

**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 December 31, 2019

OR

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

Commission File Number 0-3295

KOSS CORPORATION

(Exact Name of Registrant as Specified in its Charter)

DELAWARE

(State or other jurisdiction of
incorporation or organization)

39-1168275

(I.R.S. Employer Identification No.)

4129 North Port Washington Avenue, Milwaukee, Wisconsin
(Address of principal executive offices)

53212
(Zip Code)

Registrant's telephone number, including area code: **(414) 964-5000**

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

| Title of each class | Trading Symbol(s) | Name of each exchange on which registered |
|---------------------|-------------------|---|
| Common | KOSS | NASDAQ |

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, 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

(Do not check if a 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

At January 27, 2020, there were 7,404,831 shares outstanding of the registrant's common stock.

KOSS CORPORATION
FORM 10-Q
December 31, 2019

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PART I
FINANCIAL INFORMATION

Item 1. Financial Statements

KOSS CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS

| | (Unaudited) December 31, 2019 | June 30, 2019* |
|---|----------------------------------|----------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 2,229,084 | \$ 2,228,282 |
| Accounts receivable, less allowance for doubtful accounts of \$4,358 and \$2,617, respectively | 2,467,767 | 3,655,143 |
| Inventories, net | 6,701,311 | 6,851,448 |
| Prepaid expenses and other current assets | 234,613 | 133,889 |
| Income taxes receivable | 56,229 | 45,660 |
| Total current assets | <u>11,689,004</u> | <u>12,914,422</u> |
| Equipment and leasehold improvements, net | <u>940,364</u> | <u>890,110</u> |
| Other assets: | | |
| Deferred income taxes | 1,626 | 13,276 |
| Operating lease right-of-use assets | 2,716,532 | 2,847,846 |
| Cash surrender value of life insurance | 6,828,027 | 6,569,628 |
| Total other assets | <u>9,546,185</u> | <u>9,430,750</u> |
| Total assets | <u>\$ 22,175,553</u> | <u>\$ 23,235,282</u> |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 829,274 | \$ 1,436,373 |
| Accrued liabilities | 761,825 | 650,513 |
| Deferred revenue | 495,144 | 645,470 |
| Operating lease liability | 271,134 | 265,443 |
| Total current liabilities | <u>2,357,377</u> | <u>2,997,799</u> |
| Long-term liabilities: | | |
| Deferred compensation | 2,381,978 | 2,419,962 |
| Deferred revenue | 160,268 | 163,018 |
| Operating lease liability | 2,445,397 | 2,582,402 |
| Total long-term liabilities | <u>4,987,643</u> | <u>5,165,382</u> |
| Total liabilities | <u>7,345,020</u> | <u>8,163,181</u> |
| Stockholders' equity: | | |
| Common stock, \$0.005 par value, authorized 20,000,000 shares; issued and outstanding 7,404,831 | 37,024 | 37,024 |
| Paid in capital | 6,618,029 | 6,333,135 |
| Retained earnings | 8,175,480 | 8,701,942 |
| Total stockholders' equity | <u>14,830,533</u> | <u>15,072,101</u> |
| Total liabilities and stockholders' equity | <u>\$ 22,175,553</u> | <u>\$ 23,235,282</u> |

*As adjusted for change in accounting principle (Note 2)

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

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CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

| | Three Months Ended December 31 | | Six Months Ended December 31 | |
|--|-----------------------------------|--------------|---------------------------------|---------------|
| | 2019 | 2018* | 2019 | 2018* |
| Net sales | \$ 4,162,659 | \$ 5,411,227 | \$ 9,573,421 | \$ 11,196,066 |
| Cost of goods sold | 2,798,572 | 3,748,732 | 6,861,880 | 7,702,387 |
| Gross profit | 1,364,087 | 1,662,495 | 2,711,541 | 3,493,679 |
| Selling, general and administrative expenses | 1,586,705 | 1,559,346 | 3,251,305 | 3,348,935 |
| (Loss) income from operations | (222,618) | 103,149 | (539,764) | 144,744 |
| Interest income | 6,927 | - | 13,324 | - |
| (Loss) income before income tax provision | (215,691) | 103,149 | (526,440) | 144,744 |
| Income tax provision | 22 | - | 22 | 25 |
| Net (loss) income | \$ (215,713) | \$ 103,149 | \$ (526,462) | \$ 144,719 |
| (Loss) income per common share: | | | | |
| Basic | \$ (0.03) | \$ 0.01 | \$ (0.07) | \$ 0.02 |
| Diluted | \$ (0.03) | \$ 0.01 | \$ (0.07) | \$ 0.02 |
| Weighted-average number of shares: | | | | |
| Basic | 7,404,831 | 7,404,831 | 7,404,831 | 7,397,291 |
| Diluted | 7,404,831 | 7,413,391 | 7,404,831 | 7,423,517 |

*As adjusted for change in accounting principle (Note 2)

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

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CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

| | Six Months Ended December 31 | |
|---|---|---------------------|
| | 2019 | 2018* |
| Operating activities: | | |
| Net (loss) income | \$ (526,462) | \$ 144,719 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| (Recovery of) provision for doubtful accounts | (13,338) | 30,806 |
| Depreciation of equipment and leasehold improvements | 189,138 | 248,830 |
| Stock-based compensation expense | 284,894 | 251,169 |
| Deferred income taxes | 11,650 | - |
| Change in cash surrender value of life insurance | (145,605) | (24,744) |
| Change in deferred compensation accrual | 37,016 | 87,977 |
| Deferred compensation paid | (75,000) | (75,000) |
| Net changes in operating assets and liabilities: | | |
| Accounts receivable | 1,200,714 | 1,669,262 |
| Inventories | 150,137 | (1,046,995) |
| Prepaid expenses and other current assets | (100,724) | (59,861) |
| Income taxes receivable | (10,569) | 25 |
| Accounts payable | (607,099) | 360,477 |
| Accrued liabilities | 111,312 | (151,210) |
| Deferred revenue | (153,076) | (81,388) |
| Net cash provided by operating activities | <u>352,988</u> | <u>1,354,067</u> |
| Investing activities: | | |
| Purchase of equipment and leasehold improvements | (239,392) | (112,599) |
| Life insurance premiums paid | (112,794) | (122,915) |
| Net cash (used in) investing activities | <u>(352,186)</u> | <u>(235,514)</u> |
| Financing activities: | | |
| Proceeds from exercise of stock options | - | 46,677 |
| Net cash provided by financing activities | <u>-</u> | <u>46,677</u> |
| Net increase in cash and cash equivalents | 802 | 1,165,230 |
| Cash and cash equivalents at beginning of period | 2,228,282 | 1,081,533 |
| Cash and cash equivalents at end of period | <u>\$ 2,229,084</u> | <u>\$ 2,246,763</u> |

*As adjusted for change in accounting principle (Note 2)

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

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KOSS CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (Unaudited)

| | Six Months Ended December 31, 2019 | | | | |
|---|---|------------------|----------------------------|------------------------------|----------------------|
| | Common Stock | | Paid in Capital | Retained Earnings | Total |
| | Shares | Amount | | | |
| Balance, June 30, 2019, as previously reported | 7,404,831 | \$ 37,024 | \$ 6,186,393 | \$ 8,848,684 | \$ 15,072,101 |
| Retrospective change in accounting principle (see Note 2) | - | - | 146,742 | (146,742) | - |
| Adjusted Balance, June 30, 2019 | 7,404,831 | \$ 37,024 | \$ 6,333,135 | \$ 8,701,942 | \$ 15,072,101 |
| Net (loss) | - | - | - | (526,462) | (526,462) |
| Stock-based compensation expense | - | - | 284,894 | - | 284,894 |
| Balance, December 31, 2019 | <u>7,404,831</u> | <u>\$ 37,024</u> | <u>\$ 6,618,029</u> | <u>\$ 8,175,480</u> | <u>\$ 14,830,533</u> |

| | Six Months Ended December 31, 2018 | | | | |
|---|---|------------------|----------------------------|------------------------------|----------------------|
| | Common Stock | | Paid in Capital | Retained Earnings | Total |
| | Shares | Amount | | | |
| Balance, June 30, 2018, as previously reported | 7,382,706 | \$ 36,914 | \$ 5,752,270 | \$ 8,414,570 | \$ 14,203,754 |
| Retrospective change in accounting principle (see Note 2) | - | - | 18,617 | (18,617) | - |
| Adjusted Balance, June 30, 2018 | 7,382,706 | \$ 36,914 | \$ 5,770,887 | \$ 8,395,953 | \$ 14,203,754 |
| Net income, as restated | - | - | - | 144,719 | 144,719 |
| Stock-based compensation expense, as restated | - | - | 251,169 | - | 251,169 |
| Exercise of common stock options | 22,125 | 110 | 46,567 | - | 46,677 |
| Balance, December 31, 2018 | <u>7,404,831</u> | <u>\$ 37,024</u> | <u>\$ 6,068,623</u> | <u>\$ 8,540,672</u> | <u>\$ 14,646,319</u> |

| | Three Months Ended December 31, 2019 | | | | |
|----------------------------------|---|------------------|----------------------------|------------------------------|----------------------|
| | Common Stock | | Paid in Capital | Retained Earnings | Total |
| | Shares | Amount | | | |
| Balance, September 30, 2019 | 7,404,831 | \$ 37,024 | \$ 6,481,323 | \$ 8,391,193 | \$ 14,909,540 |
| Net (loss) | - | - | - | (215,713) | (215,713) |
| Stock-based compensation expense | - | - | 136,706 | - | 136,706 |
| Balance, December 31, 2019 | <u>7,404,831</u> | <u>\$ 37,024</u> | <u>\$ 6,618,029</u> | <u>\$ 8,175,480</u> | <u>\$ 14,830,533</u> |

| | Three Months Ended December 31, 2018 | | | | |
|---|---|------------------|----------------------------|------------------------------|----------------------|
| | Common Stock | | Paid in Capital | Retained Earnings | Total |
| | Shares | Amount | | | |
| Balance, September 30, 2018 | 7,404,831 | \$ 37,024 | \$ 5,940,096 | \$ 8,437,523 | \$ 14,414,643 |
| Net income, as restated | - | - | - | 103,149 | 103,149 |
| Stock-based compensation expense, as restated | - | - | 128,527 | - | 128,527 |
| Balance, December 31, 2018 | <u>7,404,831</u> | <u>\$ 37,024</u> | <u>\$ 6,068,623</u> | <u>\$ 8,540,672</u> | <u>\$ 14,646,319</u> |

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

KOSS CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2019
(Unaudited)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A) BASIS OF PRESENTATION

The condensed consolidated balance sheet as of December 31, 2019, the condensed consolidated statements of operations for the three and six months ended December 31, 2019 and 2018, the condensed consolidated statements of cash flows for the six months ended December 31, 2019 and 2018 and the condensed consolidated statements of stockholders' equity for the three and six months ended December 31, 2019 and 2018 have been prepared by the Company in accordance with generally accepted accounting principles in the United States of America ("U.S. GAAP") and have not been audited. In the opinion of management, all adjustments (consisting of normal recurring adjustments) necessary to present fairly the financial position, results of operations and cash flows for all periods presented have been made. The operating results for any interim period are not necessarily indicative of the operating results that may be experienced for the full fiscal year.

Certain information and footnote disclosure normally included in consolidated financial statements prepared in accordance with U.S. GAAP have been condensed or omitted. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2019.

The preparation of financial statements in conformity with U.S. GAAP requires the company to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses. Significant estimates and assumptions are used for, but are not limited to, allowances for doubtful accounts, reserves for excess and obsolete inventories, long-lived and intangible assets, income tax valuation allowance, non-cash stock-based compensation and deferred compensation. Actual results could differ from the company's estimates.

B) INCOME TAXES

A tax provision of \$22 and \$25 was recorded during the six months ended December 31, 2019 and 2018 respectively. No income tax benefit was recorded for the six months ended December 31, 2019, due to the uncertainty of utilizing the related deferred tax asset. Utilization of net operating tax carryforwards and a full valuation allowance against deferred tax assets reduced the income tax expense to zero for the six months ended December 31, 2018.

C) PATENT COSTS

The Company incurs on-going legal fees and filing costs related to the patent portfolio. These costs are expensed in the period they are incurred.

2. CHANGE IN ACCOUNTING PRINCIPLE

During the first quarter of fiscal 2020, the Company changed its method of recording stock-based compensation expense. Under the new accounting principle, stock-based compensation expense is recorded on a straight-line basis over the vesting period and forfeitures are recognized when they occur. Under the previous method, the Company estimated future forfeitures and the expected number of awards that would vest and subsequently adjusted for forfeitures. The Company believes this method of recording stock-based compensation expense on a straight-line basis over the vesting period is preferable since it is more reflective of the stock options that will actually vest.

The cumulative effect of the changes in the June 30, 2019 Consolidated Balance Sheet for the change in principle related to stock-based compensation expense using the full retrospective method was as follows:

| Balance Sheet June 30, 2019 | As Previously Reported | Stock-Based Compensation Adjustment | As Adjusted |
|--|-----------------------------------|--|------------------------|
| Equity: | | | |
| Paid in capital | \$ 6,186,393 | \$ 146,742 | \$ 6,333,135 |
| Retained earnings | \$ 8,848,684 | \$ (146,742) | \$ 8,701,942 |

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The impact of the change in principle on the Consolidated Statement of Operations for the three and six months ended December 31, 2018 was as follows:

| Statement of Operations Three Months Ended December 31, 2018 | As Previously Reported | Stock-Based Compensation Adjustment | As Adjusted |
|---|-----------------------------------|--|------------------------|
| Selling, general and administrative expenses | \$ 1,528,374 | \$ 30,972 | \$ 1,559,346 |
| Income from operations | 134,121 | (30,972) | 103,149 |
| Net income | \$ 134,121 | \$ (30,972) | \$ 103,149 |
| Income per common share | | | |
| Basic | \$ 0.02 | \$ (0.01) | \$ 0.01 |
| Diluted | \$ 0.02 | \$ (0.01) | \$ 0.01 |

| Statement of Operations Six Months Ended December 31, 2018 | As Previously Reported | Stock-Based Compensation Adjustment | As Adjusted |
|---|-----------------------------------|--|------------------------|
| Selling, general and administrative expenses | \$ 3,292,122 | \$ 56,813 | \$ 3,348,935 |
| Income from operations | 201,557 | (56,813) | 144,744 |
| Net income | \$ 201,532 | \$ (56,813) | \$ 144,719 |
| Income per common share | | | |
| Basic | \$ 0.03 | \$ (0.01) | \$ 0.02 |
| Diluted | \$ 0.03 | \$ (0.01) | \$ 0.02 |

The impact of the change in principle on the Consolidated Statement of Cash Flows for the six months ended December 31, 2018 was as follows:

| Statement of Cash Flows Six Months Ended December 31, 2018 | As Previously Reported | Stock-Based Compensation Adjustment | As Adjusted |
|---|-----------------------------------|--|------------------------|
| Operating activities: | | | |
| Net income | \$ 201,532 | \$ (56,813) | \$ 144,719 |
| Stock-based compensation expense | \$ 194,356 | \$ 56,813 | \$ 251,169 |

3. INVENTORIES

The components of inventories were as follows:

| | December 31, 2019 | June 30, 2019 |
|--------------------------------|--------------------------|----------------------|
| Raw materials | \$ 2,035,398 | \$ 1,848,340 |
| Finished goods | 6,193,573 | 6,604,408 |
| Inventories, gross | 8,228,971 | 8,452,748 |
| Reserve for obsolete inventory | (1,527,660) | (1,601,300) |
| Inventories, net | \$ 6,701,311 | \$ 6,851,448 |

4. CREDIT FACILITY

On May 14, 2019, the Company entered into a secured credit facility ("Credit Agreement") with Town Bank ("Lender") for a two-year term expiring on May 14, 2021. The Credit Agreement provides for an \$5,000,000 revolving secured credit facility with interest rates of 1.50% over LIBOR. The Credit Agreement also provides for letters of credit for the benefit of the Company of up to a sublimit of \$1,000,000. There are no unused line fees in the credit facility. The Company and the Lender also entered into a General Business Security Agreement dated May 14, 2019 under which the Company granted the Lender a security interest in substantially all of the Company's assets in connection with the Company's obligations under the Credit Agreement. The Credit Agreement contains certain affirmative and negative covenants customary for financings of this type. The negative covenants include restrictions on other indebtedness, liens, fundamental changes, certain investments, disposition of assets, mergers and liquidations, among other restrictions. The Company is currently in compliance with all covenants related to the Credit Agreement. As of December 31, 2019, and June 30, 2019, there were no outstanding borrowings on the facility.

5. REVENUE RECOGNITION

The Company disaggregates its net sales by geographical location as it believes it best depicts how the nature, timing and uncertainty of net sales and cash flows are affected by economic factors. The following table summarizes net sales by geographical location:

| | Three Months Ended December 31 | | Six Months Ended December 31 | |
|---------------|---|--------------|---|---------------|
| | 2019 | 2018 | 2019 | 2018 |
| United States | \$ 3,081,853 | \$ 3,172,401 | \$ 7,585,159 | \$ 7,006,267 |
| Export | 1,080,806 | 2,238,826 | 1,988,262 | 4,189,799 |
| Net Sales | \$ 4,162,659 | \$ 5,411,227 | \$ 9,573,421 | \$ 11,196,066 |

Deferred revenue relates primarily to consumer and customer warranties. These constitute future performance obligations and the Company defers revenue related to these future performance obligations. The Company recognized revenue, which was included in the deferred revenue liability at the beginning of the periods, of \$278,577 and \$312,041 in the six months ended December 31, 2019 and 2018, respectively, for performance obligations related to consumer and customer warranties. The deferred revenue liability was \$859,370 and \$777,982 as of June 30, 2018 and December 31, 2018, respectively.

6. (LOSS) INCOME PER COMMON AND COMMON STOCK EQUIVALENT SHARE

Basic (loss) income per share is computed based on the weighted-average number of common shares outstanding. Diluted income per common share is calculated assuming the exercise of stock options except where the result would be anti-dilutive. The following table reconciles the numerator and denominator used to calculate basic and diluted income per share:

| | Three Months Ended December | | Six Months Ended December | |
|--|-----------------------------|------------------|---------------------------|------------------|
| | 31, | | 31, | |
| | 2019 | 2018* | 2019 | 2018* |
| Numerator | | | | |
| Net (loss) income | \$ (215,713) | \$ 103,149 | \$ (526,462) | \$ 144,719 |
| Denominator | | | | |
| Weighted average shares, basic | 7,404,831 | 7,404,831 | 7,404,831 | 7,397,291 |
| Dilutive effect of stock compensation awards | - | 8,560 | - | 26,226 |
| Diluted shares | <u>7,404,831</u> | <u>7,413,391</u> | <u>7,404,831</u> | <u>7,423,517</u> |
| Net (loss) income attributable to common shareholders per share: | | | | |
| Basic | <u>\$ (0.03)</u> | <u>\$ 0.01</u> | <u>\$ (0.07)</u> | <u>\$ 0.02</u> |
| Diluted | <u>\$ (0.03)</u> | <u>\$ 0.01</u> | <u>\$ (0.07)</u> | <u>\$ 0.02</u> |

*As adjusted for change in accounting principle (Note 2)

7. LEASES

The Company leases its facility in Milwaukee, Wisconsin from Koss Holdings, LLC, which is wholly-owned by the former Chairman. On January 5, 2017 the lease was renewed for a period of five years, ending June 30, 2023, and is being accounted for as an operating lease. The lease extension maintained the rent at a fixed rate of \$380,000 per year and included an option to renew at the same rate for an additional five years ending June 30, 2028. The Company is responsible for all property maintenance, insurance, taxes and other normal expenses related to ownership.

8. LEGAL MATTERS

The Company is subject to a variety of claims and suits that arise from time to time in the ordinary course of business. Although management currently believes that resolving these claims against us, individually or in the aggregate, will not have a material adverse impact on the Consolidated Financial Statements, these matters are subject to inherent uncertainties and management's view of these matters may change in the future.

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This Form 10-Q contains forward-looking statements within the meaning of that term in the Private Securities Litigation Reform Act of 1995 (the “Act”) (Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934). Additional written or oral forward-looking statements may be made by the Company from time to time in filings with the Securities Exchange Commission, press releases, or otherwise. Statements contained in this Form 10-Q that are not historical facts are forward-looking statements made pursuant to the safe harbor provisions of the Act. Forward-looking statements may include, but are not limited to, projections of revenue, income or loss and capital expenditures, statements regarding future operations, anticipated financing needs, compliance with financial covenants in loan agreements, plans for acquisitions or sales of assets or businesses, plans relating to products or services of the Company, assessments of materiality, predictions of future events, the effects of pending and possible litigation and assumptions relating to the foregoing. In addition, when used in this Form 10-Q, the words “anticipates,” “believes,” “estimates,” “expects,” “intends,” “plans,” “may,” “will,” “should,” “forecasts,” “predicts,” “potential,” “continue” and variations thereof and similar expressions are intended to identify forward-looking statements.

Forward-looking statements are inherently subject to risks and uncertainties, some of which cannot be predicted or quantified based on current expectations. Consequently, future events and actual results could differ materially from those set forth in, contemplated by, or underlying the forward-looking statements contained in this Form 10-Q, or in other Company filings, press releases, or otherwise. In addition to the factors discussed in this Form 10-Q, other factors that could contribute to or cause such differences include, but are not limited to, developments in any one or more of the following areas: future fluctuations in economic conditions, the receptivity of consumers to new consumer electronics technologies, the rate and consumer acceptance of new product introductions, competition, pricing, the number and nature of customers and their product orders, production by third party vendors, foreign manufacturing, sourcing, and sales (including foreign government regulation, trade and importation concerns), borrowing costs, changes in tax rates, pending or threatened litigation and investigations, and other risk factors which may be detailed from time to time in the Company’s Securities and Exchange Commission filings.

Readers are cautioned not to place undue reliance on any forward-looking statements contained herein, which speak only as of the date hereof. The Company undertakes no obligation to publicly release the result of any revisions to these forward-looking statements that may be made to reflect events or circumstances after the date hereof or to reflect new information.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**Overview**

The Company developed stereo headphones in 1958 and has been a leader in the industry. Koss markets a complete line of high-fidelity headphones, wireless Bluetooth® headphones, wireless Bluetooth® speakers, computer headsets, telecommunications headsets, and active noise canceling headphones. The Company operates as one business segment.

Results of Operations Summary

- Net sales for the quarter ended December 31, 2019, decreased \$1,248,568 to \$4,162,659, compared to the same quarter last year. For the six months ended December 31, 2019, net sales decreased \$1,622,645 to \$9,573,421. Completion of an export OEM project last year and lower sales to European distributors caused the decreased sales.
- Gross profit as a percent of net sales increased for the three months ended December 31, 2019 compared to the same quarter last year. For the six months ended December 31, 2019, gross profit as a percent of net sales decreased. Gross profit fluctuations were primarily driven by a change in the mix of business by product, customer and sales channel. A significant factor in the six month decrease was the large back-to-school sale to a domestic retailer at low margin.
- Selling, general and administrative expenses for the three and six months ended December 31, 2019 were similar to last year.
- Tax expense for the three and six months ended December 31, 2019 was minimal due to an offsetting change in the valuation allowance for deferred tax assets. The Company is not recording a tax benefit on the pretax loss because of the uncertainty in realizing the benefits of deferred tax assets.

Financial Results

The following table presents selected financial data for the three and six months ended December 31, 2019 and 2018

| Financial Performance Summary | Three Months Ended December 31 | | Six Months Ended December 31 | |
|--|---|--------------|---|---------------|
| | 2019 | 2018* | 2019 | 2018* |
| Net sales | \$ 4,162,659 | \$ 5,411,227 | \$ 9,573,421 | \$ 11,196,066 |
| Net sales (decrease) % | (23.1)% | (8.1)% | (14.5)% | (6.5)% |
| Gross profit | \$ 1,364,087 | \$ 1,662,495 | \$ 2,711,541 | \$ 3,493,679 |
| Gross profit as % of net sales | 32.8% | 30.7% | 28.3% | 31.2% |
| Selling, general and administrative expenses | \$ 1,586,705 | \$ 1,559,346 | \$ 3,251,305 | \$ 3,348,935 |
| Selling, general and administrative expenses as % of net sales | 38.1% | 28.8% | 34.0% | 29.9% |
| Interest income | \$ 6,927 | \$ - | \$ 13,324 | \$ - |
| (Loss) income before income tax provision | \$ (215,691) | \$ 103,149 | \$ (526,440) | \$ 144,744 |
| (Loss) income before income tax as % of net sales | (5.2)% | 1.9% | (5.5)% | 1.3% |
| Income tax provision | \$ 22 | \$ - | \$ 22 | \$ 25 |
| Income tax provision as % of income before income tax | 0% | 0% | 0% | 0% |

*As adjusted for change in accounting principle (Note 2)

2019 Results Compared with 2018

(comments refer to both the three and six month periods unless otherwise noted)

For the three and six months ended December 31, 2019 net sales declined 23.1% and 14.5%, respectively, due to a decrease in the export markets. Sales in the domestic markets for the six months ended December 31, 2019, increased 8.3% over the same period last year. For the three months ended December 31, 2019, domestic sales declined 2.8%.

Net sales in the domestic market were approximately \$3,082,000 in the three months ended December 31, 2019, compared to last year's approximately \$3,172,000. For the six months ended December 31, 2019, domestic net sales increased from approximately \$7,006,000 to approximately \$7,585,000. Sales to mass retail customers increased in the six months ended December 31, 2019 but declined in the last three months compared to last year. Mass retail net sales included a large back-to-school promotion in the early part of the six months ended December 31, 2019. Sales of these promotional products slowed in the last three months. Education related customers showed strong sales increases both year to date and in the current quarter. Certain domestic distributors and consumer direct customers had lower sales. Management believes this was due to inventory reduction efforts at those customers.

Export net sales decreased 51.7% to approximately \$1,081,000 for the three months ended December 31, 2019, compared to approximately \$2,239,000 for the three months ended December 31, 2018. For the six months ended December 31, 2019, sales decreased 52.6% to approximately \$1,988,000 from \$4,190,000 last year. Sales to an export OEM customer, for which the contract ended in December 2018, were approximately \$416,000 and \$973,000 in the three and six months ended December 31, 2018 and accounted for a significant portion of the decrease in net sales. Sales to distributors in Europe were the primary drivers for the remainder of the decrease. Management believes these declines were due to timing of sales related to introduction of new products.

Gross profit decreased to 28.3% for the six months ended December 31, 2019, compared to 31.2% for the six months ended December 31, 2018. The lower gross profit in the current year was largely due to the promotional back-to-school sale to a domestic mass retail customer at very low margin. For the three months ended December 31, 2019, gross profit increased to 32.8% from 30.7% due to more favorable mix of sales by market and product.

Selling, general and administrative expenses for the three months ended December 31, 2019, increased approximately \$28,000 or 1.8% compared to the prior year. For the six months ended December 31, 2019, there was a decrease of approximately \$98,000 or 2.9% in selling general and administrative expenses. For

the three months ended December 31, 2019, the primary factors were an increase in legal and professional fees of approximately \$36,000, an increase in employee benefit costs of approximately \$24,000 and a decrease in deferred compensation expense of approximately \$44,000. An increase of approximately \$120,000 cash surrender value income was the most significant factor causing the decrease in the six months ended December 31, 2019. For the six months ended December 31, 2019, deferred compensation expense declined by approximately \$51,000 compared to the prior year. Bad debt expense declined by approximately \$44,000 this year compared to last year when the bad debt for a domestic mass retail customer was recorded as a result of a Chapter 11 filing. Legal and professional fees increased by approximately \$49,000 compared to the prior year.

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Income tax provision for the three and six months ended December 31, 2019 was comprised of the U.S. federal statutory rate of 21% and the effect of state income taxes fully offset by an adjustment to the valuation allowance for deferred tax assets. The Company is not recording a tax benefit on the pretax loss because of the uncertainty in realizing the benefits of deferred tax assets.

The Company has launched a program focused on enforcing its intellectual property and, in particular, certain of its patent portfolio. The Company has incurred costs and will continue to incur costs related to enforcing this program. These costs primarily relate to legal fees and other costs involved with the underlying efforts to enforce this portfolio. Depending on the response to and the underlying results of the enforcement program, the Company may enter into licensing arrangements or initiate lawsuits as part of the Company's efforts to enforce this program. If successful, the Company may receive royalties, offers to purchase its intellectual property, or other proceeds in amounts that could have a material effect on its financial statements.

Liquidity and Capital Resources

Cash Flows

The following table summarizes cash flows from operating, investing and financing activities for the six months ended December 31, 2019 and 2018

| Total cash provided by (used in): | 2019 | 2018 |
|---|------------|--------------|
| Operating activities | \$ 352,988 | \$ 1,354,067 |
| Investing activities | (352,186) | (235,514) |
| Financing activities | - | 46,677 |
| Net increase in cash and cash equivalents | \$ 802 | \$ 1,165,230 |

Operating Activities

The decrease in accounts payable and the loss from operations were the driving factors for the decrease in cash provided by operating activities during the six months ended December 31, 2019. There was significant inventory inbound to the U.S. from China as of June 30, 2019 that was paid for during the quarter ended September 30, 2019. The impact of these factors was partially offset by a decrease in accounts receivable.

Investing Activities

Cash used in investing activities was higher for the six months ended December 31, 2019, as the Company had increased expenditures for leasehold improvements and for tooling related to new product introductions. During the fiscal year ending June 30, 2020, the Company anticipates it will incur total expenditures for tooling, leasehold improvements and capital expenditures of approximately \$500,000 to \$700,000. The Company expects to generate sufficient cash flow through operations or through the use of its available cash and its credit facility to fund these expenditures.

Financing Activities

As of December 31, 2019 and 2018, the Company had no outstanding borrowings on its bank line of credit facility.

There were no purchases of common stock in 2019 or 2018 under the stock repurchase program. Cash provided in 2018 was from stock options exercised which resulted in the issuance of 22,125 shares of common stock. No stock options were exercised in 2019.

Liquidity

The Company's capital expenditures are primarily for leasehold improvements and tooling. In addition, it has interest payments on its borrowings when it uses its line of credit facility. The Company believes that cash generated from operations, together with cash reserves and borrowings available under its credit facility, provide it with adequate liquidity to meet operating requirements, debt service requirements and planned capital expenditures for the next twelve months and thereafter for the foreseeable future. The Company regularly evaluates new product offerings, inventory levels and capital expenditures to ensure that it is effectively allocating resources in line with current market conditions.

Credit Facility

On May 14, 2019, the Company entered into a secured credit facility ("Credit Agreement") with Town Bank ("Lender") for a two-year term expiring on May 14, 2021. The Credit Agreement provides for an \$5,000,000 revolving secured credit facility with interest rates of 1.50% over LIBOR. The Credit Agreement also provides for letters of credit for the benefit of the Company of up to a sublimit of \$1,000,000. There are no unused line fees in the credit facility. The Company and the Lender also entered into a General Business Security Agreement dated May 14, 2019 under which the Company granted the Lender a security interest in substantially all of the Company's assets in connection with the Company's obligations under the Credit Agreement. The Credit Agreement contains certain affirmative and negative covenants customary for financings of this type. The negative covenants include restrictions on other indebtedness, liens, fundamental changes, certain investments, disposition of assets, mergers and liquidations, among other restrictions. The Company is currently in compliance with all covenants related to the Credit Agreement. As of December 31, 2019, and June 30, 2019, there were no outstanding borrowings on the facility.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Not applicable.

Item 4. Controls and Procedures

Disclosure Controls and Procedures

Disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e)) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”) are designed to ensure that: (1) information required to be disclosed in reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms; and (2) such information is accumulated and communicated to management, including the chief executive officer and principal financial officer, to allow timely decisions regarding required disclosures. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives.

The Company’s management, including the Company’s Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of the Company’s disclosure controls and procedures as of December 31, 2019. The Company’s management has concluded that the Company’s disclosure controls and procedures as of December 31, 2019 were effective.

Changes in Internal Control Over Financial Reporting

There have been no significant changes in the Company’s internal control over financial reporting (as defined in Exchange Act Rules 13a–15(f) and 15d–15(f)) that occurred during the Company’s most recent fiscal quarter 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

As of December 31, 2019, the Company is currently involved in legal matters that are described in Note 8 to the condensed consolidated financial statements, which description is incorporated herein by reference.

Item 1A. Risk Factors

Not applicable.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

The following table presents information with respect to purchases of common stock of the Company made during the six months ended December 31, 2019, by the Company.

COMPANY REPURCHASES OF EQUITY SECURITIES

| Period (2019) | Total # of Shares Purchased | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plan (1) | Approximate Dollar Value of Shares Available under Repurchase Plan |
|----------------------|------------------------------------|-------------------------------------|--|---|
| July 1 - December 31 | - | \$ - | - | \$ 2,139,753 |

(1) In April of 1995, the Board of Directors approved a stock repurchase program authorizing the Company to purchase from time to time up to \$2,000,000 of its common stock for its own account. Subsequently, the Board of Directors periodically has approved increases in the stock repurchase program. The most recent increase was for an additional \$2,000,000 in October 2006, for a maximum of \$45,500,000 of which \$43,360,247 had been expended through December 31, 2019.

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Item 6. Exhibits

| Exhibit No. | Exhibit Description |
|--------------------|---|
| 31.1 | Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer * |
| 31.2 | Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer * |
| 32.1 | Section 1350 Certification of Chief Executive Officer ** |
| 32.2 | Section 1350 Certification of Chief Financial Officer ** |
| 101 | The following financial information from Koss Corporation's Quarterly Report on Form 10-Q for the quarter ended December 31, 2019, formatted in XBRL (eXtensible Business Reporting Language): (i) Condensed Consolidated Balance Sheets as of December 31, 2019 and June 30, 2019, (ii) Condensed Consolidated Statements of Operations (Unaudited) for the three and six months ended December 31, 2019 and 2018 (iii) Condensed Consolidated Statements of Cash Flows (Unaudited) for the six months ended December 31, 2019 and 2018 (iv) Condensed Consolidated Statements of Stockholders' Equity (Unaudited) for the three and six months ended December 31, 2019 and 2018 and (v) the Notes to Condensed Consolidated Financial Statements (Unaudited). * |

* Filed herewith
** Furnished herewith

SIGNATURES

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

KOSS CORPORATION

/s/ Michael J. Koss January 31, 2020
Michael J. Koss
Chairman
Chief Executive Officer

/s/ David D. Smith January 31, 2020
David D. Smith
Chief Financial Officer
Principal Accounting Officer

**Certification of Chief Executive Officer
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Michael J. Koss, certify that:

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

Dated: January 31, 2020

/s/ Michael J. Koss

Michael J. Koss
Chairman and Chief Executive Officer

**Certification of Chief Financial Officer
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, David D. Smith, certify that:

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

Dated: January 31, 2020

/s/ David D. Smith
David D. Smith
Chief Financial Officer

**Certification of Chief Executive Officer
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002,
18 U.S.C. Section 1350**

I, Michael J. Koss, Chief Executive Officer of Koss Corporation (the "Company"), hereby certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350 that to my knowledge:

- (i) the Quarterly Report on Form 10-Q of the Company for the quarter ended December 31, 2019 (the "Report") fully complies with the requirements of Section 13(a) or Section 15(d), as applicable, of the Securities Exchange Act of 1934, as amended; and
- (ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Michael J. Koss

Michael J. Koss
Chairman and Chief Executive Officer
Dated: January 31, 2020

Note: This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not be deemed filed, except to the extent required by the Sarbanes-Oxley Act of 2002, by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.

**Certification of Chief Financial Officer
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002,
18 U.S.C. Section 1350**

I, David D. Smith, Chief Financial Officer of Koss Corporation (the "Company"), hereby certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350 that to my knowledge:

- (i) the Quarterly Report on Form 10-Q of the Company for the quarter ended December 31, 2019 (the "Report") fully complies with the requirements of Section 13(a) or Section 15(d), as applicable, of the Securities Exchange Act of 1934, as amended; and
- (ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ David D. Smith

David D. Smith
Chief Financial Officer
Dated: January 31, 2020

Note: This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not be deemed filed, except to the extent required by the Sarbanes-Oxley Act of 2002, by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.