

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES NO

There were 28,550,792 shares of the registrant's common stock, par value \$0.001 per share, issued and outstanding as of November 7, 2018.

Table of Contents

INDEX

	Page
<u>Part I</u>	
Item 1. <u>Financial Statements</u>	2
<u>Condensed Consolidated Balance Sheets</u>	2
<u>Condensed Consolidated Statements of Operations (Unaudited)</u>	3
<u>Condensed Consolidated Statements of Comprehensive Income and Loss (Unaudited)</u>	4
<u>Condensed Consolidated Statement of Changes in Stockholders' Equity (Unaudited)</u>	5
<u>Condensed Consolidated Statements of Cash Flows (Unaudited)</u>	6
<u>Notes to the Condensed Consolidated Financial Statements (Unaudited)</u>	8
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	33
<u>Overview</u>	33
<u>Results of Operations</u>	34
<u>Liquidity and Capital Resources</u>	42
Item 3. <u>Quantitative and Qualitative Disclosure about Market Risk</u>	46
Item 4. <u>Controls and Procedures</u>	47
<u>Part II</u>	
Item 1. <u>Legal Proceedings</u>	48
Item 1A. <u>Risk Factors</u>	48
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds. Common Stock Issued</u>	48
Item 5. <u>Other Information</u>	49
Item 6. <u>Exhibits</u>	49
<u>Exhibit Index</u>	49
<u>Signatures</u>	50

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

CUI Global, Inc.

Condensed Consolidated Balance Sheets

	September 30, 2018 (Unaudited)	December 31, 2017
(in thousands, except share and per share amounts)		
Assets:		
Current Assets:		
Cash and cash equivalents	\$ 2,690	\$12,646
Trade accounts receivable, net of allowance of \$124 and \$135, respectively	12,174	10,833
Inventories, net of allowance of \$1,204 and \$946, respectively	16,052	13,892
Contract assets	1,575	2,299
Note receivable, current portion	337	13
Prepaid expenses and other	1,769	1,593
Total current assets	34,597	41,276
Property and equipment, less accumulated depreciation of \$4,905 and \$4,155, respectively	10,906	11,242
Goodwill	16,243	17,641
Other intangible assets, less accumulated amortization of \$13,014 and \$11,900, respectively	14,397	15,568
Note receivable, less current portion	—	317
Restricted cash	523	—
Convertible note receivable	500	—
Deposits and other assets	1,791	1,865
Total assets	\$ 78,957	\$87,909
Liabilities and Stockholders' Equity:		
Current Liabilities:		
Accounts payable	\$ 5,712	\$5,110
Short-term overdraft facility	1,278	—
Line of credit	657	—
Mortgage note payable, current portion	97	94
Accrued expenses	4,528	4,186
Contract liabilities	3,657	8,829
Refund liabilities	2,518	695
Total current liabilities	18,447	18,914

Long term mortgage note payable, less current portion	3,182	3,256
Long term note payable, related party	5,304	5,304
Derivative liability	192	356
Deferred tax liabilities	1,922	2,414
Other long-term liabilities	195	179
Total liabilities	29,242	30,423
Commitments and contingencies		
Stockholders' Equity:		
Preferred stock, par value \$0.001; 10,000,000 shares authorized; no shares issued at September 30, 2018 or December 31, 2017	—	—
Common stock, par value \$0.001; 325,000,000 shares authorized; 28,529,606 shares issued and outstanding at September 30, 2018 and 28,406,856 shares issued and outstanding at December 31, 2017	28	28
Additional paid-in capital	169,856	169,527
Accumulated deficit	(116,229)	(108,559)
Accumulated other comprehensive loss	(3,940)	(3,510)
Total stockholders' equity	49,715	57,486
Total liabilities and stockholders' equity	\$ 78,957	\$87,909

See accompanying notes to condensed consolidated financial statements

Table of Contents

CUI Global, Inc.

Condensed Consolidated Statements of Operations

(Unaudited)

(in thousands, except share and per share amounts)	For the Three Months		For the Nine Months	
	Ended September 30, 2018	2017	Ended September 30, 2018	2017
Total revenues	\$24,744	\$21,796	\$69,837	\$62,141
Cost of revenues	16,482	14,356	47,363	40,793
Gross profit	8,262	7,440	22,474	21,348
Operating expenses:				
Selling, general and administrative	8,499	8,212	26,944	25,480
Depreciation and amortization	535	521	1,618	1,636
Research and development	685	696	2,088	1,920
Provision (credit) for bad debt	24	30	(10)	(21)
Impairment of goodwill and intangible assets	—	—	1,263	3
Other operating expenses	3	—	3	9
Total operating expenses	9,746	9,459	31,906	29,027
Loss from operations	(1,484)	(2,019)	(9,432)	(7,679)
Other income (expense)	(61)	77	(39)	169
Interest expense	(132)	(137)	(370)	(374)
Loss before taxes	(1,677)	(2,079)	(9,841)	(7,884)
Income tax benefit	(143)	(177)	(280)	(560)
Net loss	\$(1,534)	\$(1,902)	\$(9,561)	\$(7,324)
Basic and diluted weighted average common shares outstanding	28,527,234	20,991,534	28,507,286	20,969,735
Basic and diluted loss per common share	\$(0.05)	\$(0.09)	\$(0.34)	\$(0.35)

See accompanying notes to condensed consolidated financial statements

Table of Contents

CUI Global, Inc.

Condensed Consolidated Statements of Comprehensive Income and Loss

(Unaudited)

	For the Three Months		For the Nine Months	
(in thousands)	Ended September 30,		Ended September 30,	
	2018	2017	2018	2017
Net loss	\$(1,534)	\$(1,902)	\$(9,561)	\$(7,324)
Other comprehensive income (loss)				
Foreign currency translation adjustment	(48)	771	(430)	1,971
Comprehensive loss	\$(1,582)	\$(1,131)	\$(9,991)	\$(5,353)

See accompanying notes to condensed consolidated financial statements

Table of Contents

CUI Global, Inc.

Condensed Consolidated Statement of Changes in Stockholders' Equity

For the Nine Months Ended September 30, 2018

(Unaudited)

(In thousands, except share amounts)	Common Stock		Additional		Accumulated		Total
	Shares	Amount	Paid-in Capital	Accumulated Deficit	Other Comprehensive Loss	Stockholders' Equity	
Balance, December 31, 2017	28,406,856	\$ 28	\$ 169,527	\$ (108,559)	\$ (3,510)		\$ 57,486
Cumulative effect of accounting change (1)	—	—	—	1,891	—		1,891
Balance at January 1, 2018, adjusted	28,406,856	28	169,527	(106,668)	(3,510)		59,377
Common stock issued for compensation, services, and royalty payments	122,750	—	329	—	—		329
Net loss for the period ended September 30, 2018	—	—	—	(9,561)	—		(9,561)
Other comprehensive loss	—	—	—	—	(430)		(430)
Balance, September 30, 2018	28,529,606	\$ 28	\$ 169,856	\$ (116,229)	\$ (3,940)		\$ 49,715

(1) Represents adjustment to accumulated deficit upon the adoption of Accounting Standards Codification Topic 606.

See accompanying notes to condensed consolidated financial statements

Table of Contents

CUI Global, Inc.

Condensed Consolidated Statements of Cash Flows

(Unaudited)

(in thousands)

For the Nine
Months Ended
September 30,
2018 2017

CASH FLOWS FROM OPERATING ACTIVITIES:

Net loss	\$ (9,561)	\$ (7,324)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation	816	744
Amortization of intangibles	1,429	1,388
Stock issued and stock to be issued for compensation, royalties and services	188	313
Unrealized gain on derivative liability	(164)	(55)
Provision for (credit to) bad debt expense and returns allowances	(10)	(21)
Deferred income taxes	(352)	(666)
Inventory reserve	274	317
Non-cash unrealized foreign currency (gains) losses	135	(307)
Impairment of goodwill and intangible assets	1,263	3
Loss on disposal of assets	3	9
(Increase) decrease in operating assets:		
Trade accounts receivable	(1,439)	(1,667)
Inventories	(3,727)	(902)
Contract assets	160	1,402
Prepaid expenses and other current assets	(285)	(562)
Deposits and other assets	13	(515)
Increase (decrease) in operating liabilities:		
Accounts payable	520	(321)
Accrued expenses	684	(499)
Refund liabilities	953	(30)
Contract liabilities	(853)	2,932
NET CASH USED IN OPERATING ACTIVITIES	(9,953)	(5,761)

CASH FLOWS FROM INVESTING ACTIVITIES:

Purchases of property and equipment	(644)	(635)
Proceeds from sale of property and equipment	—	2
Investments in other intangible assets	(348)	(448)
Proceeds from notes receivable	—	19
Investment in convertible note receivable	(500)	—
NET CASH USED IN INVESTING ACTIVITIES	(1,492)	(1,062)

CASH FLOWS FROM FINANCING ACTIVITIES:

Edgar Filing: CUI Global, Inc. - Form 10-Q

Proceeds from overdraft facility	13,895	2,146
Payments on overdraft facility	(12,570)	(1,174)
Proceeds from line of credit	6,696	19,585
Payments on line of credit	(6,039)	(17,653)
Payments on capital lease obligations	(2)	(27)
Payments on mortgage note payable	(71)	(66)
Payments on contingent consideration	(45)	(61)
NET CASH PROVIDED BY FINANCING ACTIVITIES	1,864	2,750
Effect of exchange rate changes on cash	148	214
Net decrease in cash, cash equivalents and restricted cash	(9,433)	(3,859)
Cash, cash equivalents and restricted cash at beginning of period	12,646	4,617
CASH, CASH EQUIVALENTS AND RESTRICTED CASH AT END OF PERIOD	\$3,213	\$758

See accompanying notes to condensed consolidated financial statements

Table of Contents

CUI Global, Inc.

Condensed Consolidated Statements of Cash Flows (continued)

(Unaudited)

(in thousands)	For the Nine Months Ended September 30, 2018 2017	
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Income taxes paid	\$205	\$130
Interest paid, net of capitalized interest	\$373	\$375
SUPPLEMENTAL DISCLOSURE OF NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Common stock issued and to be issued for royalties payable pursuant to product agreements, related party	\$9	\$8
Common stock issued and to be issued for consulting services and compensation in common stock	\$320	\$389
Partial settlement of note receivable via offset against royalty payable netted with (increase) to note receivable from accrued interest	\$(6)	\$(6)
Accrued property and equipment purchases at September 30	\$52	\$21
Accrued investment in other intangible assets at September 30	\$129	\$83

See accompanying notes to condensed consolidated financial statements

Table of Contents

CUI Global, Inc.

Notes to the Condensed Consolidated Financial Statements

(Unaudited)

1. NATURE OF OPERATIONS, BASIS OF PRESENTATION AND COMPANY CONDITIONS

Nature of Operations

CUI Global Inc. (CUI Global) is a platform company composed of two segments, the Power and Electromechanical segment and the Energy segment, along with an "Other" category.

The Power and Electromechanical segment consists of the wholly owned subsidiaries: CUI, Inc. (CUI), based in Tualatin, Oregon; CUI Japan, based in Tokyo, Japan; CUI-Canada, based in Toronto, Canada; and the entity holding the corporate building, CUI Properties. All three operating subsidiaries are providers of power and electromechanical components for Original Equipment Manufacturers (OEMs).

The Power and Electromechanical segment aggregates its product offerings into two categories: **power solutions** - including external and embedded ac-dc power supplies, dc-dc converters and basic digital point of load modules, ICE (Intelligent Control of Energy) products enabled by the VPS patented software system and offering a technology architecture that addresses power and related accessories; and **components** - including connectors, speakers, buzzers, and industrial control solutions including encoders and sensors. These offerings provide a technology architecture that addresses power and related accessories to industries as broadly ranging as telecommunications, consumer electronics, medical and defense.

The Company's Energy segment consists of the Orbital Gas Systems Ltd subsidiary (Orbital-UK) and the Orbital Gas Systems, North America, Inc. subsidiary, collectively referred to as "Orbital." Orbital has developed a portfolio of products, services and resources to offer a diverse range of personalized gas engineering solutions to the gas utilities, power generation, emissions, manufacturing and automotive industries. Its proprietary VE® Technology enhances the capability and speed of our GasPT® Technology. VE Technology provides a superior method of penetrating the gas flow without the associated vortex vibration, thereby making it a "stand-alone" product for thermal sensing (thermowells) and trace-element sampling.

The Other category represents the remaining activities that are not included as part of the other reportable segments and primarily represents corporate activity.

Basis of Presentation

The accompanying interim unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America and the rules and regulations of the United States Securities and Exchange Commission for interim financial information, which includes condensed consolidated financial statements. Accordingly, they do not include all the information and notes necessary for a comprehensive presentation of financial position and results of operations and should be read in conjunction with the Company's Annual Report, Form 10-K for the year ended December 31, 2017.

It is management's opinion that all material adjustments (consisting of normal recurring adjustments as well as an adjustment for goodwill impairment) have been made, which are necessary for a fair financial statement presentation. Significant intercompany accounts and transactions have been eliminated in consolidation. The results for the interim period are not necessarily indicative of the results to be expected for the year ending December 31, 2018.

Table of Contents

As a result of the adoption of ASC 606 (Note 2), the following items have been reclassified from the captions in the December 31, 2017 consolidated balance sheet included in our Form 10-K for the year ended December 31, 2017 to the captions in the December 31, 2017 condensed consolidated balance sheet appearing herein:

Captions in December 31, 2017 consolidated balance sheet within Form 10-K	Reclassified to	Captions in December 31, 2017 condensed consolidated balance sheet herein
Costs in excess of billings		Contract assets
Billings in excess of costs		Contract liabilities
Unearned revenue		Contract liabilities
Unearned revenue		Refund liabilities

Changes in these accounts as reclassified are reflected on the condensed consolidated statement of cash flows for the nine months ended September 30, 2018 and 2017.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, 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. Actual results could differ from those estimates. Significant estimates include estimates used to review the Company's goodwill, impairments and estimations of long-lived assets, impairment of prepaid royalties, revenue recognition on cost-to-cost-method type contracts, inventory valuation, trading securities, warranty reserves, refund liabilities/returns allowances, valuations of non-cash capital stock issuances and the valuation allowance on deferred tax assets. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable in the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Reclassification

Certain reclassifications have been made to the 2017 condensed consolidated balance sheet, and statement of operations and statement of cash flows in order to conform to the 2018 presentation.

Company Conditions

The continued delays in shipment of GasPTs on a significant project due to governmental delays in Italy and the related slower than expected acceptance of this new disruptive technology has caused a delay in our expected profitability.

The Company had losses of \$9.6 million and cash used in operating activities of \$(10.0) million during the nine months ended September 30, 2018. As of September 30, 2018, our accumulated deficit is \$116.2 million.

Management believes the Company's present cash flows will not enable it to meet its obligations for twelve months from the date these financial statements are available to be issued. However, management has developed a plan to address this issue. The plan includes obtaining a new long-term financing in the form of a renewed line of credit, and the issuances of a signed letter of intent signed on October 4, 2018 for the sale/leaseback of our Tualatin headquarters. The line of credit renewal and sale/leaseback transaction are both expected to close during the fourth quarter of 2018 and will result in significant cash inflow. In addition to these plans, as of September 30, 2018, the Company has unused availability of \$3.3 million on its current line of credit and unused availability of \$0.7 million under its Overdraft Facility. Including our cash balance, we further have \$16.2 million of positive working capital primarily related to trade accounts receivable and our inventory less current liabilities that we will manage in the next twelve months to create positive cash flow. It is probable that management's plans will be achieved and will enable the Company to meet its obligations for the twelve-month period from the date the financial statements are available to be issued.

Table of Contents

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - UPDATE

Our significant accounting policies are detailed in "Note 2 Summary of Significant Accounting Policies" within Item 8 of our Annual Report on Form 10-K for the year ended December 31, 2017 filed with the SEC on March 14, 2018. Significant changes to our accounting policies as a result of adopting Topic 606 are discussed below:

Revenue Recognition

On January 1, 2018, we adopted the new accounting standard ASC 606, "Revenue from Contracts with Customers" and all the related amendments ("new revenue standard"), which supersedes nearly all existing revenue recognition guidance under U.S. GAAP. This guidance includes the required steps to achieve the core principle that a company should recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. The new revenue standard was applied using the modified retrospective method. We recognized the cumulative effect of initially applying the new revenue standard as an adjustment to accumulated deficit as of January 1, 2018. As a result of the adoption of this standard, certain changes have been made to the condensed consolidated balance sheets. We expect the ongoing impact of the adoption of the new standard to primarily affect the timing of revenue recognition. The most significant impact was on Power and Electromechanical segment revenue that was previously recorded as "sell through." This revenue was previously recorded upon the sale by our customers, who are distributors. Under the new accounting guidance, we record the revenue upon sale to the distributor with an appropriate amount reserved for estimated returns and allowances as the Company recognizes revenue at the time the related performance obligation is satisfied by transferring a promised good or service to its customers. For the Power and Electromechanical segment, their revenue is based upon the transfer of goods and satisfaction of its performance obligations as of a point in time. During the transition this had the effect of having a certain amount of revenue not recorded as revenue but as part of the cumulative effect of the accounting change. In the Energy segment, for the majority of contracts, revenue is still measured over time using the cost-to-cost method. The change that most affected the transition adjustment on Energy revenue was the requirement to limit revenue recognition on contracts without an enforceable right to payment for performance completed to date. Revenue on contracts without a specific enforceable right to payment on work performed to date was "clawed back" as part of the Company's transition adjustment. The cumulative effect adjustment recorded as of January 1, 2018 was a net \$1.9 million decrease to accumulated deficit due to a \$2.8 million transition adjustment from the Power and Electromechanical segment partially offset by a \$(0.9) million transition adjustment from the Energy segment, net of deferred tax. See Note 3 for further discussion of our revenue recognition policies.

Table of Contents**3. REVENUE FROM CONTRACTS WITH CUSTOMERS**

On January 1, 2018, we adopted ASC Topic 606 and the related amendments ("ASC 606") using the modified retrospective method applied to those contracts which were not completed as of December 31, 2017. Results for operating periods beginning after January 1, 2018 are presented under ASC 606, while comparative information has not been restated and continues to be reported in accordance with the accounting standards in effect for those periods. See Note 2 for a description of our accounting policy resulting from adoption of ASC 606. We recognized the cumulative effect of initially applying ASC 606 as an adjustment to accumulated deficit in the balance sheet as of January 1, 2018 as follows:

	Balance at December 31, 2017	Adjustments Due to ASC 606	Balance at January 1, 2018
(in thousands)			
<u>Assets</u>			
Inventories	\$ 13,892	\$ (1,064)	) \$ 12,828
Contract assets	2,299	(516)	) 1,783
Total current assets	41,276	(1,580)	) 39,696
Total assets	\$ 87,909	\$ (1,580)	) \$ 86,329
<u>Liabilities</u>			
Contract liabilities	\$ 8,829	\$ (4,168)	) \$ 4,661
Refund liabilities	695	870	) 1,565
Total current liabilities	18,914	(3,298)	) 15,616
Deferred tax liabilities	2,414	(173)	) 2,241
Total liabilities	30,423	(3,471)	) 26,952
<u>Stockholders' Equity</u>			
Accumulated deficit	(108,559)	1,891	(106,668)
Total stockholders' equity	57,486	1,891	59,377
Total liabilities and stockholders' equity	\$ 87,909	\$ (1,580)	) \$ 86,329

The impact of adoption on our condensed consolidated balance sheet and condensed consolidated statement of operations as of and for the period ended September 30, 2018 was as follows:

For the Three Months Ended
September 30, 2018

		Balances	Effect
		Without	of
(in thousands except per share amounts)	As Reported	Adoption of	Change Higher /
		ASC 606	(Lower)
<u>Statement of Operations</u>			
Total revenues	\$24,744	\$23,581	\$1,163
Cost of revenues	16,482	15,799	683
Gross profit	8,262	7,782	480
Loss from operations	(1,484)	(1,964)	480
Loss before taxes	(1,677)	(2,157)	480
Net loss	\$(1,534)	\$(2,014)	\$480
Basic and diluted loss per common share	\$(0.05)	\$(0.07)	\$0.02

Table of Contents

(in thousands except per share amounts)	For the Nine Months Ended September 30, 2018		
	Balances	Effect of	
	Without		
	As Reported	Adoption of	Change Higher /
		ASC 606	(Lower)

Statement of Operations

Total revenues	\$69,837	\$67,080	\$ 2,757
Cost of revenues	47,363	46,248	1,115
Gross profit	22,474	20,832	1,642
Loss from operations	(9,432)	(11,074)	1,642
Loss before taxes	(9,841)	(11,483)	1,642
Income tax (benefit) expense	(280)	(453)	173
Net loss	\$(9,561)	\$(11,030)	\$ 1,469
Basic and diluted loss per common share	\$(0.34)	\$(0.39)	\$ 0.05

	As of September 30, 2018		
	Balances	Effect of	
	Without		
	As Reported	Adoption of	Change Higher /
		ASC 606	(Lower)

(in thousands)

Assets

Inventories	\$16,052	\$18,212	\$(2,160)
Contract assets	1,575	2,534	(959)
Total current assets	34,597	37,716	(3,119)
Total assets	\$78,957	\$82,076	\$(3,119)

Liabilities

Accrued expenses	\$4,528	\$4,441	\$87
Contract liabilities	3,657	11,772	(8,115)
Refund liabilities	2,518	976	1,542
Total current liabilities	18,447	24,933	(6,486)
Total liabilities	29,242	35,728	(6,486)

Stockholders' Equity

Accumulated deficit	(116,229)	(119,589)	3,360
Accumulated other comprehensive loss	(3,940)	(3,947)	7
Total stockholders' equity	49,715	46,348	3,367

Total liabilities and stockholders' equity \$78,957 \$82,076 \$(3,119)

The adoption of ASC 606 had no impact on the Company's cash flows from operations.

Table of Contents

Power and Electromechanical segment

The Power and Electromechanical segment generates its revenue from two categories of products: **power solutions** - including external and embedded ac-dc power supplies, dc-dc converters and basic digital point of load modules, ICE (Intelligent Control of Energy) products enabled by the VPS patented software system and offering a technology architecture that addresses power and related accessories; and **components** - including connectors, speakers, buzzers, and industrial control solutions including encoders and sensors. These offerings provide a technology architecture that addresses power and related accessories to industries as broadly ranging as telecommunications, consumer electronics, medical and defense. The production and delivery of these products are considered single performance obligations. Revenue is recognized when we satisfy a performance obligation and this occurs upon shipment and ownership transfer of our products to our customers at a point in time.

Energy segment

The Energy segment subsidiaries, collectively referred to as Orbital, generate their revenue from a portfolio of products, services and resources that offer a diverse range of personalized gas engineering solutions to the gas utilities, power generation, emissions, manufacturing and automotive industries.

Orbital accounts for a majority of its contract revenue proportionately over time. For our performance obligations satisfied over time, we recognize revenue by measuring the progress toward complete satisfaction of that performance obligation. The selection of the method to measure progress towards completion can be either an input method or an output method and requires judgment based on the nature of the goods or services to be provided.

For our construction contracts, revenue is generally recognized over time as our performance creates or enhances an asset that the customer controls. Our fixed price construction projects generally use a cost-to-cost input method to measure our progress towards complete satisfaction of the performance obligation as we believe it best depicts the transfer of control to the customer. Under the cost-to-cost measure of progress, the extent of progress towards completion is measured based on the ratio of costs incurred to date to the total estimated costs at completion of the performance obligation.

The timing of revenue recognition for Energy products also depends on the payment terms of the contract, as our performance does not create an asset with an alternative use to us. For those contracts which we have a right to payment for performance completed to date at all times throughout our performance, inclusive of a cancellation, we recognize revenue over time. As discussed above, these performance obligations use a cost-to-cost input method to measure our progress towards complete satisfaction of the performance obligation as we believe it best depicts the transfer of control to the customer. However, for those contracts for which we do not have a right, at all times, to payment for performance completed to date, we recognize revenue at the point in time when control is transferred to the customer.

For our services contracts, revenue is also generally recognized over time as the customer simultaneously receives and consumes the benefits of our performance as we perform the service. For our fixed price service contracts with specified service periods, revenue is generally recognized on a straight-line basis over such service period when our inputs are expended evenly, and the customer receives and consumes the benefits of our performance throughout the contract term.

For certain of our revenue streams, such as call-out repair and service work, and outage services, that are performed under time and materials contracts, our progress towards complete satisfaction of such performance obligations is measured using an output method as the customer receives and consumes the benefits of our performance completed to date.

Table of Contents

Due to uncertainties inherent in the estimation process, it is possible that estimates of costs to complete a performance obligation will be revised in the near-term. For those performance obligations for which revenue is recognized using a cost-to-cost input method, changes in total estimated costs, and related progress towards complete satisfaction of the performance obligation, are recognized on a cumulative catch-up basis in the period in which the revisions to the estimates are made. When the current estimate of total costs for a performance obligation indicate a loss, a provision for the entire estimated loss on the unsatisfied performance obligation is made in the period in which the loss becomes evident.

Product-type contracts (for example, sale of GasPt units) for which revenue does not qualify to be recognized over time are recognized at a point in time. Revenues from warranty and maintenance activities are recognized ratably over the term of the warranty and maintenance period.

Accounts Receivable, Contract Assets and Contract Liabilities

Accounts receivable are recognized in the period when our right to consideration is unconditional. Accounts receivable are recognized net of an allowance for doubtful accounts. A considerable amount of judgment is required in assessing the likelihood of realization of receivables.

The timing of revenue recognition may differ from the timing of invoicing to customers. Contract assets include unbilled amounts from our construction projects when revenue recognized under the cost-to-cost measure of progress exceed the amounts invoiced to our customers, as the amounts cannot be billed under the terms of our contracts. Such amounts are recoverable from our customers based upon various measures of performance, including achievement of certain milestones, completion of specified units or completion of a contract. Also included in contract assets are amounts we seek or will seek to collect from customers or others for errors or changes in contract specifications or design, contract change orders or modifications in dispute or unapproved as to both scope and/or price or other customer-related causes of unanticipated additional contract costs (claims and unapproved change orders). Our contract assets do not include capitalized costs to obtain and fulfill a contract. Contract assets are generally classified as current within the Condensed Consolidated Balance Sheets.

Contract liabilities from our construction contracts occur when amounts invoiced to our customers exceed revenues recognized under the cost-to-cost measure of progress. Contract liabilities additionally include advanced payments from our customers on certain contracts. Contract liabilities decrease as we recognize revenue from the satisfaction of the related performance obligation and are recorded as either current or long-term, depending upon when we expect to recognize such revenue.

Table of Contents

Activity in the current contract liabilities for the nine months ended September 30, 2018 was as follows:

(in thousands)

Current contract liabilities - January 1, 2018	\$4,661
Long-term contract liabilities - January 1, 2018 ⁽¹⁾	84
Total Contract liabilities - January 1, 2018	\$4,745
 Total Contract liabilities - January 1, 2018	 \$4,745
Contract Additions, net	2,610
Revenue recognized	(3,451)
Translation	(145)
Total contract liabilities - September 30, 2018	\$3,759
 Current contract liabilities - September 30, 2018	 \$3,657
Long-term contract liabilities - September 30, 2018 ⁽¹⁾	102
Total Contract liabilities - September 30, 2018	\$3,759

⁽¹⁾ Long-term contract liabilities are included in Other long-term liabilities on the Condensed Consolidated Balance Sheets.

Refund Liabilities and Corresponding Inventory Adjustment

Refund liabilities primarily represent estimated future new product introduction returns and estimated future scrap returns. Future new product returns are based on a percent of current inventory of newly introduced products held by our distributor customers. The liability for estimated returns of newly introduced product is reversed to revenue as the inventory is sold. Future scrap returns are based on a percentage of total revenues. In addition to the refund liabilities recorded for future returns, the Company also records an adjustment to inventory and corresponding adjustment to cost of revenue for the Company's right to recover products from customers upon settling the refund liability.

Performance Obligations

Remaining Performance Obligations

Remaining performance obligations, represents the transaction price of firm orders for which work has not been performed and excludes unexercised contract options and potential orders under ordering-type contracts. As of September 30, 2018, the Company's remaining performance obligations are generally expected to be filled within the next 12 months.

Any quarterly adjustments to net revenues, cost of revenues, and the related impact to operating income are recognized as necessary in the period they become known. These adjustments may result from positive program performance, and may result in an increase in operating income during the performance of individual performance obligations, if we determine we will be successful in mitigating risks surrounding the technical, schedule and cost aspects of those performance obligations. Likewise, these adjustments may result in a decrease in operating income if we determine we will not be successful in mitigating these risks. Changes in estimates of net revenues, cost of revenues and the related impact to operating income are recognized quarterly on a cumulative catch-up basis, which recognizes in the current period the cumulative effect of the changes on current and prior periods based on a performance obligation's percentage of completion. A significant change in one or more of these estimates could affect the profitability of one or more of our performance obligations. For separately priced extended warranty or product maintenance performance obligations, when estimates of total costs to be incurred on the performance obligation exceed total estimates of revenue to be earned, a provision for the entire loss on the performance obligation is recognized in the period the loss is determined.

Table of Contents

Performance Obligations Satisfied Over Time

To determine the proper revenue recognition method for contracts for our Energy segment, we evaluate whether a single contract should be accounted for as more than one performance obligation. This evaluation requires significant judgment and the decision to separate the single contract into multiple performance obligations could change the amount of revenue and profit recorded in a given period.

For most of our contracts, the customer contracts with us to provide a significant service of integrating a complex set of tasks and components into a single project or capability (even if that single project results in the delivery of multiple units). Hence, the entire contract is accounted for as one performance obligation. Less commonly, however, we may promise to provide distinct goods or services within a contract in which case we separate the contract into more than one performance obligation. If a contract is separated into more than one performance obligation, we allocate the total transaction price to each performance obligation in an amount based on the estimated relative standalone selling prices of the promised goods or services underlying each performance obligation. We infrequently sell standard products with observable standalone sales. In cases where we do, the observable standalone sales are used to determine the standalone selling price. More frequently, we sell a customized customer specific solution, and in these cases we typically use the expected cost plus a margin approach to estimate the standalone selling price of each performance obligation.

Performance Obligations Satisfied at a Point in Time.

Revenue from goods and services transferred to customers at a single point in time accounted for 86% of revenues for the nine-month period ended September 30, 2018. The majority of our revenue recognized at a point in time is in our Power and Electromechanical segment. Revenue on these contracts is recognized when the product is shipped and the customer takes ownership of the product. Determination of ownership and control transfer is determined by shipping terms delineated on the customer purchase orders.

Variable Consideration

The nature of our contracts gives rise to several types of variable consideration, including new product returns and scrap returns allowances primarily in our Power and Electromechanical segment. In rare instances in our Energy segment, we include in our contract estimates, additional revenue for submitted contract modifications or claims against the customer when we believe we have an enforceable right to the modification or claim, the amount can be estimated reliably and its realization is probable. In evaluating these criteria, we consider the contractual/legal basis for the claim, the cause of any additional costs incurred, the reasonableness of those costs and the objective evidence available to support the claim. We include new product introduction and scrap return estimates in our calculation of net revenue when there is a basis to reasonably estimate the amount of the returns. These estimates are based on historical return experience, anticipated returns and our best judgment at the time. These amounts are included in our calculation of net revenue recorded for our contracts and the associated remaining performance obligations.

Table of Contents

The following table presents our revenues disaggregated by revenue source for the three months ended September 30, 2018:

(in thousands)	Power and Electromechanical	Energy	Total
Distributor sales	\$ 11,736	\$—	\$11,736
Direct Sales	7,853	5,155	13,008
Total revenues	\$ 19,589	\$5,155	\$24,744

The following table presents our revenues disaggregated by revenue source for the nine months ended September 30, 2018:

(in thousands)	Power and Electromechanical	Energy	Total
Distributor sales	\$ 33,514	\$—	\$33,514
Direct Sales	23,415	12,908	36,323
Total revenues	\$ 56,929	\$12,908	\$69,837

The following table presents our revenues disaggregated by timing of revenue recognition for the three months ended September 30, 2018:

(in thousands)	Power and Electromechanical	Energy	Total
Revenues recognized at point in time	\$ 19,589	\$1,437	\$21,026
Revenues recognized over time	—	3,718	3,718
Total revenues	\$ 19,589	\$5,155	\$24,744

The following table presents our revenues disaggregated by timing of revenue recognition for the nine months ended September 30, 2018:

(in thousands)	Power and Electromechanical		Energy	Total
Revenues recognized at point in time	\$ 56,929		\$3,370	\$60,299
Revenues recognized over time	—		9,538	9,538
Total revenues	\$ 56,929		\$12,908	\$69,837

Table of Contents

The following table presents our revenues disaggregated by region for the three months ended September 30, 2018:

(in thousands)	Power and Electromechanical	Energy	Total
North America	\$ 14,883	\$1,092	\$15,975
Europe	1,010	3,843	4,853
Asia	3,445	154	3,599
Other	251	66	317
Total revenues	\$ 19,589	\$5,155	\$24,744

The following table presents our revenues disaggregated by region for the nine months ended September 30, 2018:

(in thousands)	Power and Electromechanical	Energy	Total
North America	\$ 42,973	\$3,185	\$46,158
Europe	3,201	9,425	12,626
Asia	10,394	189	10,583
Other	361	109	470
Total revenues	\$ 56,929	\$12,908	\$69,837

4. INVENTORIES

Inventories consist of raw materials, work-in-process and finished goods and are stated at the lower of cost or market using the first-in, first-out (FIFO) method or through the moving average cost method. At September 30, 2018 and December 31, 2017, accrued liabilities included \$1.8 million and \$1.3 million of accrued inventory payable, respectively. At September 30, 2018 and December 31, 2017, inventory by category is valued net of reserves and consists of:

(in thousands)	September 30, 2018	December 31, 2017
Finished goods	\$ 9,872	\$ 10,792
Raw materials	3,830	3,287

Work-in-process	3,554	759
Inventory reserves	(1,204)	(946)
Total inventories	\$ 16,052	\$ 13,892

Table of Contents**5. PREPAID EXPENSES, DEPOSITS AND OTHER**

	September 30, 2018	December 31, 2017
(in thousands)		
Prepaid expenses and other	\$ 1,769	\$ 1,593
Deposits and other assets	\$ 1,791	\$ 1,865

During the second quarter of 2017, prepaid royalties in the amount of \$1.6 million were transferred to long-term and included in Deposits and other assets from prepaid expenses due to a change in the estimated period of when those prepayments will be amortized based upon management's assessment of future GasPT sales. At September 30, 2018 and December 31, 2017, there were \$1.7 million and \$1.8 million of prepaid royalties included in Deposits and other assets, respectively.

6. GOODWILL AND INDEFINITE-LIVED INTANGIBLES

The Company tests for impairment of Indefinite-lived intangibles and Goodwill in the second quarter of each year and when events or circumstances indicate that the carrying amount of Goodwill exceeds its fair value and may not be recoverable. The Company's qualitative assessment of impairment for indefinite-lived assets at May 31, 2018, followed the guidance in ASC 350-30-35-18A and 18B and determined there was no impairment of indefinite-lived intangibles at that time.

Under current accounting guidance, CUI Global is not required to calculate the fair value of a reporting unit unless the entity determines, based on a qualitative assessment, that it is more likely than not that its fair value is less than its carrying amount. The guidance includes a number of factors to consider in conducting the qualitative assessment. The Company tests for goodwill impairment in the second quarter of each year and whenever events or changes in circumstances indicate that the carrying amount of the asset exceeds its fair value and may not be recoverable.

As detailed in ASC 350-20-35-3A, in performing its testing for impairment of goodwill as of May 31, 2018, management completed a qualitative analysis to determine whether it was more likely than not that the fair value of a reporting unit is less than its carrying amount, including goodwill. To complete the qualitative review, management follows the steps in ASC 350-20-35-3C to evaluate the fair values of the goodwill and considers all known events and circumstances that might trigger an impairment of goodwill.

During our review of goodwill as of May 31, 2018, the Company determined that there were indicators present to suggest that it was more likely than not that the fair value of the Orbital-UK reporting unit was less than its carrying amount.

The significant changes for the Orbital-UK reporting unit subsequent to the most recent impairment test performed as of December 31, 2017 included a decline in the 2018 actual revenue, operating income and cash flows compared to prior forecasts for the same period and a negative change in the 2018 forecasted revenue, operating income and cash flows for the remainder of the year due in part to the longer than expected temporary halt in shipping of its GasPT product to a major customer in Italy and market uncertainty due to the continuing effects of Brexit.

To test the Orbital-UK reporting unit for impairment as of May 31, 2018, the Company used a quantitative test. The Company estimated the fair value of the Orbital-UK reporting unit using a blend of a market approach and an income approach, which was deemed to be the most indicative of fair value in an orderly transaction between market participants. Under the income approach, the Company determined fair value based on estimated future cash flows of the Orbital-UK reporting unit discounted by an estimated weighted-average cost of capital, reflecting the overall level of inherent risk of the Orbital-UK reporting unit and the rate of return an outside investor would expect to earn. The Company based its cash flow projections for the Orbital-UK reporting unit using a forecast of cash flows and a terminal value developed by capitalizing an assumed stabilized cash flow figure. The forecast and related assumptions were derived from an updated financial forecast prepared during the second quarter of 2018. At this time, a key assumption related to the recoverability of the Orbital-UK reporting unit goodwill is the resumption of delivery of GasPT product to one of our major customers and continued strengthening of our integration revenues. Under the market approach, appropriate valuation multiples were derived from the historical operating data of selected guideline companies. The valuation multiples were evaluated and adjusted based on the strengths and weaknesses of the Company relative to the selected guideline companies and the multiple was then applied to the appropriate operating data of the Company to arrive at an indication of fair market value. As a result of the analysis, the Company concluded that the carrying value of the Orbital-UK reporting unit exceeded its estimated fair value. The quantitative test for the Orbital-UK reporting unit resulted in an impairment for the Orbital-UK reporting unit, and the Company recorded a goodwill impairment charge of \$1.3 million during the second quarter of 2018.

Table of Contents

The remaining goodwill related to the Orbital-UK reporting unit as of September 30, 2018 and December 31, 2017 was \$3.2 million and \$4.5 million, respectively, which is included in the Energy segment. As of September 30, 2018, there was also goodwill remaining for CUI Inc., CUI-Canada and CUI-Japan reporting units, which are included in the Power and Electromechanical segment.

The carrying value of goodwill and the activity for the nine months ended September 30, 2018 are as follows:

	Power and			
(in thousands)	Electro -	Energy	Other	Total
	Mechanical			
Balance, December 31, 2017	\$ 13,092	\$ 4,549	\$ —	\$ 17,641
Currency translation adjustments	(3)	(132)	—	(135)
Goodwill impairment	—	(1,263)	—	(1,263)
Balance, September 30, 2018	\$ 13,089	\$ 3,154	\$ —	\$ 16,243

7. INVESTMENTS

During the three months ended March 31, 2016, CUI Global's 8.5% ownership investment in Test Products International, Inc. ("TPI"), recognized under the cost method, was exchanged for a note receivable from TPI of \$0.4 million (\$0.3 million balance at September 30, 2018 and December 31, 2017), which was the carrying value of the investment, earning interest at 5% per annum, due June 30, 2019. The Company recorded \$4 thousand and \$5 thousand of interest income from the note in the three months ended September 30, 2018 and 2017, respectively. The Company recorded \$13 thousand and \$13 thousand of interest income from the note in the nine months ended September 30, 2018 and 2017, respectively. The interest receivable is settled on a quarterly basis via a non-cash offset against the finders-fee royalties earned by TPI on GasPT sales. Any remaining finders-fee royalties balance is offset against the note receivable quarterly. The Company also received a \$19 thousand cash payment against the note in the nine months ended September 30, 2017. CUI Global reviewed the note receivable for non-collectability as of September 30, 2018 and concluded that no allowance was necessary. For more details on this investment see Note 2 - Summary of Significant Accounting policies to CUI Global's financial statements filed in Item 8 of the Company's latest Form 10-K filed with the SEC on March 14, 2018.

During July 2018, CUI Global made an investment of \$0.5 million in a convertible note receivable with Virtual Power Systems ("VPS") to support the two companies' continued collaboration and development of industry transforming Software Defined Power technologies. The note accrues interest at 2% per annum and the interest is compounded annually. Unless converted into shares earlier, principal and accrued interest will convert automatically on the maturity date (October 27, 2019) into shares of VPS common stock at the then current fair market value. If VPS

receives gross proceeds greater than \$3 million prior to the maturity date in a sale or series of sales of equity securities, the principal and unpaid accrued interest of the note will automatically convert into shares at 80% of the price paid per share for equity securities by investors at that time. The fair market value of the investment at September 30, 2018 is estimated to be the same as its current carrying value with no gains recorded since acquisition.

Table of Contents

8. DERIVATIVE INSTRUMENTS

The Company uses various derivative instruments including forward currency contracts, and interest rate swaps to manage certain exposures. These instruments are entered into under the Company's corporate risk management policy to minimize exposure and are not for speculative trading purposes. The Company recognizes all derivatives as either assets or liabilities in the condensed consolidated balance sheet and measures those instruments at fair value. Changes in the fair value of derivatives are recognized in earnings. For additional information on fair value of derivatives, see Note 12, "Investments and Fair Value Measurements," of these condensed consolidated financial statements. The Company has limited involvement with derivative instruments and does not trade them. The Company has entered into one interest rate swap, which has a maturity date of ten years from the date of inception, and is used to minimize the interest rate risk on the variable rate mortgage. During the three and nine months ended September 30, 2018, the Company had \$38 thousand and \$164 thousand, respectively of unrealized gain related to the derivative liabilities. During the three and nine months ended September 30, 2017, the Company had \$20 thousand and \$55 thousand, respectively of unrealized gain related to the derivative liabilities.

Embedded Derivative Liabilities

The Company evaluates embedded conversion features pursuant to FASB Accounting Standards Codification No. 815 ("FASB ASC 815"), "Derivatives and Hedging," which requires a periodic valuation of the fair value of derivative instruments and a corresponding recognition of liabilities associated with such derivatives.

9. STOCK-BASED PAYMENTS FOR COMPENSATION, SERVICES AND ROYALTIES

The Company records its stock-based compensation expense under its stock option plans and the Company also issues stock for services and royalties. A detailed description of the awards under these plans and the respective accounting treatment is included in the "Notes to the Consolidated Financial Statements" included in the Company's Annual Report on Form 10-K for the year ended December 31, 2017 and filed with the SEC on March 14, 2018. The Company did not grant any stock options in the three and nine months ended September 30, 2018. For the three and nine months ended September 30, 2018, the Company recorded stock-based expense of \$42 thousand and \$188 thousand, respectively and for the three and nine months ended September 30, 2017, the Company recorded stock-based expense of \$109 thousand and \$313 thousand, respectively.

10. SEGMENT REPORTING

Operating segments are defined in accordance with ASC 280-10 as components of an enterprise for which separate financial information is available that is evaluated regularly by the chief operating decision maker, or decision making group, in deciding how to allocate resources and in assessing performance. The measurement basis of segment profit or loss is income (loss) from operations.

Management has identified six operating segments based on the activities of the Company in accordance with the ASC 280-10. These operating segments have been aggregated into two reportable segments, and an Other category. The two reportable segments are Power and Electromechanical and Energy. The Power and Electromechanical segment is focused on the operations of CUI, CUI-Canada and CUI Japan for the sale of internal and external power supplies, related components and industrial controls. The Power and Electromechanical segment also includes CUI Properties, LLC that owns the Company's Tualatin, Oregon facility. The Energy segment is focused on the operations of Orbital Gas Systems Ltd. and Orbital Gas Systems, North America, Inc. which includes gas related test and measurement systems, including the GasPT. The Other category represents the remaining activities that are not included as part of the other reportable segments and represents primarily corporate activity.

Table of Contents

During the three months ended September 30, 2018, the Company's total revenues consisted of 79% from the Power and Electromechanical segment and 21% from the Energy segment. During the three months ended September 30, 2017, the Company's total revenues consisted of 77% from the Power and Electromechanical segment and 23% from the Energy segment. During the nine months ended September 30, 2018, the Company's total revenues consisted of 82% from the Power and Electromechanical segment and 18% from the Energy segment. During the nine months ended September 30, 2017, the Company's total revenues consisted of 78% from the Power and Electromechanical segment and 22% from the Energy segment.

The following information represents segment activity for the three months ended September 30, 2018 and selected balance sheet items as of September 30, 2018:

	Power and			
(in thousands)	Electro-	Energy	Other	Total
	Mechanical			
Revenues from external customers	\$ 19,589	\$5,155	\$—	\$24,744
Depreciation and amortization ⁽¹⁾	360	382	—	742
Interest expense	59	7	66	132
Profit (loss) from operations	1,851	(2,162)	(1,173)	(1,484)
Segment assets	49,260	25,999	3,698	78,957
Other intangible assets, net	8,689	5,708	—	14,397
Goodwill	13,089	3,154	—	16,243
Expenditures for long-lived assets ⁽²⁾	139	17	—	156

The following information represents segment activity for the nine months ended September 30, 2018 and selected balance sheet items as of September 30, 2018:

	Power and			
(in thousands)	Electro-	Energy	Other	Total
	Mechanical			
Revenues from external customers	\$ 56,929	\$12,908	\$—	\$69,837
Depreciation and amortization ⁽¹⁾	1,100	1,145	—	2,245
Interest expense	165	13	192	370
Profit (loss) from operations	3,822	(9,586)	(3,668)	(9,432)
Segment assets	49,260	25,999	3,698	78,957
Other intangible assets, net	8,689	5,708	—	14,397
Goodwill	13,089	3,154	—	16,243
Expenditures for segment assets ⁽²⁾	808	184	—	992

⁽¹⁾ For the Power and Electromechanical segment, for the three and nine months ended September 30, 2018, depreciation and amortization includes \$207 thousand and \$627 thousand, respectively, classified as cost of revenues in the Condensed Consolidated Statements of Operations.

⁽²⁾ Includes purchases of property, plant and equipment and the investment in other intangible assets.

Table of Contents

The following information represents segment activity for the three months ended September 30, 2017 and selected balance sheet items as of September 30, 2017:

	Power and			
(in thousands)	Electro-	Energy	Other	Total
	Mechanical			
Revenues from external customers	\$ 16,700	\$5,096	\$—	\$21,796
Depreciation and amortization ⁽¹⁾	363	342	—	705
Interest expense	75	1	61	137
Profit (loss) from operations	890	(1,660)	(1,249)	(2,019)
Segment assets	49,377	29,495	705	79,577
Other intangibles assets, net	8,979	6,873	—	15,852
Goodwill	13,092	7,645	—	20,737
Expenditures for segment assets ⁽²⁾	157	114	—	271

The following information represents segment activity for the nine months ended September 30, 2017 and selected balance sheet items as of September 30, 2017:

	Power and			
(in thousands)	Electro-	Energy	Other	Total
	Mechanical			
Revenues from external customers	\$ 48,542	\$13,599	\$—	\$62,141
Depreciation and amortization ⁽¹⁾	1,139	993	—	2,132
Interest expense	187	3	184	374
Profit (loss) from operations	1,984	(5,924)	(3,739)	(7,679)
Segment assets	49,377	29,495	705	79,577
Other intangibles assets, net	8,979	6,873	—	15,852
Goodwill	13,092	7,645	—	20,737
Expenditures for segment assets ⁽²⁾	786	297	—	1,083

⁽¹⁾ For the Power and Electromechanical segment, depreciation and amortization totals for the three and nine months ended September 30, 2017, include \$184 thousand and \$496 thousand, respectively, classified as cost of revenues in the Condensed Consolidated Statements of Operations.

⁽²⁾ Includes purchases of property plant and equipment and the investment in other intangible assets.

The following represents revenue by country:

(dollars in thousands)	For the Three Months Ended			
	September 30,			
	2018		2017	
	Amount	%	Amount	%
USA	\$15,359	62 %	\$13,631	62 %
United Kingdom	3,811	15 %	3,634	17 %
All Others	5,574	23 %	4,531	21 %
Total	\$24,744	100 %	\$21,796	100 %

Table of Contents

(dollars in thousands)	For the Nine Months Ended					
	September 30,					
	2018		2017			
	Amount	%	Amount	%		
USA	\$44,436	64 %	\$38,209	61 %		
United Kingdom	9,205	13 %	10,434	17 %		
All Others	16,196	23 %	13,498	22 %		
Total	\$69,837	100 %	\$62,141	100 %		

11. RECENT ACCOUNTING PRONOUNCEMENTS

See Note 3 - Revenue from Contracts with Customers.

In August 2018, the FASB issued Accounting Standards Update ("ASU") No. 2018-15, *Intangibles - Goodwill and Other - Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract* ("ASU 2018-15"). The amendments in ASU 2018-15 align the requirements for capitalizing implementation costs incurred in a hosting arrangements that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal use software license). The guidance will be effective for the fiscal year beginning after December 15, 2019, including interim periods within that year. The Company is currently assessing the impact of this ASU on its consolidated financial statements and will adopt the standard in 2020.

In August 2018, the FASB issued ASU No. 2018-13, *Fair Value Measurement (Topic 820): Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement* ("ASU 2018-13"). The amendments in this update modify the disclosure requirements on fair value measurements in Topic 820, Fair Value Measurement, including requiring the disclosure of the range and weighted average of significant unobservable inputs used to develop Level 3 fair value measurements. The guidance will be effective for the fiscal year beginning after December 15, 2019, including interim periods within that year. The Company is currently assessing the impact of this ASU on its consolidated financial statements and will adopt the standard in 2020.

In June 2018, the FASB issued ASU No. 2018-07, *Compensation-Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting* ("ASU 2018-07"). These amendments expand the scope of Topic 718, Compensation—Stock Compensation (which currently only includes share-based payments to employees) to include share-based payments issued to nonemployees for goods or services. Consequently, the accounting for share-based payments to nonemployees and employees will be substantially aligned. The guidance will be effective for the fiscal year beginning after December 15, 2018, including interim periods within that year. The Company is currently assessing the impact of this ASU on its consolidated financial statements and will adopt the standard in 2019.

In June 2016, the FASB issued ASU No. 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments* (“ASU 2016-13”). ASU 2016-13 is intended to provide financial statement users with more useful information about expected credit losses on financial assets held by a reporting entity at each reporting date. The new standard replaces the existing incurred loss impairment methodology with a methodology that requires consideration of a broader range of reasonable and supportable forward-looking information to estimate all expected credit losses. This ASU is effective for fiscal years and interim periods within those years beginning after December 15, 2019 and early adoption is permitted for fiscal years and interim periods within those years beginning after December 15, 2018. The Company is currently assessing the impact of this ASU on its consolidated financial statements and will adopt the standard in 2020.

Table of Contents

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)* (“ASU 2016-02”). ASU 2016-02 requires lessees to present right-of-use assets and lease liabilities (with the exception of short-term leases) on the balance sheet. The new guidance will be effective for public business entities for fiscal years beginning after December 15, 2018 including interim periods within that fiscal year. We are currently evaluating the impact of the Company’s pending adoption of ASU 2016-02 on the Company’s consolidated financial statements and will adopt the standard in 2019.

12. INVESTMENTS AND FAIR VALUE MEASUREMENTS

The Company’s fair value hierarchy for its cash equivalents, marketable securities and derivative instruments, including contingent consideration, as of September 30, 2018 and December 31, 2017, respectively, was as follows:

(in thousands)

	Level 1	Level 2	Level 3	Total
September 30, 2018				
Money market securities	\$ 16	\$—	\$—	\$ 16
Certificates of Deposit	523	—	—	523
Convertible note receivable	—	—	500	500
Total assets	\$ 539	\$—	\$ 500	\$ 1,039
Derivative instrument payable	\$—	\$ 193	\$—	\$ 193
Total liabilities	\$—	\$ 193	\$—	\$ 193

	Level 1	Level 2	Level 3	Total
December 31, 2017				
Money market securities	\$ 16	\$—	\$—	\$ 16
Total assets	\$ 16	\$—	\$—	\$ 16
Derivative instrument payable	\$—	\$ 356	\$—	\$ 356
Contingent consideration	—	—	45	45
Total liabilities	\$—	\$ 356	\$ 45	\$ 401

Changes in Fair Value Measurements

Using Significant Unobservable Inputs (Level 3)

	Contingent consideration	Convertible note receivable
(in thousands)		
Balance at December 31, 2017	\$ 45	\$ —
Purchase of convertible note receivable		500

Payments	(45	)	—
Fair value adjustments	—		—
Balance at September 30, 2018	\$	—	\$ 500

There were no transfers between Level 3 and Level 2 in 2018 as determined at the end of the reporting period. The contingent consideration liability is associated with the acquisition of Tectrol in March 2015 and represents the present value of the expected future contingent payment based on revenue projections of select Tectrol legacy products. The inputs used to measure contingent consideration are classified as Level 3 within the valuation hierarchy. The valuation is not supported by market criteria and reflects the Company's internal revenue forecasts. Since the valuation is not supported by market criteria, the valuation is completely dependent on unobservable inputs. During quarterly updates of the valuation, the calculation of the value is based on actual and reasonably estimated future revenues. The final amount of contingent consideration of \$45 thousand was paid out during the nine months ended September 30, 2018.

Table of Contents

In the three months ended September 30, 2018, the Company invested \$500 thousand in a convertible note receivable. In the future, this note will be evaluated as a level three investment in a debt security. The fair value of the investment at September 30, 2018 is estimated to be the same as its current carrying value with no gains recorded since acquisition. This valuation was determined by the fact that other investors invested during the quarter at substantially the same terms and at the same price as our investment.

13. LOSS PER COMMON SHARE

In accordance with FASB Accounting Standards Codification Topic 260 ("FASB ASC 260"), "Earnings per Share," basic net loss per share is computed by dividing the net loss available to common stockholders for the period by the weighted average number of common shares outstanding during the period. Diluted net loss per share is computed by dividing net loss available to common stockholders by the weighted average number of diluted shares outstanding during the period calculated using the treasury stock method. Due to the Company's net loss in the three and nine months ended September 30, 2018 and September 30, 2017, the assumed exercise of stock options using the treasury stock method would have had an antidilutive effect and therefore 1.0 million shares related to stock options were excluded from the computation of diluted net loss per share for both the three and nine months ended September 30, 2018 and 2017. Accordingly, diluted net loss per share is the same as basic net loss per share for the three and nine months ended September 30, 2018 and 2017.

(in thousands, except share and per share amounts)	For the Three Months		For the Nine Months	
	Ended September 30, 2018	2017	Ended September 30, 2018	2017
Net loss	\$(1,534	) \$(1,902	) \$(9,561	) \$(7,324
Basic and diluted weighted average number of shares outstanding	28,527,234	20,991,534	28,507,286	20,969,735
Basic and diluted loss per common share	\$(0.05	) \$(0.09	) \$(0.34	) \$(0.35

14. CAPITALIZED INTEREST

The cost of constructing facilities, equipment and project assets includes interest costs incurred during the assets' construction period. The components of interest expense and capitalized interest are as follows:

(in thousands)	For the Three	For the Nine
----------------	------------------	--------------

Edgar Filing: CUI Global, Inc. - Form 10-Q

	Months Ended		Months Ended	
	September 30,		September 30,	
	2018	2017	2018	2017
Interest cost incurred	\$133	\$143	\$379	\$389
Interest cost capitalized - property and equipment and other intangible assets	(1)	(6)	(9)	(15)
Interest expense, net	\$132	\$137	\$370	\$374

Table of Contents

15. INCOME TAXES

The Company is subject to taxation in the U.S., as well as various state and foreign jurisdictions. The Company continues to record a full valuation allowance against the Company's U.S. net deferred tax assets as it is not more likely than not that the Company will realize a benefit from these assets in a future period. During the nine months ended September 30, 2018, the Company recorded a valuation allowance of \$0.6 million against the Company's foreign UK net deferred tax assets as it is not more likely than not that the Company will realize a benefit from those assets in a future period. In future periods, tax benefits and related deferred tax assets will be recognized when management concludes realization of such amounts is more likely than not.

A net income tax benefit of \$143 thousand and \$280 thousand was recorded to the income tax provision for the three and nine months ended September 30, 2018, respectively, resulting in an effective tax rate of 8.5% and 2.8%, respectively. The income tax benefit for the three and nine months ended September 30, 2018 includes realizable benefits on losses in certain foreign jurisdictions offset by taxes on profitable foreign operations, domestic state minimum taxes and a valuation allowance on the net deferred tax assets of the foreign UK operations. During the three months ended September 30, 2018 the Company received notice that the Canada Revenue Agency had accepted the Company's applications for a Scientific Research and Experimental Development (SRED) tax credit for research and development performed in Canada for a prior year. Accordingly, for the three and nine months ended September 30, 2018, the Company recorded a tax benefit of \$206 thousand related to the SRED credit. Starting with the third quarter 2018 tax provision, current year estimated SRED credits of approximately \$37 thousand are included as part of the Company's normal quarterly tax provision calculation and are included in the total shown above. All of our USA and the foreign UK net deferred tax assets were reduced by a valuation allowance.

The Company's total income tax benefit and effective tax rate for the three and nine months ended September 30, 2017 was \$177 thousand and \$560 thousand, respectively resulting in an effective tax rate of 8.5% and 7.1%, respectively. The income tax benefit for the three months and nine months ended September 30, 2017 related to realizable benefits on losses in certain foreign jurisdictions offset by taxes on profitable foreign operations and domestic state minimum taxes. During the three months ended September 30, 2017 the Company recorded a tax benefit of \$51 thousand related to the SRED credit. All of our USA deferred tax assets were reduced by a valuation allowance.

Table of Contents**16. OVERDRAFT FACILITY AND WORKING CAPITAL LINE OF CREDIT**

On October 5, 2016, Orbital Gas Systems Ltd. signed a five-year agreement with the London branch of Wells Fargo Bank N.A. for a multi-currency variable rate overdraft facility with the following terms:

(in thousands)

September			
Credit Limit	30, 2018	Expiration Date	Interest rate
Balance			
£1,500			
pounds			
sterling			
\$ 1,278	October 5, 2021	Base rate plus a 2.25% margin (2.5% as of September 30, 2018).	
(\$1,954 at			
September 30,			
2018)			

The London branch of Wells Fargo Bank N.A. can demand repayment of amounts on overdraft at any time. The overdraft facility is primarily secured by land, equipment, intellectual property rights, and rights to potential future insurance proceeds held by Orbital Gas Systems Ltd.

During the period ended September 30, 2018, the Company's wholly owned subsidiary, CUI, Inc., maintained a two-year revolving Line of Credit (LOC) with Wells Fargo Bank with the following terms:

(in thousands)

Credit Limit	September 30, 2018 Balance	Expiration Date	Interest rate
\$4,000	\$ 657	(1) June 1, 2019	Fixed rate at 2.25% above the LIBOR in effect on the first day of the applicable fixed-rate term, or Variable rate at 2.25% above the daily one-month LIBOR rate.

⁽¹⁾ As a result of the Company's cash management system, checks issued but not presented to the bank for payment may create negative book cash balances. When those checks are presented for payment if there isn't sufficient cash in the bank account, the checks would be honored by the bank with a corresponding increase to CUI's draw on its line of credit. There were no negative book cash balances included in the balance on the line of credit as of September 30, 2018.

The line of credit is secured by the following collateral via a security agreement with CUI Inc. and CUI-Canada at September 30, 2018:

(in thousands)

CUI Inc. and CUI-Canada General intangibles, net	\$8,690
CUI Inc. and CUI-Canada Accounts receivable, net	\$8,284
CUI Inc. and CUI-Canada Inventory, net	\$11,168
CUI Inc. and CUI-Canada Equipment, net	\$1,690

The borrowing base for the line of credit is based on a percent of CUI Inc. and CUI-Canada's inventory plus a percent of CUI Inc.'s accounts receivable.

CUI Global, Inc., the parent company, is a payment guarantor of the LOC. Other terms included in this revolving line of credit for CUI limit capital expenditures by CUI Inc. and CUI-Canada to \$1.75 million in any fiscal year. The LOC is supported by a single long-term note that does not require repayment until maturity although the Company at its option can repay and re-borrow amounts up to the LOC limit. The LOC contains certain financial covenants. The Company was in compliance with the financial covenants as of September 30, 2018. At September 30, 2018, there was a \$0.7 million balance outstanding on the LOC and \$3.3 million of credit was available. The Company expects to renew the line of credit in the fourth quarter.

Table of Contents**17. ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)**

The components of accumulated other comprehensive income (loss) are as follows:

(in thousands)	As of September 30, 2018	As of December 31, 2017
Foreign currency translation adjustment	\$ (3,940)	\$ (3,510)
Accumulated other comprehensive income (loss)	\$ (3,940)	\$ (3,510)

18. NOTES PAYABLE

Notes payable is summarized as follows:

(in thousands)	As of September 30, 2018	As of December 31, 2017
Mortgage note payable ⁽¹⁾	\$ 3,279	\$ 3,350
Acquisition Note Payable - related party ⁽²⁾	5,304	5,304
Total Notes Payable	\$ 8,583	\$ 8,654

On October 1, 2013, the purchase of the Company's Tualatin, Oregon corporate offices was completed for \$5.1 million. The purchase was funded, in part, by a promissory note payable to Wells Fargo Bank in the amount of \$3.7 million plus interest at the rate of 2% above LIBOR, payable over ten years with a balloon payment due at maturity.

It was secured by a deed of trust on the purchased property which was executed by CUI Properties, LLC and

⁽¹⁾guaranteed by CUI Global, Inc. During the nine months ended September 30, 2018, the Company made principal payments of \$71 thousand against the mortgage promissory note payable. At September 30, 2018, the balance owed on the mortgage promissory note payable was \$3.3 million, of which \$97 thousand and \$3.2 million were in current and long-term liabilities, respectively. See Note 16, Working Capital Line of Credit and Overdraft Facility, for more information on the Company's debt covenants.

- (2) The note payable to International Electronic Devices, Inc. (formerly CUI, Inc.) is associated with the acquisition of CUI, Inc. The promissory note is due May 15, 2020 and includes a 5% interest rate per annum, with interest payable monthly and the principal due as a balloon payment at maturity. The note contains a contingent conversion feature, such that in the event of default on the note the holder of the note can, at the holder's option, convert the note principal into common stock at \$0.001 per share. As of September 30, 2018, the Company is in compliance with all terms of this promissory note and the conversion feature is not effective.

Table of Contents**19. CONCENTRATIONS**

The Company's major product lines are natural gas infrastructure and high-tech solutions in the Energy segment and power and electromechanical products in the Power and Electromechanical segment. The Company had the following revenue concentrations by customer greater than 10% of consolidated revenue:

For the Three Months Ended

September 30, 2018:

Customer	Segment	Percent	
Digi-Key Corporation	Power and Electromechanical	26	%
Future Electronics	Power and Electromechanical	13	%
Total concentrations		39	%

For the Three Months Ended

September 30, 2017:

Customer	Segment	Percent	
Digi-Key Corporation	Power and Electromechanical	27	%
Total concentrations		27	%

For the Nine Months Ended

September 30, 2018:

Customer	Segment	Percent	
Digi-Key Corporation	Power and Electromechanical	26	%
Future Electronics	Power and Electromechanical	13	%
Total concentrations		39	%

For the Nine Months Ended

September 30, 2017:

Customer	Segment	Percent	
Digi-Key Corporation	Power and Electromechanical	26	%
Total concentrations		26	%

The Company had the following geographic revenue concentrations outside the U.S.A. greater than 10% of consolidated revenue:

For the Three Months Ended

September 30, 2018:

Country	Percent	
United Kingdom	15	%
Total concentrations	15	%

For the Three Months Ended

September 30, 2017:

Country	Percent	
United Kingdom	17	%
Total concentrations	17	%

Table of Contents

For the Nine Months Ended

September 30, 2018:

Country	Percent	
United Kingdom	13	%
Total concentrations	13	%

For the Nine Months Ended

September 30, 2017:

Country	Percent	
United Kingdom	17	%
Total concentrations	17	%

The Company had the following gross trade accounts receivable concentrations by customer greater than 10% of gross trade accounts receivable:

As of September 30, 2018

Customer	Segment	Percent	
Future Electronics	Power and Electromechanical	12	%
Total concentrations		12	%

As of December 31, 2017

Customer	Segment	Percent	
GL Industrial Services UK Ltd.	Energy	11	%
Digi-Key Electronics	Power and Electromechanical	10	%
Total concentrations		21	%

The Company had the following geographic concentrations of gross trade accounts receivable outside of the U.S.A. greater than 10% of gross trade accounts receivable:

As of September 30, 2018:

Country	Percent	
United Kingdom	26	%
Canada	11	%
Total concentrations	37	%

As of December 31, 2017:

Country	Percent
United Kingdom	28 %
Canada	11 %
Total concentrations	39 %

CUI had one supplier concentration of approximately 10% during the three months ended September 30, 2018. There were no supplier concentrations of 10% or greater in the nine months ended September 30, 2018. CUI had one concentration of approximately 11% and 12% for the three and nine months ended September 30, 2017.

Table of Contents**20. OTHER EQUITY TRANSACTIONS**

The following shares issued during 2018 were recorded in expense using the grant-date fair value of the stock:

Date of issuance	Type of issuance	Expense/ Prepaid/ Cash	Stock issuance recipient	Reason for issuance	Total no. of shares	Grant date fair value recorded at issuance (in thousands)	
January, April and July 2018	Vested restricted common stock	Expense	Four board members	Director compensation	50,971	\$ 137	
January and July 2018	Common stock	Expense	Three Employees	Approved bonuses	68,118	183	(1)
July 2018	Common stock	Expense	Related Party, James McKenzie	Pursuant to royalty agreement	3,661	9	
Total other equity transactions					122,750	\$ 329	(2)(3)

(1) Includes bonus of \$163 thousand that was accrued and expensed in 2017.

(2) Total excludes \$5 thousand of stock compensation related to royalties that were recorded as expense but not issued and outstanding as of September 30, 2018 and includes \$7 thousand of stock compensation related to 2017 royalties.

(3) Excludes \$24 thousand of stock compensation for stock issued in 2017 that was amortized from prepaid expense in 2018.

Table of Contents

Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations.

Important Note about Forward-Looking Statements

The following discussion and analysis should be read in conjunction with the Company’s unaudited condensed consolidated financial statements as of September 30, 2018 and notes thereto included in this document and the audited consolidated financial statements in the Company’s 10-K filing for the period ended December 31, 2017 and the notes thereto. In addition to historical information, the following discussion and other parts of this Form 10-Q contain forward-looking information that involves risks and uncertainties. The Company’s actual results could differ materially from those anticipated by such forward-looking information due to factors discussed elsewhere in this Form 10-Q.

The statements that are not historical constitute “forward-looking statements.” Said forward-looking statements involve risks and uncertainties that may cause the actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements, express or implied by such forward-looking statements. These forward-looking statements are identified by their use of such terms and phrases as “expects,” “intends,” “goals,” “estimates,” “projects,” “plans,” “anticipates,” “should,” “future,” “believes,” and “scheduled.”

The variables which may cause differences include, but are not limited to, the following: general economic and business conditions; changes in regulatory environment; competition; success of operating initiatives; operating costs; advertising and promotional efforts; the existence or absence of adverse publicity; changes in business strategy or development plans; the ability to retain management; availability, terms and deployment of capital; business abilities and judgment of personnel; availability of qualified personnel; labor and employment benefit costs; availability and costs of raw materials and supplies; and changes in, or failure to comply with various government regulations. Although the Company believes that the assumptions underlying the forward-looking statements contained herein are reasonable, any of the assumptions could be inaccurate; therefore, there can be no assurance that the forward-looking statements included in this Form 10-Q 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 the Company or any person that the objectives and expectations of the Company will be achieved.

Overview

CUI Global is a platform company dedicated to maximizing shareholder value through the acquisition and development of innovative companies, products and technologies. Through its subsidiaries, CUI Global has built a diversified portfolio of industry leading technologies that touch many markets.

For the three and nine months ended September 30, 2018, CUI Global had consolidated loss from operations of \$1.5 million and \$9.4 million, respectively, compared to consolidated loss from operations in the three and nine months ended September 30, 2017 of \$2.0 million and \$7.7 million, respectively. During the three and nine months ended September 30, 2018, CUI Global had consolidated net loss of \$1.5 million and \$9.6 million, respectively, compared to a consolidated net loss in the three and nine months ended September 30, 2017 of \$1.9 million and \$7.3 million, respectively. The higher consolidated losses for the three and nine months ended September 30, 2018, was the result of lower gross profit and overall higher expenses in the Energy segment due to a less favorable product mix in the segment and an impairment of Goodwill in the Energy segment of \$1.3 million. Less favorable gross profit in the Energy segment was partially offset by improved gross profit in the Power and Electromechanical segment for both the three and nine month periods due to higher distributor sales volume. On the strength of the Power and Electromechanical distributor revenues, consolidated revenues increased for both the three and nine month periods. Revenues in the Energy segment were relatively flat for the three months ended September 30, 2018 and down for the year-to-date period.

Table of Contents

In the first nine months of 2018, we had continued development of the Power and Electromechanical segment's Intelligent Control of Energy ("ICE") based line of products, utilizing Virtual Power Systems ("VPS") software, including successfully receiving UL 9540 certification for our Intelligent Control of Energy (ICE) Block technology and seeing our first order for an ICE Block Data Center Power Utilization Solution.

Results of Operations

The following tables set forth, for the period indicated, certain financial information regarding revenue and costs by segment.

For the three months ended September 30, 2018:

(dollars in thousands)	Power and Electro- mechanical	Percent of Segment Revenues	Energy	Percent of Segment Revenues	Other	Percent of Segment Revenues	Total	Percent of Total Revenues	Total	Percent of Total Revenues
	\$	%	\$	%	\$	%	\$	%	\$	%
Total revenues	\$ 19,589	100.0	% \$5,155	100.0	% \$—	—	% \$24,744	100.0	%	%
Cost of revenue	12,648	64.6	% 3,834	74.4	% —	—	% 16,482	66.6	%	%
Gross profit	6,941	35.4	% 1,321	25.6	% —	—	% 8,262	33.4	%	%
Operating expenses:										
Selling, general and administrative	4,277	21.8	% 3,049	59.1	% 1,173	—	% 8,499	34.3	%	%
Depreciation and amortization	153	0.8	% 382	7.4	% —	—	% 535	2.2	%	%
Research and development	638	3.3	% 47	0.9	% —	—	% 685	2.8	%	%
Provision (credit) for bad debt	20	0.1	% 4	0.1	% —	—	% 24	0.1	%	%
Other operating Expenses	3	—	% —	—	% —	—	% 3	—	%	%
Total operating expenses	5,091	26.0	% 3,482	67.5	% 1,173	—	% 9,746	39.4	%	%
Income (loss) from operations	\$ 1,850	9.4	% \$(2,161)	(41.9)	)% \$(1,173)	—	% \$(1,484)	(6.0)	)%	)%

Table of Contents

For the three months ended September 30, 2017:

(dollars in thousands)	Power and Electro-	Percent of Segment	Energy	Percent of Segment	Other	Percent of Segment	Total	Percent of Total	
	mechanical	Revenues		Revenues		Revenues		Revenues	
	\$	%	\$	%	\$	%	\$	%	
Total Revenues	\$ 16,700	100.0	% \$ 5,096	100.0	% \$ —	—	% \$ 21,796	100.0	%
Cost of revenue	11,006	65.9	% 3,350	65.7	% —	—	% 14,356	65.9	%
Gross Profit	5,694	34.1	% 1,746	34.3	% —	—	% 7,440	34.1	%
Operating expenses:									
Selling, general and administrative	3,975	23.8	% 2,988	58.6	% 1,249	—	% 8,212	37.7	%
Depreciation and amortization	179	1.1	% 342	6.7	% —	—	% 521	2.4	%
Research and development	620	3.7	% 76	1.5	% —	—	% 696	3.2	%
Provision (credit) for bad debt	30	0.2	% —	—	% —	—	% 30	0.1	%
Other operating expenses	—	—	% —	—	% —	—	% —	—	%
Total operating expenses	4,804	28.8	% 3,406	66.8	% 1,249	—	% 9,459	43.4	%
Income (loss) from operations	\$ 890	5.3	% \$(1,660)	(32.5	)% \$(1,249)	—	% \$(2,019)	(9.3	)%

Table of Contents

For the nine months ended September 30, 2018:

(dollars in thousands)	Power and Electro-	Percent of Segment	Energy	Percent of Segment	Other	Percent of Segment	Total	Percent of Total		
	mechanical	Revenues		Revenues		Revenues		Revenues		
	\$	%	\$	%	\$	%	\$	%		
Total Revenues	\$ 56,929	100.0	% \$ 12,908	100.0	% \$ —	—	% \$ 69,837	100.0	%	
Cost of revenue	37,503	65.9	% 9,860	76.4	% —	—	% 47,363	67.8	%	
Gross Profit	19,426	34.1	% 3,048	23.6	% —	—	% 22,474	32.2	%	
Operating expenses:										
Selling, general and administrative	13,171	23.1	% 10,105	78.3	% 3,668	—	% 26,944	38.6	%	
Depreciation and amortization	473	0.8	% 1,145	8.9	% —	—	% 1,618	2.3	%	
Research and development	1,972	3.5	% 116	0.9	% —	—	% 2,088	3.0	%	
Provision (credit) for bad debt	(15)	—	% 5	—	% —	—	% (10)	—	%	
Impairment of goodwill and intangible assets	—	—	% 1,263	9.8	% —	—	% 1,263	1.8	%	
Other operating Expenses	3	—	% —	—	% —	—	% 3	—	%	
Total operating expenses	15,604	27.4	% 12,634	97.9	% 3,668	—	% 31,906	45.7	%	
Income (loss) from operations	\$ 3,822	6.7	% \$(9,586)	(74.3)	% \$(3,668)	—	% \$(9,432)	(13.5)	%	

For the nine months ended September 30, 2017:

(dollars in thousands)	Power and Electro-	Percent of Segment	Energy	Percent of Segment	Other	Percent of Segment	Total	Percent of Total		
	mechanical	Revenues		Revenues		Revenues		Revenues		
	\$	%	\$	%	\$	%	\$	%		
Total Revenues	\$ 48,542	100.0	% \$ 13,599	100.0	% \$ —	—	% \$ 62,141	100.0	%	
Cost of revenue	31,900	65.7	% 8,893	65.4	% —	—	% 40,793	65.6	%	
Gross Profit	16,642	34.3	% 4,706	34.6	% —	—	% 21,348	34.4	%	
Operating expenses:										
	12,249	25.3	% 9,492	69.8	% 3,739	—	% 25,480	41.0	%	

Selling, general and administrative												
Depreciation and amortization	643	1.3	%	993	7.3	%	—	—	%	1,636	2.6	%
Research and development	1,766	3.6	%	154	1.1	%	—	—	%	1,920	3.1	%
Provision (credit) for bad debt	(3)	—	%	(18)	(0.1)	%	—	—	%	(21)	—	%
Impairment of intangibles assets	3	—	%	—	—	%	—	—	%	3	—	%
Other operating expenses	—	—	%	9	0.1	%	—	—	%	9	—	%
Total operating expenses	14,658	30.2	%	10,630	78.2	%	3,739	—	%	29,027	46.7	%
Income (loss) from operations	\$ 1,984	4.1	%	\$(5,924)	(43.6)	%	\$(3,739)	—	%	\$(7,679)	(12.3)	%

Table of ContentsRevenue

(dollars in thousands)

Revenues by Segment or Category	For the Three Months Ended				
	September 30,				
	2018	2017	\$ Change	% Change	
Power and Electromechanical	\$19,589	\$16,700	\$2,889	17.3	%
Energy	5,155	5,096	59	1.2	%
Total revenues	\$24,744	\$21,796	\$2,948	13.5	%

Revenues by Segment or Category	For the Nine Months Ended				
	September 30,				
	2018	2017	\$ Change	% Change	
Power and Electromechanical	\$56,929	\$48,542	\$8,387	17.3	%
Energy	12,908	13,599	(691)	(5.1)	%
Total revenues	\$69,837	\$62,141	\$7,696	12.4	%

The revenues for the three and nine months ended September 30, 2018 were higher than the comparable periods due to higher revenues in both our Power and Electromechanical segment and Energy segment for the three months ended September 30, 2018 and higher revenues in our Power and Electromechanical segment for the nine months ended September 30, 2018, partially offset by lower revenues in our Energy segment in the nine-month period. Higher revenues in the Power and Electromechanical segment are due to higher sales through our distribution customers and the revenue recognition accounting change while sales to direct customers were relatively flat in both the three and nine month periods. Lower revenue in the Energy segment in the nine-month period are associated with the timing of customer project delivery schedules and the continued delay in shipment of GasPTs toward a significant project due to governmental delays in Italy. Lower revenue from our UK facility was partially offset by higher revenue from our Houston facility. Revenue from our UK facility benefited from higher exchange rates in 2018 on the British pound as the pound has rebounded following the initial fall following Brexit.

Customer orders related to the Power and Electromechanical segment are associated with the existing product offering, continued new product introductions, continued sales and marketing programs, new customer engagements, distribution channel sales, and the addition in March 2015 of the products from CUI-Canada. In October 2017, the Company announced its first order for its new power monitoring and switching system (ICE Switch) for data centers that was delivered in the first quarter of 2018. Also in the first quarter of 2018, we received our first order for an ICE Block data center power utilization solution.

The Power and Electromechanical segment and Energy segment held backlogs of customer orders of approximately \$25.6 million and \$16.0 million, respectively, as of September 30, 2018. These are both significant increases from December 31, 2017 backlogs of \$20.2 million and \$12.6 million for the Power and Electromechanical and Energy segments, respectively.

Cost of revenues

(dollars in thousands)

Cost of revenues by Segment or Category	For the Three Months Ended		September 30,		
	2018	2017	\$ Change	% Change	
Power and Electromechanical	\$ 12,648	\$ 11,006	\$ 1,642	14.9	%
Energy	3,834	3,350	484	14.4	%
Total cost of revenues	\$ 16,482	\$ 14,356	\$ 2,126	14.8	%

Table of Contents

Cost of revenues by Segment or Category	For the Nine Months Ended				
	September 30,				
	2018	2017	\$	%	
			Change	Change	
Power and Electromechanical	\$37,503	\$31,900	\$ 5,603	17.6	%
Energy	9,860	8,893	967	10.9	%
Total cost of revenues	\$47,363	\$40,793	\$ 6,570	16.1	%

For the three months ended September 30, 2018, the cost of revenues as a percentage of revenue increased to 67% from 66% during the prior-year comparative period. For the nine months ended September 30, 2018, the cost of revenues as a percent of revenue increased to 68% from 66% during the prior year comparative period. This percentage will vary based upon the power and electromechanical product mix sold, the mix of natural gas systems sold, contract labor necessary to complete gas related projects, the competitive markets in which the Company competes, and foreign exchange rates.

The cost of revenues as a percentage of revenue for the Power and Electromechanical segment for the three and nine month period ended September 30, 2018 was 65% and 66%, respectively, compared to 66% and 66%, respectively, during the prior-year comparative period. Cost of revenues as a percentage of revenue was flat in the Power and Electromechanical segment despite a significant royalty expense paid related to the revenues of the ICE switch recognized in the first quarter of 2018. The royalty rate is higher on the first \$1.4 million of ICE product revenues. The cost of revenues as a percentage of revenue for the Energy segment for the three and nine months ended September 30, 2018 was 74% and 76%, respectively, compared to 66% and 65%, in the three and nine months ended September 30, 2017. The higher cost percentage in the Energy segment was due to a less favorable product mix during the three and nine months ended September 30, 2018 compared to the three and nine months ended September 30, 2017 and lower overall sales volumes for the nine months ended September 30, which affected the gross profit percentage due to certain fixed costs that do not decrease based on sales volume. As previously noted, the Energy segment was affected by a temporary halt in shipments of higher margin GasPT units to an Italian customer. The Company expects gross margins to improve upon the resumption of GasPT deliveries on the Italian contract as well as with continued increases in revenues from integration related solutions.

Selling, General and Administrative Expenses

(dollars in thousands)

Selling, general, and administrative expense by Segment or Category	For the Three Months Ended	
	September 30, 2018	2017

			\$	%	
			Change	Change	
Power and Electromechanical	\$4,277	\$3,975	\$ 302	7.6	%
Energy	3,049	2,988	61	2.0	%
Other	1,173	1,249	(76)	(6.1)	%
Total SG&A	\$8,499	\$8,212	\$ 287	3.5	%

Table of Contents

Selling, general, and administrative expense by Segment or Category	For the Nine Months Ended				
	September 30,				
	2018	2017	\$	%	
			Change	Change	
Power and Electromechanical	\$ 13,171	\$ 12,249	\$ 922	7.5	%
Energy	10,105	9,492	613	6.5	%
Other	3,668	3,739	(71)	(1.9)	%
Total SG&A	\$ 26,944	\$ 25,480	\$ 1,464	5.7	%

Selling, General and Administrative (SG&A) expenses include such items as wages, commissions, consulting, general office expenses, business promotion expenses and costs of being a public company, including legal and accounting fees, insurance and investor relations. SG&A expenses are generally associated with the ongoing activities to reach new customers, promote new product lines including ICE, GasPT, IRIS, VE, and new product introductions.

During the three and nine months ended September 30, 2018, SG&A increased \$0.3 million and \$1.5 million, respectively, compared to the prior-year comparative period. These increases in SG&A in the three and nine months ended September 30, 2018 were due to increased costs in both the Power and Electromechanical and the Energy segment, primarily due to higher selling expenses on the higher sales in the Power and Electromechanical segment and higher professional fees in the Energy segment in the nine months ended September 30, 2018 compared to the three and nine month periods ended in 2017 and higher SG&A expenses at the Houston facility on comparatively higher revenues in both the three and nine months ended September 30, 2018. Also contributing to the higher SG&A expenses in the Energy segment in the nine months ended September 30, 2018 were increased marketing expenses related to the World Gas Conference.

Depreciation and Amortization

(dollars in thousands)

Depreciation and amortization by Segment or Category	For the Three Months Ended				
	September 30,				
	2018	2017	\$	%	
			Change	Change	
Power and Electromechanical	\$ 360	\$ 363	\$ (3)	(0.8)	%
Energy	382	342	40	11.7	%

Edgar Filing: CUI Global, Inc. - Form 10-Q

Total depreciation and amortization	\$742	\$705	\$ 37	5.2	%
-------------------------------------	-------	-------	-------	-----	---

Depreciation and amortization by Segment or Category	For the Nine Months Ended				
	September 30,				
	2018	2017	\$	%	
			Change	Change	
Power and Electromechanical	\$1,100	\$1,139	\$ (39)	(3.4)%	
Energy	1,145	993	152	15.3	%
Total depreciation and amortization	\$2,245	\$2,132	\$ 113	5.3	%

The depreciation and amortization expenses are associated with depreciation on buildings, furniture, equipment, vehicles, and intangible assets over the estimated useful lives of the related assets.

Table of Contents

The total depreciation and amortization expense for the three months ended September 30, 2018 and 2017 included \$207 thousand and \$184 thousand, respectively, which was included in cost of revenues. Depreciation and amortization expense for the nine months ended September 30, 2018 and 2017 included \$627 thousand and \$496 thousand, respectively, included in cost of revenue. The increase in depreciation and amortization included in cost of sales was due to increased allocation of depreciation and amortization to cost of revenues at CUI Inc. and CUI-Canada.

Depreciation and amortization expense in the three and nine months ended September 30, 2018 were up slightly compared to the three and nine months ended September 30, 2017 as a result of higher translated depreciation and amortization at our U.K. operation due to higher pound Sterling translation rates during the current periods.

Research and Development

(dollars in thousands)

Research and development by Segment or Category	For the Three Months Ended				
	September 30,				
	2018	2017	\$ Change	% Change	
Power and Electromechanical	\$638	\$620	\$ 18	2.9	%
Energy	47	76	(29)	(38.2)	%
Total research and development	\$685	\$696	\$ (11)	(1.6)	%

Research and development by Segment or Category	For the Nine Months Ended				
	September 30,				
	2018	2017	\$ Change	% Change	
Power and Electromechanical	\$1,972	\$1,766	\$ 206	11.7	%
Energy	116	154	(38)	(24.7)	%
Total research and development	\$2,088	\$1,920	\$ 168	8.8	%

Research and development costs are associated with the continued research and development of new and existing technologies including advanced power technologies, ICE, GasPT, VE Technology and other products. Research and development expense was relatively flat in the Energy segment and up in the Power and Electromechanical segment for the three and nine months ended September 30, 2018 compared to the three and nine months ended September 30,

2017. Research and development activities were primarily focused on the ICE technology in Power and Electromechanical Segment and GasPT and VE technologies in the Energy segment.

Impairment Loss

As of May 31, 2018, management performed its annual assessment of goodwill impairment which resulted in a \$1.3 million impairment. See Note 6 Goodwill and Indefinite-lived Intangibles for more information on the impairment loss.

Provision (Credit) for Bad Debt

(dollars in thousands)

Provision (credit) for bad debt by Segment or Category	For the Three Months Ended		September 30,			
	2018	2017	\$	%	Change	Change
Power and Electromechanical	\$ 20	\$ 30	\$ (10)	(33.3)%		
Energy	4	—	4	—	%	
Total provision (credit) for bad debt	\$ 24	\$ 30	\$ (6)	(20.0)%		

Table of Contents

Provision (credit) for bad debt by Segment or Category	For the Nine Months Ended			
	September 30,			
	2018	2017	\$ Change	% Change
Power and Electromechanical	\$(15)	\$(3)	\$(12)	400.0 %
Energy	5	(18)	23	(127.8)%
Total provision (credit) for bad debt	\$(10)	\$(21)	\$ 11	(52.4)%

The changes in bad debt are due to normal fluctuations in bad debt reserves based on the age of receivables. Collections are strong across all businesses in the three and nine months ended September 30, 2018.

Other Income (Expense)

(dollars in thousands)

Other Income (Expense)	For the Three Months Ended			
	September 30,			
	2018	2017	\$ Change	% Change
Foreign exchange gain (loss)	\$(119)	\$ 43	\$(162)	(376.7)%
Interest income	10	4	6	150.0 %
Unrealized gain (loss) on derivative	38	20	18	90.0 %
Other, net	10	10	—	— %
Total Other income (expense)	\$(61)	\$ 77	\$(138)	(179.2)%

Other Income (Expense)	For the Nine Months Ended	
	September 30,	
	2018	2017

			\$	%	
			Change	Change	
Foreign exchange gain (loss)	\$(258)	\$76	\$ (334)	(439.5)	%
Interest income	22	14	8	57.1	%
Unrealized gain (loss) on derivative	164	55	109	198.2	%
Other, net	33	24	9	37.5	%
Total Other income (expense)	\$(39)	\$169	\$ (208)	(123.1)	%

Other income (expense) changes were due primarily to interest rate and exchange rate fluctuations in the three and nine months ended September 30, 2018.

Interest Expense

For both the three months ended September 30, 2018 and 2017, the Company incurred interest expense, net of amounts capitalized, of \$0.1 million.

For both the nine months ended September 30, 2018 and 2017, the Company incurred interest expense, net of amounts capitalized, of \$0.4 million.

Interest expense in 2018 and 2017 is associated with interest on the line of credit, bank overdraft facility, bank and secured promissory notes.

Income Tax Expense (Benefit)

The Company is subject to taxation in the U.S., various state and foreign jurisdictions. We continue to record a full valuation allowance against the Company's U.S. net deferred tax assets as it is not more likely than not that the Company will realize a benefit from these assets in a future period. During the nine months ended September 30, 2018, the Company also recorded a valuation allowance of \$0.6 million against the Company's foreign UK net deferred tax assets as it is not more likely than not that the Company will realize a benefit from these assets in a future period. In future periods, tax benefits and related deferred tax assets will be recognized when management concludes realization of such amounts is more likely than not.

For additional analysis, see Note 15, "Income Taxes," of the condensed consolidated financial statements in Part I - Item I, "Financial Statements."

Table of Contents

Liquidity and Capital Resources

General

As of September 30, 2018, the Company held Cash and cash equivalents of \$3.2 million including \$0.5 million of restricted cash. Operations, investments, patents and equipment have been funded through cash on hand and debt. Trade accounts receivable and accounts payable increased since December 31, 2017 due to an increased volume of business in the Power and Electromechanical segment. Inventories increased due to the increased volume of business in the Power and Electromechanical segment and the ASC 606 revenue recognition transition in the Energy segment offset by the ASC 606 revenue recognition transition in the Power and Electromechanical segment.

Cash Used In Operations

Cash used in operations of \$10.0 million was a \$4.2 million increase in cash used compared to the comparable period in 2017. The nine months ended September 30, 2018 were benefited from higher revenue and the related gross profits in the Power and Electromechanical segment. In the first nine months of 2018, cash used in operations by the Energy segment was approximately \$9.3 million, and cash used in operations by the Other category was approximately \$4.4 million. These uses of cash were partially offset by cash provided by operating activities in the Power and Electromechanical segment of approximately \$3.7 million. We believe cash used in operations will improve in the Energy segment in the fourth quarter of 2018 due to the expected increases in revenue from other integration-related products including biomethane to grid solutions. The Power and Electromechanical segment is expected to continue to provide cash from operations and we believe the cash usage rate in the other category to be flat to slightly lower due to cost cutting initiatives put in place over the last year.

The change in cash used in operating activities, exclusive of net loss, is primarily the result of increased trade receivables of \$1.4 million, an increase to inventories of \$3.7 million and a decrease to contract liabilities of \$0.9 million offset by increased payables and accrued expenses of \$0.5 million and \$0.7 million, respectively, the \$0.2 million cash effect of a decrease in contract assets, and the \$1.0 million cash effect from an increase in refund liabilities for the nine months ended September 30, 2018.

During the first nine months of 2018 and 2017, the Company used stock as a form of payment to certain employees, vendors and consultants. For the nine months ended September 30, 2018 and 2017, the Company recorded a total of \$188 thousand and \$313 thousand, respectively for share-based compensation related to equity given, or to be given to employees and consultants for services provided and as payment for royalties earned. The decrease in expense was due to lower accrued share-based bonuses.

S-3 registration

The Company filed an S-3 registration statement on March 14, 2017 containing a prospectus that was effective March 29, 2017. With this filing, CUI Global may from time to time issue various types of securities, including common stock, preferred stock, debt securities and/or warrants, up to an aggregate amount of \$100 million.

On October 23, 2017, the Company closed on an underwritten public offering of 7,392,856 shares at a public offering price of \$2.80 per share, including 964,285 shares sold at the public offering price pursuant to the underwriter's exercise in full of its option to purchase additional shares to cover over-allotments. The net proceeds to CUI Global (after deducting underwriting discount and other expenses payable by the Company) were approximately \$18.9 million. The Company has used the net proceeds from the offering primarily for general corporate purposes, which includes operating expenses, working capital to improve and promote its commercially available products, advance product candidates, to expand international presence and commercialization, research and development, for general capital expenditures and for satisfaction of debt obligations. In 2017, the Company used some of the proceeds of the public offering to pay off its line of credit and overdraft facility.

As the Company focuses on strategic acquisitions, technology development, product line additions, developing CUI-Canada operations, and developing Orbital Gas Systems, North America, Inc., it will fund these activities together with related sales and marketing efforts for its various product offerings with cash on hand, including proceeds from future issuances of equity through the S-3 registration statement, and available debt.

Table of Contents

CUI Global may raise additional capital needed to fund the further development and marketing of its products as well as payment of its debt obligations.

See the section entitled Recent Sales of Unregistered Securities for a complete listing of all unregistered securities transactions.

Capital Expenditures and Investments

During the first nine months of 2018 and 2017, CUI Global invested \$0.6 million and \$0.6 million, respectively, in property and equipment. These investments typically include additions to equipment, tooling for manufacturing, furniture, computer equipment, buildings and leasehold improvements and other fixed assets as needed for operations. The Company anticipates further investment in property and equipment during the remainder of 2018 in support of its on-going business and continued development of product lines and technologies.

During the nine months ended September 30, 2018 and 2017, CUI Global invested \$0.3 million and \$0.4 million, respectively, in other intangible assets. These investments typically include product certifications, capitalized website development, software for engineering and research and development and software upgrades for office personnel.

During July 2018, CUI Global made an investment of \$0.5 million in a convertible note receivable with Virtual Power Systems (“VPS”) to support the two companies’ continued collaboration and development of industry transforming Software Defined Power technologies. The note accrues interest at 2% per annum and the interest is compounded annually. Unless converted into shares earlier, principal and accrued interest will convert automatically on the maturity date (October 27, 2019) into shares of VPS common stock at the then current fair market value. If VPS receives gross proceeds greater than \$3 million prior to the maturity date in a sale or series of sales of equity securities, the principal and unpaid accrued interest of the note will automatically convert into conversion shares at 80% of the price paid per share for equity securities by investors at that time.

Financing Activities

For the nine months ended September 30, 2018 and 2017, the Company recorded net proceeds of \$1.3 million and \$1.0 million, respectively, from the overdraft facility in the U.K., recorded net proceeds of \$0.7 million and \$1.9 million, respectively, from the line of credit, and made payments of \$2 thousand and \$27 thousand, respectively, toward capital lease obligations, \$71 thousand and \$66 thousand, respectively, toward the mortgage note payable and \$45 thousand and \$61 thousand, respectively, toward the contingent liability related to the Tectrol, Inc. acquisition.

As a result of the Company's cash management system at CUI, checks issued but not presented to the bank for payment may create a negative book cash balance. Such a negative balance would be included in the Company's two-year revolving line of credit (LOC). There was not a negative book cash balance as of September 30, 2018. At September 30, 2018, the Company had a \$0.7 million balance on its \$4.0 million LOC with \$3.3 million available. There was a \$1.3 million balance on the Company's Overdraft facility at Orbital UK at September 30, 2018 and \$0.7 million available on the facility.

Financing activities – related party activity

For the nine months ended September 30, 2018 and 2017, \$0.2 million of interest payments were made in relation to the promissory note issued to related party, IED, Inc.

Table of Contents

Recap of Liquidity and Capital Resources

The Wells Fargo mortgage promissory note has a balance at September 30, 2018 of \$3.3 million, of which \$97 thousand is the current portion. Additionally, at September 30, 2018, the Company had a balance on its \$4.0 million LOC with Wells Fargo Bank of \$0.7 million. The LOC contains certain financial covenants, all of which the Company was in compliance with at September 30, 2018 and December 31, 2017. CUI Global, Inc., the parent company, is a payment guarantor of the LOC.

On October 5, 2016, Orbital Gas Systems Ltd. signed a five-year agreement with the London branch of Wells Fargo Bank N.A. for a multi-currency variable rate overdraft facility with a facility limit of £1.5 million pounds sterling (\$2.0 million at September 30, 2018) that expires on October 5, 2021. The balance at September 30, 2018 was \$1.3 million.

At September 30, 2018, the Company had unrestricted cash and cash equivalents balances of \$2.7 million. In addition, the Company had \$0.5 million of restricted cash related to a contract guarantee. At September 30, 2018, the Company had \$0.6 million of cash and cash equivalents balances at domestic financial institutions that were covered under the FDIC insured deposits programs and \$2 thousand and \$77 thousand, respectively, at foreign financial institutions covered under the United Kingdom Financial Services Compensation (FSC) and the Canada Deposit Insurance Corporation (CDIC). The money market balance of \$16 thousand is covered under the SIPC insured program for investments up to a maximum of \$500,000. At September 30, 2018, the Company had cash and cash equivalents of \$0.2 million in Japanese bank accounts, \$2 thousand in European bank accounts and \$0.1 million in Canadian bank accounts.

As described in Item 1A - Risk factors included in the Company's 2017 10-K, the United Kingdom's proposed withdrawal from the European Union could have an adverse effect on our business and financial results but the extent of the effect, if any, is not yet determinable. See Item 1A - Risk factors in our 2017 10-K, for more information on the potential risks that are associated with the United Kingdom's pending withdrawal from the European Union.

See Note 1 Nature of Operations, Basis of Presentation and Company Conditions for additional discussion of the Company's financial condition and current liquidity.

In the short-term, the Company expects its Orbital operation in Houston to continue to need cash support as it continues to grow revenues and expand its operations. The CUI-Canada operation in the Power and Electromechanical segment acquired in 2015 will also continue to be near break even in the short-term. If revenues and other funds are not sufficient to cover all operating and other expenses, additional funding may be required. There is no assurance the Company will be able to raise such additional capital. The failure to raise capital or generate product sales in the expected time frame would have a material adverse effect on the Company.

Table of Contents

Critical Accounting Policies

We have adopted various accounting policies to prepare the consolidated financial statements in accordance with GAAP. Certain of our accounting policies require the application of significant judgment by management in selecting the appropriate assumptions for calculating financial estimates. In our 2017 Annual Report on Form 10-K filed on March 14, 2018, we identified the critical accounting policies that affect our more significant estimates and assumptions used in preparing our consolidated financial statements. Significant changes to our critical accounting estimates as a result of adopting ASC 606 are discussed below:

Revenue Recognition

ASC 606 requires significant estimates as it relates to the timing of revenue recognition, particularly in the Power and Electromechanical segment. The most significant affect was on revenue recorded at distributors that was recorded as "sell through" under prior accounting guidance.

Certain distributor revenue under the previous revenue guidance was deferred until the inventory was sold by the distributor to the end customer. Current guidance requires management to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity expects to be entitled for those goods or services. This generally requires management to record revenue sooner than under the previous standard and requires more extensive estimates and reserves on current sales.

Under ASC 606, we record revenue upon sale to the distributor with an appropriate amount reserved for estimated returns and allowances. This is a significant estimate as it relates to the timing of revenue recognition.

In the Energy segment, for the majority of contracts, revenue will still be measured over time using the cost-to-cost method. The change that most affected the transition adjustment on Energy revenue was the requirement to limit revenue recognition on contracts without an enforceable right to payment for performance completed to date. Revenue on contracts without a specific enforceable right to payment on work performed to date was "clawed back" as part of the Company's transition adjustment. On future contracts, the Company will make efforts to include an enforceable right to payment on work performed to date so the ongoing effect on the timing of revenue in the Energy segment will be limited.

During the transition, a certain amount of revenue will not be recorded as revenue but as part of the cumulative effect of the accounting change. The cumulative effect adjustment recorded as of January 1, 2018 was a net \$1.9 million decrease to accumulated deficit due to a \$2.8 million transition adjustment from the Power and Electromechanical segment partially offset by a \$(0.9) million transition adjustment from the Energy segment.

Recent Accounting Pronouncements

See Note 11 Recent Accounting Pronouncements of the condensed consolidated financial statements in Part I—Item I, “Financial Statements” for a description of recent accounting pronouncements, including the dates of adoption and estimated effects on financial position, results of operations and cash flows.

Off-Balance Sheet Arrangements

As of September 30, 2018, the Company had no off-balance sheet arrangements.

Table of Contents

Item 3. Quantitative and Qualitative Disclosure about Market Risk.

The Company is exposed to market risk in the ordinary course of business. Market risk represents the risk of loss that may impact the Company's financial position due to adverse changes in financial market prices and rates. This market risk exposure is primarily a result of fluctuations in foreign currency exchange rates and interest rates. The Company neither holds nor issues financial instruments for trading purposes.

The following sections provide quantitative information on the Company's exposure to foreign currency exchange rate risk. The Company makes use of sensitivity analyses that are inherently limited in estimating actual losses in fair value that can occur from changes in market conditions.

Foreign Currency Exchange Rates

The Company conducts operations in four principal currencies: the U.S. dollar, the British pound sterling, the Canadian dollar and the Japanese yen. These currencies operate primarily as the functional currency for the Company's U.S., U.K., Canadian and Japanese operations, respectively. Cash is managed centrally within each of the four regions.

Because of fluctuations in currency exchange rates, the Company is subject to currency translation exposure on the results of its operations. Foreign currency translation risk is the risk that exchange rate gains or losses arise from translating foreign entities' statements of earnings and balance sheets from functional currency to the Company's reporting currency, the U.S. dollar, for consolidation purposes. As currency exchange rates fluctuate, translation of the Company's statements of operations into U.S. dollars affects the comparability of revenues and operating expenses between years.

Revenues and operating expenses are primarily denominated in the currencies of the countries in which the Company's operations are located, the U.S., U.K., Canada and Japan. The Company's consolidated results of operations and cash flows are, therefore, subject to fluctuations due to changes in foreign currency exchange rates and may be adversely affected in the future due to changes in foreign exchange rates.

The table below details the percentage of revenues and expenses by the four principal currencies for the three and nine months ended September 30, 2018 and 2017:

Canadian Japanese

	U.S. Dollar		British Pound Sterling		Dollar		Yen	
For the Three Months Ended September 30, 2018								
Revenues	83	%	16	%	—	%	1	%
Operating expenses	67	%	23	%	9	%	1	%
For the Three Months Ended September 30, 2017								
Revenues	81	%	18	%	—	%	1	%
Operating expenses	66	%	24	%	9	%	1	%

Table of Contents

	U.S. Dollar		British Pound Sterling		Canadian Dollar		Japanese Yen	
For the Nine Months Ended September 30, 2018								
Revenues	84	%	14	%	—	%	2	%
Operating expenses	63	%	28	%	8	%	1	%
For the Nine Months Ended September 30, 2017								
Revenues	81	%	18	%	—	%	1	%
Operating expenses	66	%	25	%	8	%	1	%

To date, the Company has not entered into any hedging arrangements with respect to foreign currency risk and have limited activity with forward foreign currency contracts or other similar derivative instruments. We believe that during the nine months ended September 30, 2018, the effect of a hypothetical 100 basis point shift in foreign currency exchange rates applicable to the Company's business would not have had a material impact on the Company's condensed consolidated financial statements.

Investment Risk

The Company has an Investment Policy that, among other things, provides an internal control structure that takes into consideration safety (credit risk and interest rate risk), liquidity and yield. The Company's investment officers, CEO and CFO, oversee the investment portfolio and compile a quarterly analysis of the investment portfolio, if any investments exist during the period.

Investments made by the Company are subject to an investment policy, which limits the Company's risk of loss exposure by setting appropriate credit quality requirements for investments held, limiting maturities to be 1 year or less, and also setting appropriate concentration levels to prevent concentrations. This includes a requirement that no more than 3% of the portfolio, or \$0.5 million, whichever is greater, may be invested in one particular issue.

Cash and cash equivalents are diversified and maintained with several financial institutions. Deposits held with banks may exceed the amount of insurance provided on such deposits. Generally, these deposits may be redeemed upon demand and are maintained with financial institutions of reputable credit, therefore, bear minimal credit risk.

The Company has trade receivable and revenues concentrations with large customers. Additionally, the Company has a large concentration of cash, trade receivables and revenues in foreign countries including the United Kingdom, Canada and Japan.

Item 4. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures

The Company's management, with the participation of the Company's Chief Executive Officer (CEO) and its Chief Financial Officer (CFO), evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of the end of the period covered by this quarterly report. In designing and evaluating the Company's disclosure controls and procedures, the Company's management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and the Company's management is required to apply their judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based upon that evaluation, the Company's management, including the CEO and the CFO, concluded that, as of September 30, 2018, the Company's disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed in the reports that the Company files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the applicable rules and forms, and that it is accumulated and communicated to management, including the CEO and CFO, as appropriate, to allow timely decisions regarding required disclosure.

Table of Contents

Changes in Internal Control over Financial Reporting

There were no significant changes in the Company's internal control over financial reporting during the three months ended September 30, 2018, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings.

CUI Global, Inc. and its subsidiaries are not a party in any legal proceedings where they are a defendant. No director, officer or affiliate of CUI Global, Inc., any owner of record or beneficially of more than five percent of any class of voting securities of CUI Global, Inc. or any associate of any such director, officer, affiliate of CUI Global, Inc. or security holder is a party adverse to CUI Global, Inc. or any of its subsidiaries or has a material interest adverse to CUI Global, Inc. or any of its subsidiaries.

Item 1A. Risk Factors.

There are no material changes from Risk Factors as previously disclosed in the Company's Form 10-K filed with the Commission on March 14, 2018.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds. Common Stock Issued.

During the three months ended September 30, 2018, the Company issued the following shares of common stock, which were not registered under the Securities Act. The Company relied on Section 4(2) of the Securities Act of 1933 as the basis for an exemption from registration for the following issuances.

Date of issuance	Type of issuance	Expense/ Prepaid/ Cash	Stock issuance recipient	Reason for issuance	Total no. of shares	Grant date fair value recorded at issuance
---------------------	------------------	------------------------------	--------------------------------	------------------------	------------------------------	--

Edgar Filing: CUI Global, Inc. - Form 10-Q

						(in thousands)
July 2018	Vested restricted common stock	Expense	Three board members	Director compensation	13,635	\$ 37
July 2018	Common stock	Expense	Two Employees	Approved bonuses	7,256	20
July 2018	Common stock	Expense	Related Party, James McKenzie	Pursuant to royalty agreement	3,661	9
					24,552	\$ 66

Table of Contents

Item 5. Other Information.

None.

Item 6. Exhibits.

The following exhibits are included as part of this Form 10-Q.

Exhibit No.	Description
31.1 ¹	<u>Certification of Chief Executive Officer Pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934</u>
31.2 ¹	<u>Certification of Chief Financial Officer Pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934</u>
32.1 ¹	<u>Certification of Chief Executive Officer Pursuant to Rule 13a-14(b)/15d-14(b) of the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350</u>
32.2 ¹	<u>Certification of Chief Financial Officer Pursuant to Rule 13a-14(b)/15d-14(b) of the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350</u>
101.INS ¹	XBRL Instance Document
101.SCH ¹	XBRL Taxonomy Extension Schema Document
101.CAL ¹	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF ¹	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB ¹	XBRL Taxonomy Extension Label Linkbase Document
101.PRE ¹	XBRL Taxonomy Extension Presentation Linkbase Document

Footnotes to Exhibits:

¹Filed herewith.

Table of Contents

SIGNATURES

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

Signed and submitted this 7th day of November, 2018.

CUI Global, Inc.
By: /s/ William J. Clough
William J. Clough,
Chief Executive
Officer/President
(Principle Executive
Officer)

By: /s/ Daniel N. Ford
Daniel N. Ford,
Chief Financial
Officer
(Principle Financial
Officer)