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 June 30, 2021

OR

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

For the transition period from __________ to __________

Commission File Number: 000-27687

BSQUARE CORPORATION
(Exact name of registrant as specified in its charter)

Washington **(State or other jurisdiction of incorporation or organization)**	**91-1650880** **(I.R.S. Employer Identification No.)**
1415 Western Ave, Suite 700, **Seattle, WA** **(Address of principal executive offices)**	**98101** **(Zip Code)**

(425) 519-5900
(Registrant's telephone number, including area code)

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common stock, no par value	BSQR	The NASDAQ Stock Market LLC

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☒ No ☐

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

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

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

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

The number of shares of common stock outstanding as of July 31, 2021: 20,327,917

BSQUARE CORPORATION
FORM 10-Q
For the Quarterly Period Ended June 30, 2021
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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

BSQUARE CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share amounts)

	June 30, 2021 (Unaudited)	December 31, 2020
ASSETS		
Current assets:		
Cash and cash equivalents	$ 8,892	$ 12,623
Restricted cash	337	337
Accounts receivable, net of allowance for doubtful accounts of $50 and $50 at June 30, 2021 and December 31, 2020, respectively	6,318	6,177
Contract assets	46	456
Prepaid expenses and other current assets	743	409
Total current assets	16,336	20,002
Property and equipment, net of accumulated depreciation	654	322
Deferred tax assets	7	7
Intangible assets, net of accumulated amortization	22	71
Right-of-use lease asset, net	1,712	1,853
Other non-current assets	24	27
Total assets	$ 18,755	$ 22,282
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Third-party software fees payable	$ 5,665	$ 6,458
Accounts payable	263	489
Paycheck Protection Program loan	—	950
Accrued compensation	567	717
Other accrued expenses	211	216
Deferred revenue	1,028	2,088
Operating lease	348	344
Total current liabilities	8,082	11,262
Deferred revenue, long-term	300	28
Operating lease, long-term	1,487	1,630
Paycheck Protection Program loan, long-term	—	634
Shareholders' equity:		
Preferred stock, no par: 10,000,000 shares authorized; no shares issued and outstanding	—	—
Common stock, no par: 37,500,000 shares authorized: 13,479,220 and 13,235,038 shares issued and outstanding at June 30, 2021 and December 31, 2020, respectively	140,494	139,726
Accumulated other comprehensive loss	(1,035)	(992)
Accumulated deficit	(130,573)	(130,006)
Total shareholders' equity	8,886	8,728
Total liabilities and shareholders' equity	$ 18,755	$ 22,282

See notes to condensed consolidated financial statements.

BSQUARE CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS
(In thousands, except per share amounts)
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2021	2020	2021	2020
Revenue:				
Partner Solutions	$ 9,960	$ 8,110	$ 18,755	$ 24,015
Edge to Cloud	711	814	1,888	1,638
Total revenue	10,671	8,924	20,643	25,653
Cost of revenue:				
Partner Solutions	8,578	6,944	16,037	20,100
Edge to Cloud	901	934	1,821	1,922
Total cost of revenue	9,479	7,878	17,858	22,022
Gross profit	1,192	1,046	2,785	3,631
Operating expenses:				
Selling, general and administrative	2,148	2,067	4,424	4,964
Research and development	365	54	533	181
Total operating expenses	2,513	2,121	4,957	5,145
Loss from operations	(1,321)	(1,075)	(2,172)	(1,514)
Other income (loss), net	1,614	2	1,605	(33)
Income (loss) before income taxes	293	(1,073)	(567)	(1,547)
Income taxes	—	—	—	—
Net income (loss)	$ 293	$ (1,073)	$ (567)	$ (1,547)
Basic earnings (loss) per share	$ 0.02	$ (0.08)	$ (0.04)	$ (0.12)
Diluted earnings (loss) per share	$ 0.02	$ (0.08)	$ (0.04)	$ (0.12)
Shares used in per share calculations:				
Basic	13,332	13,110	13,267	13,051
Diluted	13,881	13,110	13,267	13,051
Net income (loss)	$ 293	$ (1,073)	$ (567)	$ (1,547)
Other comprehensive loss				
Foreign currency translation, net of tax	(34)	(4)	(66)	(38)
Unrealized gain (loss) on investments, net of tax	—	—	—	(1)
Total other comprehensive loss	(34)	(4)	(66)	(39)
Comprehensive income (loss)	$ 259	$ (1,077)	$ (633)	$ (1,586)

See notes to condensed consolidated financial statements.

BSQUARE CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Six Months Ended June 30, 2021	Six Months Ended June 30, 2020
Cash flows from operating activities:		
Net loss	$ (567)	$ (1,547)
Adjustments to reconcile net loss to net cash (used in) provided by operating activities:		
Depreciation and amortization	297	360
Stock-based compensation	378	320
Gain on extinguishment of PPP loan	(1,584)	—
Changes in operating assets and liabilities:		
Accounts receivable, net	(141)	2,973
Contract assets	(20)	(25)
Prepaid expenses and other assets	(224)	(598)
Third-party software fees payable	(793)	(1,026)
Accounts payable and accrued expenses	(381)	(36)
Operating lease	2	(46)
Deferred revenue	(788)	301
Net cash (used in) provided by operating activities	(3,821)	676
Cash flows from investing activities:		
Additions to property and equipment	(257)	(233)
Proceeds from maturities of short-term investments	—	2,250
Net cash (used in) provided by investing activities	(257)	2,017
Cash flows from financing activities:		
Proceeds from Paycheck Protection Program loan	—	1,576
Proceeds from sale of common stock	360	—
Proceeds from exercise of stock options	53	—
Net cash provided by financing activities	413	1,576
Effect of exchange rate changes on cash and cash equivalents	(66)	1
Net (decrease) increase in cash and cash equivalents	(3,731)	4,270
Cash, restricted cash, and cash equivalents, beginning of period	12,960	8,312
Cash, restricted cash, and cash equivalents, end of period	$ 9,229	$ 12,582

See notes to condensed consolidated financial statements.

BSQUARE CORPORATION
CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY
(In thousands, except share amounts)
(Unaudited)

For the Three Months Ended June 30, 2021	Preferred Stock Shares	Preferred Stock Amount	Common Stock Shares	Common Stock Amount	Accumulated Other Comprehensive Income (Loss)	Accumulated Deficit	Total Shareholders' Equity
Balance as of March 31, 2021	—	$ —	13,298,150	$ 139,907	$ (1,001)	$ (130,866)	$ 8,040
Exercise of stock options	—	—	72,191	17	—	—	17
Sale of common stock	—	—	108,879	360	—	—	360
Share-based compensation, including issuance of restricted stock	—	—	—	210	—	—	210
Net income	—	—	—	—	—	293	293
Foreign currency translation adjustment, net of tax	—	—	—	—	(34)	—	(34)
Balance as of June 30, 2021	—	$ —	13,479,220	$ 140,494	$ (1,035)	$ (130,573)	$ 8,886

For the Six Months Ended June 30, 2021	Preferred Stock Shares	Preferred Stock Amount	Common Stock Shares	Common Stock Amount	Accumulated Other Comprehensive Income (Loss)	Accumulated Deficit	Total Shareholders' Equity
Balance as of December 31, 2020	—	$ —	13,235,038	$ 139,726	$ (992)	$ (130,006)	$ 8,728
Exercise of stock options	—	—	135,303	53	—	—	53
Sale of common stock	—	—	108,879	360	—	—	360
Share-based compensation, including issuance of restricted stock	—	—	—	378	—	—	378
Net loss	—	—	—	—	—	(567)	(567)
Foreign currency translation adjustment, net of tax	—	—	—	(23)	(43)	—	(66)
Balance as of June 30, 2021	—	$ —	13,479,220	$ 140,494	$ (1,035)	$ (130,573)	$ 8,886

See notes to condensed consolidated financial statements

BSQUARE CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. Description of Business and Summary of Significant Accounting Policies

Description of Business

BSQUARE Corporation ("Bsquare," "we," "us" and "our") builds technology that is powering the next generation of connected devices and intelligent systems. We help companies realize the promise of the Internet of Things ("IoT") through the development of devices and systems that are cloud-enabled, share data seamlessly, facilitate distributed learning and control, and operate securely at scale. We believe that IoT-enabled systems can not only deliver value to our customers but also help people make better use of the resources of our planet. Bsquare's suite of services and software components create new revenue streams and operating models for our customers while providing opportunities for lowering costs and improving operations.

Since our founding in 1994, Bsquare has been at the intersection of hardware and software. Today that intersection is the "edge" where cloud-enabled devices connect to create intelligent systems that share data, facilitate distributed control and machine learning, and operate securely at scale. We believe that our expertise, products, and services are applicable in customer projects and initiatives ranging from device hardware, to the operating system, to IoT software solutions, and cloud services that make intelligent systems possible.

Our business has largely been focused on providing software solutions (including reselling software from Microsoft) and related engineering services to businesses that develop, market and sell dedicated-purpose standalone intelligent systems. Examples of dedicated-purpose standalone intelligent systems include smart, connected computing devices such as point-of-sale terminals, kiosks, tablets and handheld devices, as well as smart vending machines, ATM machines, digital signs, smart phones, set-top boxes and in-vehicle telematics and entertainment devices.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of Bsquare have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC") for interim financial reporting and include the accounts of Bsquare and our wholly owned subsidiaries. Certain information and footnote disclosures normally included in the annual consolidated financial statements prepared in accordance with U.S. generally accepted accounting principles ("GAAP") have been condensed or omitted pursuant to such rules and regulations. In management's opinion, the unaudited condensed consolidated financial statements include all material adjustments, all of which are of a normal and recurring nature, necessary to present fairly our financial position as of June 30, 2021 and our operating results and cash flows for the six months ended June 30, 2021 and 2020. The accompanying financial information as of December 31, 2020 is derived from our audited financial statements as of that date.

These unaudited condensed financial statements and related notes should be read in conjunction with our audited financial statements and related notes included in our Annual Report on Form 10-K for the year ended December 31, 2020, as filed with the SEC on March 18, 2021.

Basis of consolidation

The consolidated financial statements include the accounts of Bsquare and our wholly owned subsidiaries. All intercompany balances and transactions have been eliminated.

Revision of prior period financial statements

In connection with the preparation of our condensed consolidated financial statements, we identified an immaterial error related to the recognition of certain revenues in our Edge to Cloud segment in the third quarter of 2019 that had a rollforward effect on consolidated equity and deferred revenue in all quarterly and annual periods through the first quarter of fiscal year 2021. In accordance with SEC Staff Accounting Bulletin ("SAB") No. 99, "Materiality," and SAB No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements," we evaluated the error and determined that the related impact was not material to our financial statements for any prior annual or interim period, but that correcting the cumulative impact of the error would be material to our results of operations for the three months ended June 30, 2021. Accordingly, we have revised our consolidated balance sheets and statements of shareholder's equity as of September 31, 2019, December 31, 2019, and December 31, 2020 and condensed consolidated statements of operations and comprehensive loss and cash flows for the year-ended December 31, 2019 and the three and nine months ended September 30, 2019. A summary of revisions to certain previously reported financial information presented herein for comparative purposes is included in Note 12 – Revision of Prior Period Financial Statements.

Use of estimates

Preparing financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, and expenses. Examples include provisions for bad debts and income taxes, estimates of progress on professional engineering service arrangements, bonus accruals, useful lives of intangible assets and property and equipment, fair values of stock-based awards, and assumptions used to determine the net present value of operating lease liabilities, among other estimates and assumptions. Actual results may differ from these estimates and assumptions.

Income (loss) per share

We compute basic income (loss) per share using the weighted average number of shares of common stock outstanding during the period. We consider restricted stock units as outstanding shares of common stock and include them in the computation of basic loss per share only when vested. We compute diluted loss per share using the weighted average number of shares of common stock outstanding and common stock equivalent shares outstanding during the period using the treasury stock method. We exclude common stock equivalent shares from the computation if their effect is anti-dilutive.

The following potentially dilutive weighted shares were excluded from the calculation of diluted net loss per share because their effect would have been anti-dilutive for the periods presented:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2021	2020	2021	2020
Stock options	406,960	1,922,935	299,743	1,748,717
Restricted stock units	—	39,152	84,527	57,806

2. Revenue Recognition

Disaggregation of revenue

The following table provides information about disaggregated revenue by primary geographical area and includes a reconciliation of the disaggregated revenue with reportable segments (in thousands):

	Three Months Ended June 30, 2021			Three Months Ended June 30, 2020		
	Partner Solutions	Edge to Cloud	Total	Partner Solutions	Edge to Cloud	Total
Primary geographic area:						
North America	$ 7,555	$ 666	$ 8,221	$ 7,114	$ 640	$ 7,754
Europe	93	45	$ 138	305	90	395
Asia	2,312	—	$ 2,312	691	84	775
Total	$ 9,960	$ 711	$ 10,671	$ 8,110	$ 814	$ 8,924

	Six Months Ended June 30, 2021			Six Months Ended June 30, 2020		
	Partner Solutions	Edge to Cloud	Total	Partner Solutions	Edge to Cloud	Total
Primary geographic area:						
North America	$ 15,078	$ 1,731	$ 16,809	$ 20,285	$ 1,245	$ 21,530
Europe	202	157	359	731	303	1,034
Asia	3,475	—	3,475	2,999	90	3,089
Total	$ 18,755	$ 1,888	$ 20,643	$ 24,015	$ 1,638	$ 25,653

Contract balances

We receive payments from customers based upon contractual billing schedules; accounts receivable is recorded when the right to consideration becomes unconditional. Contract assets include amounts related to our contractual right to consideration for completed performance obligations not yet invoiced. Contract liabilities, presented as deferred revenue on our condensed consolidated balance sheets, include payments received in advance of performance under the contract and are realized when the associated revenue is recognized. We had no asset impairment charges related to contract assets for each of the three and six months ended June 30, 2021 and 2020.

Significant changes in the contract assets and the deferred revenue balances during the three and six months ended June 30, 2021 were as follows:

	Three Months Ended June 30, 2021	Six Months Ended June 30, 2021
	Contract Assets	Contract Assets
Transferred to receivables from contract assets outstanding at December 31, 2020	—	—

	Three Months Ended June 30, 2021	Six Months Ended June 30, 2021
	Deferred Revenue	Deferred Revenue
Revenue recognized that was included in deferred revenue at December 31, 2020	$ 323,647	$ 1,079,243

Contract acquisition costs

We capitalize contract acquisition costs for contracts with a life exceeding one year. Amortization of contract acquisition costs was $31,000 and $35,000 for the three months ended June 30, 2021 and 2020, respectively, and was $53,000 and $70,000 for the six months ended June 30, 2021 and 2020, respectively. There were no asset impairment charges for contract acquisition costs for any of the periods noted above.

Transaction price allocated to the remaining performance obligations

The following table includes estimated revenue expected to be recognized in the future related to performance obligations that are unsatisfied or partially unsatisfied at the end of the reporting period. The estimated revenue does not include contracts with original durations of one year or less, amounts of variable consideration attributable to royalties, or contract renewals that were unexercised as of June 30, 2021:

	Remainder of 2021	2022	After 2022

Edge to Cloud	(862,052)	(1,374,163)	(451,537)

Practical expedients and exemptions

We generally expense sales commissions when incurred because the amortization period would have been less than one year. We record these costs within selling, general and administrative expenses.

When applicable and appropriate, the Company utilizes the ‘as-invoiced’ practical expedient which permits revenue recognition upon invoicing.

3. Cash, Cash Equivalents and Restricted Cash

Cash, cash equivalents and restricted cash consisted of the following (in thousands):

	June 30, 2021	December 31, 2020
Cash	$ 2,778	$ 6,509
Cash equivalents (see detail in Note 4)	6,114	6,114
Restricted cash	337	337
Total cash and cash equivalents	9,229	12,960

4. Fair Value Measurements

We measure our cash equivalents and restricted cash at fair value. Fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or a liability. A three-tier fair value hierarchy is established as a basis for considering such assumptions and for inputs used in the valuation methodologies in measuring fair value:

Level 1: Quoted prices in active markets for identical assets or liabilities.
Level 2: Directly or indirectly observable market-based inputs or unobservable inputs used in models or other valuation methodologies.
Level 3: Unobservable inputs that are not corroborated by market data. The inputs require significant management judgment or estimation.

We classify our cash equivalents and restricted cash within Level 1 or Level 2 because our cash equivalents and restricted cash are valued using quoted market prices or alternative pricing sources and models utilizing market observable inputs.

Assets measured at fair value on a recurring basis as of June 30, 2021 and December 31, 2020 are summarized below (in thousands):

	June 30, 2021			December 31, 2020		
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Direct or Indirect Observable Inputs (Level 2)	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Direct or Indirect Observable Inputs (Level 2)	Total
Assets						
Cash equivalents:						
Money market funds	$ 6,114	$ —	$ 6,114	$ 6,114	$ —	$ 6,114
Total cash equivalents	6,114	—	6,114	6,114	—	6,114
Restricted cash:						
Money market funds	337	—	337	337	—	337
Total assets measured at fair value	$ 6,451	$ —	$ 6,451	$ 6,451	$ —	$ 6,451

5. Intangible Assets

Intangible assets relate to customer relationships that we acquired from TestQuest, Inc. in November 2008 and from the acquisition of Bsquare EMEA, Ltd. in September 2011 and were as follows (in thousands):

	June 30, 2021			December 31, 2020		
	Gross Carrying Amount	Accumulated Amortization	Net Book Value	Gross Carrying Amount	Accumulated Amortization	Net Book Value
Customer relationships	$ 982	$ (960)	$ 22	$ 982	$ (911)	$ 71

Amortization expense was $25,000 for each of the three months ended June 30, 2021 and 2020. Amortization in future periods is expected to be as follows (in thousands):

Remainder of 2021	$ 22
Total	$ 22

6. Leases

We determine if an arrangement is a lease at inception. On our balance sheet, our office leases are included in right-of-use ("ROU") lease asset, net and related lease liabilities are included in operating lease and operating lease, long-term. We determined that we do not currently have any leases that we are required to classify as finance leases.

ROU assets represent our right to use the underlying assets for the lease term and operating lease liabilities represent our obligation to make lease payments arising from the lease agreements. Operating lease ROU assets and liabilities are recognized at the lease commencement date based on the present value of lease payments over the term of the lease. For leases that do not provide an implicit rate, we use an incremental borrowing rate based on information available at the commencement date to determine the present value of lease payments. We use the implicit rate in the lease when readily determinable. Lease expense for lease payments is recognized on a straight-line basis over the lease term.

In November 2020, we renewed the lease for our office facility in the UK. The term of the lease is 120 months, with rent payments starting on November 30, 2020 and the lease term ending on November 8, 2030. The Company has an opportunity to break the lease at the five-year mark in November 2025. As it is reasonably certain that we will utilize this option, the accounting for this lease utilized November 2025 as the end date. The lease commencement date was November 9, 2020. As a result of entering into this lease agreement, we recorded additional ROU assets and net lease liabilities of $365,559 on our consolidated balance sheet as of December 31, 2020. There was no material impact to our statement of operations or statement of cash flows as a result of entering into this lease.

Our leases have remaining terms of five to seven years. The only leases that contain renewal options are for office space leases at our Seattle and Trowbridge locations. In the fourth quarter of 2019, we made the decision not to renew our Bellevue lease, which expired at the end of May 2020, and we made the decision not to renew our Taiwan lease, exiting that facility in February 2020. Because of changes in our business, we are not able to determine with reasonable certainty whether we will renew our Seattle lease. As a result, we have not considered renewal options when recording ROU assets, lease liabilities or lease expense.

The following tables present the components of our lease expense and supplemental cash flow information related to our leases for the six months ended June 30, 2021 (in thousands):

	Six Months Ended June 30, 2021
Total component lease expense was as follows:	
Operating leases	$ 206
Supplemental cash flow information related to leases was as follows:	
Cash paid for amounts included in the measurement of lease liabilities	$ 206

The following table presents supplemental balance sheet information related to our operating leases as of June 30, 2021 (dollars in thousands):

	June 30, 2021
Right-of-use lease assets	$ 1,712
Current portion of operating lease liability	$ 348
Operating lease liability, net of current portion	1,487
Total operating lease liabilities	$ 1,835
Weighted average remaining lease term (years)	5.7
Weighted average discount rate	8.5%

The following table presents the amounts we are obligated to pay, by maturity, under our operating leases liabilities as of June 30, 2021 (in thousands):

Years Ending December 31,	
2021, remainder of year	$ 156
2022	317
2023	324
2024	331
2025	326
After 2025	440
Total minimum lease payments	1,894
Less: amount representing interest	(59)
Present value of lease liabilities	$ 1,835

7. Shareholders' Equity

Equity Compensation Plans

We have a stock plan (the "Stock Plan") and an inducement stock plan for newly hired employees (together with the Stock Plan, the "Plans"). Under the Plans, stock options to purchase shares of our common stock may be granted with a fixed exercise price that is equal to the fair market value of our common stock on the date of grant. These options have a term of up to 10 years and vest over a predetermined period, generally four years. Incentive stock options granted under the Stock Plan may only be granted to our employees. The Plans also allow for awards of non-qualified stock options, stock appreciation rights, restricted and unrestricted stock awards, and restricted stock units ("RSUs").

Stock-Based Compensation

The estimated fair value of stock-based awards is recognized as compensation expense over the vesting period of the award, net of estimated forfeitures. We estimate forfeitures based on historical experience and expected future activities. The fair value of RSUs is determined based on the number of shares granted and the quoted price of our common stock on the date of grant. The fair value of stock option awards is estimated at the grant date based on the fair value of each vesting tranche as calculated by the Black-Scholes-Merton ("BSM") option-pricing model. The BSM model requires various highly judgmental assumptions including expected volatility and option life. If any of the assumptions used in the BSM model change significantly, stock-based compensation expense may differ materially in the future from that recorded in the current period. The fair values of our stock option grants and RSUs were estimated with the following weighted average assumptions:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2021	2020	2021	2020
Dividend yield	0%	0%	0%	0%
Expected life (years)	4.8	4.9	4.8	4.9
Expected volatility	105%	63%	105%	63%
Risk-free interest rate	0.6%	0.3%	0.5%	0.7%

The impact on our results of operations from stock-based compensation expense was as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2021	2020	2021	2020
Cost of revenue — Edge to Cloud	$ 9	$ 20	$ 24	$ 24
Selling, general and administrative	181	80	327	286
Research and development	20	5	27	10
Total stock-based compensation expense	$ 210	$ 105	$ 378	$ 320

Stock Option Activity

The following table summarizes stock option activity under the Plans:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value
Balance at December 31, 2020	1,786,891	$ 2.04	7.75	$ 330,831
Granted	160,000	2.89		
Exercised	(24,255)	2.20		
Forfeited	(43,450)	1.51		
Expired	(62,200)	2.60		
Balance at June 30, 2021	1,816,986	2.11	7.49	4,987,776
Vested and expected to vest at June 30, 2021	1,670,128	2.15	7.39	4,527,651
Exercisable at June 30, 2021	860,520	$ 2.67	6.36	$ 1,957,927

At June 30, 2021, total compensation cost related to stock options granted but not yet recognized, net of estimated forfeitures, was $373,173. This cost will be amortized on the straight-line method over a weighted-average period of approximately 1.3 years. The following table summarizes certain information about stock options:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2021	2020	2021	2020
Weighted average grant-date fair value of options granted during the period	$ 2.64	$ 1.66	$ 2.89	$ 1.02
Options in-the-money (in shares)	706,620	25,344	706,620	25,344
Aggregate intrinsic value of options exercised during the period	$ 1.02	$ —	$ 2.20	$ —

The aggregate intrinsic value represents the difference between the exercise price of the underlying options and the quoted price of our common stock for the number of options exercised during the periods indicated. We issue new shares of common stock upon exercise of stock options.

Restricted Stock Unit Activity

The following table summarizes RSU activity under the Plans:

	Number of Shares	Weighted Average Award Price
Unvested at December 31, 2020	164,697	$ 1.48
Granted	90,343	2.72
Vested	(109,798)	1.48
Forfeited	(21,115)	1.48
Unvested at June 30, 2021	124,127	2.38
Expected to vest after June 30, 2021	118,839	$ 2.37

At June 30, 2021, total compensation cost not yet recognized related to granted RSUs was approximately $183,164, net of estimated forfeitures. This cost will be amortized on the straight-line method over a weighted-average period of approximately 0.3 years.

Performance Stock Units

In January 2021 we issued 500,000 performance stock units (PSUs) to our executives. The PSUs vest based on a combination of Bsquare's stock price performance and executive service (continued employment). The first vesting measurement date is January 5, 2022 and the final measurement date is July 5, 2025. We estimated the fair value of the awards utilizing Monte Carlo simulations. Based on the Monte Carlo model, expense of approximately $17,000 and $34,000 was recorded in the selling, general and administrative line of our statement of operations for the three and six months ended June 30, 2021, respectively. The PSUs had no impact on our cash flow statement.

Award Modifications

In June 2021, the outstanding RSU and non-qualified stock option awards of two Board members were modified. In accordance with ASC 718, we recorded incremental expense of $41,000 during the period related to the revaluation of these modified awards.

Common Stock Reserved for Future Issuance

The following table summarizes our shares of common stock reserved for future issuance under the Plans as of June 30, 2021:

	June 30, 2021
Stock options outstanding	1,816,986
Restricted stock units and performance stock units outstanding	624,127
Stock options and restricted stock units available for future grant	1,426,792
Common stock reserved for future issuance	3,867,905

Common Stock Sales

In the second quarter of 2021, we received net cash proceeds of approximately $349,000 from the sale of 108,879 shares of our common stock pursuant to a registration statement on Form S-3 under the Securities Act of 1933, as amended (the "Securities Act") filed in March 2021. The issued shares and total paid-in capital are reflected in the consolidated statement of shareholder’s equity for the three and six months ended June 30, 2021.

8. Commitments and Contingencies

Lease and rent obligations

Our commitments include obligations outstanding under operating leases, which expire through 2027. We have lease commitments for office space in Seattle, Washington and Trowbridge, UK. See Note 6 - Leases.

Loss Contingencies

From time to time, we are subject to legal proceedings, claims, and litigation arising in the ordinary course of business including tax assessments. We defend ourselves vigorously against any such claims. When (i) it is probable that an asset has been impaired or a liability has been incurred and (ii) the amount of the loss can be reasonably estimated, we record the estimated loss. We provide disclosure in the notes to the consolidated financial statements for loss contingencies that do not meet both conditions if there is a reasonable possibility that a loss may have been incurred that would be material to the financial statements. Significant judgment is required to determine the probability that a liability has been incurred and whether such liability is reasonably estimable. We base accruals made on the best information available at the time, which can be highly subjective. As of June 30, 2021, we have not recorded any loss contingency accruals.

9. Information about Geographic Areas and Operating Segments

Our chief operating decision-makers (i.e. our Chief Executive Officer and certain direct reports) review financial information presented on a consolidated basis, accompanied by disaggregated information for purposes of allocating resources and evaluating financial performance. There are no segment managers who are held accountable by our chief operating decision-makers, or anyone else, for operations, operating results, or planning for levels or components below the consolidated unit level. We operate within a single industry segment of computer software and services.

We have two major product lines, Partner Solutions and Edge to Cloud, each of which we consider to be operating and reportable segments. We do not allocate costs other than direct cost of goods sold to the segments or produce segment income statements, and we do not produce asset information by reportable segment. The following table sets forth profit and loss information about our segments (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2021	2020	2021	2020
Partner Solutions:				
Revenue	$ 9,960	$ 8,110	$ 18,755	$ 24,015
Cost of revenue	8,578	6,944	16,037	20,100
Gross profit	1,382	1,166	2,718	3,915
Edge to Cloud:				
Revenue	711	814	1,888	1,638
Cost of revenue	901	934	1,821	1,922
Gross profit	(190)	(120)	67	(284)
Total gross profit	1,192	1,046	2,785	3,631
Operating expenses	2,513	2,121	4,957	5,145
Other income (expense), net	1,614	2	1,605	(33)
Income tax benefit (expense)	—	—	—	—
Net income (loss)	$ 293	$ (1,073)	$ (567)	$ (1,547)

Revenue by geographic area is based on the sales region of the customer. The following tables set forth total revenue and long-lived assets by geographic area (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2021	2020	2021	2020
Total revenue:				
North America	$ 8,221	$ 7,754	$ 16,809	$ 21,530
Europe	138	395	359	1,034
Asia	2,312	775	3,475	3,089
Total revenue	$ 10,671	$ 8,924	$ 20,643	$ 25,653

	June 30, 2021	December 31, 2020
Long-lived assets:		
North America	$ 1,666	$ 1,179
Europe	171	179
Total long-lived assets	$ 1,837	$ 1,358

Long-lived assets increased due to additions of internally developed software during the quarter in North America.

10. Significant Risk Concentrations

Significant Customers

GES Singapore Pte, LTD accounted for $1.0 million or approximately 10% of our total revenue for the three months ended June 30, 2021. ParTech, Inc. accounted for $1.1 million or approximately 11% of our total revenue for the three months ended June 30, 2021. CCIntegration, Inc. accounted for $1.2 million or approximately 14% of our total revenue for the three months ended June 30, 2020.

No customers accounted for 10% or more of total revenue for each of the six months ended June 30, 2021 and 2020.

GES Singapore Pte, LTD had accounts receivable balances of $801,000 or approximately 13% of our total accounts receivable at June 30, 2021. Honeywell International, Inc. and affiliated entities ("Honeywell") had accounts receivable balances of $680,000 or approximately 12% of our total accounts receivable at December 31, 2020. Kodak Alaris had accounts receivable balances of $866,000 or approximately 15% of our total accounts receivable at December 31, 2020.

Significant Supplier

We are authorized to sell Windows IoT operating systems in Canada, the United States, Argentina, Brazil, Chile, Mexico, Peru, Venezuela, Puerto Rico, Columbia, and several Caribbean countries. Our distribution agreement for sales of Windows IoT operating systems in the European Union ("E.U."), the European Free Trade Association, Turkey and Africa, expired on June 30, 2019 and was not renewed thereafter.

We have also entered into Original Equipment Manufacturer Distribution Agreements ("ODAs") with Microsoft pursuant to which we are licensed to sell Microsoft Windows Mobile operating systems to customers in North America, South America, Central America (excluding Cuba), Japan, Taiwan, Europe, the Middle East, and Africa. The ODAs to sell Windows Mobile operating systems are effective through April 30, 2022.

There is no automatic renewal provision in any of these agreements, and these agreements can be terminated unilaterally by Microsoft at any time.

The majority of our revenue continues to be derived from reselling Microsoft Windows Embedded and IoT operating system software to device makers. The sale of Microsoft operating systems has historically accounted for substantially all of our Partner Solutions revenue.

Microsoft currently offers a distributor incentives program through which we earn rebates pursuant to predefined objectives related to sales of Microsoft Windows IoT operating systems. In accordance with program rules, we allocate a portion of the incentive earnings to reduce cost of revenue with the remaining portion utilized to offset qualified marketing expenses in the period the expenditures are claimed and approved. During the second quarter of 2020 the program allocation was changed by Microsoft to a 50/50 split between the two components.

Under this rebate program, we recorded rebate credits as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2021	2020	2021	2020
Reductions to cost of revenue	$ 103	$ 41	$ 209	$ 154
Reductions to marketing expense	120	721	177	940

11. Paycheck Protection Program (PPP) loan

We obtained a $1.5 million loan (the "PPP Loan") from JPMorgan Chase Bank, N.A. (the "Lender") under the Paycheck Protection Program ("PPP") on April 7, 2020 (the "Note"). The Note had a two-year term, bore interest at the rate of 0.98% per annum, and could be prepaid at any time without payment of any premium or penalty. The principal and accrued interest under the Note was forgivable after an eight- or 24-week period if we used the PPP Loan proceeds for eligible purposes, including payroll, benefits, rent and utilities, and otherwise comply with PPP requirements. In April 2021, we applied for forgiveness of this loan in accordance with the program, and in June 2021, we received confirmation that the loan principal (and related accrued interest) was forgiven in its entirety. The gain on loan forgiveness is included in other income (loss), net on the statement of operations for the three and six months ended June 30, 2021, and as a gain on extinguishment of debt in the statement of cash flows for the six months ended June 30, 2021.

At June 30, 2021 and December 31, 2020, the PPP Loan balance was as follows (in thousands):

	June 30, 2021	December 31, 2020
PPP Loan, .98%, due April 2022:		
Principal	$ -	$ 1,572
Accrued interest	-	12
	$ -	$ 1,584
PPP Loan payable:		
Current portion	$ -	950
Long-term portion	-	634
	$ -	$ 1,584

12. Revision of Prior Period Financial Statements

We revised certain prior period financial statements due to a $77,000 error related to the recognition of certain revenues in our Edge to Cloud segment. The error occurred in the third quarter of 2019 and had a rollforward effect on consolidated equity and deferred revenue in all quarterly and annual periods through the first quarter of 2021. See Note 1 - Description of Business and Summary of Significant Accounting Policies. A summary of the revisions to our previously reported financial statements is presented below (in thousands).

Revised Consolidated Balance Sheets

	As of December 31, 2019		
	As reported	Adjustment	As revised
Deferred revenue, current portion	$ 1,559	$ (77)	$ 1,482
Total current liabilities	11,200	(77)	11,123
Accumulated deficit	(128,194)	77	(128,117)
Total shareholders' equity	9,696	77	9,773

	As of December 31, 2020		
	As reported	Adjustment	As revised
Deferred revenue, current portion	$ 2,165	$ (77)	$ 2,088
Total current liabilities	11,339	(77)	11,262
Accumulated deficit	(130,083)	77	(130,006)
Total shareholders' equity	8,651	77	8,728

Revised Consolidated Statement of Shareholders' Equity

	Year Ended December 31, 2019		
	As reported	Adjustment	As revised
Net loss	$ (9,181)	$ 77	$ (9,104)
Accumulated deficit	(128,194)	77	(128,117)

	Three Months Ended September 30, 2019		
	As reported	Adjustment	As revised
Net loss	$ (1,107)	$ 77	$ (1,030)
Accumulated deficit	(126,834)	77	(126,757)

	Nine Months Ended September 30, 2019		
	As reported	Adjustment	As revised
Net loss	$ (7,821)	$ 77	$ (7,744)
Accumulated deficit	(126,834)	77	(126,757)

	Year Ended December 31, 2020		
	As reported	Adjustment	As revised
Accumulated deficit	$ (130,083)	$ 77	$ (130,006)

Revised Condensed Consolidated Statements of Operations and Comprehensive Loss

	Year Ended As of December 31, 2019		
	As reported	Adjustment	As revised
Edge to Cloud revenue	$ 8,655	$ 77	$ 8,732
Total revenue	59,283	77	59,360
Gross profit	10,096	77	10,173
Loss from operations	(9,314)	77	(9,237)
Loss before income taxes	(9,165)	77	(9,088)
Net loss	(9,181)	77	(9,104)
Basic loss per share	(0.71)	-	(0.71)
Diluted loss per share	(0.71)	-	(0.71)
Comprehensive loss	(9,242)	77	(9,165)

	Three Months Ended September 30, 2019		
	As reported	Adjustment	As revised
Edge to Cloud revenue	$ 2,085	$ 77	$ 2,162
Total revenue	14,641	77	14,718
Gross profit	2,632	77	2,709
Loss from operations	(1,129)	77	(1,052)
Loss before income taxes	(1,107)	77	(1,030)
Net loss	(1,107)	77	(1,030)
Basic loss per share	(0.09)	0.01	(0.08)
Diluted loss per share	(0.09)	0.01	(0.08)
Comprehensive loss	(1,111)	77	(1,034)

	Nine Months Ended September 30, 2019		
	As reported	Adjustment	As revised
Edge to Cloud revenue	$ 6,576	$ 77	$ 6,653
Total revenue	43,917	77	43,994
Gross profit	7,446	77	7,523
Loss from operations	(7,937)	77	(7,860)
Loss before income taxes	(7,821)	77	(7,744)
Net loss	(7,821)	77	(7,744)
Basic loss per share	(0.60)	-	(0.60)
Diluted loss per share	(0.60)	-	(0.60)
Comprehensive loss	(7,899)	77	(7,822)

Revised Condensed Consolidated Statements of Cash Flows

We revised our condensed consolidated statements of cash flows for the year ended December 31, 2019 and the nine months ended September 31, 2019 for this correction, which had no impact to net cash used by operating activities in each such period.

	Year Ended December 31, 2019		
	As reported	**Adjustment**	**As revised**
Cash flows from operating activities:			
Net loss	$ (9,181)	$ 77	$ (9,104)
Deferred revenue	(227)	(77)	(304)
Net cash used by operating activities	(5,995)	-	(5,995)

	Nine Months Ended September 30, 2019		
	As reported	**Adjustment**	**As revised**
Cash flows from operating activities:			
Net loss	$ (7,821)	$ 77	$ (7,744)
Deferred revenue	(48)	(77)	(125)
Net cash used in operating activities	(4,994)	-	(4,994)

Revised Segment Information

Edge to Cloud revenue and gross profit were impacted for each of the applicable prior periods by the same amount as consolidated revenue and gross profit for the respective periods.

13. Subsequent Events

In July 2021, we entered into a Side Letter (the “Side Letter”) with B. Riley Securities, Inc. (the “Agent”) in connection with the At-Market Issuance Sales Agreement dated April 2, 2021 (the “Sales Agreement”) between us and the Agent. The Side Letter confirmed the understanding of the parties that the Sales Agreement applies to the issuance and sale of shares (the “Shares”) of our common stock having an aggregate offering price of up to $50.0 million pursuant to our existing shelf registration statement on Form S-3 (File No. 333-254458) originally filed with the SEC on March 18, 2021 and which became effective on March 26, 2021 (the “Registration Statement”). All other terms and conditions of the Sales Agreement remain in full force and effect.

We previously filed a prospectus supplement dated April 2, 2021 relating to the offering of up to $25.0 million in Shares under the Sales Agreement (the “Prior Offering”). We also filed a prospectus supplement dated July 7, 2021 relating to the offering of up to an additional $25.0 million in Shares under the Sales Agreement (the “Current Offering”).

During July 2021, we received $31.8 million in net cash proceeds from the sale of 6,793,798 Shares, no par value under the terms of the Prior Offering and the Current Offering.

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

The following discussion should be read in conjunction with our condensed consolidated financial statements and related notes. Some statements and information contained in this discussion are not historical facts but are forward-looking statements within the meaning of Section 27A of the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). In some cases, readers can identify forward- looking statements by terms such as "may," "will," "should," "expect," "plan," "intend," "forecast," "anticipate," "believe," "estimate," "predict," "potential," "continue," or the negative of these terms or other comparable terminology, which when used are meant to signify the statement as forward-looking. These forward-looking statements include, but are not limited to, statements about our plans, objectives, expectations and intentions and other statements that are not historical facts. These forward-looking statements are not guarantees of future performance and involve known and unknown risks, uncertainties and situations that are difficult to predict and that may cause our own, or our industry's actual results, to be materially different from the future results that are expressed or implied by these statements. Accordingly, actual results may differ materially from those anticipated or expressed in such statements as a result of a variety of factors, including those discussed in the sections entitled "Risk Factors" in this Quarterly Report on Form 10-Q and in in Item 1A of Part I of our Annual Report on Form 10-K for the year ended December 31, 2020 as well as similar discussions contained in our periodic reports, and other documents or filings and documents that we may from time to time file or furnish with the SEC. Readers are cautioned not to place undue reliance on the forward-looking statements, which speak only as of the date made. Except as required by law, we undertake no obligation to update any forward-looking statement, whether as a result of new information, future events or otherwise.

Overview

Bsquare is a software and services company that designs, configures, and deploys technologies that solve difficult problems for manufacturers and operators of connected devices. Our customers choose Bsquare to help realize the promise of the Internet of Things (IoT) to transform their businesses. Our products include software that connects devices to create intelligent systems that are cloud-enabled, contribute critical data, and facilitate distributed control and decision making. Our services include 24/7 IoT operations that allow our customers to focus on their businesses while we take care of security, monitoring, and general technology updates. The opportunity to help companies explore and capture the value of IoT is attractive and growing. In the last two years alone, we helped hundreds of companies deploy and manage over two million devices. We operate large IoT systems for our customers with device fleets that range in size and complexity. We believe we offer a unique combination of expertise in device-level solutions, embedded operating systems, and IoT services and software that is valued by a global customer base, from start-ups to Fortune 100 companies, across a diverse set of industries.

In the first half of 2021, we continued our ongoing initiatives to strategically build our business and are pursuing business opportunities at the intersection of our two business segments. In the Partner Solutions segment, customers who have been purchasing Operating System (OS) software from us are recognizing that their products, essentially interconnected devices and associated software, cannot be sold, installed, and then forgotten. For these customers, we offer software-based solutions that address the operational headaches caused by this relatively new and increasingly complex business requirement. In the Edge to Cloud segment, customers are relying on Bsquare for a complete solution, ranging from OS configuration to 24/7 support, dev/ops, and cloud management – the services that are critical when a customer puts an IoT solution into production. Experience with those customers has shown that Bsquare's role can last well beyond the development phase and continue into their on-going operations. Our software and edge expertise combined with our position as a supply chain partner makes us uniquely suited to address these complex requirements, in both business segments.

Revenue

The COVID-19 pandemic, including its impact on the microchip supply chain, continues to affect our Partner Solutions customer ordering patterns and has caused ongoing disruptions and revenue variability in the Partner Solutions segment. Decreases in segment revenue that began in the second quarter of 2020 persisted through the first quarter of 2021. Second quarter 2021 revenue improved over first quarter 2021 as COVID-19 related supply chain issues eased for some of our Partner Solutions customers during the quarter. It is not clear that this is an indication of sustained recovery. Revenue in 2021 remains at levels lower than our pre-COVID-19 expectations. We believe our Partner Solutions revenue is also affected by other Microsoft distributors offering deep discounts on Windows IoT OS software as part of hardware / software bundles. We expect this market trend may continue in future quarters. We are working to retain and attract customers with superior service and technical support, pricing that rewards loyalty, and a path to IoT operations.

In our Edge to Cloud segment, investments we made to ensure we were meeting our operating commitments, while re-tooling and addressing issues with software previously delivered to some of our larger IoT customers, started to generate revenue for us in 2020. In the first quarter of 2021, we worked closely with Itron, Inc. to help them build their intelligent utility grid. We anticipate investments in our other large IoT customers will continue in 2021, but at lower levels than in 2020 as the bulk of the rework is now complete. Beyond gaining credibility as a reliable technology partner, we believe the experience we have gained serving Itron and our other large IoT customers positions us to improve our IoT software and services in 2021 and beyond.

Expenses

Our work in 2020 to reduce our operating expense structure has provided a foundation from which we are strategically building our business. Our operating expenses in the first half of 2021 were nearly $200,000 less than our operating expenses the first half of 2020. Our current cost structure fits our business model and our entrepreneurial leadership team acts on changing business circumstances and opportunities as they emerge. We believe this operating discipline demonstrates our ability to manage through adversity.

Cash and Liquidity

Our cash and cash equivalents decreased by $3.7 million in the first half of 2021. This cash use was driven by investment in strategic growth opportunities, operational results (primarily soft Partner Solutions revenue) and variations in working capital.

During the second quarter of 2021 we received net cash proceeds of $0.3 million from sales of Shares under the terms of the Prior Offering. After the quarter, in July 2021, we received net cash proceeds of $31.8 million from additional sales of Shares under the terms of the Prior Offering and the Current Offering.

Critical Accounting Judgments

Our condensed consolidated financial statements have been prepared in accordance with GAAP. The preparation of these condensed consolidated financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, sales, cost of sales and expenses and related disclosure of contingent assets and liabilities. We evaluate our estimates on an on-going basis. We base our estimates on historical experience and on various other assumptions that we believe are reasonable in the circumstances, which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. There have been no significant changes to our critical accounting judgments, policies and estimates as described in our Annual Report on Form 10-K for the year ended December 31, 2020.

Results of Operations

The following table presents our summarized results of operations for the periods indicated. Our historical operating results are not necessarily indicative of the results for any future period.

(In thousands, except percentages)	Three Months Ended June 30, 2021	2020	$ Change	% Change	Six Months Ended June 30, 2021	2020	$ Change	% Change
Total revenue	$ 10,671	$ 8,924	$ 1,747	20%	$ 20,643	$ 25,653	$ (5,010)	(20)%
Total cost of revenue	9,479	7,878	1,601	20%	17,858	22,022	(4,164)	(19)%
Gross profit	1,192	1,046	146	14%	2,785	3,631	(846)	(23)%
Operating expenses	2,513	2,121	392	18%	4,957	5,145	(188)	(4)%
Loss from operations	(1,321)	(1,075)	(246)	(23)%	(2,172)	(1,514)	(658)	(43)%
Other income (loss), net	1,614	2	1,612	80600%	1,605	(33)	1,638	(4963)%
Income (loss) before income taxes	293	(1,073)	1,366	127%	(567)	(1,547)	980	63%
Income tax benefit	—	—	—	—%	—	—	—	—%
Net income (loss)	$ 293	$ (1,073)	$ 1,366	127%	$ (567)	$ (1,547)	$ 980	63%

Revenue

We generate revenue from the sale of software, both embedded operating system software that we resell and our own proprietary software, and related professional services.

Total revenue for the three months ended June 30, 2021 increased compared to the same period in 2020, primarily due to increased sales in our Partner Solutions segment in North America and Europe, slightly offset by lower revenue in our Edge to Cloud segment.

Total revenue for the six months ended June 30, 2021 decreased compared to the same period in 2020, primarily due to decreased sales in our Partner Solutions segment in North America and Europe, slightly offset by higher revenue in our Edge to Cloud segment.

Additional revenue details are as follows:

(In thousands, except percentages)	Three Months Ended June 30, 2021	2020	$ Change	% Change	Six Months Ended June 30, 2021	2020	$ Change	% Change
Revenue								
Partner Solutions	$ 9,960	$ 8,110	$ 1,850	23%	$ 18,755	$ 24,015	$ (5,260)	(22)%
Edge to Cloud	711	814	(103)	(13)%	1,888	1,638	250	15%
Total revenue	$ 10,671	$ 8,924	$ 1,747	20%	$ 20,643	$ 25,653	$ (5,010)	(20)%
As a percentage of total revenue:								
Partner Solutions	93%	91%			91%	94%		
Edge to Cloud	7%	9%			9%	6%		

Partner Solutions revenue

Partner Solutions revenue increased $1.9 million or 23% for the quarterly period ended June 30, 2021 compared to the same period in 2020. The current period results were favorably impacted by the easing of COVID-19 supply chain issues for some of our customers while the prior period results reflect the disruptions and uncertainty caused by the onset of the global COVID-19 pandemic.

Partner Solutions revenue decreased $5.3 million or 22% for the six months ended June 30, 2021 compared to the same period in 2020. Revenue decreased $7.1 million in the first quarter of 2021 compared to the same period in 2020 while revenue increased, as discussed above, in the second quarter.

Edge to Cloud revenue

Edge to Cloud revenue decreased for the three months ended June 30, 2021 compared to the same period in 2020, primarily due to a decrease in professional services revenue from our smaller customers. Edge to Cloud revenue increased for the six months ended June 30, 2021 compared to the same period in 2020 due to an increase in professional services revenue. We expect Edge to Cloud revenue will continue to vary in timing and amount.

Gross profit and gross margin

Cost of revenue for the Partner Solutions segment consists primarily of embedded operating system software product costs payable to third-party vendors, net of rebate credits earned through Microsoft's distributor incentive program. Cost of revenue for the Edge to Cloud segment consists primarily of salaries and benefits and re-billable expenses, and amortization of certain intangible assets. Gross profit and gross margin were as follows:

	Three Months Ended June 30,				Six Months Ended June 30,			
(In thousands, except percentages)	**2021**	**2020**	**$ Change**	**% Change**	**2021**	**2020**	**$ Change**	**% Change**
Partner Solutions	$ 1,382	$ 1,166	$ 216	19%	$ 2,718	$ 3,915	$ (1,197)	(31)%
Partner Solutions gross margin	*14%*	*14%*		—%	*14%*	*16%*		(2)%
Edge to Cloud	(190)	(120)	(70)	58%	67	(284)	351	(124)%
Edge to Cloud gross margin	*(27)%*	*(15)%*		(12)%	*4%*	*(17)%*		21%
Total gross profit	$ 1,192	$ 1,046	$ 146	14%	$ 2,785	$ 3,631	$ (846)	(23)%
Total gross margin	*11%*	*12%*		(1)%	*13%*	*14%*		(1)%

Partner Solutions gross profit and gross margin

Partner Solutions gross profit increased for the three months ended June 30, 2021 primarily due to increased segment revenue. Gross margin rate was approximately the same for each period.

Partner Solutions gross profit decreased for the six months ended June 30, 2021 primarily due to decreased segment revenue. Gross margin rate decreased year-over-year due to customer and product mix.

Gross profit on Partner Solutions is impacted by rebate credits earned through Microsoft's distributor incentives program. In accordance with program rules, we allocate a portion of the incentive earnings to reduce cost of revenue with the remaining portion utilized to offset qualified marketing expenses in the period the expenditures are claimed and approved. For the three and six month periods ended June 30, 2021, we allocated 50% of rebates to reduce cost of sales and 50% to marketing expenses, and for the three and six month periods ended June 30, 2020, we allocated 20% of rebates to reduce cost of sales and 80% to marketing expenses. See Footnote 10 – Significant Risk Concentrations for further information about these rebates.

Edge to Cloud gross profit and gross margin

Edge to Cloud gross profit and gross margin decreased for the three months ended June 30, 2021 primarily due to decreased revenue.

Edge to Cloud gross profit and gross margin increased for the six months ended June 30, 2021 primarily due to increased revenue.

Operating expenses

The following table presents our operating expenses for the periods indicated:

	Three Months Ended June 30,				Six Months Ended June 30,			
(In thousands, except percentages)	**2021**	**2020**	**$ Change**	**% Change**	**2021**	**2020**	**$ Change**	**% Change**
Operating expenses:								
Selling, general and administrative	$ 2,148	$ 2,067	$ 81	4%	$ 4,424	$ 4,964	$ (540)	(11)%
Research and development	365	54	311	576%	533	181	352	195%
Total operating expenses	$ 2,513	$ 2,121	$ 392	18%	$ 4,957	$ 5,145	$ (188)	(4)%
As a percentage of total revenue:								
Selling, general and administrative	20%	23%			21%	19%		
Research and development	3%	1%			3%	1%		

Selling, general and administrative

Selling, general and administrative ("SG&A") expenses consist primarily of salaries and related benefits, commissions and bonuses for our sales, marketing and administrative personnel, facilities and depreciation costs, as well as professional services fees (e.g., consulting, legal, audit and tax). SG&A expenses increased for the three months ended June 30, 2021 primarily due to an increase in professional services fees and a decrease in the incentive program rebate from Microsoft. These were partially offset by lower salaries and related benefits resulting from our prior restructuring efforts.

SG&A expenses decreased for the six months ended June 30, 2021 primarily due to labor and benefit savings resulting from our prior restructuring efforts combined with decreased marketing spend, partially offset by a reduction in the incentive program rebates from Microsoft.

Research and development

Research and development ("R&D") expenses consist primarily of salaries and related benefits for software development and quality assurance personnel, contractor and consultant costs. R&D expenses increased for the three and six months ended June 30, 2021 primarily due to higher salaries and related benefits and other costs related to product development.

Other income (loss), net

Other income (loss), net consists primarily of interest income on our cash and investments, gains and losses we may recognize on our investments, and gains and losses on foreign exchange transactions and other items. For the three and six months ended

June 30, 2021 this line-item also includes a $1.6 million gain on extinguishment of debt related to the forgiveness of our loan under the Paycheck Protection Program. See Footnote 11 – Paycheck Protection Program Loan for additional information.

Income taxes

Income taxes were not recorded for the quarterly periods ended June 30, 2021 and June 30, 2020, respectively.

Liquidity and Capital Resources

As of June 30, 2021, we had $9.2 million of cash, restricted cash, and cash equivalents. Subsequent to June 30, 2021, we received $31.8 million in net cash proceeds from the Prior Offering and the Current Offering. We generally invest our excess cash in high quality marketable investments. These investments typically include corporate notes and bonds, commercial paper, and money market funds, although specific holdings can vary from period to period depending upon our cash requirements. There were no investments held at June 30, 2021.

We believe that our existing cash and cash equivalents will be sufficient to meet our needs for working capital and capital expenditures for at least the next 12 months.

Cash Flows from Operating Activities

Operating activities used cash of approximately $3.7 million for the six months ended June 30, 2021, which included our net loss increased by non-cash adjustments of $0.9 million and a working capital decrease of approximately $2.3 million. The working capital decrease primarily included cash outflows related to third-party software fees payable of $0.8 million, $0.8 million related to deferred revenue, a $0.2 million change in prepaid expenses and other assets, and a $0.4 million change in accounts payable and accrued expenses.

Cash Flows from Investing Activities

Investing activities used cash of approximately $0.3 million for the six months ended June 30, 2021, related to additions to property and equipment.

Cash Flows from Financing Activities

Financing activities provided cash of approximately $0.4 million for the six months ended June 30, 2021, related primarily to proceeds from sales of our common stock. See Note 7 - Shareholders' Equity.

Cash Commitments

Our future or potential cash commitments relate to minimum rents payable under operating leases, which total $0.2 million for the remainder of 2021, $0.3 million in 2022, $0.3 million in 2023, $0.3 million in 2024, $0.3 million in 2025, and $0.4 million thereafter.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Not applicable.

Item 4. Controls and Procedures

We maintain disclosure controls and procedures that are designed to provide reasonable assurance that the information required to be disclosed in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. Our management carried out an evaluation, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this report. Based upon this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report.

There were no changes in our internal control over financial reporting during the three months ended June 30, 2021 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1A. Risk Factors

There have been no material changes in the risk factors set forth in Part I, Item 1A, “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2020, other than as listed below.

Future sales of substantial amounts of our common stock, or the possibility that such sales could occur, could adversely affect the market price of our common stock.

As part of the Current Offering, we may issue up to $25.0 million of common stock from time to time. The issuance from time to time of shares in the Current Offering, as well as the possibility that we may issue shares in future offerings, could have the effect of depressing the market price, or increasing the market price volatility, of our common stock. The number of shares we may sell, and any resulting impact on market price or volatility, is highly uncertain because we have the broad discretion regarding the number of shares we instruct the Sales Agent to sell, the market price of the common stock during the sales period, the limits we set with the Sales Agent in any applicable placement notice, and the demand for our common stock during the sales period. It is not currently possible to predict the number of shares that will be sold or the gross proceeds to be raised in connection with those sales.

You may experience future dilution as a result of future equity offerings.

In order to raise additional capital, we may in the future offer additional shares of our common stock or other securities convertible into or exchangeable for our common stock. We may not be able to sell shares or other securities in any offering at a price per share that is equal to or greater than prevailing market prices, and investors purchasing shares or other securities in the future could have rights superior to existing shareholders. The price per share at which we sell additional shares of our common stock or other securities convertible into or exchangeable for our common stock in future transactions may be higher or lower than currently prevailing prices per share.

Our common stock has experienced and may continue to experience price and volume fluctuations, which could cause you to lose a significant portion of your investment, lead to costly litigation for us and interfere with our efforts to grow our business.

Stock markets are subject to significant price and volume fluctuations that may be unrelated to the operating performance of particular companies, and accordingly the market price of our common stock may frequently and meaningfully change. For example, during the year ended December 31, 2020, the high and low closing prices per share of our common stock were $1.83 and $0.93, respectively, with an intraday high of $2.00 and an intraday low $0.83 per share, and with daily trading volume at a low of 500 shares and a high of 837,100 shares. In 2021, through June 30, 2021, the high and low closing prices per share of our common stock were $8.40 and $1.44, respectively, with an intraday high of $11.83 and an intraday low of $1.40 per share, and with a daily trading volume at a low of 32,100 shares and a high of 240,691,000 shares. We have not had any recent change in our financial condition or results of operations that is consistent with the recent change in our stock price. In addition, the market price of our common stock has fluctuated and may continue to fluctuate substantially due to a variety of other factors, including quarterly fluctuations in our results of operations (including as a result of fluctuations in our revenue), our ability to execute on our current growth strategy in a timely fashion, announcements about technological innovations or new products or services by us or our competitors, market acceptance of new products and services offered by us, developments in the IoT market, changes in our relationships with our suppliers or customers, our ability to meet analysts’ expectations, changes in the information technology environment, changes in earnings estimates by analysts, sales of our common stock by existing holders and the loss of key personnel. Possible exogenous incidents and trends may also impact the capital markets generally and our common stock prices specifically, such as foreign and cross border altercations, political unrest, cyberterrorism on a global scale, and disruptive weather systems. The timing of your purchase of our common stock relative to fluctuations in its trading price may result in you losing all or a significant portion of your investment.

In the past, following periods of volatility in the market price of a company’s stock, class action securities litigation has often been instituted against such companies. Litigation may arise out of facts and circumstances, or disclosure relating thereto, that we do not currently regard as material. For example, in 2021, we pre-released our expected financial results for the first quarter of 2021, we announced that our shareholders approved amended and restated articles of incorporation then retracted the filing, we pre-released our expected financial results for the second quarter of 2021, and we revised certain prior period financial statements due to a $77,000 error related to the recognition of certain revenues in our Edge to Cloud segment. We have also recently sold shares in the public markets during periods of volatile market activity. Such volatility may entice shareholders to challenge our disclosure, whether or not they are correct. Any litigation, if instituted against us, could result in substantial costs and diversion of management’s attention and resources, which would interfere with our ability to execute our business plan, sell our software and services, and otherwise materially adversely affect our business, financial condition and operating results.

Our common stock may become the target of a “short squeeze.”

In 2021, the securities of several companies have increasingly experienced significant and extreme volatility in stock price due to short sellers of shares of common stock and buy-and-hold decisions of longer investors, resulting in what is sometimes described as a “short squeeze.” Short squeezes have caused extreme volatility in those companies and in the market and have led to the price per share of those companies to trade at a significantly inflated rate that is disconnected from the underlying value of the company. Sharp rises in a company’s stock price may force traders in a short position to buy the stock to avoid even greater losses. Many investors who have purchased shares in those companies at an inflated rate face the risk of losing a significant portion of their original investment as the price per share has declined steadily as interest in those stocks have abated. We may be a target of a short squeeze, and investors may lose a significant portion or all of their investment if they purchase our shares at a rate that is significantly disconnected from our underlying value.

If securities or industry analysts fail to continue publishing research about our business, if they change their recommendations adversely or if our results of operations do not meet their expectations, our stock price and trading volume could decline.

The trading market for our common stock will be influenced by the research and reports that industry or securities analysts publish about us or our business. If one or more of these analysts cease coverage of our company or fail to publish reports on us regularly, we could lose visibility in the financial markets, which in turn could cause our stock price or trading volume to decline. In addition, it is likely that in some future period our operating results will be below the expectations of securities analysts or investors. If one or more of the analysts who cover us downgrade our stock, or if our results of operations do not meet their expectations, our stock price could decline.

Because we do not intend to declare cash dividends on our shares of common stock in the foreseeable future, shareholders must rely on appreciation of the value of our common stock for any return on their investment.

We currently anticipate that we will retain future earnings for the development, operation and expansion of our business and do not anticipate declaring or paying any cash dividends in the foreseeable future. In addition, the terms of any existing or future debt agreements may preclude us from paying dividends. As a result, we expect that only appreciation of the price of our common stock, if any, will provide a return to investors in this offering for the foreseeable future.

Item 6. Exhibits

(b) Exhibits

Exhibit Number	Description	Filed or Furnished Herewith	Incorporated by Reference			
			Form	Filing Date	Exhibit	File No.
3.1	Amended and Restated Articles of Incorporation		S-1	August 17, 1999	3.1(a)	333-85351
3.1(a)	Articles of Amendment to Amended and Restated Articles of Incorporation		10-Q	August 7, 2000	3.1	000-27687
3.1(b)	Articles of Amendment to Amended and Restated Articles of Incorporation		8-K	October 11, 2005	3.1	000-27687
3.2	Amended and Restated Bylaws, effective August 6, 2020		8-K	August 10, 2020	3.1	000-27687
10.1	At Market Issuance Sales Agreement, dated April 2, 2021, by and between Bsquare Corporation and B. Riley Securities, Inc.		8-K	April 2, 2021	10.1	000-27687
31.1	Certification of Chief Executive Officer pursuant to Exchange Act Rule 13a-14(a) under the Securities and Exchange Act of 1934	X				
31.2	Certification of Chief Financial Officer pursuant to Exchange Act Rule 13a-14(a) under the Securities and Exchange Act of 1934	X				
32.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	X				
32.2	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	X				
101.INS	Inline XBRL Instance Document - the instance does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document	X				
101.SCH	Inline XBRL Taxonomy Extension Schema Document	X				
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document	X				
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document	X				
101.LAB	Inline XBRL Taxonomy Extension Presentation Linkbase Document	X				
101.PRE	Inline XBRL Taxonomy Extension Presentation Document	X				
104	Cover Page Interactive Data File (formatted in Inline XBRL and included in Exhibit 101)	X				

* Indicates a management contract or compensatory plan or arrangement.

SIGNATURES

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

BSQUARE CORPORATION
(Registrant)

Date: August 12, 2021

By: /s/ Christopher Wheaton

Christopher Wheaton
Chief Financial and Operating Officer,
Secretary and Treasurer
(Principal Financial Officer and Duly Authorized Signatory)

Exhibit 31.1

CERTIFICATION OF CHIEF EXECUTIVE OFFICER PURSUANT TO RULE 13(a)-14(a) UNDER THE SECURITIES EXCHANGE ACT OF 1934

I, Ralph C. Derrickson, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of BSQUARE Corporation;

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

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: August 12, 2021

/s/ Ralph C. Derrickson
Ralph C. Derrickson
President and Chief Executive Officer

Exhibit 31.2

CERTIFICATION OF CHIEF FINANCIAL OFFICER PURSUANT TO RULE 13(a)-14(a) UNDER THE SECURITIES EXCHANGE ACT OF 1934

I, Christopher Wheaton, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of BSQUARE Corporation;

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

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: August 12, 2021

/s/ Christopher Wheaton
Christopher Wheaton
Chief Financial and Operating Officer, Secretary and Treasurer

Exhibit 32.1

CERTIFICATION OF PRESIDENT AND CHIEF EXECUTIVE OFFICER PURSUANT TO 18 U.S.C. SECTION 1350

Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002,

I, Ralph C. Derrickson, President and Chief Executive Officer, certify that:

1. To my knowledge, this report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. To my knowledge, the information contained in this report fairly presents, in all material respects, the financial condition and results of operations of BSQUARE Corporation.

Dated: August 12, 2021	/s/ Ralph C. Derrickson Ralph C. Derrickson President and Chief Executive Officer

Exhibit 32.2

CERTIFICATION OF CHIEF FINANCIAL OFFICER PURSUANT TO 18 U.S.C. SECTION 1350

Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002,

I, Christopher Wheaton, Chief Financial and Operating Officer, Secretary and Treasurer, certify that:

1. To my knowledge, this report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. To my knowledge, the information contained in this report fairly presents, in all material respects, the financial condition and results of operations of BSQUARE Corporation.

Dated: August 12, 2021

/s/ Christopher Wheaton
Christopher Wheaton
Chief Financial and Operating Officer, Secretary and Treasurer