SemiLEDs Corp
Form 10-Q
April 12, 2019
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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 February 28, 2019

or

TRANSITION REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to

Commission File Number: 001-34992

SemiLEDs Corporation

(Exact name of registrant as specified in its charter)

Delaware	20-2735523
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

3F, No. 11 Ke Jung Rd., Chu-Nan Site, Hsinchu Science Park, Chu-Nan 350, Miao-Li County, Taiwan, R.O.C.	350
(Address of principal executive offices)	(Zip Code)

+886-37-586788
(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 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, smaller reporting company, or an emerging growth company. See 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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 3,589,015 shares of common stock, par value $0.0000056 per share, outstanding as of April 8, 2019.

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SEMILEDS CORPORATION

FORM 10-Q for the Quarter Ended February 28, 2018

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PART I — FINANCIAL INFORMATION

Item 1. Financial Statements

SEMILEDS CORPORATION AND SUBSIDIARIES

Unaudited Condensed Consolidated Balance Sheets

(In thousands of U.S. dollars and shares, except par value)

	February 28, 2019	August 31, 2018
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$1,635	$3,421
Accounts receivable (including related parties), net of allowance for doubtful accounts of $480 and $477 as of February 28, 2019 and August 31, 2018, respectively	736	282
Inventories	2,073	1,818
Prepaid expenses and other current assets	355	340
Total current assets	4,799	5,861
Property, plant and equipment, net	6,448	7,213
Intangible assets, net	93	98
Investments in unconsolidated entities	912	914
Other assets	176	164
TOTAL ASSETS	$12,428	$14,250
LIABILITIES AND EQUITY		
CURRENT LIABILITIES:		
Current installments of long-term debt	$337	$335
Accounts payable	973	894
Advance receipt toward the convertible note	500	500
Accrued expenses and other current liabilities	2,149	5,505
Total current liabilities	3,959	7,234
Long-term debt, excluding current installments	5,040	2,013
Total liabilities	8,999	9,247
Commitments and contingencies (Note 5)		
EQUITY:		
SemiLEDs stockholders' equity		
Common stock, $0.0000056 par value—7,500 shares authorized; 3,589 shares and 3,559 shares issued and outstanding as of February 28, 2019 and August 31, 2018, respectively	—	—
Additional paid-in capital	175,745	175,527
Accumulated other comprehensive income	3,714	3,727
Accumulated deficit	(176,076)	(174,251)
Total SemiLEDs stockholders' equity	3,383	5,003
Noncontrolling interests	46	—

Total equity	3,429	5,003
TOTAL LIABILITIES AND EQUITY	$12,428	$14,250

See notes to unaudited condensed consolidated financial statements.

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SEMILEDS CORPORATION AND SUBSIDIARIES

Unaudited Condensed Consolidated Statements of Operations

(In thousands of U.S. dollars and shares, except per share data)

	Three Months Ended February 28, 2019	February 28, 2018	Six Months Ended February 28, 2019	February 28, 2018
Revenues, net	$ 1,630	$ 1,543	$ 2,602	$ 3,546
Cost of revenues	1,628	1,987	2,819	3,938
Gross profit (loss)	2	(444)	(217)	(392)
Operating expenses:				
Research and development	298	223	632	407
Selling, general and administrative	619	781	1,376	1,514
Gain on disposals of long-lived assets, net	—	(209)	(288)	(209)
Total operating expenses	917	795	1,720	1,712
Loss from operations	(915)	(1,239)	(1,937)	(2,104)
Other income (expenses):				
Interest expenses, net	(36)	(7)	(41)	(15)
Other income (losses), net	(126)	49	(46)	547
Foreign currency transaction gain, net	233	65	197	48
Total other income, net	71	107	110	580
Loss before income taxes	(844)	(1,132)	(1,827)	(1,524)
Income tax expense	—	—	—	—
Net loss	(844)	(1,132)	(1,827)	(1,524)
Less: Net gain (loss) attributable to noncontrolling interests	3	—	(2)	—
Net loss attributable to SemiLEDs stockholders	$ (847)	$ (1,132)	$ (1,825)	$ (1,524)
Net loss per share attributable to SemiLEDs stockholders:				
Basic and diluted	$ (0.24)	$ (0.32)	$ (0.51)	$ (0.43)
Shares used in computing net loss per share attributable to SemiLEDs stockholders:				
Basic and diluted	3,579	3,545	3,569	3,545

See notes to unaudited condensed consolidated financial statements.

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SEMILEDS CORPORATION AND SUBSIDIARIES

Unaudited Condensed Consolidated Statements of Comprehensive Loss

(In thousands of U.S. dollars)

	Three Months Ended		Six Months Ended	
	February 28, 2019	February 28, 2018	February 28, 2019	February 28, 2018
Net loss	$(844)	$(1,132)	$(1,827)	$(1,524)
Other comprehensive loss, net of tax:				
Foreign currency translation adjustments, net of tax of $0 for all periods presented	$(17)	109	(13)	135
Comprehensive loss	$(861)	$(1,023)	$(1,840)	$(1,389)
Comprehensive loss attributable to noncontrolling interests	$4	$—	$(2)	$—
Comprehensive loss attributable to SemiLEDs stockholders	$(865)	$(1,023)	$(1,838)	$(1,389)

See notes to unaudited condensed consolidated financial statements.

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SEMILEDS CORPORATION AND SUBSIDIARIES

Unaudited Condensed Consolidated Statement of Changes in Equity

(In thousands of U.S. dollars and shares)

	Common Shares	Stock Amount	Additional Paid-in Capital	Accumulated Other Comprehensive Income	Accumulated Deficit	Total SemiLEDs Shareholders' Equity	Non-Controlling Interests	Total Equity
BALANCE—September 1, 2018	3,559	$ —	$ 175,527	$ 3,727	$ (174,251)	$ 5,003	$ —	$ 5,003
Issuance of common stock under equity incentive plans	30	—	—	—	—	—	—	—
Stock-based compensation		—	90	—	—	90	—	90
Common stock issued by SBDI*	—	—	128	—	—	128	48	176
Comprehensive loss:								—
Other comprehensive income (loss)	—	—	—	(13)	—	(13)	—	(13)
Net loss	—	—	—	—	(1,825)	(1,825)	(2)	(1,827)
BALANCE—February 28, 2019	3,589	$ —	$ 175,745	$ 3,714	$ (176,076)	$ 3,383	$ 46	$ 3,429

See notes to unaudited condensed consolidated financial statements.

*SBDI (Taiwan Bandaoti Zhaoming Co., Ltd.) is one of the Company's subsidiaries.

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SEMILEDS CORPORATION AND SUBSIDIARIES

Unaudited Condensed Consolidated Statements of Cash Flows

(In thousands of U.S. dollars)

	Six Months Ended February 28, 2019	February 28, 2018
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$(1,827)	$(1,524)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	545	520
Stock-based compensation expense	90	48
Provisions for inventory write-downs	312	413
Gain on disposals of long-lived assets, net	(288)	(209)
Changes in :		
Accounts receivable, net	(455)	811
Inventories	(559)	103
Prepaid expenses and other	(26)	61
Accounts payable	391	(191)
Accrued expenses and other current liabilities	(161)	130
Net cash provided by (used in) operating activities	(1,978)	162
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property, plant and equipment	(64)	(131)
Proceeds from sales of property, plant and equipment	512	327
Return the received-in-advance	(3,000)	—
Payments for development of intangible assets	(2)	(1)
Proceeds from patents assignment	—	1
Net cash provided by (used in) investing activities	(2,554)	196
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from long-term debt	3,200	—
Repayments of long-term debt	(167)	(173)
Acquisition of noncontrolling interests	(1)	—
Net cash provided by (used in) financing activities	3,032	(173)
Effect of exchange rate changes on cash and cash equivalents	(286)	90
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(1,786)	275
CASH AND CASH EQUIVALENTS—Beginning of period	3,421	3,582
CASH AND CASH EQUIVALENTS—End of period	$1,635	$3,857
NONCASH INVESTING AND FINANCING ACTIVITIES:		
Accrual related to property, plant and equipment	$13	$114

See notes to unaudited condensed consolidated financial statements.

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SEMILEDS CORPORATION AND SUBSIDIARIES

Notes to Unaudited Condensed Consolidated Financial Statements

1. Business

SemiLEDs Corporation ("SemiLEDs" or the "parent company") was incorporated in Delaware on January 4, 2005 and is a holding company for various wholly owned subsidiaries. SemiLEDs and its subsidiaries (collectively, the "Company") develop, manufacture and sell high performance light emitting diodes ("LEDs"). The Company's core products are LED components, as well as LED chips and lighting products. LED components have become the most important part of its business. A portion of the Company's business consists of the sale of contract manufactured LED products. The Company's customers are concentrated in a few select markets, including Taiwan, the United States and China.

As of February 28, 2019, SemiLEDs had four wholly owned subsidiaries. SemiLEDs Optoelectronics Co., Ltd., or Taiwan SemiLEDs, is the Company's wholly owned operating subsidiary, where a substantial portion of the assets is held and located, and where a portion of our research, development, manufacturing and sales activities take place. Taiwan SemiLEDs owns a 97% equity interest in Taiwan Bandaoti Zhaoming Co., Ltd., formerly known as Silicon Base Development, Inc., which is engaged in the research, development, manufacturing and a substantial portion of marketing and sale of LED components, and where most of the Company's employees are based.

SemiLEDs' common stock began trading on the NASDAQ Global Select Market under the symbol "LEDS" on December 8, 2010 and was transferred to the NASDAQ Capital Market effective November 5, 2015 where it continues to trade under the same symbol.

2. Summary of Significant Accounting Policies

Basis of Presentation —The Company's unaudited interim condensed consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP") and applicable provisions of the rules and regulations of the U.S. Securities and Exchange Commission ("SEC") regarding interim financial reporting. Certain information and disclosures normally included in financial statements prepared in accordance with U.S. GAAP have been condensed or omitted as permitted by the rules and regulations of the SEC. Accordingly, these unaudited interim condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto contained in the Company's Annual Report on Form 10-K filed with the SEC on November 26, 2018. The unaudited condensed consolidated balance sheet as of August 31, 2018 included herein was derived from the audited consolidated financial statements as of that date.

The unaudited interim condensed consolidated financial statements have been prepared on the same basis as the audited consolidated financial statements and include all adjustments, consisting only of normal recurring adjustments, necessary for the fair presentation of the Company's consolidated balance sheet as of February 28, 2019, the statements of operations and comprehensive loss for the three and six months ended February 28, 2019 and 2018, the statement of changes in equity for the six months ended February 28, 2019, and the statements of cash flows for the six months ended February 28, 2019 and 2018. The results for the three or six months ended February 28, 2019 are not necessarily indicative of the results to be expected for the year ending August 31, 2019.

The accompanying unaudited interim condensed consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. The realization of assets and the satisfaction of liabilities in the normal course of business are dependent on, among other things, the Company's ability to operate profitably, to generate cash flows from operations, and to pursue financing arrangements to support its working capital requirements.

The Company suffered losses from operations of $3.7 million and $4.3 million, and net cash used in operating activities of $1.2 million and $2.1 million for the years ended August 31, 2018 and 2017, respectively. Gross loss on product sales was $435 thousand for the year ended August 31, 2018, and gross profit was $82 thousand for the year ended August 31, 2017. Loss from operations for the three and six months ended February 28, 2019 were $915 thousand and $1.9 million, respectively. Net cash used in operating activities for the six months ended February 28, 2019 was $2.0 million. Further, at February 28, 2019, the Company's cash and cash equivalents was down to $1.6 million. These facts and conditions raise substantial doubt about the Company's ability to continue as a going concern. However, management believes that it has developed a liquidity plan, as summarized below, that, if executed successfully, should provide sufficient liquidity to meet the Company's obligations as they become due for a reasonable period of time, and allow the development of its core business.

- Gaining positive cash-inflow from operating activities through continuous cost reductions and the sales of new higher margin products. Steady growth of module products and the continued commercial sales of its UV LED product are expected to improve the Company's future gross margin, operating results and cash flows. The Company is targeting niche markets and focusing on product enhancement and developing its LED product into many other applications or devices.

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- Continuing to monitor prices, work with current and potential vendors to decrease costs and, consistent with its existing contractual commitments, may possibly decrease its activity level and capital expenditures further. This plan reflects its strategy of controlling capital costs and maintaining financial flexibility.
- Raising additional cash through further equity offerings, sales of assets and/or issuance of debt as considered necessary and looking at other potential business opportunities.

While the Company's management believes that the measures described in the above liquidity plan will be adequate to satisfy its liquidity requirements for the twelve months after the date that the financial statements are issued, there is no assurance that the liquidity plan will be successfully implemented. Failure to successfully implement the liquidity plan may have a material adverse effect on its business, results of operations and financial position, and may adversely affect its ability to continue as a going concern. These unaudited interim condensed consolidated financial statements do not include any adjustments related to the recoverability and classification of recorded assets or the amounts and classification of liabilities or any other adjustments that might be necessary should the Company be unable to continue as a going concern.

Revenue Recognition —Effective September 1 2018, the Company adopted ASC 606 using the modified retrospective transition method. The Company applied the following five steps to achieve the core principles of ASC 606: 1) identified the contract with a customer; 2) identified the performance obligations (promises) in the contract; 3) determined the transaction price; 4) allocated the transaction price to the performance obligations in the contract; and 5) recognized revenue when (or as) the Company satisfies a performance obligation. The Company recognizes the amount of revenue when the Company satisfies a performance obligation to which it expects to be entitled for the transfer of promised goods or services to customers. The Company obtains written purchase authorizations from its customers as evidence of an arrangement and these authorizations generally provide for a specified amount of product at a fixed price. Generally, the Company considers delivery to have occurred at the time of shipment as this is generally when title and risk of loss for the products will pass to the customer. The Company provides its customers with limited rights of return for non conforming shipments and product warranty claims. Based on historical return percentages, which have not been material to date, and other relevant factors, the Company estimates its potential future exposure on recorded product sales, which reduces product revenues in the consolidated statements of operations and reduces accounts receivable in the consolidated balance sheets. The Company also provides standard product warranties on its products, which generally range from three months to two years. Management estimates the Company's warranty obligations as a percentage of revenues, based on historical knowledge of warranty costs and other relevant factors. To date, the related estimated warranty provisions have been insignificant.

Principles of Consolidation —The unaudited interim condensed consolidated financial statements include the accounts of SemiLEDs and its consolidated subsidiaries. All intercompany transactions and balances have been eliminated during consolidation.

On September 1, 2018, the Company adopted ASC 825-10, "Financial Instruments- Overall: Recognition and Measurement of Financial Assets and Financial Liabilities". This standard allows equity investments that do not have readily determinable fair values to be re-measured at fair value either upon the occurrence of an observable price change or upon identification of impairment. The standard also simplifies the impairment assessment of equity investments without readily determinable fair values by requiring assessment for impairment qualitatively at each reporting period.

Investments in which the Company has the ability to exercise significant influence over the investee but not a controlling financial interest, are accounted for using the equity method of accounting and are not consolidated. These investments are in joint ventures that are not subject to consolidation under the variable interest model, and for which the Company: (i) does not have a majority voting interest that would allow it to control the investee, or (ii) has a majority voting interest but for which other shareholders have significant participating rights, but for which the Company has the ability to exercise significant influence over operating and financial policies. Under the equity method, investments are stated at cost after adding or removing the Company's portion of equity in undistributed earnings or losses, respectively. The Company's investment in these equity method entities is reported in the consolidated balance sheets in investments in unconsolidated entities, and the Company's share of the income or loss of these equity method entities, after the elimination of unrealized intercompany profits, is reported in the consolidated statements of operations in equity in losses from unconsolidated entities. When net losses from an equity method investee exceed its carrying amount, the carrying amount of the investment is reduced to zero. The Company then suspends using the equity method to provide for additional losses unless the Company has guaranteed obligations or is otherwise committed to provide further financial support to the equity method investee. The Company resumes accounting for the investment under the equity method if the investee subsequently returns to profitability and the Company's share of the investee's income exceeds its share of the cumulative losses that have not been previously recognized during the period the equity method is suspended.

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Investments in entities that are not consolidated or accounted for under the equity method are recorded as investments without readily determinable fair values. Investments without readily determinable fair values are reported on the consolidated balance sheets in investments in unconsolidated entities, at cost minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for an identical or similar investment of the same issuer. Dividend income, if any, received is reported in the consolidated statements of operations in equity in losses from unconsolidated entities.

If the fair value of an equity investment declines below its respective carrying amount and the decline is determined to be other than temporary, the investment will be written down to its fair value.

Use of Estimates —The preparation of unaudited interim condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the unaudited interim condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Significant items subject to such estimates and assumptions include the preparation of the Company's consolidated financial statements on the basis that the Company will continue as a going concern, the collectibility of accounts receivable, inventory net realizable values, realization of deferred tax assets, valuation of stock-based compensation expense, the useful lives of property, plant and equipment and intangible assets, the recoverability of the carrying amount of property, plant and equipment, intangible assets and investments in unconsolidated entities, the fair value of acquired tangible and intangible assets, income tax uncertainties, provision for potential litigation costs and other contingencies. Management bases its estimates on historical experience and also on assumptions that it believes are reasonable. Management assesses these estimates on a regular basis; however, actual results could differ materially from those estimates.

Certain Significant Risks and Uncertainties —The Company is subject to certain risks and uncertainties that could have a material and adverse effect on the Company's future financial position or results of operations, which risks and uncertainties include, among others: it has incurred significant losses over the past few years, any inability of the Company to compete in a rapidly evolving market and to respond quickly and effectively to changing market requirements, any inability of the Company to grow its revenue and/or maintain or increase its margins, it may experience fluctuations in its revenues and operating results, any inability of the Company to protect its intellectual property rights, claims by others that the Company infringes their proprietary technology, and any inability of the Company to raise additional funds in the future.

Concentration of Supply Risk —Some of the components and technologies used in the Company's products are purchased and licensed from a limited number of sources and some of the Company's products are produced by a limited number of contract manufacturers. The loss of any of these suppliers and contract manufacturers may cause the Company to incur transition costs to another supplier or contract manufacturer, result in delays in the manufacturing and delivery of the Company's products, or cause it to carry excess or obsolete inventory. The Company relies on a limited number of such suppliers and contract manufacturers for the fulfillment of its customer orders. Any failure of such suppliers and contract manufacturers to perform could have an adverse effect upon the Company's reputation and its ability to distribute its products or satisfy customers' orders, which could adversely affect the Company's business, financial position, results of operations and cash flows.

Concentration of Credit Risk —Financial instruments that subject the Company to concentrations of credit risk consist primarily of cash, cash equivalents and accounts receivable.

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The Company keeps its cash and cash equivalents in demand deposits with prominent banks of high credit quality and invests only in money market funds. Deposits held with banks may exceed the amount of insurance provided on such deposits. As of February 28, 2019 and August 31, 2018, cash and cash equivalents of the Company consisted of the following (in thousands):

Cash and Cash Equivalents by Location	February 28, 2019	August 31, 2018
United States;		
Denominated in U.S. dollars	$ 53	$ 194
Taiwan;		
Denominated in U.S. dollars	364	2,220
Denominated in New Taiwan dollars	28	55
Denominated in other currencies	1,142	910
China (including Hong Kong);		
Denominated in U.S. dollars	4	7
Denominated in Renminbi	36	29
Denominated in H.K. dollars	8	6
Total cash and cash equivalents	$ 1,635	$ 3,421

The Company's revenues are substantially derived from the sales of LED products. A significant portion of the Company's revenues are derived from a limited number of customers and sales are concentrated in a few select markets. Management performs ongoing credit evaluations of its customers and generally does not require collateral on accounts receivable. Management evaluates the need to establish an allowance for doubtful accounts for estimated potential credit losses at each reporting period. The allowance for doubtful accounts is based on the management's assessment of the collectibility of its customer accounts. Management regularly reviews the allowance by considering certain factors, such as historical experience, industry data, credit quality, age of accounts receivable balances and current economic conditions that may affect a customer's ability to pay.

Net revenues generated from sales to the top ten customers represented 88% and 82% of the Company's total net revenues for the three and six months ended February 28, 2019 respectively, and 73% and 64% of the Company's net revenues for the three and six months ended February 28, 2018, respectively.

The Company's revenues have been concentrated in a few select markets, including the Netherlands, Taiwan, the United States, and China (including Hong Kong). Net revenues generated from sales to customers in these markets, in the aggregate, accounted for 72% and 70% of the Company's net revenues for the three and six months ended February 28, 2019, respectively, and 68% and 74% of the Company's net revenues for the three and six months ended February 28, 2018, respectively.

Noncontrolling Interests —Noncontrolling interests are classified in the consolidated statements of operations as part of consolidated net income (loss) and the accumulated amount of noncontrolling interests in the consolidated balance sheets as part of equity. Changes in ownership interest in a consolidated subsidiary that do not result in a loss of control are accounted for as an equity transaction. If a change in ownership of a consolidated subsidiary results in loss of control and deconsolidation, any retained ownership interests are remeasured with the gain or loss reported in net earnings. On September 1, 2018, Taiwan Bandaoti Zhaoming Co., Ltd. (“SBDI”), the Company’s wholly owned operating subsidiary, issued 414,000 common shares and amended its certificate of incorporation to increase its issued common stock from 12,087,715 to 12,501,715. As of the issuance date, the increased capital of $176 thousand (NT$5.4 million) has been completely received in cash by Taiwan Bandaoti Zhaoming Co., Ltd. The Company did not subscribe for the newly issued common shares, and, as a result, noncontrolling interest in SBDI was increased from zero to 3.31%. In December 2018, Taiwan SemiLEDs purchased 3,000 common shares of SBDI from non-controlling interests. As of February 28 2019, noncontrolling interest in SBDI was down to 3.29%.

Recent Accounting Pronouncements

In August 2018, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2018-13, Fair Value Measurement (Topic 820) Disclosure Framework – Change to the Disclosure Requirements for Fair Value Measurement. The amendments in this Update modify the disclosure requirements of fair value measurements in Topic 820, Fair Value Measurement, based on the concepts in the Concepts Statement, including the consideration of costs and benefits. This standard will be effective for the Company on September 1, 2020. The Company is currently evaluating the impact the adoption of this ASU will have on its consolidated financial statements.

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In June 2018, the FASB issued ASU No. 2018-07, Compensation – Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting. The amendments specify that Topic 718 applies to all share-based payment transactions in which a grantor acquires goods or services to be used or consumed in a grantor's own operations by issuing share-based payment awards. The amendments also clarify that Topic 718 does not apply to share-based payments used to effectively provide (1) financing to the issuer or (2) awards granted in conjunction with selling goods or services to customers as part of a contract accounted for under Topic 606, Revenue from Contracts with Customers. This standard will be effective for the Company on September 1, 2019. The Company does not expect the adoption of this standard to have a material impact on its consolidated financial position, results of operations or cash flows.

In June 2016, the FASB issued ASU No. 2016-13, Financial Instruments – Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments. This standard requires a financial asset (or group of financial assets) measured at amortized cost basis to be presented at the net amount expected to be collected. The allowance for credit losses is a valuation account that is deducted from the amortized cost basis of the financial asset(s) to present the net carrying value at the amount expected to be collected on the financial asset. This standard will be effective for the Company on September 1, 2020. The Company is currently evaluating the impact the adoption of this ASU will have on its consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, Leases, which is intended to improve financial reporting on leasing transactions. This standard requires a lessee to record on the balance sheet the assets and liabilities for the rights and obligations created by lease terms of more than 12 months. This standard will be effective for the Company on September 1, 2019. The Company is currently evaluating the impact the adoption of this ASU will have on its consolidated financial statements.

3. Balance Sheet Components

Inventories

Inventories as of February 28, 2019 and August 31, 2018 consisted of the following (in thousands):

	February 28, 2019	August 31, 2018
Raw materials	$ 473	$ 577
Work in process	744	505
Finished goods	856	736
Total	$ 2,073	$ 1,818

Inventory write-downs to estimated net realizable values were $140 thousand and $312 thousand for the three and six months ended February 28, 2019, respectively, and $207 thousand and $413 thousand for the three and six months ended February 28, 2018, respectively.

Property, Plant and Equipment

Property, plant and equipment as of February 28, 2019 and August 31, 2018 consisted of the following (in thousands):

	February 28, 2019	August 31, 2018
Buildings and improvements	$13,497	$13,558
Machinery and equipment	38,702	39,391
Leasehold improvements	150	150
Other equipment	2,304	2,312
Total property, plant and equipment	54,653	55,411
Less: Accumulated depreciation and amortization	(48,217)	(48,487)
Construction in progress	12	289
Property, plant and equipment, net	$6,448	$7,213

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Intangible Assets

Intangible assets as of February 28, 2019 and August 31, 2018 consisted of the following (in thousands):

	February 28, 2019			
	Weighted Average Amortization Period (Years)	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Patents and trademarks	15	$ 543	$ 450	$ 93
Acquired technology	5	493	493	—
Total		$ 1,036	$ 943	$ 93

	August 31, 2018			
	Weighted Average Amortization Period (Years)	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Patents and trademarks	15	$ 544	$ 446	$ 98
Acquired technology	5	494	494	—
Total		$ 1,038	$ 940	$ 98

4. Investments in Unconsolidated Entities

The Company's ownership interest and carrying amounts of investments in unconsolidated entities as of February 28, 2019 and August 31, 2018 consisted of the following (in thousands, except percentages):

	February 28, 2019		August 31, 2018	
	Percentage Ownership	Amount	Percentage Ownership	Amount
Equity method investments:				
Xurui Guangdian Co., Ltd. ("China SemiLEDs")	49%	$ —	49%	$ —
Equity investment wihout readily determinable fair value	Various	912	Various	914
Total investments in unconsolidated entities		$ 912		$ 914

There were no dividends received from unconsolidated entities through February 28, 2019.

Equity Method Investments

The Company owns a 49% equity interest in China SemiLEDs. However, this investment has a carrying amount of zero as a result of a previously recognized impairment.

Equity Investments without Readily Determinable Fair Value

Equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the Company) which do not have readily determinable fair values are recorded as equity investment without readily determinable fair value. All equity investments without readily determinable fair value are assessed for impairment when events or changes in circumstances indicate that the carrying amounts may not be recoverable, and measured at cost minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for an identical or similar investment of the same issuer.

5. Commitments and Contingencies

Operating Lease Agreements —The Company has several operating leases with unrelated parties, primarily for land, plant and office spaces in Taiwan, which include cancellable and noncancellable and which expire at various dates between April 2019 and December 2021. Lease expense related to these noncancellable operating leases was $37 thousand and $75 thousand for the three and six months ended February 28, 2019, respectively, and $135 thousand and $247 thousand for the three and six months ended February 28, 2018, respectively. Lease expense is recognized on a straight-line basis over the term of the lease.

The aggregate future noncancellable minimum rental payments for the Company's operating leases as of February 28, 2019 consisted of the following (in thousands):

Years Ending August 31,	Operating Leases
Remainder of 2019	$ 77
2020	151
2021	50
2022	—
2023	—
Thereafter	—
Total	$ 278

Purchase Obligations —The Company had purchase commitments for inventory, property, plant and equipment in the amount of $158 thousand and $1.6 million as of February 28, 2019 and August 31, 2018, respectively.

Litigation —The Company is directly or indirectly involved from time to time in various claims or legal proceedings arising in the ordinary course of business. The Company recognizes a liability when it is probable that a loss has been incurred and the amount is reasonably estimable. There is significant judgment required in assessing both the likelihood of an unfavorable outcome and whether the amount of loss, if any, can be reasonably estimated. However, the Company cannot predict the outcome of any litigation or the potential for future litigation.

On June 21, 2017, Well Thrive Ltd. ("Well Thrive") filed a complaint against SemiLEDs Corporation in the United States District Court for the District of Delaware. The complaint alleges that Well Thrive is entitled to return of $500 thousand paid toward a note purchase pursuant to a purchase agreement (the "Purchase Agreement") effective July 6, 2016 with Dr. Peter Chiou, which was assigned to Well Thrive on August 4, 2016. Pursuant to the terms of the Purchase Agreement, we have retained the $500 thousand payment as liquidated damages. Well Thrive alleges that the liquidated damages provision is unenforceable as an illegal penalty and does not reflect the amount of purported damages. On March 13, 2018, the Company filed a motion to enforce a settlement agreement between the parties to dismiss the lawsuit with prejudice. On March 27, 2018, Well Thrive filed an answering brief in opposition to the Company's motion on the basis that Well Thrive never consented to dismiss the case. On January 2, 2019, the judge denied without prejudice the motion filed by us, because there remains some question as to whether Well Thrive's former lawyers and Dr. Chiou had authority from Well Thrive to settle this case. The judge's order allows us to conduct depositions of Well Thrive's former lawyer, Dr. Chiou, and Mr. Chang Sheng-Chun, Well Thrive's director, and to request documents relating to the issues surrounding the settlement. Based on this order, we intend to arrange the depositions to obtain more evidence in support of a motion to enforce the settlement agreement. The Court set a trial date of March 2, 2020, if needed.

On December 28, 2018, the Company received a notification from the Court in Miao-Li County, Taiwan that Epistar Corporation (the successor to Formosa Epitaxy Incorporation, the "Plaintiff") filed a motion requesting that the Company return the $3 million prepayment plus value-added-tax for the headquarters building sale and pay interest during this period and litigation fee. The Plaintiff also petitioned the Court to do a provisional execution upon the Company, which would permit the Plaintiff to sell the building and/or other assets belonging to the Company to recover the prepayment. On January 4, 2019, the Company filed a statement of defense arguing that the Plaintiff's action and motion for provisional execution should be dismissed and the litigation fees should be borne by the Plaintiff. On January 25, 2019, the Company and the Plaintiff entered into a settlement, agreeing that the Company would return the $3 million plus value-added-tax of $150 thousand and penalty of $200 thousand, and on February 1, 2019, the Plaintiff withdrawal the motion. As of February 28, 2019, the Company has paid the $3.2 million, and accrued a payable of $150 thousand.

Except as described above, as of February 28, 2019, there was no pending or threatened litigation that could have a material impact on the Company’s financial position, results of operations or cash flows.

6. Stock-based Compensation

The Company currently has one equity incentive plan (the “2010 Plan”), which provides for awards in the form of restricted shares, stock units, stock options or stock appreciation rights to the Company’s employees, officers, directors and consultants. In April 2014, SemiLEDs’ stockholders approved an amendment to the 2010 Plan that increased the number of shares authorized for issuance under the plan by an additional 250 thousand shares. Prior to SemiLEDs’ initial public offering, the Company had another stock-based compensation plan (the “2005 Plan”), but awards are made from the 2010 Plan after the initial public offering. Options outstanding under the 2005 Plan continue to be governed by its existing terms.

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A total of 521 thousand shares was reserved for issuance under the 2010 Plan, respectively, as of both February 28, 2019 and 2018. As of February 28, 2019 and 2018, there were 189 thousand and 196 thousand shares of common stock available for future issuance under the equity incentive plans, respectively.

In July 2018, SemiLEDs granted 7.5 thousand restricted stock units to its directors that will vest 100% on the earlier of June 29, 2019 or the date of the next annual meeting. The grant-date fair value of the restricted stock units was $4.75 per unit.

In January 2018, SemiLEDs granted 56.7 thousand restricted stock units to its employees among which 50% will vest each year on January 1 of 2019 and 2020 and will become fully vested upon a change in control. The grant-date fair value of the restricted stock units was $4.10 per unit.

In November 2017, SemiLEDs granted 2.5 thousand restricted stock units to its directors that vested 100% on June 28, 2018. The grant-date fair value of the restricted stock units was $4.15 per unit.

The grant date fair value of stock options is determined using the Black-Scholes option-pricing model. The Black-Scholes option-pricing model requires inputs including the market price of SemiLEDs' common stock on the date of grant, the term that the stock options are expected to be outstanding, the implied stock volatilities of several of the Company's publicly-traded peers over the expected term of stock options, risk-free interest rate and expected dividend. Each of these inputs is subjective and generally requires significant judgment to determine. The grant date fair value of stock units is based upon the market price of SemiLEDs' common stock on the date of the grant. This fair value is amortized to compensation expense over the vesting term.

Stock-based compensation expense is recorded net of estimated forfeitures such that expense is recorded only for those stock-based awards that are expected to vest. A forfeiture rate is estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from initial estimates. A forfeiture rate of zero is estimated for stock-based awards with vesting term that is less than or equal to one year from the date of grant.

A summary of the stock-based compensation expense for the three and six months ended February 28, 2019 and 2018 was as follows (in thousands):

	Three Months Ended		Six Months Ended	
	February 28, 2019	February 28, 2018	February 28, 2019	February 28, 2018
Cost of revenues	$13	$ 7	$24	$ 14
Research and development	8	3	15	6
Selling, general and administrative	26	14	51	28
	$47	$ 24	$90	$ 48

7. Net Loss Per Share of Common Stock

The following stock-based compensation plan awards were excluded from the computation of diluted net loss per share of common stock for the periods presented because including them would have been anti-dilutive (in thousands of shares):

	Three Months Ended February 28, 2019	February 28, 2018	Six Months Ended February 28, 2019	February 28, 2018
Stock units and stock options to purchase common stock	11	58	20	40

8. Income Taxes

The Company’s income (loss) before income taxes for the three and six months ended February 28, 2019 and 2018 consisted of the following (in thousands):

	Three Months Ended February 28, 2019	February 28, 2018	Six Months Ended February 28, 2019	February 28, 2018
U.S. operations	$(141)	$(140)	$(291)	$93
Foreign operations	(703)	(992)	(1,536)	(1,617)
Loss before income taxes	$(844)	$(1,132)	$(1,827)	$(1,524)

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Unrecognized Tax Benefits

On December 22, 2017, the U.S. Tax Cuts and Jobs Act was adopted, which among other effects, reduced the U.S. federal corporate income tax rate to 21% from 34% (or 35% in certain cases) beginning in 2018, requires companies to pay a one-time transition tax on certain unrepatriated earnings from non-U.S. subsidiaries that is payable over eight years, makes the receipt of future non-U.S. sourced income of non-U.S. subsidiaries tax-free to U.S. companies and creates a new minimum tax on the earnings of non-U.S. subsidiaries relating to the parent's deductions for payments to the subsidiaries. Provisional estimate of the Company is that no tax will be due under this provision.

As of both February 28, 2019 and August 31, 2018, the Company had no unrecognized tax benefits related to tax positions taken in prior periods. The Company files income tax returns in the United States, various U.S. states and certain foreign jurisdictions. The tax years 2005 through 2018 remain open in most jurisdictions. The Company is not currently under examination by income tax authorities in federal, state or foreign jurisdictions.

9. Related Party Transactions

On January 8, 2019, the Company entered into loan agreements with each of its Chairman and Chief Executive Officer and its largest shareholder, with aggregate amounts of $3.2 million, and an annual interest rate of 8%. All proceeds of the loans were exclusively used to return the deposit to Formosa Epitaxy Incorporation in connection with the canceled sale of the Company's headquarters building pursuant to the agreement dated December 15, 2015. The Company is required to repay the loans of $1.5 million on January 14, 2021 and $1.7 million on January 22, 2021, respectively, unless the loans are sooner accelerated pursuant to the loan agreements. As of February 28, 2019, these loans totaled $3.2 million. The Loans are secured by a second priority security interest on our headquarters building.

10. Subsequent Events

The Company has analyzed its operations subsequent to February 28, 2019 to the date these unaudited condensed consolidated financial statements were issued, and has determined that it does not have any material subsequent events to disclose in these unaudited condensed consolidated financial statements.

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

Forward Looking Statements

This Quarterly Report on Form 10-Q, or this Quarterly Report, contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act. All statements other than statements of historical facts contained in this Quarterly Report, including statements regarding the future results of operations of SemiLEDs Corporation, or "we," "our" or the "Company," and financial position, strategy and plans, and our expectations for future operations, including the execution of our restructuring plan and any resulting cost savings, are forward-looking statements. Any statements contained herein that are not statements of historical facts may be deemed to be forward-looking statements. The words "believe," "may," "should," "plan," "potential," "project," "will," "estimate," "continue," "anticipate," "design," "intend," "expect" and similar expressions are intended to identify forward-looking statements. We have based these forward-looking statements largely on our current expectations and projections about future events and trends that we believe may affect our financial condition, results of operations, strategy, short-term and long-term business operations and objectives, and financial needs. These forward-looking statements are subject to a number of risks, uncertainties and assumptions, and actual results and the timing of certain events could differ materially and adversely from those anticipated or implied in the forward-looking statements as a result of many factors. These factors include, among other things,

- Declining cash position.
- The ability to retain the $500,000 partial payment of the uncompleted $1.6 million note financing as liquidated damages.
- Our ability to improve our liquidity, access alternative sources of funding and obtain additional equity capital or credit when necessary for our operations, the difficulty of which may increase if our common stock is delisted from the NASDAQ Stock Market.
- The inability of our suppliers or other contract manufacturers to produce products that satisfy our requirements.
- Our ability to implement our cost reduction programs and to execute our restructuring plan effectively.
- Our ability to improve our gross margins, reduce our net losses and restore our operations to profitability.
- Our ability to successfully introduce new products that we can produce and that customers will purchase in such amounts as to be sufficiently profitable to cover the costs of developing and producing these products, as well as providing us additional net income from operations.
- Our ability to effectively develop, maintain and expand our sales and distribution channels, especially in the niche LED markets, including the UV LED and architectural lighting that we focus on.
- Our ability to successfully manage our operations in the face of the cyclicality, rapid technological change, rapid product obsolescence, declining average selling prices and wide fluctuations in supply and demand typically found in the LED market.
- Competitive pressures from existing and new companies.
- Our ability to grow our revenues generated from the sales of our products and to control our expenses.
- Loss of any of our key personnel, or our failure to attract, assimilate and retain other highly qualified personnel.
- Intellectual property infringement or misappropriation claims by third parties against us or our customers, including our distributor customers.
- The failure of LEDs to achieve widespread adoption in the general lighting market, or if alternative technologies gain market acceptance.
- The loss of key suppliers or contract manufacturers.
- Our ability to effectively expand or upgrade our production facilities or do so in a timely or cost-effective manner.
- Difficulty in managing our future growth or in responding to a need to contract operations, and the associated changes to our operations.

- Adverse development in those selected markets, including the Netherlands, Taiwan, the United States and China, where our revenues are concentrated.
- Our ability to develop and execute upon a new strategy to exploit the China and India market.

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- The reduction or elimination of government investment in LED lighting or the elimination of, or changes in, policies in certain countries that encourage the use of LEDs over some traditional lighting technologies.
- Our ability to implement our product innovation strategy effectively, particularly in view of the prohibition against our (and/or our assisting others in) making, using, importing, selling and/or offering to sell in the United States our accused products and/or any device that includes an accused product after October 1, 2012 as a result of the injunction agreed to in connection with the Cree Inc., or Cree, litigation.
- Loss of customers.
- Failure of our strategy of marketing and selling our products in jurisdictions with limited intellectual property enforcement regimes.
- Lack of marketing and distribution success by our third-party distributors.
- Our customers' ability to produce and sell products incorporating our LED products.
- Our failure to adequately prevent disclosure of trade secrets and other proprietary information.
- Ineffectiveness of our disclosure controls and procedures and our internal control over financial reporting.
- Our ability to profit from existing and future joint ventures, investments, acquisitions and other strategic alliances.
- Impairment of long-lived assets or investments.
- Undetected defects in our products that harm our sales and reputation and adversely affect our manufacturing yields.
- The availability of adequate and timely supply of electricity and water for our manufacturing facilities.
- Our ability to comply with existing and future environmental laws and the cost of such compliance.
- The ability of SemiLEDs Optoelectronics Co., Ltd., or Taiwan SemiLEDs, to make dividends and other payments to SemiLEDs Corporation.
- Our ability to obtain necessary regulatory approvals to make further investments in Taiwan SemiLEDs.
- Our ability to appoint a new independent director to regain compliance with the Nasdaq continued listing requirements necessary to avert delisting of our common stock.
- Catastrophic events such as fires, earthquakes, floods, tornados, tsunamis, typhoons, pandemics, wars, terrorist activities and other similar events, particularly if these events occur at or near our operations, or the operations of our suppliers, contract manufacturers and customers.
- The effect of the legal system in the People's Republic of China, or the PRC.
- Labor shortages, strikes and other disturbances that affect our operations.
- Deterioration in the relations between the PRC and Taiwan governments.
- Fluctuations in the exchange rate among the U.S. dollar, the New Taiwan, or NT, dollar, the Japanese Yen and other currencies in which our sales, raw materials and component purchases and capital expenditures are denominated.
- The effect of the disclosure requirements under the provisions of the Dodd-Frank Act relating to "conflict minerals," which could increase our costs and limit the supply of certain metals used in our products and affect our reputation with customers and shareholders.

Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. We have not assumed any obligation to, and you should not expect us to, update or revise these statements because of new information, future events or otherwise.

For more information on the significant risks that could affect the outcome of these forward-looking statements, see Item 1A "Risk Factors" in Part I of our Annual Report on Form 10-K for the fiscal year ended August 31, 2018, or the 2018 Annual Report, and those contained in Part II, Item 1A of this Quarterly Report, and other information provided from time to time in our filings with the Securities and Exchange Commission, or the SEC.

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The following discussion and analysis of our financial condition and results of operations is based upon and should be read in conjunction with the unaudited interim condensed consolidated financial statements and the notes and other information included elsewhere in this Quarterly Report, in our 2018 Annual Report, and in other filings with the SEC.

Company Overview

We develop, manufacture and sell light emitting diode (LED) chips and LED components. Our products are used for general lighting applications, including street lights and commercial, industrial, system and residential lighting. Our LED chips may also be used in specialty industrial applications, such as ultraviolet, or UV, curing of polymers, LED light therapy in medical/cosmetic applications, counterfeit detection, LED lighting for horticulture applications, architectural lighting and entertainment lighting.

Utilizing our patented and proprietary technology, our manufacturing process begins by growing upon the surface of a sapphire wafer, or substrate, several very thin separate semiconductive crystalline layers of gallium nitride, or GaN, a process known as epitaxial growth, on top of which a mirror-like reflective silver layer is then deposited. After the subsequent addition of a copper alloy layer and finally the removal of the sapphire substrate, we further process this multiple-layered material to create individual vertical LED chips.

We package our LED chips into LED components, which we sell to distributors and a customer base that is heavily concentrated in a few select markets, including Taiwan, the United States and China (including Hong Kong). We also sell our “Enhanced Vertical,” or EV, LED product series in blue, white, green and UV in selected markets. We sell our LED chips to packagers or to distributors, who in turn sell to packagers. Our lighting products customers are primarily original design manufacturers, or ODMs, of lighting products and the end users of lighting devices. We also contract other manufacturers to produce for our sale certain LED products, and for certain aspects of our product fabrication, assembly and packaging processes, based on our design and technology requirements and under our quality control specifications and final inspection process.

We have developed advanced capabilities and proprietary know-how in:

- reusing sapphire substrate in subsequent production runs;
- optimizing our epitaxial growth processes to create layers that efficiently convert electrical current into light;
- employing a copper alloy base manufacturing technology to improve our chip’s thermal and electrical performance;
- utilizing nanoscale surface engineering to improve usable light extraction;
- developing a LED structure that generally consists of multiple epitaxial layers which are vertically-stacked on top of a copper alloy base; and
- developing low cost Chip Scaled Packaging (CSP) technology.

These technical capabilities enable us to produce LED chips and LED component products. We believe these capabilities, know-how and partnership should also allow us to reduce our manufacturing costs and our dependence on sapphire, a costly raw material used in the production of sapphire-based LED devices.

We were incorporated in the State of Delaware on January 4, 2005 and sold our first LED chips in November 2005. We are a holding company for various wholly and majority owned subsidiaries. SemiLEDs Optoelectronics Co., Ltd., or Taiwan SemiLEDs, is our wholly owned operating subsidiary, where a substantial portion of our assets are held and located, where a portion of our research, development, manufacturing and sales activities take place. Taiwan SemiLEDs owns a 97% equity interest in Taiwan Bandaoti Zhaoming Co., Ltd., formerly known as Silicon Base Development, Inc., which is engaged in the research, development, manufacture, and substantial portion of marketing and sale of LED products, and where most of our employees are based.

Key Factors Affecting Our Financial Condition, Results of Operations and Business

The following are key factors that we believe affect our financial condition, results of operations and business:

- Our ability to raise additional debt, sell additional equity securities and improve our liquidity. We may need to improve our liquidity, access alternative sources of funding and obtain additional equity capital or credit when necessary for our operations. However, we may not be able to obtain such debt funding or sell equity securities on terms that are favorable to us, or at all. The raising of additional debt funding by us, if required and available, would result in increased debt service obligations and could result in additional operating and financing covenants, or liens on our assets, that would restrict our operations. The sale of additional equity securities, if required and available, could result in dilution to our stockholders.

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- Our ability to get chips from other chip suppliers. Our reliance on our chip suppliers exposes us to a number of significant risks, including reduced control over delivery schedules, quality assurance and production costs, lack of guaranteed production capacity or product supply. If our chip suppliers are unable or unwilling to continue to supply our chips at requested quality, quantity, performance and costs, or in a timely manner, our business and reputation could be seriously harmed. Our inability to procure chips from other chip suppliers at the desired quality, quantity, performance and cost might result in unforeseen manufacturing and operations problems. In such events, our customer relationships, business, financial condition and results of operations would be adversely affected.
- Industry growth and demand for products and applications using LEDs. The overall adoption of LED lighting devices to replace traditional lighting sources is expected to influence the growth and demand for LED chips and component products and impact our financial performance. We believe the potential market for LED lighting will continue to expand. LEDs for efficient generation of UV light are also starting to gain attention for various medical, germicidal and industrial applications. Since a substantial portion of our LED chips, LED components and our lighting products are used by end- users in general lighting applications and specialty industrial applications such as UV curing, medical/cosmetic, counterfeit detection, horticulture, architectural lighting and entertainment lighting the adoption of LEDs into these applications will have a strong impact on the demand of LED chips generally and, as a result, for our LED chips, LED components and LED lighting products.
- Average selling price of our products. The average selling price of our products may decline for a variety of factors, including prices charged by our competitors, the efficacy of our products, our cost basis, changes in our product mix, the size of the order and our relationship with the relevant customer, as well as general market and economic conditions. Competition in the markets for LED products is intense, and we expect that competition will continue to increase, thereby creating a highly aggressive pricing environment. For example, some of our competitors have in the past reduced their average selling prices, and the resulting competitive pricing pressures have caused us to similarly reduce our prices, accelerating the decline in our revenues and the gross margin of our products. When prices decline, we must also write down the value of our inventory. Furthermore, the average selling prices for our LED products have typically decreased over product life cycles. Therefore, our ability to continue to innovate and offer competitive products that meet our customers’ specifications and pricing requirements, such as higher efficacy LED products at lower costs, will have a material influence on our ability to improve our revenues and product margins, although in the near term the introduction of such higher performance LED products may further reduce the selling prices of our existing products or render them obsolete.
- Changes in our product mix. We anticipate that our gross margins will continue to fluctuate from period to period as a result of the mix of products that we sell and the utilization of our manufacturing capacity in any given period, among other things. For example, we continue to pursue opportunities for profitable growth in areas of our business where we see the best opportunity to develop as an end-to-end LED module solution supplier by providing our customers with high quality, flexible and more complete LED system solution, customer technical support and LED module/system design, as opposed to just providing customers with individual components. As a strategic plan, we have placed greater emphasis on the sales of LED components rather than the sales of LED chips where we have been forced to cut prices on older inventory. Steady growth of the module product and the continued commercial sales of our UV LED product are expected to improve our gross margin, operating results and cash flows. In addition, we have adjusted the lower-priced LED components strategy as appropriate. We have adopted a strategy to adjust our product mix by exiting certain high volume but low unit selling price product lines in response to the general trend of lower average selling prices for products that have been available in the market for some time. However, as we expand and diversify our product offerings and with varying average selling prices, or execute new business initiatives, a change in the mix of products that we sell in any given period may increase volatility in our revenues and gross margin from period to period.
- Our ability to reduce cost to offset lower average selling prices. Competitors may reduce average selling prices faster than our ability to reduce costs, and competitive pricing pressures may accelerate the rate of decline of our average selling prices. To address increased pricing pressure, we have improved and increased our production yields

to reduce the per-unit cost of production of our products. However, such cost savings currently have limited impact on our gross profit, as we currently suffer from the underutilization of manufacturing capacity and must absorb a high level of fixed costs, such as depreciation. While we intend to focus on managing our costs and expenses, over the long term we expect to be required to invest substantially in LED component products development and production equipment if we are to grow.

- Our ability to continue to innovate. As part of our growth strategy, we plan to continue to be innovative in product design, to deliver new products and to improve our manufacturing efficiencies. Our continued success depends on our ability to develop and introduce new, technologically advanced and lower cost products, such as more efficient, better performance LED component products. If we are unable to introduce new products that are commercially viable and meet rapidly evolving customer requirements or keep pace with evolving technological standards and market developments or

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are otherwise unable to execute our product innovation strategy effectively, we may not be able to take advantage of market opportunities as they arise, execute our business plan or be able to compete effectively. To differentiate ourselves from other LED package manufacturers, we are putting more resources towards module and system design. Along with our technical know-how in the chip and package sectors, we are able to further integrate electrical, thermal and mechanical manufacturing resources to provide customers with one-stop system services. Services include design, prototyping, OEM and ODM. Key markets that we intend to target at the system end include different types of UV LED industrial printers, aquarium lighting, medical applications, niche imaging light engines, horticultural lighting and high standard commercial lighting. The modules are designed for various printing, curing, and PCB exposure industrial equipments, providing uncompromised reliability and optical output. Our LED components include different sizes and wattage to accommodate different demands in the LED market.

- General economic conditions and geographic concentration. Many countries including the United States and the European Union (the “E.U.”) members have instituted, or have announced plans to institute, government regulations and programs designed to encourage or mandate increased energy efficiency in lighting. These actions include in certain cases banning the sale after specified dates of certain forms of incandescent lighting, which are advancing the adoption of more energy efficient lighting solutions such as LEDs. When the global economy slows or a financial crisis occurs, consumer and government confidence declines, with levels of government grants and subsidies for LED adoption and consumer spending likely to be adversely impacted. Our revenues have been concentrated in a few select markets, including the Netherlands, Taiwan, the United States and China (including Hong Kong). Given that we are operating in a rapidly changing industry, our sales in specific markets may fluctuate from quarter to quarter. Therefore, our financial results will be impacted by general economic and political conditions in such markets. For example, the aggressive support by the Chinese government for the LED industry through significant government incentives and subsidies to encourage the use of LED lighting and to establish the LED sector companies has resulted in production overcapacity in the market and intense competition. Furthermore, due to Chinese package manufacturers increasing usage of domestic LED chips, prices are increasingly competitive, leading to Chinese manufacturers growing market share in the global LED industry. In addition, we have historically derived a significant portion of our revenues from a limited number of customers. Some of our largest customers and what we produce/have produced for them have changed from quarter to quarter primarily as a result of the timing of discrete, large project based purchases and broadening customer base, among other things. For the three and the six months ended February 28, 2019, sales to our three largest customers, in the aggregate, accounted for 64% and 52% of our revenues, respectively.
- Intellectual property issues. Competitors of ours and other third parties have in the past and will likely from time to time in the future allege that our products infringe on their intellectual property rights. Defending against any intellectual property infringement claims would likely result in costly litigation and ultimately may lead to our not being able to manufacture, use or sell products found to be infringing. In June 2012, we settled an intellectual property dispute involving Cree. We agreed to dismiss amended complaints filed against each other without prejudice. We agreed to the entry of a permanent injunction that was effective October 1, 2012 that precludes us from (and/or from assisting others in) making, using, importing, selling and/or offering to sell in the United States certain accused products and/or any device that includes such an accused product after that date and to payment of a settlement fee for past damages. All remaining claims between Cree and us were withdrawn without prejudice, with each retaining the right to assert them in the future. However, other third parties may also assert infringement claims against our customers with respect to our products, or our customers’ products that incorporate our technologies or products. Any such legal action or the threat of legal action against us, or our customers, could impair such customers’ continued demand for our products. This could prevent us from growing or even maintaining our revenues, or cause us to incur additional costs and expenses, and adversely affect our financial condition and results of operations.
- Cash position. Our cash and cash equivalents decreased to $1.6 million as of February 28, 2019 primarily due to the combination of our net cash used in operating activities offset by proceeds from long-term debt. We have implemented actions to accelerate operating cost reductions and improve operational efficiencies. The plan is further

enhanced through the fabless business model in which we implemented certain workforce reductions and are exploring the opportunities to sell certain equipment related to the manufacturing of vertical LED chips, in order to reduce the idle capacity charges, minimize our research and development activities associated with chips manufacturing operation. We believe we will be able to generate positive cash inflows through the restructuring of our chip operation and the significant ongoing cost savings in the form of reduced payroll and research and development activities. The shipment of our new module product and the continued commercial sales of our UV LED product are expected to grow steadily. Based on our current financial projections, we believe that we will have sufficient sources of liquidity to fund our operations and capital expenditure plans for the next 12 months. Please see "Critical Accounting Policies and Estimates" for more information about our liquidity plans.

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Critical Accounting Policies and Estimates

Effective September 1, 2018, we adopted ACS 606 using the modified retrospective transition method. Under this approach, we apply the new standards to all new contracts initiated on and after September 1 2018, and, for contracts which have remaining obligations as of September 1 2018, we recognized no adjustment to the opening balance of our retained earnings account.

On September 1, 2018, we adopted ASC 825-10, “Financial Instruments- Overall: Recognition and Measurement of Financial Assets and Financial Liabilities”. This standard allows equity investments that do not have readily determinable fair values to be re-measured at fair value either upon the occurrence of an observable price change or upon identification of impairment. The standard also simplifies the impairment assessment of equity investments without readily determinable fair values by requiring assessment for impairment qualitatively at each reporting period. There was no material impact on our consolidated financial position, results of operations or cash flows due to the adoption.

Effective September 1, 2018, we adopted ASU No. 2017-09, “Compensation- Stock Compensation: Scope of Modification Accounting”. The guidance provides clarity and reduces diversity in practice and cost and complexity when accounting for a change to the terms or conditions of a share-based payment award. Adoption of this standard did not have a material impact on our consolidated financial position, results of operations or cash flows.

Except as described above, there have been no material changes in the matters for which we make critical accounting policies and estimates in the preparation of our unaudited interim condensed consolidated financial statements for the six months ended February 28, 2019 as compared to those disclosed in our 2018 Annual Report.

Exchange Rate Information

We are a Delaware corporation and, under SEC requirements, must report our financial position, results of operations and cash flows in accordance with accounting principles generally accepted in the United States of America, or U.S. GAAP. At the same time, our subsidiaries use the local currency as their functional currency. For example, the functional currency for Taiwan SemiLEDs is the NT dollar. The assets and liabilities of the subsidiaries are, therefore, translated into U.S. dollars at exchange rates in effect at each balance sheet date, and income and expense accounts are translated at average exchange rates during the period. The resulting translation adjustments are recorded to a separate component of accumulated other comprehensive income (loss) within equity. Any gains and losses from transactions denominated in currencies other than their functional currencies are recognized in the consolidated statements of operations as a separate component of other income (expense). Due to exchange rate fluctuations, such translated amounts may vary from quarter to quarter even in circumstances where such amounts have not materially changed when denominated in their functional currencies.

The translations from NT dollars to U.S. dollars were made at the exchange rates as set forth in the statistical release of the Bank of Taiwan. On February 28, 2019, the exchange rate was 30.77 NT dollars to one U.S. dollar. On April 8, 2019, the exchange rate was 30.84 NT dollars to one U.S. dollar.

No representation is made that the NT dollar or U.S. dollar amounts referred to herein could have been or could be converted into U.S. dollars or NT dollars, as the case may be, at any particular rate or at all.

Results of Operations

Three Months Ended February 28, 2019 Compared to the Three Months Ended February 28, 2018

	Three Months Ended February 28, 2019		February 28, 2018			
	$	% of Revenues	$	% of Revenues	Change $	Change %
	(in thousands)					
LED chips	$15	1 %	$74	5 %	$ (59)	(80)%
LED components	1,438	88 %	941	61 %	497	53 %
Lighting products	141	9 %	290	19 %	(149)	(51)%
Other revenues[1]	36	2 %	238	15 %	(202)	(85)%
Total revenues, net	1,630	100 %	1,543	100 %	87	6 %
Cost of revenues	1,628	100 %	1,987	129 %	(359)	(18)%
Gross profit (loss)	$2	— %	$(444)	(29)%	$ 446	(100)%

(1) Other includes primarily revenues attributable to the sale of epitaxial wafers, scraps and raw materials and the provision of services.

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Revenues, net

Our revenues increased by 6% to $1.6 million for the three months ended February 28, 2019 from $1.5 million for the three months ended February 28, 2018. The increase in revenues was driven primarily by a $497 thousand increase in sales of LED components offset in part by a $202 thousand decrease in other revenue and by a $149 decrease in lighting products.

Revenues attributable to the sales of our LED chips were $15 thousand and $74 thousand, representing 1% and 5%, respectively, of our revenues for the three months ended February 28, 2019 and 2018, primarily due to lower volume sold for the LED chips. We have adopted a strategy to adjust our product mix by exiting certain high volume but low unit selling price product lines in response to the general trend of lower average selling prices for products that have been available in the market for some time and to focus on profitable products.

Revenues attributable to the sales of our LED components represented 88% and 61% of our revenues for the three months ended February 28, 2019 and 2018, respectively. The increase in revenues attributable to sales of LED components was primarily due to a higher average selling price for the UV LED product, which we particularly focus on within the niche LED markets, offset in part by a lower volume sold. We have adopted a strategy to adjust our product mix by exiting certain high volume but low unit selling price product lines as more fully mentioned above.

Revenues attributable to the sales of lighting products represented 9% and 19% of our revenues for the three months ended February 28, 2019 and 2018, respectively. Revenues attributable to the sales of lighting products were slightly lower for the three months ended February 28, 2019 primarily due to lower volumes sold.

Cost of Revenues

Our cost of revenues decreased by 18% from $2.0 million for the three months ended February 28, 2018 to $1.6 million for the three months ended February 28, 2019. The decrease in cost of revenues was primarily due to the effect of our ongoing cost reduction efforts, a decrease in volume sold and decreases in depreciation expenses and idle capacity charges associated with property, plant and equipment.

Gross Profit (Loss)

Our gross profit increased from a loss of $444 thousand for the three months ended February 28, 2018 to a profit of $2 thousand for the three months ended February 28, 2019. Our gross margin percentage increased from negative 29% to breakeven for the three months ended February 28, 2019 as a consequence of the reduction in cost of revenues as more fully described above.

Operating Expenses

	Three Months Ended					
	February 28, 2019		February 28, 2018			
	$	% of Revenues	$	% of Revenues	Change $	Change %
	(in thousands)					

Research and development	$298	19	%	$223	15	%	$ 75		34		%
Selling, general and administrative	619	38	%	781	51	%	(162	)	(21	)	%
Gain on disposals of long-lived assets, net	—	—	%	(209)	(14	)%	209		(100	)	%
Total operating expenses	$917	56	%	$795	52	%	$ 122		15		%

Research and development Our research and development expenses were $298 thousand and $223 thousand for the three months ended February 28, 2019 and 2018, respectively. The increase was primary due to a $77 thousand increase in payroll and compensation and a $31 increase in materials and supplies used for our new products.

Selling, general and administrative Our selling, general and administrative expenses decreased from $781 thousand for the three months ended February 28, 2018 to $619 thousand for the three months ended February 28, 2019. The decrease was mainly attributable to a $92 thousand decrease in payroll and stock based compensation and a $28 thousand decrease in Delaware Franchise tax due to a reversal of an accrual.

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Loss on disposal of long-lived assets, net Due to the excess capacity charges that we have suffered for a few years, considering the risk of technological obsolescence and according to the production plan built based on our sales forecast, we disposed of certain of our idle equipment and a gain of $209 thousand was recognized as a result for the three months ended February 28, 2018.

Other Income (Expenses)

	Three Months Ended			
	February 28, 2019		February 28, 2018	
	$	% of Revenues	$	% of Revenues
	(in thousands)			
Interest expenses, net	$(36)	(2)%	$(7)	— %
Other income (expenses), net	(126)	(8)%	49	3 %
Foreign currency transaction gain, net	233	14 %	65	4 %
Total other income (expenses), net	$71	4 %	$107	7 %

Interest expenses, net. The increase in interest expenses, net was primarily due to the increase in debt balance, resulting from our entry into loan agreements on January 8, 2019 with each of our Chairman and Chief Executive Officer and our largest shareholder, with aggregate amounts of $3.2 million, and an annual interest rate of 8%.

Other income (expenses), net Other income (expenses), net decreased from an income of $49 thousand for the three months ended February 28, 2018 to an expense of $126 thousand for the three months ended February 28, 2019, primarily due to the settlement of the lawsuit with Epistar in the three months ended February 28, 2019.

Foreign currency transaction gain, net We recognized a net foreign currency transaction gain of $233 thousand and $65 thousand for the three months ended February 28, 2019 and 2018, respectively, primarily due to the depreciation of the U.S. dollar against the NT dollar from bank deposits and accounts receivables.

Income Tax Expense

Our effective tax rate is expected to be approximately zero for fiscal 2019 and was zero for fiscal 2018, since Taiwan SemiLEDs incurred losses, and because we provided a full valuation allowance on all deferred tax assets, which consisted primarily of net operating loss carryforwards and foreign investment loss.

On December 22, 2017, the U.S. Tax Cuts and Jobs Act was adopted, which among other effects, reduced the U.S. federal corporate income tax rate to 21% from 34% (or 35% in certain cases) beginning in 2018, requires companies to pay a one-time transition tax on certain unrepatriated earnings from non-U.S. subsidiaries that is payable over eight years, makes the receipt of future non-U.S. sourced income of non-U.S. subsidiaries tax-free to U.S. companies and creates a new minimum tax on the earnings of non-U.S. subsidiaries relating to the parent’s deductions for payments to the subsidiaries.

Net Gain Attributable to Noncontrolling Interests

	Three Months Ended			
	February 28, 2019		February 28, 2018	
	$	% of Revenues	$	% of Revenues
	(in thousands)			
Net gain attributable to noncontrolling interests	$3	— %	$ —	— %

We recognized net gain attributable to non-controlling interests of $3 thousand for the three months ended February 28, 2019, which was attributable to the share of the net losses of Taiwan Bandaoti Zhaoming Co., Ltd held by the remaining non-controlling holders. As of February 28, 2019, non-controlling interests represented 3.29% equity interest in Taiwan Bandaoti Zhaoming CO., Ltd.

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Six Months Ended February 28, 2019 Compared to the Six Months Ended February 28, 2018

	Six Months Ended February 28, 2019		February 28, 2018		Change	Change
	$	% of Revenues	$	% of Revenues	$	%
	(in thousands)					
LED chips	$84	3 %	$150	4 %	$(66)	(44)%
LED components	2,117	82 %	2,352	66 %	(235)	(10)%
Lighting products	314	12 %	556	16 %	(242)	(44)%
Other revenues[1]	87	3 %	488	14 %	(401)	(82)%
Total revenues, net	2,602	100 %	3,546	100 %	(944)	(27)%
Cost of revenues	2,819	108 %	3,938	111 %	(1,119)	(28)%
Gross profit (loss)	$(217)	(8)%	$(392)	(11)%	$175	(45)%

(1) Other includes primarily revenues attributable to the sale of epitaxial wafers, scraps and raw materials and the provision of services.

Revenues, net

Our revenues decreased by 27% from $3.5 million for the six months ended February 28, 2018 to $2.6 million for the six months ended February 28, 2019. The $944 thousand decrease in revenues reflects a $66 thousand decrease in revenues attributable to sales of LED chips, a $235 thousand decrease in sales of LED components, a $242 thousand decrease in revenues attributable to sales of lighting products, and a $401 thousand decrease in revenues attributable to other revenues.

Revenues attributable to the sales of our LED chips represented 3% and 4% of our revenues for the six months ended February 28, 2019 and 2018, respectively. The decrease of 44% in revenues attributable to sales of LED chips was a result of a decrease in the volume of LED chips sold, offset slightly by a higher average selling price, primarily due to our strategic plan to place greater emphasis on the sales of LED components rather than the sales of LED chips.

Revenues attributable to the sales of our LED components represented 82% and 66% of our revenues for the six months ended February 28, 2019 and 2018, respectively. The decrease in revenues attributable to sales of LED components was primarily due to lower volumes sold for the UV LED product, which we particularly focus on within the niche LED markets.

Revenues attributable to the sales of lighting products represented 12% and 16% of our revenues for the six months ended February 28, 2019 and 2018, respectively. Revenues attributable to the sales of lighting products was $242 thousand lower for the six months ended February 28, 2019 primarily due to a slowdown in demand on LED luminaries and retrofits and fewer non-recurring project-based orders for LED lighting products compared to the six months ended February 28, 2018.

Cost of Revenues

Our cost of revenues decreased by 28% from $3.9 million for the six months ended February 28, 2018 to $2.8 million for the six months ended February 28, 2019. The decrease in cost of revenues was primarily due to the effect of our ongoing cost reduction efforts, a decrease in volume sold and decreases in depreciation expenses and idle capacity charges associated with property, plant and equipment.

Gross Profit (Loss)

Our gross loss decreased from a loss of $392 thousand for the six months ended February 28, 2018 to $217 thousand for the six months ended February 28, 2019. Our gross margin percentage was negative 8% for the six months ended February 28, 2019, as compared to negative 11% for the six months ended February 28, 2018 as a consequence of the reduction in cost of revenues as more fully described above.

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Operating Expenses

	Six Months Ended February 28, 2019		February 28, 2018		Change	Change
	$	% of Revenues	$	% of Revenues	$	%
	(in thousands)					
Research and development	$632	24 %	$407	11 %	$ 225	55 %
Selling, general and administrative	1,376	53 %	1,514	43 %	(138)	(9)%
Gain on disposals of long-lived assets, net	(288)	(11)%	(209)	(6)%	(79)	38 %
Total operating expenses	$1,720	66 %	$1,712	48 %	$ 8	— %

Research and development Our research and development expenses were $632 thousand and $407 thousand for the six months ended February 28, 2019 and 2018, respectively. The increase was primary due to a $143 thousand increase in payroll and compensation and an $80 increase in materials and supplies used for our new products, offset by a decrease in depreciation and amortization expense.

Selling, general and administrative Our selling, general and administrative expenses decreased from $1.5 million for the six months ended February 28, 2018 to $1.4 million for the six months ended February 28, 2019. The decrease was mainly attributable to a decrease in payroll, and decreases in various other expenses.

Gain on disposal of long-lived assets, net

We recognized a net gain of $288 thousand and $209 thousand on the disposal of long-lived assets for the six months ended February 28, 2019 and 2018, respectively. Due to the excess capacity charges that we have experienced for the last few years, considering the risk of technological obsolescence and according to the production plan built based on our sales forecast, we disposed of certain of our idle equipment.

Other Income (Expenses)

	Six Months Ended February 28, 2019		February 28, 2018	
	$	% of Revenues	$	% of Revenues
	(in thousands)			
Interest expenses, net	$(41)	(2)%	$(15)	— %
Other income (expenses), net	(46)	(2)%	547	15 %
Foreign currency transaction gain, net	197	8 %	48	1 %
Total other income (expenses), net	$110	4 %	$580	16 %

Interest expenses, net The increase in interest expenses, net was primarily due to the increase in debt balance, resulting from our entry into loan agreements on January 8, 2019 with each of our Chairman and Chief Executive

Officer and our largest shareholder, with aggregate amounts of $3.2 million, and an annual interest rate of 8%.

Other income (expenses), net Other income for the six months ended February 28, 2018 primarily consists of sales of patents offset by their commission expense and cost. Other expenses for the six months ended February 28, 2019 primarily due to the settlement of a lawsuit with Epistar.

Foreign currency transaction gain, net We recognized net foreign currency transaction gain of $197 thousand and $48 thousand for the six months ended February 28, 2019 and 2018, respectively, primarily due to the depreciation of the U.S. dollar against the NT dollar from bank deposits and accounts receivables held by Taiwan SemiLEDs and Taiwan Bandaoti Zhaoming Co., Ltd. in currency other than the functional currency of such subsidiaries.

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Income Tax Expense

Our effective tax rate is expected to be approximately zero for fiscal 2019 and was zero for fiscal 2018, since Taiwan SemiLEDs incurred losses, and because we provided a full valuation allowance on all deferred tax assets, which consisted primarily of net operating loss carryforwards and foreign investment loss.

On December 22, 2017, the U.S. Tax Cuts and Jobs Act was adopted, which among other effects, reduced the U.S. federal corporate income tax rate to 21% from 34% (or 35% in certain cases) beginning in 2018, requires companies to pay a one-time transition tax on certain unrepatriated earnings from non-U.S. subsidiaries that is payable over eight years, makes the receipt of future non-U.S. sourced income of non-U.S. subsidiaries tax-free to U.S. companies and creates a new minimum tax on the earnings of non-U.S. subsidiaries relating to the parent's deductions for payments to the subsidiaries.

Net Loss Attributable to Noncontrolling Interests

	Six Months Ended			
	February 28, 2019		February 28, 2018	
	$	% of Revenues	$	% of Revenues
	(in thousands)			
Net loss attributable to noncontrolling interests	$(2)	—%	$ —	—

We recognized net loss attributable to non-controlling interests of $2 thousand for the six months ended February 28, 2019, which was attributable to the share of the net losses of Taiwan Bandaoti Zhaoming Co., Ltd held by the remaining non-controlling holders. As of February 28, 2019, non-controlling interests represented 3.29% equity interest in Taiwan Bandaoti Zhaoming CO., Ltd.

Liquidity and Capital Resources

As of February 28, 2019 and August 31, 2018, we had cash and cash equivalents of $1.6 million and $3.4 million, respectively, which were predominately held in U.S. dollar denominated demand deposits and/or money market funds.

As of April 8, 2019, we had no available credit facility.

Our long-term debt, which consisted of NT dollar denominated long-term notes and loans from our Chairman and our largest shareholder, totaled $5.4 million and $2.3 million as of February 28, 2019 and August 31, 2018, respectively.

Our NT dollar denominated long-term notes, totaled $2.2 million and $2.3 million as of February 28, 2019 and August 31, 2018, respectively. These long-term notes carry an interest rate of 1.62%, based on the annual time deposit rate plus a specific spread, as of both February 28, 2019 and August 31, 2018, are payable in monthly installments, and are secured by our property, plant and equipment. These long-term notes do not have prepayment penalties or balloon payments upon maturity.

- The first note payable requires monthly payments of principal and interest in the amount of $13 thousand over the 15-year term of the note with final payment to occur in May 2024 and, as of February 28, 2019, our outstanding balance on this note payable was approximately $787 thousand.
- The second note payable requires monthly payments of principal and interest in the amount of $18 thousand over the 15-year term of the note with final payment to occur in December 2025 and, as of February 28, 2019, our outstanding balance on this note payable was approximately $1.4 million.

Property, plant and equipment pledged as collateral for our notes payable were $4.0 million and $4.2 million as of February 28, 2019 and August 31, 2018, respectively.

On January 8, 2019, we entered into loan agreements with each of our Chairman and Chief Executive Officer and our largest shareholder, with aggregate amounts of $3.2 million, and an annual interest rate of 8%. All proceeds of the loans were exclusively used to return the deposit to Formosa Epitaxy Incorporation in connection with the proposed sale of our headquarters building pursuant to the agreement dated December 15, 2015. We are required to repay the loans of $1.5 million on January 14, 2021 and $1.7 million on January 22, 2021, respectively, unless the loans are sooner accelerated pursuant to the loan agreements. As of February 28, 2019, these loans totaled $3.2 million. The Loans are secured by a second priority security interest on our headquarters building.

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We have incurred significant losses since inception, including net losses attributable to SemiLEDs stockholders of $3.0 million and $4.1 million during the years ended August 31, 2018 and 2017, respectively. Net cash used in operating activities for the year ended August 31, 2018 was $1.2 million. As of August 31, 2018, we had cash and cash equivalents of $3.4 million. We have undertaken actions to decrease losses incurred and implemented cost reduction programs in an effort to transform the Company into a profitable operation.

Based on our current financial projections and assuming the successful implementation of our liquidity plans, we believe that we will have sufficient sources of liquidity to fund our operations and capital expenditure plans for the next 12 months. However, there can be no assurances that our planned activities will be successful in reducing losses and preserving cash. If we are not able to generate positive cash flows from operations, we may need to consider alternative financing sources and seek additional funds through public or private equity financings or from other sources, or refinance our indebtedness, to support our working capital requirements or for other purposes. There can be no assurance that additional debt or equity financing will be available to us or that, if available, such financing will be available on terms favorable to us. Please see "Critical Accounting Policies and Estimates" for more information on our liquidity plans.

Cash Flows

The following summary of our cash flows for the periods indicated has been derived from our unaudited interim condensed consolidated financial statements, which are included elsewhere in this Quarterly Report (in thousands):

	Six Months Ended	
	February 28, 2019	February 28, 2018
Net cash provided by (used in) operating activities	$(1,978)	$ 162
Net cash provided by (used in) investing activities	$(2,554)	$ 196
Net cash provided by (used in) financing activities	$3,032	$ (173)

Cash Flows Provided by (Used In) Operating Activities

Net cash used in operating activities for the six months ended February 28, 2019 was $2.0 million while net cash provided by operating activities for the six months ended February 28, 2018 was $162 thousand. Cash flows used in operating activities for the six months ended February 28, 2019 was $2.1 million more, primary attributable to and a decrease of $1.3 million in cash collected from customers and an increase in inventory.

Cash Flows Provided by (Used In) Investing Activities

Net cash used by investing activities for the six months ended February 28, 2019 was $2.6 million, consisting primarily of the return of $3 million to Epistar and $64 thousand of purchases of machinery and equipment, offset in part by $512 thousand of proceeds from the sales of machinery and equipment.

Net cash provided by investing activities for the six months ended February 28, 2018 was $196 thousand, consisting primarily of $327 thousand of proceeds from the sales of machinery and equipment, offset in part by the purchases of machinery and equipment.

Cash Flows Provided by (Used In) Financing Activities

Net cash provided by financing activities for the six months ended February 28, 2019 was $3 million, consisting primarily of $3.2 million of proceeds from Chairman and shareholder loans, offset in part by the repayments on long-term notes.

Net cash used in financing activities for the six months ended February 28, 2018 was $173 thousand, primarily attributable to the repayments on long-term debt.

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Capital Expenditures

We had capital expenditures of $64 thousand and $131 thousand for the six months ended February 28, 2019 and 2018, respectively. Our capital expenditures consisted primarily of the purchases of machinery and equipment, construction in progress, prepayments for our manufacturing facilities and prepayments for equipment purchases. We expect to continue investing in capital expenditures in the future as we expand our business operations and invest in such expansion of our production capacity as we deem appropriate under market conditions and customer demand. However, in response to controlling capital costs and maintaining financial flexibility, our management continues to monitor prices and, consistent with its existing contractual commitments, may decrease further its activity level and capital expenditures as appropriate.

Off-Balance Sheet Arrangements

As of February 28, 2019, we did not engage in any off-balance sheet arrangements. We do not have any interests in variable interest entities.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Not applicable.

Item 4. Controls and Procedures

Evaluation of disclosure controls and procedures

Our management, with the participation of our chief executive officer, or CEO, and our chief financial officer, or CFO, has evaluated the effectiveness of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, as of February 28, 2019. In designing and evaluating the disclosure controls and procedures, 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. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints and that management is required to apply its judgment in evaluating the benefits of possible controls and procedures relative to their costs.

Based upon the aforementioned evaluation, our CEO and CFO have concluded that, as of February 28, 2019, our disclosure controls and procedures are designed at a reasonable assurance level and are effective to provide reasonable assurance that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC rules and forms and that such information is accumulated and communicated to our management, including our CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

Changes in internal control over financial reporting

There were no changes in our internal control over financial reporting that occurred during the quarter ended February 28, 2019 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II — OTHER INFORMATION

Item 1. Legal Proceedings

Due to the complex technology required to compete successfully in the LED industry, participants in our industry are often engaged in significant intellectual property licensing arrangements, negotiations, disputes and litigation. We are directly or indirectly involved from time to time and may be named in various other claims or legal proceedings arising in the ordinary course of our business or otherwise.

On June 21, 2017, Well Thrive Ltd. ("Well Thrive") filed a complaint against SemiLEDs Corporation in the United States District Court for the District of Delaware. The complaint alleges that Well Thrive was entitled to return of $500 thousand paid toward a note purchase pursuant to a purchase agreement (the "Purchase Agreement") effective July 6, 2016 with Dr. Peter Chiou, which was assigned to Well Thrive on August 4, 2016. Pursuant to the terms of the Purchase Agreement, we retained the $500 thousand payment as liquidated damages. Well Thrive alleged that the liquidated damages provision was unenforceable as an illegal penalty and did not reflect the amount of purported damages. On March 13, 2018, we filed a motion to enforce a settlement agreement between the parties to dismiss the lawsuit with prejudice. On March 27, 2018, Well Thrive filed an answering brief in opposition to our motion on the basis that Well Thrive never consented to dismiss the case. On January 2, 2019, the judge denied without prejudice the motion filed by us, because there remains some question as to whether Well Thrive's former lawyers and Dr. Chiou had authority from Well Thrive to settle this case. The judge's order allows us to conduct depositions of Well Thrive's former lawyer, Dr. Chiou, and Mr. Chang Sheng-Chun, Well Thrive's director, and to request documents relating to the issues surrounding the settlement. Based on this order, we intend to arrange the depositions to obtain more evidence in support of a motion to enforce the settlement agreement. The Court set a trial date of March 2, 2020, if needed.

On December 28, 2018, the Company received a notification from the Court in Miao-Li County, Taiwan that Epistar Corporation (the successor to Formosa Epitaxy Incorporation, the "Plaintiff") filed a motion requesting that the Company return the $3 million prepayment plus value-added-tax for the headquarters building sale and pay interest during this period and litigation fees. The Plaintiff also petitioned the Court to do a provisional execution upon the Company, which would permit the Plaintiff to sell the building and/or other assets belonged to the Company to recover the prepayment. On January 4, 2019, the Company filed a statement of defense arguing that the Plaintiff's action and motion for provisional execution should be dismissed and the litigation fees should be borne by the Plaintiff. On January 25, 2019, the Company and the Plaintiff entered into a settlement, agreeing that the Company would return the $3 million plus value-added-tax of $150 thousand and penalty of $200 thousand, and on February 1, 2019, the Plaintiff withdrawal the motion. As of February 28, 2019, the Company has paid $3.2 million, and accrued a payable of $150 thousand.

Except as described above, there was no material pending legal proceedings or claims as of February 28, 2019.

Item 1A. Risk Factors

Except as set forth below, there are no material changes related to risk factors from the risk factors described in Item 1A "Risk Factors" in Part I of our 2018 Annual Report.

We may fail to qualify for continued listing on NASDAQ which could make it more difficult for investors to sell their shares.

In December 2010, our common stock was initially approved for listing on the NASDAQ Global Select Market but was transferred to the NASDAQ Capital Market effective November 5, 2015. To maintain that listing, we must satisfy the continued listing requirements of NASDAQ for inclusion in the NASDAQ Capital Market, including among other things, that our audit committee consist of three independent directors who satisfy additional requirements under the Exchange Act. On March 17, 2019, Roger Lee resigned from the Board of Directors of the Company effective immediately, which resulted in one vacancy on the audit committee. In accordance with NASDAQ Listing Rule 5605(c)(4)(B), we have been provided a cure period until the earlier of our next annual meeting of stockholders or March 17, 2020, or if the next annual stockholders' meeting is held before September 13, 2019, then we must evidence compliance no later than September 13, 2019, to regain compliance with the audit committee requirements. If we do not regain compliance with the audit committee requirements by the period provided, NASDAQ will notify us that our common stock will be delisted.

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We intend to appoint a replacement director for the vacancy on the Audit Committee. There can be no assurance that we will be able to implement our plan, regain and maintain compliance with the continued listing requirements or that our common stock will not be delisted from NASDAQ in the future. If our common stock is delisted by NASDAQ, we expect prices for our common stock to be quoted one of the OTC Markets or the OTC Bulletin Board. Under such circumstances, stockholders may find it more difficult to sell, or to obtain accurate quotations, for our common stock, and our common stock would become substantially less attractive to certain purchasers such as financial institutions, hedge funds and other similar investors. There is no assurance, however, that prices for our common stock would be quoted on one of these other trading systems or that an active trading market for our common stock would thereafter exist, which would materially and adversely impact the market value of our common stock.

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

None.

Repurchases

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits

Exhibit No.	Description
31.1	Certification of Chief Executive Officer Pursuant to Exchange Act Rule 13a-14(a)/15d-14(a) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Chief Financial Officer Pursuant to Exchange Act Rule 13a-14(a)/15d-14(a) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

		SEMILEDS CORPORATION (Registrant)	
Dated:	April 12, 2019	By:	/s/ Christopher Lee
		Name:	Christopher Lee
		Title:	Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)