# 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: March 31, 2017**

**OR**

o **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: 1-34033**

# DIGI INTERNATIONAL INC.
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| **Delaware** | **41-1532464** |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification Number) |
| **11001 Bren Road East**<br>**Minnetonka, Minnesota** | **55343** |
| (Address of principal executive offices) | (Zip Code) |

**(952) 912-3444**
(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 o

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 o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting 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. (Check one):

| | | | |
|---|---|---|---|
| Large accelerated filer | o | Accelerated filer | ☑ |
| Non-accelerated filer | o (Do not check if a smaller reporting company) | Smaller reporting company | o |
| | | Emerging growth company | o |

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. o

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

On April 30, 2017, there were 26,537,337 shares of the registrant's $.01 par value Common Stock outstanding.

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## PART I. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

### DIGI INTERNATIONAL INC.
### CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
### (UNAUDITED)

| | Three months ended March 31, | | Six months ended March 31, | |
|---|---|---|---|---|
| | 2017 | 2016 | 2017 | 2016 |
| | (in thousands, except per share data) | | | |
| Revenue: | | | | |
| Hardware product | $ 41,766 | $ 48,732 | $ 84,939 | $ 96,979 |
| Service | 3,849 | 1,430 | 5,851 | 3,442 |
| Total revenue | 45,615 | 50,162 | 90,790 | 100,421 |
| Cost of sales: | | | | |
| Cost of hardware product | 21,489 | 24,283 | 43,927 | 48,993 |
| Cost of service | 2,224 | 1,137 | 3,508 | 2,329 |
| Total cost of sales | 23,713 | 25,420 | 47,435 | 51,322 |
| Gross profit | 21,902 | 24,742 | 43,355 | 49,099 |
| Operating expenses: | | | | |
| Sales and marketing | 8,731 | 8,165 | 17,053 | 16,683 |
| Research and development | 6,979 | 7,757 | 13,884 | 15,595 |
| General and administrative | 4,680 | 5,065 | 8,484 | 9,126 |
| Restructuring charge | — | 102 | — | 753 |
| Total operating expenses | 20,390 | 21,089 | 39,421 | 42,157 |
| Operating income | 1,512 | 3,653 | 3,934 | 6,942 |
| Other (expense) income, net: | | | | |
| Interest income | 120 | 130 | 279 | 238 |
| Interest expense | (10) | (118) | (43) | (126) |
| Other (expense) income, net | (143) | (284) | 431 | (161) |
| Total other (expense) income, net | (33) | (272) | 667 | (49) |
| Income from continuing operations, before income taxes | 1,479 | 3,381 | 4,601 | 6,893 |
| Income tax provision | 148 | 1,155 | 913 | 1,536 |
| Income from continuing operations | 1,331 | 2,226 | 3,688 | 5,357 |
| (Loss) income from discontinued operations, after income taxes | — | (89) | — | 3,230 |
| Net income | $ 1,331 | $ 2,137 | $ 3,688 | $ 8,587 |
| | | | | |
| Basic net income per common share: | | | | |
| Continuing operations | $ 0.05 | $ 0.09 | $ 0.14 | $ 0.21 |
| Discontinued operations | $ — | $ — | $ — | $ 0.13 |
| Net income (1) | $ 0.05 | $ 0.08 | $ 0.14 | $ 0.34 |
| Diluted net income per common share: | | | | |
| Continuing operations | $ 0.05 | $ 0.09 | $ 0.14 | $ 0.21 |
| Discontinued operations | $ — | $ — | $ — | $ 0.12 |
| Net income (1) | $ 0.05 | $ 0.08 | $ 0.14 | $ 0.33 |
| Weighted average common shares: | | | | |
| Basic | 26,477 | 25,820 | 26,324 | 25,574 |
| Diluted | 27,252 | 25,998 | 27,134 | 26,116 |

(1) Earnings per share presented are calculated by line item and may not add due to the use of rounded amounts.

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

**DIGI INTERNATIONAL INC.**
**CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**
**(UNAUDITED)**

| | Three months ended March 31, | | Six months ended March 31, | |
|---|---|---|---|---|
| | 2017 | 2016 | 2017 | 2016 |
| | (in thousands) | | | |
| Net income | $ 1,331 | $ 2,137 | $ 3,688 | $ 8,587 |
| Other comprehensive income (loss), net of tax: | | | | |
| Foreign currency translation adjustment | 1,277 | 1,421 | (2,478) | (446) |
| Change in net unrealized gain (loss) on investments | 14 | 106 | (10) | 43 |
| Less income tax (provision) benefit | (5) | (39) | 4 | (16) |
| Reclassification of realized gain on investments included in net income (1) | — | — | — | (7) |
| Less income tax benefit (2) | — | — | — | 3 |
| Other comprehensive income (loss), net of tax | 1,286 | 1,488 | (2,484) | (423) |
| Comprehensive income | $ 2,617 | $ 3,625 | $ 1,204 | $ 8,164 |

(1) Recorded in Other (expense) income, net on our Condensed Consolidated Statements of Operations.
(2) Recorded in Income tax provision in our Condensed Consolidated Statements of Operations.

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

**DIGI INTERNATIONAL INC.**
**CONDENSED CONSOLIDATED BALANCE SHEETS**
**(UNAUDITED)**

| | March 31, 2017 | September 30, 2016 |
|---|---|---|
| | (in thousands, except share data) | |
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | $ 71,895 | $ 75,727 |
| Marketable securities | 36,081 | 58,382 |
| Accounts receivable, net | 28,720 | 28,685 |
| Inventories | 30,519 | 26,276 |
| Receivable from sale of business | 1,978 | 2,997 |
| Other | 4,399 | 3,578 |
| Total current assets | 173,592 | 195,645 |
| Marketable securities, long-term | 2,262 | 3,541 |
| Property, equipment and improvements, net | 13,613 | 14,041 |
| Identifiable intangible assets, net | 13,164 | 4,041 |
| Goodwill | 129,921 | 109,448 |
| Deferred tax assets | 6,974 | 7,295 |
| Receivable from sale of business | — | 1,959 |
| Other | 153 | 196 |
| Total assets | $ 339,679 | $ 336,166 |
| LIABILITIES AND STOCKHOLDERS’ EQUITY | | |
| Current liabilities: | | |
| Accounts payable | $ 10,754 | $ 8,569 |
| Income taxes payable | 131 | 167 |
| Accrued compensation | 4,198 | 10,787 |
| Accrued professional fees | 1,134 | 753 |
| Unearned revenue | 1,636 | 361 |
| Contingent consideration on acquired businesses | 1,234 | 513 |
| Other | 2,703 | 2,658 |
| Total current liabilities | 21,790 | 23,808 |
| Income taxes payable | 1,380 | 1,490 |
| Deferred tax liabilities | 532 | 616 |
| Contingent consideration on acquired businesses | 8,834 | 9,447 |
| Other non-current liabilities | 740 | 776 |
| Total liabilities | 33,276 | 36,137 |
| Contingencies (see Note 11) | | |
| Stockholders’ equity: | | |
| Preferred stock, $.01 par value; 2,000,000 shares authorized; none issued and outstanding | — | — |
| Common stock, $.01 par value; 60,000,000 shares authorized; 32,954,369 and 32,471,175 shares issued | 330 | 325 |
| Additional paid-in capital | 242,836 | 237,492 |
| Retained earnings | 144,800 | 141,112 |
| Accumulated other comprehensive loss | (27,175) | (24,691) |
| Treasury stock, at cost, 6,425,658 and 6,430,797 shares | (54,388) | (54,209) |
| Total stockholders’ equity | 306,403 | 300,029 |
| Total liabilities and stockholders’ equity | $ 339,679 | $ 336,166 |

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

**DIGI INTERNATIONAL INC.**
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**
**(UNAUDITED)**

| | Six months ended March 31, | |
|---|---|---|
| | 2017 | 2016 |
| | (in thousands) | |
| Operating activities: | | |
| Net income | $ 3,688 | $ 8,587 |
| Adjustments to reconcile net income to net cash (used in) provided by operating activities: | | |
| Depreciation of property, equipment and improvements | 1,449 | 1,405 |
| Amortization of identifiable intangible assets | 941 | 1,001 |
| Stock-based compensation | 2,328 | 1,719 |
| Excess tax benefits from stock-based compensation | (315) | (202) |
| Deferred income tax provision | 242 | 1,397 |
| Gain on sale of business | — | (2,870) |
| Change in fair value of contingent consideration | (684) | 123 |
| Bad debt/product return provision | 296 | 168 |
| Inventory obsolescence | 600 | 834 |
| Restructuring charges | — | 753 |
| Other | 51 | 59 |
| Changes in operating assets and liabilities (net of acquisitions) | (9,473) | (1,486) |
| Net cash (used in) provided by operating activities | (877) | 11,488 |
| Investing activities: | | |
| Purchase of marketable securities | (33,470) | (22,056) |
| Proceeds from maturities and sales of marketable securities | 57,039 | 27,509 |
| Proceeds from sale of Etherios | 3,000 | 2,849 |
| Acquisition of businesses, net of cash acquired | (29,994) | (2,860) |
| Purchase of property, equipment, improvements and certain other identifiable intangible assets | (984) | (1,209) |
| Net cash (used in) provided by investing activities | (4,409) | 4,233 |
| Financing activities: | | |
| Acquisition earn-out payments | (518) | — |
| Excess tax benefits from stock-based compensation | 315 | 202 |
| Proceeds from stock option plan transactions | 3,246 | 6,267 |
| Proceeds from employee stock purchase plan transactions | 479 | 494 |
| Purchases of common stock | (587) | (503) |
| Net cash provided by financing activities | 2,935 | 6,460 |
| Effect of exchange rate changes on cash and cash equivalents | (1,481) | 71 |
| Net (decrease) increase in cash and cash equivalents | (3,832) | 22,252 |
| Cash and cash equivalents, beginning of period | 75,727 | 45,018 |
| Cash and cash equivalents, end of period | $ 71,895 | $ 67,270 |
| | | |
| Supplemental schedule of non-cash investing and financing activities: | | |
| Receivable related to sale of Etherios | $ — | $ 4,906 |
| Liability related to acquisition of businesses | $ (1,310) | $ (10,550) |
| Accrual for purchase of property, equipment, improvements and certain other identifiable intangible assets | $ (66) | $ — |

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

**DIGI INTERNATIONAL INC.**
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(UNAUDITED)**

1. BASIS OF PRESENTATION OF UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS AND SIGNIFICANT ACCOUNTING POLICIES

*Basis of Presentation*

The interim unaudited condensed consolidated financial statements included in this Form 10-Q have been prepared by Digi International Inc. (the "Company," "Digi," "we," "our," or "us") pursuant to the rules and regulations of the United States Securities and Exchange Commission (the "SEC"). Certain information and footnote disclosures, normally included in consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP"), have been condensed or omitted pursuant to such rules and regulations. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes thereto, including (but not limited to) the summary of significant accounting policies, presented in our Annual Report on Form 10-K for the year ended September 30, 2016, as filed with the SEC ("2016 Financial Statements").

The condensed consolidated financial statements presented herein reflect, in the opinion of management, all adjustments which consist only of normal, recurring adjustments necessary for a fair presentation of the condensed consolidated balance sheets and condensed consolidated statements of operations, comprehensive income and cash flows for the periods presented. The condensed consolidated results of operations for any interim period are not necessarily indicative of results for the full year. The year-end condensed consolidated balance sheet data were derived from our 2016 Financial Statements, but do not include all disclosures required by U.S. GAAP.

*Reclassifications*

Certain prior year amounts have been reclassified to conform to our fiscal year 2017 presentation. On the Condensed Consolidated Balance Sheet for the period ended September 30, 2016, Unearned revenue and Accrued professional fees have been reclassified from Other current liabilities to its own respective line item. In the Condensed Consolidated Cash Flows, for the six months ended March 31, 2016, the Change in fair value of contingent consideration within the Operating activities was reclassified from Other to its own line item. These reclassifications had no impact on our consolidated net sales or our consolidated net income.

*Recently Issued Accounting Pronouncements*

*Not Yet Adopted*

In January 2017, the Financial Accounting Standards Board ("FASB") issued ASU 2017-04, "Intangibles-Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment." ASU 2017-04 eliminates the second step in the goodwill impairment test which requires an entity to determine the implied fair value of the reporting unit's goodwill. Instead, an entity should perform its annual or interim goodwill impairment test by comparing the fair value of a reporting unit with its carrying value and recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit's fair value, not to exceed the total amount of goodwill allocated to the reporting unit. The standard, which should be applied prospectively, is effective for fiscal years beginning after December 15, 2019, which for us is our fiscal year beginning October 1, 2020. Early adoption is permitted. We are currently evaluating the impact of the adoption of ASU 2017-04 on our consolidated financial statements.

In August 2016, FASB issued ASU 2016-15, "Statement of Cash Flows (Topic 230), Classification of Certain Cash Receipts and Cash Payments." The amendments in this update provide guidance on eight specific cash flow issues, thereby reducing the diversity in practice in how certain transaction are classified in the statement of cash flows. This ASU is effective for annual periods and interim periods for those annual periods beginning after December 15, 2017, which for us is the first quarter ended December 31, 2018. Early adoption is permitted. We are currently evaluating the impact of the adoption of ASU 2016-15 on our consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, "Financial Instruments - Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments." The amendments in this update replace the incurred loss impairment methodology in current U.S. GAAP with a methodology that reflects expected credit losses. This update is intended to provide financial statement users with more decision-useful information about the expected credit losses. This ASU is effective for annual periods and interim periods for those annual periods beginning after December 15, 2019, which for us is the first quarter ended

1. BASIS OF PRESENTATION OF UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

December 31, 2020. Entities may early adopt beginning after December 15, 2018. We are currently evaluating the impact of the adoption of ASU 2016-13 on our consolidated financial statements.

In March 2016, FASB issued ASU 2016-09, “Improvements to Employee Share-Based Payment Accounting.” This update includes provisions intended to simplify various aspects related to how share-based payments are accounted for and presented in the financial statements. This ASU is effective for annual periods and interim periods within those annual periods beginning after December 15, 2016, which for us is the first fiscal quarter ending December 31, 2017. Early adoption is permitted. We will adopt ASU 2016-09 beginning October 1, 2017. We are currently evaluating the impact of the adoption of ASU 2016-09 on our consolidated financial statements. Prospectively, beginning October 1, 2017, excess tax benefits and tax deficiencies will be reflected as income tax benefit or expense in our Consolidated Statement of Operations and could result in a material impact. The extent of the excess tax benefits or tax deficiencies are subject to variation in our stock price and the timing of restricted stock unit (“RSU”) vestings and employee stock option exercises.

In February, 2016, FASB issued ASU 2016-02, “Leases (Topic 842)”, which amends the existing guidance to require lessees to recognize lease assets and lease liabilities from operating leases on the balance sheet. This ASU is effective using the modified retrospective approach for annual periods and interim periods within those annual periods beginning after December 15, 2018, which for us is the first fiscal quarter ending December 31, 2019. Early adoption is permitted. We are currently evaluating the impact of the adoption of ASU 2016-02 on our consolidated financial statements.

In January 2016, FASB issued ASU 2016-01, “Financial Instruments - Overall: Recognition and Measurement of Financial Assets and Financial Liabilities.” ASU 2016-01 will require equity investments in unconsolidated entities (other than those accounted for using the equity method of accounting) to be measured at fair value with changes in fair value recognized in net income. The amendments in this update will also simplify the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment, eliminate the requirement for public business entities to disclose the method and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet and require these entities to use the exit price notion when measuring fair value of financial instruments for disclosure purposes. This ASU would also change the presentation and disclosure requirements for financial instruments. In addition, this ASU clarifies the guidance related to valuation allowance assessment when recognizing deferred tax assets resulting from unrealized losses on available-for-sale debt securities. The amendments in this ASU are effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years, which for us is the first fiscal quarter ending December 31, 2018. Early adoption is permitted for financial statements of fiscal years and interim periods that have not been issued. We are currently evaluating the impact of the adoption of ASU 2016-01.

In July 2015, FASB issued ASU 2015-11, “Simplifying the Measurement of Inventory.” This provision would require inventory that was previously recorded using first-in, first-out (“FIFO”) to be recorded at lower of cost or net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. This guidance is effective for fiscal years beginning after December 15, 2016 and interim periods within those years, which for us will be the first fiscal quarter ending December 31, 2017. The amendments in this guidance should be applied prospectively with earlier application permitted as of the beginning of an interim or annual period. We are currently evaluating the impact of the adoption of ASU 2015-11 and whether it would have a material impact on our consolidated financial statements.

In August 2014, FASB issued ASU 2014-15, “Presentation of Financial Statements - Going Concern.” This guidance requires management to evaluate whether there is substantial doubt about a company’s ability to continue as a going concern and to provide related footnote disclosures. These amendments are effective for the annual period ending after December 15, 2016, and for annual periods and interim periods thereafter, which for us, will be our annual period ended September 30, 2017. Early adoption is permitted. While we are evaluating the impact of the adoption of ASU 2014-15, we do not expect it to have an impact on our consolidated financial statements.

In May 2014, FASB issued ASU 2014-09, “Revenue from Contracts with Customers.” This guidance provides a five-step analysis in determining when and how revenue is recognized so that an entity will recognize revenue when it transfers promised goods or services to customers in an amount that reflects what it expects in exchange for the goods and services. It also requires more detailed disclosures to enable users of financial statements to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. In August 2015, the FASB issued ASU 2015-14 “Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date” which approved a one-year deferral of

1. BASIS OF PRESENTATION OF UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

the effective date of ASU 2014-09. As a result of this deferral, ASU 2014-09 is effective for our fiscal 2019, including interim periods within that reporting period. The FASB also agreed to allow us to choose to adopt the standard effective for our fiscal 2018. In addition, the FASB issued ASU 2016-08, ASU 2016-10 and ASU 2016-12 in March 2016, April 2016 and May 2016, respectively, to provide interpretive clarifications on the new guidance in ASC Topic 606. We are currently working through an adoption plan and have identified our revenue streams and completed a preliminary analysis of how we currently account for revenue transactions compared to the revenue accounting required under the new standard. We intend to complete our adoption plan in fiscal 2017. This plan includes a review of transactions supporting each revenue stream to determine the impact of accounting treatment under ASC 606, evaluation of the method of adoption, and completing a rollout plan for implementation of the new standard with affected functions in our organization. Because of the nature of the work that remains, at this time we are unable to reasonably estimate the impact of adoption on our consolidated financial statements. We plan to adopt the new guidance beginning October 1, 2018.

2. ACQUISITIONS

On May 4, 2017, we announced the rebranding of our Digi Cold Chain Solutions to Digi Smart Solutions™ group.

*Acquisition of SMART Temps, LLC*

On January 9, 2017, we purchased all of the outstanding interests of SMART Temps, LLC (“SMART Temps”), an Indiana-based provider of real-time temperature management for pharmacies, education, and hospital settings as well as real-time temperature management for blood bank, laboratory environments, restaurants, and grocery. We believe this is a complementary acquisition for us as the acquired technology will continue to be supported to further enhance our portfolio of products for the Digi Smart Solution’s market.

The terms of the acquisition included an upfront cash payment together with future earn-out payments. Cash of $28.8 million (excluding cash acquired of $0.5 million) was paid at time of closing. The earn-out payments are scheduled to be paid after December 31, 2017 which is the end of the earn-out period. The cumulative amount of these earn-out payments will not exceed $7.2 million. The fair value of this contingent consideration was $10,000 at the date of acquisition and March 31, 2017 (see Note 7 to the Condensed Consolidated Financial Statements). We have determined that the earn-out will be considered as part of the purchase price consideration as there are no continuing employment requirements associated with the earn-out.

The purchase price was allocated to the estimated fair value of assets acquired and liabilities assumed. The preliminary purchase price allocation resulted in the recognition of $18.6 million of goodwill. For tax purposes, this acquisition is treated as an asset acquisition, therefore the goodwill is deductible. We believe that the acquisition resulted in the recognition of goodwill because this is a complementary acquisition for us and will provide a source of recurring revenue in a new vertically focused solutions business.

The SMART Temps acquisition has been accounted for using the acquisition method of accounting which requires, among other things, that assets acquired and liabilities assumed pursuant to the purchase agreement be recognized at fair value as of the acquisition date. The following table summarizes the preliminary values of SMART Temps assets acquired and liabilities assumed as of the acquisition date (in thousands):

| | | |
|---|---|---|
| Cash | $ | 28,754 |
| Fair value of contingent consideration on acquired business | | 10 |
| Total purchase price consideration | $ | 28,764 |

| | | |
|---|---|---|
| Fair value of net tangible assets acquired | $ | 897 |
| Fair value of identifiable intangible assets acquired: | | |
| Purchased and core technology | | 4,000 |
| Customer relationships | | 4,000 |
| Trade name and trademarks | | 711 |
| Non-compete agreements | | 600 |
| Goodwill | | 18,556 |
| Total | $ | 28,764 |

2. ACQUISITIONS (CONTINUED)

Operating results for SMART Temps are included in our Condensed Consolidated Statements of Operations from January 9, 2017. The Condensed Consolidated Balance Sheet as of March 31, 2017 reflects the preliminary allocation of the purchase price to the assets acquired and liabilities assumed based on their estimated fair values at the date of acquisition. The purchase price may vary as the identifiable intangibles values and net working capital values are preliminary, and we expect to finalize them by the end of fiscal 2017.

As of the date of acquisition, the weighted average useful life for all the identifiable intangibles listed above was 10.5 years. For purposes of determining fair value, the purchased and core technology identified above is assumed to have a useful life of ten years, the customer relationships are assumed to have useful lives of twelve years, the trade name and trademarks are assumed to have useful lives of ten years and the non-compete agreements are assumed to have useful lives of five years. Useful lives for identifiable intangible assets are estimated at the time of acquisition based on the periods of time from which we expect to derive benefits from the identifiable intangible assets.

The amounts of revenue and net loss included in the Condensed Consolidated Statements of Operations from the acquisition date of January 9, 2017 were $1.3 million and $(0.4) million, respectively. Costs directly related to the acquisition, including legal, accounting and valuation fees of approximately $0.8 million have been charged directly to operations and are included in general and administrative expense in our Condensed Consolidated Statements of Operations.

The following consolidated pro forma information is as if the acquisition had occurred on October 1, 2015 (in thousands):

| | Three months ended March 31, | Six months ended March 31, | |
|---|---|---|---|
| | 2016 | 2017 | 2016 |
| Revenue | $ 51,041 | $ 91,724 | $ 103,011 |
| Income from continuing operations | $ 1,892 | $ 3,112 | $ 4,804 |
| Net income | $ 1,803 | $ 3,112 | $ 8,034 |

Pro forma income from continuing operations and net income were both adjusted to exclude interest expense related to debt that was paid off prior to acquisition, adjust amortization to the fair value of the intangibles acquired and remove any costs that SMART Temps incurred associated with the sale transaction.

*Acquisition of FreshTemp, LLC*

On November 1, 2016, we purchased all of the outstanding interests of FreshTemp, LLC (“FreshTemp”), a Pittsburgh-based provider of temperature monitoring and task management solutions for the food industry. We believe this is a complementary acquisition for us as the acquired technology will continue to be supported to create an advanced portfolio of products for the Digi Smart Solution's market.

The terms of the acquisition included an upfront cash payment together with future earn-out payments and a holdback amount. Cash of $1.7 million was paid at time of closing. The earn-out payments are based on revenue related to certain customer contracts entered into by June 30, 2017. The final calculation date will be on June 30, 2018. The cumulative amount of these earn-out payments will not exceed $2.3 million. The fair value of this contingent consideration was $1.3 million at the date of acquisition and $1.5 million at March 31, 2017 (see Note 7 to the Condensed Consolidated Financial Statements). We have determined that the earn-out will be considered as part of the purchase price consideration as there are no continuing employment requirements associated with the earn-out. Costs directly related to the acquisition, including legal, accounting and valuation fees, of approximately $50,000 have been charged directly to operations and are included in general and administrative expense in our Condensed Consolidated Statements of Operations.

The purchase price was allocated to the estimated fair value of assets acquired and liabilities assumed. The purchase price allocation resulted in the recognition of $2.7 million of goodwill. For tax purposes, this acquisition is treated as an asset acquisition, therefore the goodwill is deductible. We believe that the acquisition resulted in the recognition of goodwill because this is a complementary acquisition for us and will provide a source of recurring revenue in a new vertically focused solutions business.

The FreshTemp acquisition has been accounted for using the acquisition method of accounting which requires, among other things, that assets acquired and liabilities assumed pursuant to the purchase agreement be recognized at fair value as of the acquisition date.

2. ACQUISITIONS (CONTINUED)

The following table summarizes the final values of FreshTemp assets acquired and liabilities assumed as of the acquisition date (in thousands):

| | | |
|---|---|---|
| Cash | $ | 1,697 |
| Purchase price payable upon completion of diligence matters | | 303 |
| Fair value of contingent consideration on acquired business | | 1,300 |
| Working capital adjustment | | (37) |
| Total purchase price consideration | $ | 3,263 |
| | | |
| Fair value of net tangible assets acquired | $ | (37) |
| Fair value of identifiable intangible assets acquired: | | |
| Purchased and core technology | | 400 |
| Customer relationships | | 250 |
| Goodwill | | 2,650 |
| Total | $ | 3,263 |

Operating results for FreshTemp are included in our Condensed Consolidated Statements of Operations from November 1, 2016. The Condensed Consolidated Balance Sheet as of March 31, 2017 reflects the final allocation of the purchase price to the assets acquired and liabilities assumed based on their estimated fair values at the date of acquisition. The identifiable intangibles values and net working capital values were finalized in the second fiscal quarter of 2017.

The weighted average useful life for all the identifiable intangibles listed above is 5.8 years. For purposes of determining fair value, the purchased and core technology identified above is assumed to have a useful life of five years and the customer relationships are assumed to have useful lives of seven years. Useful lives for identifiable intangible assets are estimated at the time of acquisition based on the periods of time from which we expect to derive benefits from the identifiable intangible assets.

Since the FreshTemp acquisition occurred close to the beginning of our fiscal 2017, the pro forma amounts would not be materially different from actual amounts. Revenue for both the three and six months ended March 31, 2017 related to the FreshTemp acquisition was $0.2 million. As our operating costs related to the FreshTemp acquisition are integrated into the Company’s operating income and related earnings per share, the separate FreshTemp amounts are not determinable for fiscal 2017. Pro forma information for fiscal 2016 was not materially different from actual amounts.

*Acquisition of Bluenica Corporation*

On October 5, 2015, we purchased all of the outstanding stock of Bluenica Corporation (“Bluenica”), a company focused on temperature monitoring of perishable goods in the food industry by using wireless sensors, which are installed in grocery and convenience stores, restaurants, and in products during shipment and storage to ensure that quality, freshness and public health requirements are met.  This acquisition formed the basis for our Digi Smart Solutions.

The terms of the acquisition included an upfront cash payment together with earn-out payments.  Cash of $2.9 million was paid at time of closing.  The earn-out payments are scheduled to be paid in installments over a four-year period based on revenue achievement of the acquired business. Each of the earn-out payments will be calculated based on the revenue performance of Digi Smart Solutions for each respective earn-out period. The cumulative amount of these earn-out payments will not exceed $11.6 million.  An additional payment, not to exceed $3.5 million, may also be due depending on revenue performance.

The fair value of this contingent consideration was $10.4 million at the date of acquisition and $8.6 million at March 31, 2017 (see Note 7 to the Condensed Consolidated Financial Statements). We have determined that the earn-out will be considered as part of the purchase price consideration as there are no continuing employment requirements associated with the earn-out.

The purchase price was allocated to the estimated fair value of assets acquired and liabilities assumed. The purchase price allocation resulted in the recognition of $11.0 million of goodwill. We believe that the acquisition resulted in the recognition of goodwill because this is a complementary acquisition for us and will provide a source of recurring revenue in a new vertically focused solutions business. Operating results for Bluenica are included in our Condensed Consolidated Statements of Operations from October 6, 2015.

3. DISCONTINUED OPERATIONS

On October 23, 2015, we sold all the outstanding stock of our wholly owned subsidiary, Etherios Inc. ("Etherios") to West Monroe Partners, LLC. We sold Etherios as part of a strategy to focus on providing highly reliable machine connectivity solutions for business and mission-critical application environments. Etherios was included in our single operating segment.

The terms of the sale agreement provided that West Monroe Partners, LLC would pay us $3.0 million on October 23, 2016 and $2.0 million on October 23, 2017. The present value of these amounts was included within the total fair value of consideration received. These receivable amounts are unsecured and non-interest bearing. We received $3.0 million in October 2016. The carrying value of the remaining receivable of $2.0 million presented on our Condensed Consolidated Balance Sheet at March 31, 2017 approximates its fair value, which was determined using Level 3 cash flow fair value measurement techniques.

Goodwill was included in the net assets of Etherios based on the relative fair value of Etherios compared to the fair value of the Company, as the Company consists of a single reporting unit for goodwill impairment testing purposes.

As a condition to the sale agreement, we retained the operating leases in the Dallas and Chicago locations. Digi ceased using these facilities in October 2015 and has sublet the Dallas location to West Monroe Partners, LLC through December 31, 2017. In January 2017, we signed an early-termination agreement along with an immaterial payment to exit our Chicago lease. Also in connection with the sale, we assigned our San Francisco lease to West Monroe Partners, LLC.

Income from discontinued operations, after income taxes, as presented in the Condensed Consolidated Statements of Operations for the three and six months ended March 31, 2016 is as follows (in thousands):

| | Three months ended March 31, 2016 | Six months ended March 31, 2016 |
|---|---|---|
| Service revenue | $ — | $ 891 |
| Cost of service | — | 713 |
| Gross profit | — | 178 |
| Operating expenses: | | |
| Sales and marketing | — | 148 |
| Research and development | — | 103 |
| General and administrative | — | 43 |
| Total operating expenses | — | 294 |
| Loss from discontinued operations, before income taxes | — | (116) |
| (Loss) gain on sale of discontinued operations, before income taxes | (42) | 2,870 |
| Total (loss) income from discontinued operations, before income taxes | (42) | 2,754 |
| Income tax expense (benefit) on discontinued operations | 47 | (476) |
| (Loss) income from discontinued operations, after income taxes | $ (89) | $ 3,230 |

Income tax benefit on discontinued operations for the six months ended March 31, 2016, was $0.5 million, which primarily represented income tax benefits for deductible transaction costs, partially offset by a tax expense for equity awards for which we will not receive a tax deduction. For tax purposes, this transaction resulted in a capital loss, as the tax basis of the Etherios stock was higher than the book basis of the assets that were sold. Since we do not expect to be able to utilize this capital loss in the five year carryforward period, a deferred tax asset offset by a full valuation allowance was recorded in the third quarter of fiscal 2016 upon completion of the capital loss calculation.

The following table presents amortization, depreciation and purchases of property, equipment, improvements and certain other identifiable intangible assets of the discontinued operations related to Etherios (in thousands):

| | Six months ended March 31, 2016 |
|---|---|
| Amortization of identifiable intangible assets | $ 30 |
| Depreciation of property, equipment and improvements | $ — |
| Purchases of property, equipment, improvements and certain other identifiable intangible assets | $ — |

4. EARNINGS PER SHARE

Basic net income per common share is calculated based on the weighted average number of common shares outstanding during the period. Diluted net income per common share is computed by dividing net income by the weighted average number of common shares and potentially dilutive common shares outstanding during the period. Potentially dilutive common shares result from dilutive common stock options and restricted stock units. The following table is a reconciliation of the numerators and denominators in the net income per common share calculations (in thousands, except per common share data):

| | Three months ended March 31, | | Six months ended March 31, | |
|---|---|---|---|---|
| | 2017 | 2016 | 2017 | 2016 |
| Numerator: | | | | |
| Income from continuing operations | $ 1,331 | $ 2,226 | $ 3,688 | $ 5,357 |
| (Loss) income from discontinued operations, after income taxes | — | (89) | — | 3,230 |
| Net income | $ 1,331 | $ 2,137 | $ 3,688 | $ 8,587 |
| Denominator: | | | | |
| Denominator for basic net income per common share — weighted average shares outstanding | 26,477 | 25,820 | 26,324 | 25,574 |
| Effect of dilutive securities: | | | | |
| Stock options and restricted stock units | 775 | 178 | 810 | 542 |
| Denominator for diluted net income per common share — adjusted weighted average shares | 27,252 | 25,998 | 27,134 | 26,116 |
| Basic net income per common share: | | | | |
| Continuing operations | $ 0.05 | $ 0.09 | $ 0.14 | $ 0.21 |
| Discontinued operations | $ — | $ — | $ — | $ 0.13 |
| Net income (1) | $ 0.05 | $ 0.08 | $ 0.14 | $ 0.34 |
| Diluted net income per common share: | | | | |
| Continuing operations | $ 0.05 | $ 0.09 | $ 0.14 | $ 0.21 |
| Discontinued operations | $ — | $ — | $ — | $ 0.12 |
| Net income (1) | $ 0.05 | $ 0.08 | $ 0.14 | $ 0.33 |

(1) Earnings per share presented are calculated by line item and may not add due to the use of rounded amounts.

For the three months ended March 31, 2017 and 2016, there were 730,400 and 2,735,177 potentially dilutive shares, respectively, and for the six months ended March 31, 2017 and 2016, there were 1,077,150 and 1,495,104 potentially dilutive shares, respectively, related to stock options to purchase common shares that were not included in the above computation of diluted earnings per common share. This is because the options' exercise prices were greater than the average market price of our common shares.

5. SELECTED BALANCE SHEET DATA

The following table shows selected balance sheet data (in thousands):

| | March 31, 2017 | September 30, 2016 |
|---|---|---|
| Accounts receivable, net: | | |
| Accounts receivable | $ 31,195 | $ 30,885 |
| Less allowance for doubtful accounts | 257 | 209 |
| Less reserve for future returns and pricing adjustments | 2,218 | 1,991 |
| Accounts receivable, net | $ 28,720 | $ 28,685 |
| Inventories: | | |
| Raw materials | $ 23,922 | $ 21,116 |
| Work in process | 591 | 802 |
| Finished goods | 6,006 | 4,358 |
| Inventories | $ 30,519 | $ 26,276 |

Inventories are stated at the lower of cost or market value, with cost determined using the first-in, first-out method.

6. MARKETABLE SECURITIES

Our marketable securities consist of certificates of deposit, commercial paper, corporate bonds and government municipal bonds. We analyze our available-for-sale marketable securities for impairment on an ongoing basis. When we perform this analysis, we consider factors such as the length of time and extent to which the securities have been in an unrealized loss position and the trend of any unrealized losses. We also consider whether an unrealized loss is a temporary loss or an other-than-temporary loss based on factors such as: (a) whether we have the intent to sell the security, (b) whether it is more likely than not that we will be required to sell the security before its anticipated recovery, or (c) permanent impairment due to bankruptcy or insolvency.

In order to estimate the fair value for each security in our investment portfolio, we obtain quoted market prices and trading activity for each security where available. We obtain relevant information from our investment advisor and, if warranted, also may review the financial solvency of certain security issuers. As of March 31, 2017, 14 of our 42 securities that we held were trading below our amortized cost basis. We determined each decline in value to be temporary based upon the above described factors. We expect to realize the fair value of these securities, plus accrued interest, either at the time of maturity or when the security is sold. All of our current holdings are classified as available-for-sale marketable securities and are recorded at fair value on our consolidated balance sheet with the unrealized gains and losses recorded in accumulated other comprehensive income (loss). All of our current marketable securities will mature in less than one year and our non-current marketable securities will mature in less than two years. Our balance sheet classification of available for sale securities is based on our best estimate of when we expect to liquidate such investments and, presently, is consistent with the stated maturity dates of such investments. However, we are not committed to holding these investments until their maturity and may determine to liquidate some or all of these investments earlier based on our liquidity and other needs. During the six months ended March 31, 2017 and 2016, we received proceeds from our available-for-sale marketable securities of $57.0 million and $27.5 million, respectively.

6. MARKETABLE SECURITIES (CONTINUED)

At March 31, 2017 our marketable securities were (in thousands):

| | Amortized Cost (1) | Unrealized Gains | Unrealized Losses | Fair Value (1) |
|---|---|---|---|---|
| Current marketable securities: | | | | |
| Corporate bonds | $ 25,360 | $ — | $ (29) | $ 25,331 |
| Commercial paper | 5,988 | — | (2) | 5,986 |
| Certificates of deposit | 4,757 | 7 | — | 4,764 |
| Current marketable securities | 36,105 | 7 | (31) | 36,081 |
| Non-current marketable securities: | | | | |
| Certificates of deposit | 2,253 | 9 | — | 2,262 |
| Total marketable securities | $ 38,358 | $ 16 | $ (31) | $ 38,343 |

(1) Included in amortized cost and fair value is purchased and accrued interest of $189.

At September 30, 2016 our marketable securities were (in thousands):

| | Amortized Cost (1) | Unrealized Gains | Unrealized Losses | Fair Value (1) |
|---|---|---|---|---|
| Current marketable securities: | | | | |
| Corporate bonds | $ 28,801 | $ — | $ (34) | $ 28,767 |
| Commercial paper | 23,963 | — | (20) | 23,943 |
| Certificates of deposit | 3,755 | 13 | — | 3,768 |
| Government municipal bonds | 1,904 | — | — | 1,904 |
| Current marketable securities | 58,423 | 13 | (54) | 58,382 |
| Non-current marketable securities: | | | | |
| Certificates of deposit | 3,505 | 36 | — | 3,541 |
| Total marketable securities | $ 61,928 | $ 49 | $ (54) | $ 61,923 |

(1) Included in amortized cost and fair value is purchased and accrued interest of $271.

The following tables show the fair values and gross unrealized losses of our available-for-sale marketable securities that have been in a continuous unrealized loss position deemed to be temporary, aggregated by investment category (in thousands):

| | March 31, 2017 | | | |
|---|---|---|---|---|
| | Less than 12 Months | | More than 12 Months | |
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| Corporate bonds | $ 25,331 | $ (29) | $ — | $ — |
| Commercial paper | 5,986 | (2) | — | — |
| Total | $ 31,317 | $ (31) | $ — | $ — |

| | September 30, 2016 | | | |
|---|---|---|---|---|
| | Less than 12 Months | | More than 12 Months | |
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| Corporate bonds | $ 24,454 | $ (33) | $ 4,102 | $ (1) |
| Commercial paper | 23,943 | (20) | — | — |
| Total | $ 48,397 | $ (53) | $ 4,102 | $ (1) |

7. FAIR VALUE MEASUREMENTS

Fair value is defined as the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants as of the measurement date. This standard also establishes a hierarchy for inputs used in measuring fair value. This standard maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs are inputs market participants would use in valuing the asset or liability based on market data obtained from independent sources. Unobservable inputs are inputs that reflect our assumptions about the factors market participants would use in valuing the asset or liability based upon the best information available in the circumstances.

The categorization of financial assets and liabilities within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. The hierarchy is broken down into three levels. Level 1 inputs are quoted prices in active markets for identical assets or liabilities. Level 2 inputs include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, and inputs (other than quoted prices) that are observable for the asset or liability, either directly or indirectly. Level 3 inputs are unobservable for the asset or liability and their fair values are determined using pricing models, discounted cash flow methodologies or similar techniques and at least one significant model assumption or input is unobservable. Level 3 may also include certain investment securities for which there is limited market activity or a decrease in the observability of market pricing for the investments, such that the determination of fair value requires significant judgment or estimation.

Fair value is applied to financial assets such as our marketable securities, which are classified and accounted for as available-for-sale and to financial liabilities for contingent consideration. These items are stated at fair value at each reporting period using the above guidance.

The following tables provide information by level for financial assets and liabilities that are measured at fair value on a recurring basis (in thousands):

| | Total Fair Value at | Fair Value Measurements Using Inputs Considered as | | |
|---|---|---|---|---|
| | March 31, 2017 | Level 1 | Level 2 | Level 3 |
| Assets: | | | | |
| Money market | $ 37,125 | $ 37,125 | $ — | $ — |
| Corporate bonds | 25,331 | — | 25,331 | — |
| Commercial paper | 5,986 | — | 5,986 | — |
| Certificates of deposit | 7,026 | — | 7,026 | — |
| Total assets measured at fair value | $ 75,468 | $ 37,125 | $ 38,343 | $ — |
| Liabilities: | | | | |
| Contingent consideration on acquired businesses | 10,068 | $ — | $ — | $ 10,068 |
| Total liabilities measured at fair value | $ 10,068 | $ — | $ — | $ 10,068 |

| | Total Fair Value at | Fair Value Measurements Using Inputs Considered as | | |
|---|---|---|---|---|
| | September 30, 2016 | Level 1 | Level 2 | Level 3 |
| Assets: | | | | |
| Money market | $ 44,319 | $ 44,319 | $ — | $ — |
| Corporate bonds | 28,767 | — | 28,767 | — |
| Commercial paper | 23,943 | — | 23,943 | — |
| Certificates of deposit | 7,309 | — | 7,309 | — |
| Government municipal bonds | 1,904 | — | 1,904 | — |
| Total assets measured at fair value | $ 106,242 | $ 44,319 | $ 61,923 | $ — |
| Liabilities: | | | | |
| Contingent consideration on acquired businesses | $ 9,960 | $ — | $ — | $ 9,960 |
| Total liabilities measured at fair value | $ 9,960 | $ — | $ — | $ 9,960 |

7. FAIR VALUE MEASUREMENTS (CONTINUED)

Our money market funds, which have been determined to be cash equivalents, are measured at fair value using quoted market prices in active markets for identical assets and are therefore classified as Level 1 assets. We value our Level 2 assets using inputs that are based on market indices of similar assets within an active market. There were no transfers into or out of our Level 2 financial assets during the six months ended March 31, 2017.

The use of different assumptions, applying different judgment to matters that inherently are subjective and changes in future market conditions could result in different estimates of fair value of our securities or contingent consideration, currently and in the future. If market conditions deteriorate, we may incur impairment charges for securities in our investment portfolio. We may also incur changes to our contingent consideration liability as discussed below.

As discussed in Note 2, we are required to make contingent payments for our acquisitions. In connection with the Bluenica acquisition, we are required to make contingent payments over a period of up to four years, subject to Digi Smart Solutions achieving specified revenue thresholds. The fair value of the liability for contingent payments recognized upon acquisition was $10.4 million. In connection with the FreshTemp acquisition, we are required to make a contingent payment after June 30, 2018, for revenue related to specific customer contracts signed by June 30, 2017. The fair value of the liability recognized upon acquisition was $1.3 million. For the SMART Temps acquisition, we are required to make a contingent payment after December 31, 2017 based on achieving specified revenue thresholds. The fair value of the liability for contingent payments recognized upon acquisition was $10,000. The fair values of these contingent payments was estimated by discounting to present value the probability-weighted contingent payments expected to be made. Assumptions used in these calculations include the discount rate and various probability factors. This liability is considered to be a Level 3 financial liability that is re-measured each reporting period as a charge or credit to general and administrative expense within the Condensed Consolidated Statements of Operations.

The following table presents a reconciliation of the contingent consideration liability measured at fair value on a recurring basis using significant unobservable inputs (Level 3) (in thousands):

| | Three months ended March 31, | | Six months ended March 31, | |
|---|---|---|---|---|
| | 2017 | 2016 | 2017 | 2016 |
| Fair value at beginning of period | $ 10,660 | $ 10,400 | $ 9,960 | $ — |
| Purchase price contingent consideration | 10 | — | 1,310 | 10,400 |
| Contingent consideration payments | — | — | (518) | — |
| Change in fair value of contingent consideration | (602) | 122 | (684) | 122 |
| Fair value at end of period | $ 10,068 | $ 10,522 | $ 10,068 | $ 10,522 |

The change in fair value of contingent consideration relates to the acquisitions of Bluenica, FreshTemp and SMART Temps and is included in general and administrative expense. The change in fair value of contingent consideration reflects our estimate of the probability of achieving the relevant targets and is discounted based on our estimated discount rate. We have estimated the fair value of the contingent consideration based on the probability of achieving the specified revenue thresholds at 94.8% to 98.0% for Bluenica, between 25% and 100% for FreshTemp and 0.4% for SMART Temp. A significant increase (decrease) in our estimates of achieving the relevant targets could materially increase (decrease) the fair value of the contingent consideration liability.

## 8. GOODWILL AND OTHER IDENTIFIABLE INTANGIBLE ASSETS, NET

Amortizable identifiable intangible assets were (in thousands):

| | March 31, 2017 | | | September 30, 2016 | | |
|---|---|---|---|---|---|---|
| | Gross carrying amount | Accum. amort. | Net | Gross carrying amount | Accum. amort. | Net |
| Purchased and core technology | $ 50,720 | $ (45,079) | $ 5,641 | $ 46,594 | $ (44,999) | $ 1,595 |
| License agreements | 18 | (12) | 6 | 18 | (10) | 8 |
| Patents and trademarks | 12,334 | (10,974) | 1,360 | 11,619 | (10,871) | 748 |
| Customer relationships | 21,517 | (15,930) | 5,587 | 17,463 | (15,773) | 1,690 |
| Non-compete agreements | 600 | (30) | 570 | — | — | — |
| Total | $ 85,189 | $ (72,025) | $ 13,164 | $ 75,694 | $ (71,653) | $ 4,041 |

Amortization expense was $0.6 million and $0.5 million for the three month periods ended March 31, 2017 and 2016, respectively. Amortization expense was $0.9 million and $1.0 million for the six month periods ended March 31, 2017 and 2016, respectively. Amortization expense is recorded on our consolidated statements of operations within cost of sales and in general and administrative expense. Estimated amortization expense related to identifiable intangible assets for the remainder of fiscal 2017 and the five succeeding fiscal years is (in thousands):

| | |
|---|---|
| 2017 (six months) | $ 1,255 |
| 2018 | 2,475 |
| 2019 | 1,989 |
| 2020 | 1,476 |
| 2021 | 1,268 |
| 2022 | 1,097 |

The changes in the carrying amount of goodwill are (in thousands):

| | Six months ended March 31, | |
|---|---|---|
| | 2017 | 2016 |
| Beginning balance, October 1 | $ 109,448 | $ 100,183 |
| Acquisitions | 21,206 | 11,020 |
| Foreign currency translation adjustment | (733) | (496) |
| Ending balance, March 31 | $ 129,921 | $ 110,707 |

Goodwill is tested for impairment on an annual basis as of June 30, or more frequently if events or circumstances occur which could indicate impairment. The calculation of goodwill impairment requires us to make assumptions about the fair value of our one reporting unit, which historically has been approximated by using our market capitalization plus a control premium. Control premium assumptions require judgment and actual results may differ from assumed or estimated amounts.

Our test for potential goodwill impairment is a two-step approach. We estimate the fair value for our one reporting unit by comparing its fair value (market capitalization plus control premium) to our carrying value. If the carrying value of the reporting unit exceeds its estimated fair value, the second step of the goodwill impairment analysis requires us to measure the amount of the impairment loss. An impairment loss is calculated by comparing the implied fair value of the goodwill to its carrying amount. To calculate the implied fair value of goodwill, the fair value of the reporting unit’s assets and liabilities, excluding goodwill, is estimated. The excess of the fair value of the reporting unit over the amount assigned to its assets and liabilities, excluding goodwill, is the implied fair value of the reporting unit’s goodwill.

If our stock price or control premium declines, the first step of our goodwill impairment analysis may fail. We have identified factors that could result in additional interim goodwill impairment testing. For example, we would perform the second step of the impairment testing if our stock price fell below certain thresholds for a significant period of time, or if our control premium significantly decreased. Events or circumstances may occur that could negatively impact our stock price, including changes in our anticipated revenues and profits and our ability to execute on our strategies. In addition, our control premium could decline due to changes in economic conditions in the technology industry or more generally in the financial markets. An impairment

8. GOODWILL AND OTHER IDENTIFIABLE INTANGIBLE ASSETS, NET (CONTINUED)

could have a material effect on our consolidated balance sheet and results of operations. There were no triggering events during the second quarter of fiscal 2017. We have had no goodwill impairment losses since the adoption of Accounting Standards Codification ("ASC") 350, Intangibles-Goodwill and Others, in fiscal 2003.

9. INCOME TAXES

Income tax provision for continuing operations was $0.9 million for the six months ended March 31, 2017. Net tax benefits specific to the six months ended March 31, 2017 were $0.1 million resulting primarily from the reversal of tax reserves due to the expiration of statutes of limitation from U.S. and foreign tax jurisdictions. For the six months ended March 31, 2017, our continuing operations effective tax rate before items specific to the period was less than the U.S. statutory rate due primarily to the mix of income between taxing jurisdictions, certain of which have lower statutory tax rates than the U.S., and also due to certain tax credits in the U.S.

Income tax provision for continuing operations was $1.5 million for the six months ended March 31, 2016. Net tax benefits specific to the six months ended March 31, 2016 were $0.7 million which resulted from the reinstatement of the federal research and development tax credit for calendar year 2015 and reversal of tax reserves due to the expiration of statutes of limitation from U.S. and foreign tax jurisdictions. For the six months ended March 31, 2016, our continuing operations effective tax rate before items specific to the period was less than the U.S. statutory rate primarily due to the mix of income between taxing jurisdictions, certain of which have lower statutory tax rates than the U.S., and certain tax credits in the U.S.

Our effective tax rate will vary based on a variety of factors, including overall profitability, the geographical mix of income before taxes and related statutory tax rate in each jurisdiction, and tax items specific to the period, such as settlements of audits. We expect that we may record other benefits or expenses in the future that are specific to a particular quarter such as expiration of statutes of limitation, the completion of tax audits, or legislation that is enacted for both U.S. and foreign jurisdictions.

A reconciliation of the beginning and ending amount of unrecognized tax benefits is (in thousands):

| | | |
|---|---|---|
| Unrecognized tax benefits as of September 30, 2016 | $ | 1,708 |
| Decreases related to: | | |
| Expiration of statute of limitations | | (79) |
| Unrecognized tax benefits as of March 31, 2017 | $ | 1,629 |

The total amount of unrecognized tax benefits that, if recognized, would affect our effective tax rate is $1.4 million, after considering the impact of interest and deferred benefit items. We expect that the total amount of unrecognized tax benefits will decrease by approximately $0.7 million over the next 12 months.

10. PRODUCT WARRANTY OBLIGATION

In general, we warrant our products to be free from defects in material and workmanship under normal use and service. The warranty periods generally range from one to five years. We typically have the option to either repair or replace products we deem defective with regard to material or workmanship. Estimated warranty costs are accrued in the period that the related revenue is recognized based upon an estimated average per unit repair or replacement cost applied to the estimated number of units under warranty. These estimates are based upon historical warranty incidents and are evaluated on an ongoing basis to ensure the adequacy of the warranty accrual. The following table summarizes the activity associated with the product warranty accrual (in thousands) and is included on our Condensed Consolidated Balance Sheets within current liabilities:

| Period | Balance at January 1 | Warranties issued | Settlements made | Balance at March 31 |
|---|---|---|---|---|
| Three months ended March 31, 2017 | $ 1,025 | $ 62 | $ (195) | $ 892 |
| Three months ended March 31, 2016 | $ 968 | $ 172 | $ (196) | $ 944 |

| Period | Balance at October 1 | Warranties issued | Settlements made | Balance at March 31 |
|---|---|---|---|---|
| Six months ended March 31, 2017 | $ 1,033 | $ 231 | $ (372) | $ 892 |
| Six months ended March 31, 2016 | $ 1,014 | $ 292 | $ (362) | $ 944 |

10. PRODUCT WARRANTY OBLIGATION (CONTINUED)

We are not responsible for, and do not warrant that, custom software versions, created by original equipment manufacturer ("OEM") customers based upon our software source code, will function in a particular way, will conform to any specifications or are fit for any particular purpose. Further, we do not indemnify these customers from any third-party liability as it relates to or arises from any customization or modifications made by the OEM customer.

11. CONTINGENCIES

In the normal course of business, we are subject to various claims and litigation. There can be no assurance that any claims by third parties, if proven to have merit, will not materially adversely affect our business, liquidity or financial condition.

12. STOCK-BASED COMPENSATION

Stock-based awards were granted under the 2017 Omnibus Incentive Plan (the "2017 Plan") beginning January 30, 2017 and, prior to that, were granted under the 2016 Omnibus Incentive Plan (the "2016 Plan"). Upon stockholder approval of the 2017 Plan, we ceased granting awards under any prior plan. Shares remaining in the 2016 Plan were moved into the 2017 Plan. The authority to grant options under the 2017 Plan and to set other terms and conditions rests with the Compensation Committee of the Board of Directors.

The 2017 Plan authorizes the issuance of up to 1,500,000 common shares in connection with awards of stock options, stock appreciation rights, restricted stock, restricted stock units, performance-based full value awards or other stock-based awards. Eligible participants include our employees, our affiliates, non-employee directors of our Company and any consultant or advisor who is a natural person and provides services to us or our affiliates. Options that have been granted under the 2017 Plan typically vest over a four-year period and will expire if unexercised after seven years from the date of grant. Restricted stock unit awards ("RSUs") that have been granted to directors typically vest in one year. RSUs that have been granted to executives and employees typically vest in January over a four-year period. Awards may be granted under the 2017 Plan until January 29, 2027. Options under the 2017 Plan can be granted as either incentive stock options ("ISOs") or non-statutory stock options ("NSOs"). The exercise price of options and the grant date price of restricted stock units shall be determined by our Compensation Committee but shall not be less than the fair market value of our common stock based on the closing price on the date of grant. Upon exercise, we issue new shares of stock. As of March 31, 2017, there were approximately 1,465,545 shares available for future grants under the 2017 Plan.

The 2016 Plan, under which grants ceased upon approval of the 2017 Plan, initially authorized the issuance of up to 1,500,000 common shares in connection with awards of stock options, stock appreciation rights, restricted stock, restricted stock units, performance-based full value awards or other stock-based awards. Eligible participants included our employees, our affiliates, non-employee directors of our Company and any consultant or advisor who is a natural person and provides services to us or our affiliates. Options that were granted under the 2016 Plan typically vested over a four-year period and expired if unexercised after seven years from the date of grant. RSUs that were granted to directors typically vested in one year. RSUs that were granted to executives and employees typically vested in November or January over a four-year period. Options under the 2016 Plan could be granted as either ISOs or NSOs. The exercise price of options and the grant date price of restricted stock was determined by our Compensation Committee but were not less than the fair market value of our common stock based on the closing price on the date of grant. Upon exercise, we issued new shares of stock.

Our equity plans and corresponding forms of award agreements generally have provisions allowing employees to elect to satisfy tax withholding obligations through the delivery of shares, having us retain a portion of shares issuable under the award or paying cash to us for the withholding. During the six months ended March 31, 2017 and 2016, our employees forfeited 43,160 shares and 42,427 shares, respectively in order to satisfy $0.6 million and $0.5 million, respectively of withholding tax obligations related to stock-based compensation, pursuant to terms of awards under our board and shareholder-approved compensation plans for each respective period.

Cash received from the exercise of stock options was $3.2 million and $6.3 million during the six months ended March 31, 2017 and 2016, respectively. There were $0.3 million and $0.2 million in excess tax benefits from stock-based compensation for the six months ended March 31, 2017 and 2016, respectively.

We sponsor an Employee Stock Purchase Plan (the "Purchase Plan"), covering all domestic employees with at least 90 days of continuous service and who are customarily employed at least 20 hours per week. The Purchase Plan allows eligible participants the right to purchase common stock on a quarterly basis at the lower of 85% of the market price at the beginning or end of each three-month offering period. Employee contributions to the Purchase Plan were $0.5 million during both six

12. STOCK-BASED COMPENSATION (CONTINUED)

month periods ended March 31, 2017 and 2016. Pursuant to the Purchase Plan, 48,299 and 55,343 common shares were issued to employees during the six months ended March 31, 2017 and 2016, respectively. Shares are issued under the Purchase Plan from treasury stock. As of March 31, 2017, 465,317 common shares were available for future issuances under the Purchase Plan.

Stock-based compensation expense is included in the consolidated results of operations as follows (in thousands):

| | Three months ended March 31, | | Six months ended March 31, | |
|---|---|---|---|---|
| | 2017 | 2016 | 2017 | 2016 |
| Cost of sales | $ 54 | $ 51 | $ 116 | $ 105 |
| Sales and marketing | 345 | 227 | 685 | 426 |
| Research and development | 155 | 147 | 337 | 295 |
| General and administrative | 601 | 478 | 1,190 | 888 |
| Stock-based compensation before income taxes | 1,155 | 903 | 2,328 | 1,714 |
| Income tax benefit | (382) | (293) | (757) | (550) |
| Stock-based compensation after income taxes | $ 773 | $ 610 | $ 1,571 | $ 1,164 |

Stock-based compensation cost capitalized as part of inventory was immaterial as of March 31, 2017 and September 30, 2016.

The following table summarizes our stock option activity (in thousands, except per common share amounts):

| | Options Outstanding | Weighted Average Exercised Price | Weighted Average Contractual Term (in years) | Aggregate Intrinsic Value (1) |
|---|---|---|---|---|
| Balance at September 30, 2016 | 3,963 | $10.36 | | |
| Granted | 598 | 12.87 | | |
| Exercised | (305) | 10.64 | | |
| Forfeited / Canceled | (223) | 13.30 | | |
| Balance at March 31, 2017 | 4,033 | $10.55 | 4.7 | $ 7,283 |
| Exercisable at March 31, 2017 | 2,676 | $10.19 | 3.9 | $ 5,459 |

(1) The aggregate intrinsic value represents the total pre-tax intrinsic value, based on our closing stock price of $11.90 as of March 31, 2017, which would have been received by the option holders had all option holders exercised their options as of that date. The intrinsic value of an option is the amount by which the fair value of the underlying stock exceeds its exercise price.

The total intrinsic value of all options exercised during the six months ended March 31, 2017 was $0.9 million and during the six months ended March 31, 2016 was $1.7 million.

The table below shows the weighted average fair value, which was determined based upon the fair value of each option on the grant date utilizing the Black-Scholes option-pricing model and the related assumptions:

| | Six months ended March 31, | |
|---|---|---|
| | 2017 | 2016 |
| Weighted average per option grant date fair value | $4.64 | $3.92 |
| Assumptions used for option grants: | | |
| Risk free interest rate | 1.46% - 1.96% | 1.61% - 1.85% |
| Expected term | 6.00 years | 6.00 years |
| Expected volatility | 33% - 34% | 32% |
| Weighted average volatility | 34% | 32% |
| Expected dividend yield | 0 | 0 |

12. STOCK-BASED COMPENSATION (CONTINUED)

The fair value of each option award granted during the periods presented was estimated using the Black-Scholes option valuation model that uses the assumptions noted in the table above. Expected volatilities are based on the historical volatility of our stock. We use historical data to estimate option exercise and employee termination information within the valuation model. The expected term of options granted is derived from the vesting period and historical information and represents the period of time that options granted are expected to be outstanding. The risk-free rate used is the zero-coupon U.S. Treasury bond rate in effect at the time of the grant whose maturity equals the expected term of the option.

We use historical data to estimate pre-vesting forfeiture rates. The pre-vesting forfeiture rate used during the six months ended March 31, 2017 was 10.0%. As of March 31, 2017 the total unrecognized compensation cost related to non-vested stock options, net of expected forfeitures, was $4.3 million and the related weighted average period over which it is expected to be recognized is approximately 3.4 years.

A summary of our non-vested restricted stock units as of March 31, 2017 and changes during the six months then ended is presented below (in thousands, except per common share amounts):

| | Number of Awards | Weighted Average Grant Date Fair Value |
|---|---|---|
| Nonvested at September 30, 2016 | 505 | $ 9.67 |
| Granted | 283 | $ 12.78 |
| Vested | (178) | $ 9.31 |
| Canceled | (3) | $ 10.89 |
| Nonvested at March 31, 2017 | 607 | $ 11.22 |

As of March 31, 2017, the total unrecognized compensation cost related to non-vested restricted stock units was $4.9 million, and the related weighted average period over which it is expected to be recognized is approximately 1.7 years.

13. RESTRUCTURING

Below is a summary of the restructuring charges and other activity (in thousands):

| | Q2 2016 Restructuring | Q1 2016 Restructuring | | |
|---|---|---|---|---|
| | Employee Termination Costs | Employee Termination Costs | Other | Total |
| Balance at September 30, 2015 | $ — | $ — | $ — | $ — |
| Restructuring charge | — | 480 | 171 | 651 |
| Balance at December 31, 2015 | $ — | $ 480 | $ 171 | $ 651 |
| Restructuring charge | 78 | — | 24 | 102 |
| Payments | (76) | (113) | (195) | (384) |
| Foreign currency fluctuation | — | 13 | — | 13 |
| Balance at March 31, 2016 | $ 2 | $ 380 | $ — | $ 382 |

*Q1 2016 Restructuring*

In November 2015, we approved a restructuring plan impacting our corporate staff. The plan closed our Dortmund, Germany office and relocated certain employees to our Munich, Germany office. We also recorded a contract termination charge as we relocated employees in our Minneapolis, Minnesota office to our World Headquarters in Minnetonka, Minnesota, in December 2015. We recorded a restructuring charge of $0.7 million that included $0.5 million of severance and $0.2 million of contract termination costs during the first quarter of fiscal 2016. This restructuring resulted in an elimination of approximately 10 positions. The payments associated with these charges were completed in the third quarter of fiscal 2016.

13. RESTRUCTURING (CONTINUED)

*Q2 2016 Restructuring*

In January 2016, we approved a restructuring plan impacting our wireless design services group. This restructuring resulted in an elimination of 5 positions. We recorded a restructuring charge of $0.1 million related to severance during the second quarter of fiscal 2016 and paid the majority of the severance during that same quarter.

14. COMMON STOCK REPURCHASE

On April 26, 2016, our Board of Directors authorized a program to repurchase up to $15.0 million of our common stock primarily to return capital to shareholders. This repurchase authorization expired on May 1, 2017. Shares repurchased under the new program could be made through open market and privately negotiated transactions from time to time and in amounts that management deemed appropriate. The amount and timing of share repurchases depended upon market conditions and other corporate considerations. There were no shares repurchased under this program.

15. SUBSEQUENT EVENT

On May 2, 2017, our Board of Directors authorized a new program to repurchase up to $20.0 million of our common stock primarily to return capital to shareholders. This repurchase authorization expires on May 1, 2018. Shares repurchased under the new program will be made through open market and privately negotiated transactions from time to time and in amounts that management deems appropriate. The amount and timing of share repurchases depends upon market conditions and other corporate considerations.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Our management's discussion and analysis should be read in conjunction with our Annual Report on Form 10-K for the fiscal year ended September 30, 2016, as well as our subsequent reports on 8-K and any amendments thereto.

## SAFE HARBOR STATEMENT UNDER THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

This Form 10-Q contains certain statements that are "forward-looking statements" as that term is defined under the Private Securities Litigation Reform Act of 1995, and within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended.

*Forward-Looking Statements*

The words "anticipate," "assume," "believe," "continue," "estimate," "expect," "intend," "may," "plan," "should," or "will" or the negative thereof or other variations thereon or similar terminology, which are predictions of or indicate future events and trends and which do not relate to historical matters, identify forward-looking statements. Among other items, these statements relate to expectations of the business environment in which we operate, estimated future values and projections of future performance, perceived marketplace opportunities and statements regarding our mission and vision. Such statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions, including risks related to the highly competitive market in which our company operates, rapid changes in technologies that may displace products sold by us, declining prices of networking products, our reliance on distributors and other third parties to sell our products, delays in product development efforts, uncertainty in user acceptance of our products, the ability to integrate our products and services with those of other parties in a commercially accepted manner, potential liabilities that can arise if any of our products have design or manufacturing defects, our ability to defend or settle satisfactorily any litigation, uncertainty in global economic conditions and economic conditions within particular regions of the world which could negatively affect product demand and the financial solvency of customers and suppliers, the impact of natural disasters and other events beyond our control that could negatively impact our supply chain and customers, potential unintended consequences associated with restructuring or other similar business initiatives that may impact our operations and our ability to retain important employees, the ability to achieve the anticipated benefits and synergies associated with acquisitions or divestitures, and changes in our level of revenue or profitability, which can fluctuate for many reasons beyond our control. These and other risks, uncertainties and assumptions identified from time to time in our filings with the United States Securities and Exchange Commission, including without limitation, our Annual Report on Form 10-K for the year ended September 30, 2016, and subsequent quarterly reports on Form 10-Q and other filings, could cause the company's future results to differ materially from those expressed in any forward-looking statements made by us or on our behalf. Many of such factors are beyond our ability to control or predict. These forward-looking statements speak only as of the date for which they are made. We disclaim any intent or obligation to update any forward-looking statements, whether as a result of new information, future events or otherwise.

*Presentation of Non-GAAP Financial Measures*

This report includes EBITDA from continuing operations, which is a non-GAAP measure. We understand that there are material limitations on the use of non-GAAP measures. Non-GAAP measures are not substitutes for GAAP measures, such as net income, for the purpose of analyzing financial performance. The disclosure of these measures does not reflect all charges and gains that were actually recognized by the company. Non-GAAP measures are not prepared in accordance with, or as an alternative for measures prepared in accordance with, generally accepted accounting principles and may be different from non-GAAP measures used by other companies. In addition, non-GAAP measures are not based on any comprehensive set of accounting rules or principles. We believe that non-GAAP measures have limitations in that they do not reflect all of the amounts associated with our results of operations as determined in accordance with GAAP and that these measures should only be used to evaluate our results of operations in conjunction with the corresponding GAAP measures. Additionally, we understand that EBITDA from continuing operations does not reflect our cash expenditures, the cash requirements for the replacement of depreciated and amortized assets, or changes in or cash requirements for our working capital needs.

We believe that the presentation of EBITDA from continuing operations as a percentage of revenue is useful because it provides a reliable and consistent approach to measuring our performance from year to year and in assessing our performance against that of other companies. We believe this information helps compare operating results and corporate performance exclusive of the impact of our capital structure and the method by which assets were acquired. EBITDA from continuing operations is used as an internal metric for executive compensation, as well as incentive compensation for the rest of the employee base, and it is monitored quarterly for these purposes.

**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (CONTINUED)**

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of our condensed consolidated financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, the disclosure of contingent assets and liabilities and the values of purchased assets and assumed liabilities in acquisitions. We base our estimates on historical experience and various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

A description of our critical accounting policies and estimates was provided in the Management's Discussion and Analysis of Financial Condition and Results of Operations section of our Annual Report on Form 10-K for the year ended September 30, 2016. There have been no material changes to our critical accounting policies as disclosed in that report.

**OVERVIEW**

We are a leading global provider of business and mission-critical machine-to-machine ("M2M") and Internet-of-Things ("IoT") connectivity products and services. We help our customers create next generation connected products and deploy and manage critical communications infrastructures in demanding environments with high levels of security and reliability. We create secure, easy to implement embedded solutions and services to help customers build IoT connectivity. We also deploy ready to use, complete box solutions to connect remote machinery. In addition, we manage cloud services, offer professional services and complete IoT solutions. We formed a smart solution that offers automated wireless temperature monitoring as well as employee task management services to healthcare and food service industries. Our products and services are used by a wide range of businesses and institutions. We have a single reporting segment. We compete for customers on the basis of existing and planned product features, service and software application capabilities, company reputation, brand recognition, technical support, alliance relationships, quality and reliability, product development capabilities, price and availability.

Our revenue consists of hardware product revenue and service revenue. Our hardware product offerings are comprised of our cellular routers and gateways, radio frequency ("RF"), embedded and network products. Our cellular product category includes our cellular routers and all gateways. Our RF product category includes our XBee® modules as well as other RF Solutions. Our Embedded product category includes Digi Connect® and Rabbit® embedded systems on module and single board computers. Our network product category, which has the highest concentration of mature products, includes console and serial servers and USB connected products.

On May 4, 2017, we announced the rebranding of our Digi Cold Chain Solutions to Digi Smart Solutions™ group.

Our service offerings include Digi Smart Solutions, wireless design services, Digi Device Cloud (which includes Digi Remote Manager™) and support services. We have formed Digi Smart Solutions through a series of acquisitions including the October 2015 acquisition of Bluenica Corporation ("Bluenica"), the November 2016 acquisition of FreshTemp, LLC ("FreshTemp") and the January 2017 acquisition of SMART Temps, LLC ("SMART Temps") to enhance and expand the capabilities of Digi Smart Solutions.

We utilize many financial, operational, and other metrics to evaluate our financial condition and financial performance. Below we highlight the metrics for the second quarter of fiscal 2017 that we feel are most important in these evaluations:

*Total Revenue was $45.6 Million.* Our revenue was $45.6 million for the second quarter of fiscal 2017 compared to $50.2 million in the second quarter of fiscal 2016. There was a decrease in hardware product revenue of $7.0 million, or 14.3%. Hardware product revenue performance decreased in all product categories, with the exception of RF which increased $0.1 million in the three months ended March 31, 2017 compared to the same period a year ago. Revenue was unfavorably impacted by $0.2 million due to the weakening of the British Pound and Euro compared to the U.S. Dollar.

Service revenue increased by $2.4 million, or 169.2% in the second quarter of fiscal 2017 compared to the second quarter of fiscal 2016. This increase was driven primarily by the continued growth and expansion of Digi Smart Solutions which included incremental revenue from our recent acquisitions of SMART Temps and FreshTemp of $1.5 million (see Note 2 to our Condensed Consolidated Financial Statements).

*Gross Margin was 48.0%*. Our gross margin decreased as a percentage of revenue to 48.0% in the second quarter of fiscal 2017 as compared to 49.3% in the second quarter of fiscal 2016. Gross margin was negatively impacted by product mix, primarily resulting from lower revenue performance in our network category which are traditionally higher margin products.

*Income tax provision for the second fiscal quarter of 2017 was $0.1 million.* Income tax provision for the second fiscal quarter of 2016 was $1.2 million, which included a tax benefit of $0.5 million specific to that period for the reinstatement of the federal research and development tax credit for calendar year 2015.

*Net income for the second fiscal quarter of 2017 was $1.3 million, or $0.05 per diluted share.* Net income for the second fiscal quarter of 2016 was $2.1 million, or $0.08 per diluted share.

*EBITDA from continuing operations for the second fiscal quarter of 2017 was $2.8 Million, or 6.0% of total revenue.* In the second fiscal quarter of fiscal 2016, EBITDA from continuing operations was $4.6 million, or 9.1% of total revenue.

Below is a reconciliation of Income from continuing operations to EBITDA from continuing operations (in thousands):

| | Three months ended March 31, | | | |
|---|---|---|---|---|
| | 2017 | | 2016 | |
| | | % of total revenue | | % of total revenue |
| Total revenue | $ 45,615 | 100.0% | $ 50,162 | 100.0% |
| | | | | |
| Income from continuing operations | $ 1,331 | | $ 2,226 | |
| Interest income, net | (110) | | (12) | |
| Income tax provision | 148 | | 1,155 | |
| Depreciation and amortization | 1,389 | | 1,214 | |
| EBITDA from continuing operations | $ 2,758 | 6.0% | $ 4,583 | 9.1% |

## CONSOLIDATED RESULTS OF OPERATIONS

The following table sets forth selected information derived from our interim condensed consolidated statements of operations (dollars in thousands):

| | Three months ended March 31, | | | | % incr. | Six months ended March 31, | | | | % incr. |
|---|---|---|---|---|---|---|---|---|---|---|
| | 2017 | | 2016 | | (decr.) | 2017 | | 2016 | | (decr.) |
| Revenue: | | | | | | | | | | |
| Hardware product | $ 41,766 | 91.6 % | $ 48,732 | 97.1 % | (14.3) | $ 84,939 | 93.6% | $ 96,979 | 96.6 % | (12.4) |
| Service | 3,849 | 8.4 | 1,430 | 2.9 | 169.2 | 5,851 | 6.4 | 3,442 | 3.4 | 70.0 |
| Total revenue | 45,615 | 100.0 | 50,162 | 100.0 | (9.1) | 90,790 | 100.0 | 100,421 | 100.0 | (9.6) |
| Cost of sales: | | | | | | | | | | |
| Cost of hardware product | 21,489 | 47.1 | 24,283 | 48.4 | (11.5) | 43,927 | 48.4 | 48,993 | 48.8 | (10.3) |
| Cost of service | 2,224 | 4.9 | 1,137 | 2.3 | 95.6 | 3,508 | 3.9 | 2,329 | 2.3 | 50.6 |
| Total cost of sales | 23,713 | 52.0 | 25,420 | 50.7 | (6.7) | 47,435 | 52.3 | 51,322 | 51.1 | (7.6) |
| Gross profit | 21,902 | 48.0 | 24,742 | 49.3 | (11.5) | 43,355 | 47.7 | 49,099 | 48.9 | (11.7) |
| Operating expenses | 20,390 | 44.7 | 21,089 | 42.0 | (3.3) | 39,421 | 43.4 | 42,157 | 42.0 | (6.5) |
| Operating income | 1,512 | 3.3 | 3,653 | 7.3 | (58.6) | 3,934 | 4.3 | 6,942 | 6.9 | (43.3) |
| Other (expense) income, net | (33) | (0.1) | (272) | (0.6) | (87.9) | 667 | 0.8 | (49) | — | NM |
| Income from continuing operations, before income taxes | 1,479 | 3.2 | 3,381 | 6.7 | (56.3) | 4,601 | 5.1 | 6,893 | 6.9 | (33.3) |
| Income tax provision | 148 | 0.3 | 1,155 | 2.3 | (87.2) | 913 | 1.0 | 1,536 | 1.5 | (40.6) |
| Income from continuing operations | 1,331 | 2.9 % | 2,226 | 4.4 % | (40.2) | 3,688 | 4.1 | 5,357 | 5.4 | (31.2) |
| (Loss) income from discontinued operations, after income taxes | — | — | (89) | (0.1) | (100.0) | — | — | 3,230 | 3.2 | (100.0) |
| Net income | $ 1,331 | 2.9 % | $ 2,137 | 4.3 % | (37.7) | $ 3,688 | 4.1% | $ 8,587 | 8.6 % | (57.1) |

NM means not meaningful

## REVENUE

### *Hardware Products*

Below is our revenue by product category:

| | Three months ended March 31, | | | | % incr. | Six months ended March 31, | | | | % incr. |
|---|---|---|---|---|---|---|---|---|---|---|
| ($ in thousands) | 2017 | | 2016 | | (decr.) | 2017 | | 2016 | | (decr.) |
| Cellular routers and gateways | $ 11,448 | 27.4% | $ 12,910 | 26.5% | (11.3) | $ 25,204 | 29.7% | $ 25,070 | 25.8% | 0.5 |
| RF | 7,961 | 19.1 | 7,879 | 16.2 | 1.0 | 14,535 | 17.1 | 17,065 | 17.6 | (14.8) |
| Embedded | 11,712 | 28.0 | 13,795 | 28.3 | (15.1) | 23,553 | 27.7 | 26,923 | 27.8 | (12.5) |
| Network | 10,645 | 25.5 | 14,148 | 29.0 | (24.8) | 21,647 | 25.5 | 27,921 | 28.8 | (22.5) |
| Total hardware product revenue | $ 41,766 | 100.0% | $ 48,732 | 100.0% | (14.3) | $ 84,939 | 100.0% | $ 96,979 | 100.0% | (12.4) |

Cellular router and gateway revenue decreased $1.5 million, or 11.3%, for the three months ended March 31, 2017 compared to the same period a year ago. Cellular router and gateway revenue in the prior fiscal year included customers with larger orders and projects, which did not reoccur in the current fiscal year. In addition, revenue from our new product introductions has increased more slowly than anticipated. Cellular router and gateway revenue increased $0.1 million, or 0.5%, for the six months ended March 31, 2017 compared to the same period a year ago. The cellular router and gateway revenue is driven by large awards-based customer projects and is subject to revenue fluctuations from period to period.

RF product revenue increased $0.1 million, or 1.0%, for the three months ended March 31, 2017 compared to the same period a year ago. RF products revenue decreased $2.5 million, or 14.8%, for the six months ended March 31, 2017 compared to the same period a year ago, primarily as a result of project roll-outs in our Latin America and Europe, Middle East and Africa ("EMEA") regions that occurred in the first half of fiscal 2016. RF products can fluctuate from period to period because of large customer projects. We are encouraged by the design wins and building pipeline for our new cellular XBee, released in

March 2017. The product is an embedded module that speeds product introduction and lowers development and certification costs. We expect design wins to convert to revenues when production volumes contribute materially in fiscal 2018.

Embedded product revenue decreased $2.1 million and $3.4 million, or 15.1% and 12.5%, for the three and six months ended March 31, 2017, respectively, compared to the same periods a year ago. The decreases were primarily due to lower sales of our embedded modules particularly in the North American and EMEA region as there were significant customers moving their products to production in the prior fiscal year. We are encouraged by the design wins and building pipeline for our new ConnectCore 6UL, released for general availability in April 2017. The ConnectCore 6UL is the most power efficient, lowest cost and smallest industrial System-on-Module ("SOM") available. We expect design wins to convert to revenues when production volumes contribute materially in fiscal 2018.

Network products revenue decreased by $3.5 million and $6.3 million, or 24.8% and 22.5%, for the three and six months ended March 31, 2017, respectively, compared to the same periods a year ago. The decreases were primarily due to large terminal server sales to significant customers in the first quarter of the prior fiscal year, partially offset by an increase in USB connected products. Most of our network products are in the mature phase of their product life cycles. Our network products revenue declined in the first six months of fiscal 2017 more than anticipated and we have adjusted our expectations for this category. Our original expectations had assumed larger last time buy quantities for some of our products. We plan to dedicated additional research and development resources to this category to soften the decline in fiscal 2018.

*Services*

Revenue from our service offerings increased $2.4 million for both the three and six months ended March 31, 2017 compared to the same period a year ago. This increase was driven primarily by the continued growth and expansion of Digi Smart Solutions which included incremental revenue from our recent acquisitions of SMART Temps and FreshTemp of $1.5 million (see Note 2 to our Condensed Consolidated Financial Statements). We are now servicing nearly 12,000 sites and our recurring revenue continues to grow. Revenue also increased in wireless design services in both the three and six months ended March 31, 2017 compared to the same period a year ago.

*Revenue by Geographic Location*

The following summarizes our revenue by geographic location of our customers:

| | Three months ended March 31, | | $ incr. | % incr. | Six months ended March 31, | | $ incr. | % incr. |
|---|---|---|---|---|---|---|---|---|
| ($ in thousands) | 2017 | 2016 | (decr.) | (decr.) | 2017 | 2016 | (decr.) | (decr.) |
| North America, primarily United States | $ 29,711 | $ 33,332 | (3,621) | (10.9) | $ 59,373 | $ 63,900 | (4,527) | (7.1) |
| Europe, Middle East & Africa | 9,545 | 10,965 | (1,420) | (13.0) | 19,356 | 21,982 | (2,626) | (11.9) |
| Asia | 5,370 | 5,025 | 345 | 6.9 | 9,938 | 10,149 | (211) | (2.1) |
| Latin America | 989 | 840 | 149 | 17.7 | 2,123 | 4,390 | (2,267) | (51.6) |
| Total revenue | $ 45,615 | $ 50,162 | (4,547) | (9.1) | $ 90,790 | $ 100,421 | (9,631) | (9.6) |

Revenue in North America decreased by $3.6 million and $4.5 million, or 10.9%, and 7.1%, for the three and six months ended March 31, 2017, respectively, compared to the same periods a year ago. The decreases in both comparable periods were primarily a result of decreased sales of network and cellular products, partially offset by incremental revenue from acquired companies of $1.5 million. Wireless design services revenue increased $0.6 million and $0.4 million for the three and six months ended March 31, 2017, respectively compared to the same periods in the prior fiscal year.

Revenue in EMEA decreased by $1.4 million and $2.6 million, or 13.0% and 11.9%, for the three and six months ended March 31, 2017, respectively, compared to the same periods a year ago. The decreases in both comparable periods were primarily due to decreased revenue for embedded modules and RF products, partially offset by an increase in cellular products revenue compared to the same periods in the prior year. In addition, revenue was unfavorably impacted by $0.2 million and $0.5 million for the three and six months ended March 31, 2017, respectively, compared to the same period a year ago, as both the Euro and British Pound weakened against the U.S. Dollar (see Foreign Currency Risk in Part I, Item 3, of this Form 10-Q).

Revenue in Asia increased by $0.3 million, or 6.9%, for the three months ended March 31, 2017 compared to the same period a year ago. This increase was primarily due to an increase in revenue from network and RF products, partially offset by a decrease in embedded products revenue. Revenue in Asia decreased $0.2 million, or 2.1%, for the six months ended March 31, 2017 compared to the same period a year ago, resulting primarily from a decrease in revenue from embedded products, partially offset by an increase in RF products revenue.

Revenue in Latin America increased by $0.1 million, or 17.7% for the three months ended March 31, 2017 compared to the same period a year ago. RF product revenue increased, offset by a decrease in embedded and cellular product revenue. Revenue in Latin America decreased by $2.3 million, or 51.6% for the six months ended March 31, 2017 compared to the same period a year ago, primarily due to RF project sales in the first half of fiscal 2016 that were not replaced in the first half of fiscal 2017.

No significant changes were made to our pricing strategy that impacted revenue during the six months ended March 31, 2017 as compared to the same period in the prior fiscal year. As foreign currency rates fluctuate, we may from time to time adjust the prices of our products and services.

GROSS PROFIT

Gross profit for the three months ended March 31, 2017 and 2016 was $21.9 million and $24.7 million, respectively, a decrease of $2.8 million, or 11.5%. Gross profit for the six months ended March 31, 2017 and 2016 was $43.4 million and $49.1 million, respectively, a decrease of $5.7 million, or 11.7%.

Hardware product gross profit for the three months ended March 31, 2017 was $20.3 million, or 48.5%, compared to $24.4 million, or 50.2%, for the three months ended March 31, 2016. Hardware product gross profit for the six months ended March 31, 2017 was $41.0 million, or 48.3%, compared to $48.0 million, or 49.5%, for the six months ended March 31, 2016. The decrease for both comparative periods was due primarily to lower revenue performance in our network category, which are traditionally higher margin products. We expect the network category to continue to decline and create pressure on our gross profit in future periods.

Service gross profit was $1.6 million, or 42.2%, and $0.3 million, or 20.5% for the three months ended March 31, 2017 and 2016, respectively. Service gross profit was $2.3 million, or 40.0%, and $1.1 million, or 32.3% for the six months ended March 31, 2017 and 2016, respectively. The increases in the three and six month comparable periods were primarily a result of increased sales in our Smart Solutions which have a higher gross margin. Service gross profit may vary from quarter to quarter, as our wireless product design and development service margins are highly dependent on the utilization rates of our personnel. However, we expect our service gross margin to increase in future periods as recurring revenue from Digi Smart Solutions increases.

OPERATING EXPENSES

The following summarizes our total operating expenses in dollars and as a percentage of total revenue:

| ($ in thousands) | Three months ended March 31, 2017 | | Three months ended March 31, 2016 | | $ incr. (decr.) | Six months ended March 31, 2017 | | Six months ended March 31, 2016 | | $ incr. (decr.) |
|---|---|---|---|---|---|---|---|---|---|---|
| Sales and marketing | $ 8,731 | 19.1% | $ 8,165 | 16.3% | $ 566 | $ 17,053 | 18.8% | $ 16,683 | 16.6% | $ 370 |
| Research and development | 6,979 | 15.3% | 7,757 | 15.5% | (778) | 13,884 | 15.3% | 15,595 | 15.5% | (1,711) |
| General and administrative | 4,680 | 10.3% | 5,065 | 10.0% | (385) | 8,484 | 9.3% | 9,126 | 9.1% | (642) |
| Restructuring | — | —% | 102 | 0.2% | (102) | — | —% | 753 | 0.8% | (753) |
| Total operating expenses | $ 20,390 | 44.7% | $ 21,089 | 42.0% | $ (699) | $ 39,421 | 43.4% | $ 42,157 | 42.0% | $ (2,736) |

Sales and marketing expenses increased $0.6 million and $0.4 million for the three and six months ended March 31, 2017, respectively, compared to the same periods a year ago. The increase in both comparable periods were primarily related to incremental costs for sales and marketing expenses for SMART Temps of $0.5 million.

Research and development expenses decreased $0.8 million and $1.7 million for the three and six months ended March 31, 2017, respectively, compared to the same periods a year ago. The decreases for the three and six months ended March 31, 2017 compared to the same periods a year ago were primarily due to a reduction of bonus expenses of $0.9 million and $1.3 million, respectively, since incentive plan thresholds are not expected to be met. This was partially offset by incremental costs for research and development expenses for SMART Temps of $0.2 million for both comparable periods and an increase in internal development costs.

General and administrative expenses decreased $0.4 million and $0.6 million for the three and six months ended March 31, 2017, respectively, compared to the same periods a year ago. The decreases for the three and six months ended March 31, 2017 compared to the same periods a year ago included incentive compensation expense of $0.6 million and $1.0 million, respectively, and earn-out adjustments for fair value of contingent consideration of $0.6 million and $0.7 million, respectively. This was partially offset by an increase of $0.8 million and $1.0 million of merger and acquisition costs for the three and six months ended March 31, 2017, respectively, compared to the prior year comparable periods. Incremental expenses for SMART Temps were $0.5 million.

We incurred restructuring expenses of $0.8 million for the six months ended March 31, 2016 pertaining to our corporate staff and related employee termination costs associated with the merging of our Dortmund, Germany office into our Munich, Germany office and contract termination charges associated with the consolidation of our Minneapolis, Minnesota office into our Minnetonka, Minnesota headquarters (see Note 13 to our Condensed Consolidated Financial Statements).

OTHER INCOME, NET

We recorded an increase in other (expense) income, net of $0.2 million and $0.7 million for the three and six months ended March 31, 2017, compared to the same periods a year ago primarily related to foreign currency gains. The foreign currency gains were mostly related to the weakening of the Japanese Yen and Euro, as non-functional currencies were remeasured at the current rate.

INCOME TAXES

Income tax provision for continuing operations was $0.9 million for the six months ended March 31, 2017. Net tax benefits specific to the six months ended March 31, 2017 were $0.1 million resulting primarily from the reversal of tax reserves due to the expiration of statutes of limitation from U.S. and foreign tax jurisdictions. For the six months ended March 31, 2017, our continuing operations effective tax rate before items specific to the period was less than the U.S. statutory rate due primarily to the mix of income between taxing jurisdictions, certain of which have lower statutory tax rates than the U.S., and also due to certain tax credits in the U.S.

Income tax provision for continuing operations was $1.5 million for the six months ended March 31, 2016. Net tax benefits specific to the six months ended March 31, 2016 were $0.7 million which resulted from the reinstatement of the federal research and development tax credit for calendar year 2015 and reversal of tax reserves due to the expiration of statutes of limitation from U.S. and foreign tax jurisdictions. For the six months ended March 31, 2016, our continuing operations effective tax rate before items specific to the period was less than the U.S. statutory rate primarily due to the mix of income between taxing jurisdictions, certain of which have lower statutory tax rates than the U.S., and certain tax credits in the U.S.

Our effective tax rate will vary based on a variety of factors, including overall profitability, the geographical mix of income before taxes and related statutory tax rate in each jurisdiction, and tax items specific to the period, such as settlements of audits. We expect that we may record other benefits or expenses in the future that are specific to a particular quarter such as expiration of statutes of limitation, the completion of tax audits, or legislation that is enacted for both U.S. and foreign jurisdictions.

LIQUIDITY AND CAPITAL RESOURCES

We have financed our operations and capital expenditures principally with funds generated from operations. At March 31, 2017, cash, cash equivalents and short-term marketable securities were $108.0 million compared to $134.1 million at September 30, 2016. At March 31, 2017, our cash, cash equivalents and marketable securities, including long-term marketable securities, were $110.2 million.

Our working capital (total current assets less total current liabilities) was $151.8 million at March 31, 2017. At September 30, 2016, our working capital was $171.8 million. We presently anticipate total fiscal 2017 capital expenditures will be approximately $3.2 million, of which we have spent $1.0 million as of March 31, 2017.

Net cash used in operating activities was $0.9 million for the six months ended March 31, 2017 and net cash provided by operating activities was $11.5 million for the six months ended March 31, 2016, a net decrease of $12.4 million, resulting from decreases in net income of $4.9 million and net uses of working capital of $8.0 million, partially offset by an increase in non-cash items of $0.5 million. The decrease in working capital was driven by $8.8 million related to inventory, $2.7 million related to accrued liabilities related to additional incentive compensation payments and $0.3 million related to prepaids and other assets. This was partially offset by increases of $1.9 million for taxes payable and $1.5 million related to accounts receivable.

Net cash used in investing activities was $4.4 million during the six months ended March 31, 2017 and net cash provided by investing activities was $4.2 million for the six months ended March 31, 2016, a net decrease of $8.6 million. The decrease in cash flows used in investing activities in the first half of fiscal 2017 compared to the same period in the prior fiscal year is primarily related to $27.1 million of additional cash expenditures for acquisitions, as we spent $28.3 million for the SMART Temps acquisition, $1.7 million for the FreshTemp acquisition, partially offset $2.9 million for the Bluenica acquisition in the prior fiscal year. This was partially offset by an increase of $18.1 million for additional proceeds from sales of marketable securities.

Net cash provided by financing activities was $2.9 million and $6.4 million during the six months ended March 31, 2017 and 2016, respectively, a net decrease of $3.5 million. We received $3.0 million fewer proceeds from stock option plan exercises compared to the same period a year ago, and we used $0.5 million related to the first earn-out payment to the former shareholders of Bluenica in the first half of fiscal 2017.

We generally expect positive cash flows from operations and believe that our current cash, cash equivalents and short-term marketable securities balances, cash generated from operations and our ability to secure debt and/or equity financing will be sufficient to fund our business operations, possible acquisitions and capital expenditures for the next twelve months and beyond.

*Recently Issued Accounting Pronouncements*

For information on new accounting pronouncements, see Note 1 to our Condensed Consolidated Financial Statements.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

INTEREST RATE RISK

Our exposure to interest rate risk relates primarily to our investment portfolio. Our marketable securities are classified as available-for-sale and are carried at fair value. Our investments consist of money market funds, certificates of deposit, commercial paper, corporate bonds and government municipal bonds. Our investment policy specifies the types of eligible investments and minimum credit quality of our investments, as well as diversification and concentration limits which mitigate our risk. We do not use derivative financial instruments to hedge against interest rate risk because the majority of our investments mature in less than one year.

FOREIGN CURRENCY RISK

We are exposed to foreign currency transaction risk associated with certain sales transactions being denominated in Euros, British Pounds, Japanese Yen or Canadian Dollars and in certain cases, transactions in U.S. Dollars in our foreign entities. We are also exposed to foreign currency translation risk as the financial position and operating results of our foreign subsidiaries are translated into U.S. Dollars for consolidation. We manage our net asset or net liability position for non-functional currency accounts, primarily the U.S Dollar accounts in our foreign locations to reduce our foreign currency risk. In addition, as foreign currency rates fluctuate, we may from time to adjust the prices of our products and services. We have not implemented a formal hedging strategy.

For the six months ended March 31, 2017 and 2016, we had approximately $31.4 million and $36.5 million, respectively, of revenue from foreign customers including export sales. Of these sales, $9.6 million and $11.2 million, respectively, were denominated in foreign currency, predominantly Euros and British Pounds. In future periods, we expect a significant portion of sales will continue to be made in both Euros and British Pounds.

Total revenue was unfavorably impacted by foreign currency translation of $0.2 million and $0.4 million for the three and six months ended March 31, 2017, respectively, as compared to the same period in the prior fiscal year, due to the British Pound and Euro.

The table below compares the average monthly exchange rates of the Euro, British Pound, Japanese Yen and Canadian Dollar to the U.S. Dollar:

| | Six months ended March 31, | | % increase |
|---|---|---|---|
| | 2017 | 2016 | (decrease) |
| Euro | 1.0727 | 1.0991 | (2.4)% |
| British Pound | 1.2415 | 1.4757 | (15.9)% |
| Japanese Yen | 0.0090 | 0.0085 | 5.9 % |
| Canadian Dollar | 0.7523 | 0.7384 | 1.9 % |

A 10% change from the first six months of fiscal 2017 average exchange rate for the Euro, British Pound, Japanese Yen and Canadian Dollar to the U.S. Dollar would have resulted in a 1.1% increase or decrease in revenue and a 2.1% increase or decrease in stockholders' equity due to foreign currency translation. The above analysis does not take into consideration any pricing adjustments we might consider in response to changes in such exchange rates.

CREDIT RISK

We have some exposure to credit risk related to our accounts receivable portfolio. Exposure to credit risk is controlled through regular monitoring of customer financial status, credit limits and collaboration with sales management and customer contacts to facilitate payment.

Investments are made in accordance with our investment policy and consist of money market funds, certificates of deposit, commercial paper, corporate bonds and government municipal bonds. The fair value of our investments contains an element of credit exposure, which could change based on changes in market conditions. If market conditions deteriorate or if the issuers of these securities experience credit rating downgrades, we may incur impairment charges for securities in our investment portfolio. All of our securities are held domestically.

**ITEM 4. CONTROLS AND PROCEDURES**

EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES

As of the end of the period covered by this report, we conducted an evaluation, under the supervision and with the participation of the Chief Executive Officer and Chief Financial Officer, of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (the “Exchange Act”)). Based on this evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act was recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and is accumulated and communicated to our management, including the principal executive and principal financial officers, or persons performing similar functions, 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 quarterly period ended March 31, 2017 that have materially affected, or are reasonably likely to affect, our internal control over financial reporting.

**PART II. OTHER INFORMATION**

**ITEM 1. LEGAL PROCEEDINGS**

The disclosures set forth in Note 11 to the Condensed Consolidated Financial Statements in Part I, Item 1 of this Form 10-Q are incorporated herein by reference.

**ITEM 1A. RISK FACTORS**

There have been no material changes in our risk factors from those previously disclosed in Item 1A of Part I of our Annual Report on Form 10-K for the year ended September 30, 2016.

### ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

On April 26, 2016, our Board of Directors authorized a new program to repurchase up to $15.0 million of our common stock primarily to return capital to shareholders. This new repurchase authorization expires on May 1, 2017. Shares repurchased under the new program may be made through open market and privately negotiated transactions from time to time and in amounts that management deems appropriate. The amount and timing of share repurchases will depend upon market conditions and other corporate considerations. There were no shares repurchased under this program for the quarter ended March 31, 2017.

The following table presents the information with respect to purchases made by or on behalf of Digi International Inc. or any “affiliated purchaser” (as defined in Rule 10b-18(a)(3) under the Securities Exchange Act of 1934), of our common stock during the first quarter of fiscal 2017:

| Period | Total Number of Shares Purchased (1) | Average Price Paid per Share | Total Number of Shares Purchased as Part of a Publicly Announced Program | Maximum Dollar Value of Shares that May Yet Be Purchased Under the Program |
|---|---|---|---|---|
| January 1, 2017 - January 31, 2017 | 14,459 | $ 13.60 | — | $15,000,000.00 |
| February 1, 2017 - February 28, 2017 | — | $ — | — | $15,000,000.00 |
| March 1, 2017 - March 31, 2017 | — | $ — | — | $15,000,000.00 |
| Total | 14,459 | $ 13.60 | — | $15,000,000.00 |

(1) All shares reported were forfeited by employees in connection with the satisfaction of tax withholding obligations related to the vesting of restricted stock units.

### ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None

### ITEM 4. MINE SAFETY DISCLOSURES

None

### ITEM 5. OTHER INFORMATION

None

**ITEM 6. EXHIBITS**

| Exhibit No. | | Description |
|---|---|---|
| 2 | | Stock Purchase Agreement with West Monroe Partners, LLC dated as of October 23, 2015 (1) |
| 3 | (a) | Restated Certificate of Incorporation of the Company, as amended (2) |
| 3 | (b) | Amended and Restated By-Laws effective December 17, 2014 (3) |
| 4 | (a) | Share Rights Agreement, dated as of April 22, 2008, between the Company and Wells Fargo Bank, N.A., as Rights Agent (4) |
| 4 | (b) | Form of Amended and Restated Certificate of Powers, Designations, Preferences and Rights of Series A Junior Participating Preferred Shares (5) |
| 10 | (a) | Employment Agreement between the Company and Kevin C. Riley dated January 23, 2013* |
| 10 | (b) | Digi International Inc. 2017 Omnibus Incentive Plan (6)* |
| 10 | (b)(i) | Form of (Director) Restricted Stock Unit Award Agreement (for awards under Digi International Inc. 2017 Omnibus Incentive Plan)* |
| 10 | (b)(ii) | Form of (Executive) Restricted Stock Unit Award Agreement (for awards under Digi International Inc. 2017 Omnibus Incentive Plan)* |
| 10 | (b)(iii) | Form of (Employee) Restricted Stock Unit Award Agreement (for awards under Digi International Inc. 2017 Omnibus Incentive Plan)* |
| 10 | (b)(iv) | Form of Notice of Grant of Stock Options and Option Agreement (for grants under Digi International Inc. 2017 Omnibus Incentive Plan)* |
| 31 | (a) | Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer |
| 31 | (b) | Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer |
| 32 | | Section 1350 Certification |
| 101.INS | | XBRL Instance Document |
| 101.SCH | | XBRL Taxonomy Extension Schema Document |
| 101.CAL | | XBRL Taxonomy Calculation Linkbase Document |
| 101.DEF | | XBRL Taxonomy Definition Linkbase Document |
| 101.LAB | | XBRL Taxonomy Label Linkbase Document |
| 101.PRE | | XBRL Taxonomy Presentation Linkbase Document |

*Management contract or compensatory plan or arrangement required to be filed as an exhibit to this Form 10-Q.

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(1) Incorporated by reference to Exhibit 2.1 to the Company's Form 8-K filed October 29, 2015.
(2) Incorporated by reference to Exhibit 3(a) to the Company's Annual Report on Form 10-K for the year ended September 30, 1993 (File No. 0-17972)
(3) Incorporated by reference to Exhibit 3.2 to the Company's Current Report on Form 8-K filed December 5, 2014 (File No. 1-34033)
(4) Incorporated by reference to Exhibit 4(a) to the Company's registration statement on Form 8-A filed on April 25, 2008 (File No. 1-34033)
(5) Incorporated by reference to Exhibit 4(b) to the Company's registration statement on Form 8-A filed on April 25, 2008 (File No. 1-34033)
(6) Incorporated by reference to Appendix A to the Company's definitive proxy statement on Schedule 14A filed December 16, 2016 (File No. 1-34033)

SIGNATURE

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.

DIGI INTERNATIONAL INC.

| | | | |
|---|---|---|---|
| Date: | May 5, 2017 | By: | /s/ Michael C. Goergen |
| | | | Michael C. Goergen |
| | | | Senior Vice President, Chief Financial Officer and<br>Treasurer (Principal Financial Officer and Authorized Officer) |

| Exhibit Number | | Document Description | Form of Filing |
|---|---|---|---|
| 2 | | Stock Purchase Agreement with West Monroe Partners, LLC dated as of October 23, 2015 | Incorporated by Reference |
| 3 | (a) | Restated Certificate of Incorporation of the Company, as Amended | Incorporated by Reference |
| 3 | (b) | Amended and Restated By-Laws effective December 17, 2014 | Incorporated by Reference |
| 4 | (a) | Share Rights Agreement, dated as of April 22, 2008, between the Company and Wells Fargo Bank, N.A., as Rights Agent | Incorporated by Reference |
| 4 | (b) | Form of Amended and Restated Certificate of Powers, Designations, Preferences and Rights of Series A Junior Participating Preferred Shares | Incorporated by Reference |
| 10 | (a) | Employment Agreement between the Company and Kevin C. Riley dated January 23, 2013 | Filed Electronically |
| 10 | (b) | Digi International Inc. 2017 Omnibus Incentive Plan | Incorporated by Reference |
| 10 | (b)(i) | Form of (Director) Restricted Stock Unit Award Agreement (for awards under Digi International Inc. 2017 Omnibus Incentive Plan) | Filed Electronically |
| 10 | (b)(ii) | Form of (Executive) Restricted Stock Unit Award Agreement (for awards under Digi International Inc. 2017 Omnibus Incentive Plan) | Filed Electronically |
| 10 | (b)(iii) | Form of (Employee) Restricted Stock Unit Award Agreement (for awards under Digi International Inc. 2017 Omnibus Incentive Plan) | Filed Electronically |
| 10 | (b)(iv) | Form of Notice of Grant of Stock Options and Option Agreement (for grants under Digi International Inc. 2017 Omnibus Incentive Plan) | Filed Electronically |
| 31 | (a) | Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer | Filed Electronically |
| 31 | (b) | Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer | Filed Electronically |
| 32 | | Section 1350 Certification | Filed Electronically |
| 101.INS | | XBRL Instance Document | Filed Electronically |
| 101.SCH | | XBRL Taxonomy Extension Schema Document | Filed Electronically |
| 101.CAL | | XBRL Taxonomy Calculation Linkbase Document | Filed Electronically |
| 101.DEF | | XBRL Taxonomy Definition Linkbase Document | Filed Electronically |
| 101.LAB | | XBRL Taxonomy Label Linkbase Document | Filed Electronically |
| 101.PRE | | XBRL Taxonomy Presentation Linkbase Document | Filed Electronically |

January 23, 2013

Mr. Kevin Riley
21 Silverbrook Road
Ridgefield, CT 06877

Dear Kevin,

On behalf of Digi International Inc., I am pleased to offer you employment as Sr. Vice President, Sales reporting to Joe Dunsmore. (Please see Contingent Offer section below.)

**Compensation**

Your annualized total compensation target is $475,000. For the remainder of fiscal 2013, your annualized base salary is $268,750 with an annualized incentive target of $206,250. Effective 10/1/2013 you will move to an equal split between base salary and incentive, or $237,500 in base and $237,500 in incentive target for the year.

You will participate in Digi International's Executive Incentive Plan. For the current fiscal year, your plan will contain the following components:

**Quarterly Performance:** 40% of your incentive target will be based on achievement of quarterly revenue and profitability targets.

**Annual Performance:** 60% of your incentive target will be based on achievement of the annual revenue and profitability targets.

All payments are pro-rated based on length of service in the quarter/fiscal year.

**Stock Options**

We will recommend to the Board of Directors an initial grant of 125,000 stock options. Your options will be at the market price at the time the board approves your grant and will vest over four years at a rate of 25% (31,250 shares) upon completion of one year, then proportionate monthly vesting thereafter. This option request will be brought to the Board of Directors within three (3) weeks of your start date.

The Option, whether or not previously exercisable, shall become immediately exercisable in full upon the occurrence of any "Change in Control" which occurs contemporaneously with, or is followed within 12 months of the Change of Control by, an "Employment Termination Event". Specific details will be provided with your option agreement.

**Benefits**

Digi offers a comprehensive benefit program which includes Medical, Dental, Vision, Life and Disability Insurance, Medical and Dependent Care Reimbursement Plans, 401(k) Savings Plan, Employee Stock Purchase Plan, and a Tuition Reimbursement Program. You will be eligible for participation in Digi's health insurance programs on the first day of active employment with the company and will be eligible for participation in the 401(k) Savings Plan on the first day of the month following date of hire. Stock Purchase Plan participation eligibility begins on the first of January, April, July and October following date of hire.

You will be eligible to participate in Digi's $500,000 Executive Life Insurance program. If accepted by the carrier, Digi International will pay the full annual premium. This is in additional to the basic and optional life insurance programs offered to all employees.

Vacation eligibility begins on the date of hire. You will participate in the Executive vacation plan which provides unlimited vacation. Upon hire you will begin to accrue 6.15 hours per pay period until you reach 160 hours. Should you leave the company at any point in the future, you will be paid the balance of your vacation accrual.

**Severance Agreement**

If Digi International should terminate your employment at any time in the future for reasons other than Cause, you will be provided with the following severance package in exchange for a full release of claims against the Company:

1) Twelve months of base salary in effect at the time of termination. This shall be paid in a lump sum as soon as administratively feasible after the later of the date of termination or the date the release of claims has become irrevocable.

2) A pro-rata bonus based on number of months worked in the fiscal year prior to a qualifying termination and the Company's actual performance against annual objections. This pro-rata bonus shall be paid no later than 2.5 months after the close of the fiscal year in which the qualifying termination occurs.

For purposes of this agreement, "Cause" shall mean only the following: (i) indictment or conviction of, or a plea of nolo contendere to, (A) any felony (other than any felony arising out of negligence), or any misdemeanor involving moral turpitude with respect to the Company, or (B) any crime or offense involving dishonesty with respect to the Company; (ii) theft or embezzlement of Company property or commission of similar acts involving dishonesty or moral turpitude; (iii) material negligence in the performance of your job duties after notice; (iv) failure to devote substantially all of his working time and efforts during normal business hours to the Company's business; or (v) knowing engagement in conduct which is materially injurious to the Company.

**Relocation**

You will receive the following relocation package. Should you voluntarily terminate your employment with the company prior to twenty-four (24) months, you will be responsible for full repayment of the relocation package amount.

- $60,000 paid in one lump sum (less standard deductions), for incidental expenses, i.e. storage, utility hook-ups, closing costs on current residence, etc. This payment will be made 2 weeks prior to the closing of your primary residence in Connecticut. Additional lump sums may be paid out to reach maximum value of the package, dependent on your spending in other categories.

- Six (6) months temporary housing expenses, based on an agreed upon monthly amount.

- Roundtrip airfare to Connecticut (4 tickets monthly) for the Employee or family member for the first 6 months. This will be at coach fare.

- Packing and shipping of household goods, including insurance of goods and personal effects of the employee & family. Excluded items include recreational vehicles (RVs, boats, motorcycles, ATVs, etc.), firewood, paint, inflammable solutions, explosives, frozen foods, shrubs, plants, livestock, ammunition. Alcoholic beverage, valuable papers, stock & bonds, stamps & coin collection, sterling silver place settings, play yard systems, oversized trophies, and money & fine jewelry.

- Shipment of 2 cars plus airfare to location, or if driving, normal trip expenditures (mileage, hotel, meals, etc.

- The maximum expense reimbursement under this package is $125,000 gross. You should design components to the relocation package to fit individual needs of you and your family within this limit.

**Digi International Employment Agreement**

This offer of employment is contingent upon your signature on the enclosed Digi International Employment, Confidential Information, and Arbitration Agreement. Your signature constitutes acceptance of the terms and conditions contained in the Agreement, so please read it thoroughly prior to signing. This offer is also conditioned upon Digi's determination that you are not subject to any agreement with any former employer or any other party that would prohibit you from working in the position of Sr. Vice President, Sales. If at any time n the future the Company determines that you are subject to an agreement that, in Digi's sold discretion, would prohibit your employment by Digi, Digi my withdraw this offer of employment or terminate your employment with the Company. ***This Employment Agreement must be signed prior to your first day of employment.***

Employment with Digi International Inc. is "at will," which means that it is for no definite period and may be terminated by either you or Digi at any time for any reason without prior notice. I understand, agree, and acknowledge that any reliance on any statements by any representative of the company contrary to this "at will" arrangement is unreasonable and may not form any basis for my reliance thereon.

Digi International has partnered with Verified Credentials, a background screening organization, to administer confidential background checks. Within 48 hours, we ask that you visit Verified Credential website at http://myvci.com/digiinternationalinc to complete a personal questionnaire using your ***full legal name including middle initial***. If you are unable to access the internet within this timeframe, please contact me to further assist you in the process. This offer is contingent upon a finding of "no issue" with your background check. If information is revealed after your start date, Digi has the right to terminate employment without prior notice.

**Commencement Date**

We would like you to start no later than February 18, 2013.

**Contingent Offer**

This offer of employment is contingent upon approval by the Board of Directors and your election as an officer of Digi International.

**Relocation Contigency**

Your continued employment and your rights under the severance agreement outlined in this letter are contingent upon your relocation to the Minneapolis are within seven (7) months of your hire date.

Please inform me of your acceptance of this offer by January 25, 2013 and acknowledge your acceptance by signing on of the enclosed copies.

Sincerely,

***Digi International Inc.***

/s/ Tracy Roberts

Tracy Roberts

VP, Human Resources & Information Technology

***Offer accepted:***

| | | |
|---|---|---|
| /s/ Kevin Riley | January 24, 2013 | January 30, 2013 |
| Kevin Riley | Date | Start Date |

**Digi International Inc.**

**2017 Omnibus Incentive Plan**

**(Director) Restricted Stock Unit Award Agreement**

Digi International, Inc. (the "*Company*"), pursuant to its 2017 Omnibus Incentive Plan (the "*Plan*"), hereby grants an Award of restricted Stock Units to you, the Participant named below. The terms and conditions of this Award are set forth in this Restricted Stock Unit Award Agreement (the "*Agreement*"), consisting of this cover page and the Terms and Conditions on the following pages, and in the Plan document, which has been provided to you. To the extent any capitalized term used in this Agreement is not defined, it shall have the meaning assigned to it in the Plan as it currently exists or as it is amended in the future.

| Name of Participant: | |
|---|---|
| Number of Restricted Stock Units: | Grant Date:__________, 20__ |
| Vesting Schedule: | |
| Vesting Date(s) | Number of Stock Units that Vest |

By signing below, you agree to all of the terms and conditions contained in this Agreement and in the Plan document. You acknowledge that you have reviewed these documents and that they set forth the entire agreement between you and the Company regarding the grant to you of the number of Restricted Stock Units specified in the table above.

PARTICIPANT:

DIGI INTERNATIONAL INC.

By:

Title:

**Digi International Inc.**

**2017 Omnibus Incentive Plan**

**(Director) Restricted Stock Unit Award Agreement**

**Terms and Conditions**

1. **Grant of Restricted Stock Units**. The Company hereby grants to you, subject to the terms and conditions in this Agreement and the Plan, an Award of the number of restricted Stock Units ("*Units*") specified on the cover page of this Agreement, each representing the right to receive one Share of the Company's Stock. The Units granted to you will be credited to an account in your name maintained by the Company. This account shall be unfunded and maintained for book-keeping purposes only, with the Units simply representing an unfunded and unsecured obligation of the Company.

2. **Restrictions on Units**. Neither this Award nor the Units subject to this Award may be sold, assigned, transferred, exchanged or encumbered other than by will or the laws of descent and distribution. Any attempted transfer in violation of this Section 2 shall be of no effect and shall result in the forfeiture of all Units. The Units and your right to receive shares in settlement of the Units under this Agreement shall be subject to forfeiture as provided in Section 4 until satisfaction of the vesting conditions set forth in Section 3.

3. **Vesting of Units**.

(a) Scheduled Vesting. If you remain a member of the Board continuously from the Grant Date specified on the cover page of this Agreement, then the Units will vest in the numbers and on the dates specified in the Vesting Schedule on the cover page of this Agreement.

(b) Accelerated Vesting. Vesting of the Units may be accelerated during the term of the Award at the discretion of the Committee in accordance with Section 16.2 of the Plan and under the following circumstances:

(i) Upon a Change in Control, this Award shall become fully vested and exercisable upon the occurrence of the Change in Control.

(ii) In the event the stockholders of the Company approve the complete dissolution or liquidation of the Company, this Award shall vest and become fully exercisable, and will terminate immediately prior to the consummation of any such proposed action.

(c) Change in Control. "*Change in Control*" means one of the following:

(i) any individual, entity or Group (a "*Person*") becomes a "beneficial owner" (as defined in Rule 13d-3 or any successor rule under the Exchange Act), directly or indirectly, of 30% or more of the combined voting power of the Company's voting securities, except that the following shall not constitute a Change in Control: (A) any acquisition or beneficial ownership by the Company or a Subsidiary; (B) any acquisition or beneficial ownership by any employee benefit plan (or related trust) sponsored or maintained by the Company or one or more Subsidiary; (C) any formation of a Group consisting solely of beneficial owners of the Company's voting securities as of the effective date of this Plan, or any repurchase or other acquisition by the Company of its voting securities that causes any Person to become the beneficial owner of 30% or more of the Company's voting securities, in either case so long as such Person does not acquire beneficial ownership of additional Company voting securities after the Person initially became the beneficial owner of 30% or more of the Company's voting securities by one of the means described in this clause (C); or (D) any acquisition of beneficial ownership by any entity with respect to which, immediately following such acquisition, more than 50% of the combined voting power of such entity's then outstanding voting securities is beneficially owned, directly or indirectly, by all or substantially all of the Persons who beneficially owned the Company's voting securities immediately prior to such acquisition in substantially the same proportions as their ownership of the Company's voting securities immediately prior to such acquisition;

(ii) (ii)Individuals (A) who are, as of the effective date of the Plan, directors of the Company, or (B) who are elected as a directors of the Company subsequent to the Grant Date and whose initial election, or nomination for initial election by the Company's stockholders, was approved by at least a majority of the then Continuing Directors (collectively, "*Continuing Directors*") cease for any reason to constitute a majority of the members of the Board; or

(iii) The consummation of a Fundamental Change unless, immediately following such Fundamental Change, all or substantially all of the Persons who were the beneficial owners of the Company's voting securities immediately prior to such Fundamental Change beneficially own, directly or indirectly, more than 50% of the combined voting power of the then outstanding voting securities of the surviving or acquiring entity (or its Parent) resulting from such Fundamental Change in substantially the same proportions as their ownership, immediately prior to such Fundamental Change, of the Company's voting securities.

(iv) Notwithstanding the foregoing, to the extent that this Award constitutes a deferral of compensation subject to Code Section 409A, then no Change in Control shall be deemed to have occurred upon an event described in this Section 3(c) unless the event would also constitute a change in ownership or effective control of, or a change in the ownership of a substantial portion of the assets of, the Company under Code Section 409A.

4. **Effect of Separation from Service as Director**. Except as otherwise provided in accordance with Section 3(b), if you cease to be a member of the Board prior to the Vesting Date(s) specified on the cover page of this Agreement, you will forfeit all unvested Units.

5. **Settlement of Units**. After any Units vest pursuant to Section 3, the Company shall, as soon as practicable (but no later than March 15 of the year following the calendar year in which such Units vest), cause to be issued and delivered to you, or to your designated beneficiary or estate in the event of your death, one Share in payment and settlement of each vested Unit. Delivery of the Shares shall be effected by an appropriate entry in the stock register maintained by the Company's transfer agent with a notice of issuance provided to you, or by the electronic delivery of the Shares to a brokerage account you designate, and shall be subject to compliance with all applicable legal requirements, including compliance with the requirements of applicable federal and state securities laws, and shall be in complete satisfaction and settlement of such vested Units.

6. **No Stockholder Rights**. The Units subject to this Award do not entitle you to any rights of a holder of the Company's Stock. You will not have any of the rights of a stockholder of the Company in connection with the grant of Units subject to this Agreement unless and until Shares are issued to you in settlement of the Units as provided in Section 5.

7. **Plan Document**. This Agreement and the Award are subject to all the provisions of the Plan, and to all interpretations, rules and regulations that may, from time to time, be adopted and promulgated by the Committee pursuant to the Plan. If there is any conflict between the provisions of this Agreement and the Plan, the provisions of the Plan will govern.

8. **Choice of Law**. This Agreement will be interpreted and enforced under the laws of the state of Minnesota (without to its conflicts or choice of law principles).

9. **Effect**. This Agreement will be binding in all respects on your heirs, representatives, successors and assigns, and on the successors and assigns of the Company.

10. **Discontinuance of Service**. This Agreement does not give you a right to continued service with the Company or Affiliate, and the Company or any such Affiliate may terminate your service at any time and otherwise deal with you without regard to the effect it may have upon you under this Agreement.

11. **Section 409A of the Code**. The award of Units as provided in this Agreement and any issuance of Shares or payment pursuant to this Agreement are intended to be exempt from Section 409A of the Code under the short-term deferral specified in Treas. Reg. § 1.409A-l(b)(4).

***By signing the cover page of this Agreement, you agree to all the terms and conditions described above and in the Plan document.***

**Digi International Inc.**

**2017 Omnibus Incentive Plan**

**(Executive) Restricted Stock Unit Award Agreement**

Digi International, Inc. (the "*Company*"), pursuant to its 2017 Omnibus Incentive Plan (the "*Plan*"), hereby grants an Award of restricted Stock Units to you, the Participant named below. The terms and conditions of this Award are set forth in this Restricted Stock Unit Award Agreement (the "*Agreement*"), consisting of this cover page and the Terms and Conditions on the following pages, and in the Plan document, which has been provided to you. To the extent any capitalized term used in this Agreement is not defined, it shall have the meaning assigned to it in the Plan as it currently exists or as it is amended in the future.

| | |
|---|---|
| Name of Participant: | |
| Number of Restricted Stock Units: | Grant Date:___________, 20__ |
| Vesting Schedule: | |
| Vesting Date(s) | Number of Stock Units that Vest |

By signing below, you agree to all of the terms and conditions contained in this Agreement and in the Plan document. You acknowledge that you have reviewed these documents and that they set forth the entire agreement between you and the Company regarding the grant to you of the number of Restricted Stock Units specified in the table above.

| | |
|---|---|
| PARTICIPANT: | DIGI INTERNATIONAL INC. |
| | By: |
| | Title: |

**Digi International Inc.**

**2017 Omnibus Incentive Plan**

**(Executive) Restricted Stock Unit Award Agreement**

**Terms and Conditions**

1. **Grant of Restricted Stock Units**. The Company hereby grants to you, subject to the terms and conditions in this Agreement and the Plan, an Award of the number of restricted Stock Units ("Units") specified on the cover page of this Agreement, each representing the right to receive one Share of the Company's Stock. The Units granted to you will be credited to an account in your name maintained by the Company. This account shall be unfunded and maintained for book-keeping purposes only, with the Units simply representing an unfunded and unsecured obligation of the Company.

2. **Restrictions on Units**. Neither this Award nor the Units subject to this Award may be sold, assigned, transferred, exchanged or encumbered other than by will or the laws of descent and distribution. Any attempted transfer in violation of this Section 2 shall be of no effect and shall result in the forfeiture of all Units. The Units and your right to receive shares in settlement of the Units under this Agreement shall be subject to forfeiture as provided in Section 4 until satisfaction of the vesting conditions set forth in Section 3.

3. **Vesting of Units**.

(a) Scheduled Vesting. If you remain employed (which includes other service relationships described in Section 5 of the Plan) by the Company or any of its Affiliates continuously from the Grant Date specified on the cover page of this Agreement, then the Units will vest in the numbers and on the dates specified in the Vesting Schedule on the cover page of this Agreement.

(b) Effect of Change in Control. The following provisions shall apply if a Change in Control (as defined in Section 3(c) occurs while Units remain outstanding pursuant to this Award.:

(1) If the surviving or successor entity (which may include the Company), or such entity's parent corporation, continues, assumes or replaces this Award (with such adjustments as may be required or permitted by Section 17 of the Plan), this Award or its replacement shall remain outstanding and be governed by its terms, including Section 3(b)(3) below. For these purposes, this Award shall be considered assumed or replaced if, in connection with the Change in Control, either (i) the contractual obligations represented by the Award are expressly assumed by the surviving or successor entity (or its parent corporation) with appropriate adjustments to the number and type of securities subject to the Award that preserves the intrinsic value of the Award existing at the time of the Change in Control, or (ii) you have received a comparable equity-based award that preserves the intrinsic value of this Award existing at the time of the Change in Control and contains terms and conditions that are substantially similar to those of this Award.

(2) If and to the extent that this Award is not continued, assumed or replaced in connection with a Change in Control, then all outstanding Units shall fully vest at or immediately prior to the effective time of the Change in Control. The Committee may alternatively provide that this Award shall be canceled at or immediately prior to the effective time of the Change in Control in exchange for a payment to you in an amount equal to the fair market value (as determined in good faith by the Committee) of the consideration that would otherwise be received in the Change in Control transaction by a Company stockholder for the number of Shares for which outstanding Units could then be settled (or, if no consideration would be received by the Company's stockholders in the Change of Control transaction, the fair market value (as determined in good faith by the Committee) of such number of Shares immediately prior to the Change in Control). Payment of any such amount may be made in such form, on such terms and subject to such conditions as the Committee determines in its discretion,

which may or may not be the same as the form, terms and conditions applicable to payments to the Company's stockholders in connection with the Change in Control, and may, in the Committee's discretion, include subjecting such payments to escrow or holdback terms comparable to those imposed upon the Company's stockholders under the Change in Control, or calculating and paying the present value of payments that would otherwise be subject to escrow or holdback terms.

(3) If and to the extent that this Award is continued, assumed or replaced under the circumstances described in Section 3(b)(1), and if within 12 months after the Change in Control you experience an Employment Termination Event (as defined in Section 3(d)), then this Award and any outstanding Units shall immediately vest in full.

(c) Change in Control. "*Change in Control*" means one of the following:

(i) any individual, entity or Group (a "*Person*") becomes a "beneficial owner" (as defined in Rule 13d-3 or any successor rule under the Exchange Act), directly or indirectly, of 30% or more of the combined voting power of the Company's voting securities, except that the following shall not constitute a Change in Control: (A) any acquisition or beneficial ownership by the Company or a Subsidiary; (B) any acquisition or beneficial ownership by any employee benefit plan (or related trust) sponsored or maintained by the Company or one or more Subsidiary; (C) any formation of a Group consisting solely of beneficial owners of the Company's voting securities as of the effective date of the Plan, or any repurchase or other acquisition by the Company of its voting securities that causes any Person to become the beneficial owner of 30% or more of the Company's voting securities, in either case so long as such Person does not acquire beneficial ownership of additional Company voting securities after the Person initially became the beneficial owner of 30% or more of the Company's voting securities by one of the means described in this clause (C); or (D) any acquisition of beneficial ownership by any entity with respect to which, immediately following such acquisition, more than 50% of the combined voting power of such entity's then outstanding voting securities is beneficially owned, directly or indirectly, by all or substantially all of the Persons who beneficially owned the Company's voting securities immediately prior to such acquisition in substantially the same proportions as their ownership of the Company's voting securities immediately prior to such acquisition;

(ii) individuals (A) who are, as of the effective date of the Plan, directors of the Company, or (B) who are elected as directors of the Company subsequent to the Grant Date and whose initial election, or nomination for initial election by the Company's stockholders, was approved by at least a majority of the then Continuing Directors (collectively, "*Continuing Directors*") cease for any reason to constitute a majority of the members of the Board; or

(iii) the consummation of a Fundamental Change unless, immediately following such Fundamental Change, all or substantially all of the Persons who were the beneficial owners of the Company's voting securities immediately prior to such Fundamental Change beneficially own, directly or indirectly, more than 50% of the combined voting power of the then outstanding voting securities of the surviving or acquiring entity (or its Parent) resulting from such Fundamental Change in substantially the same proportions as their ownership, immediately prior to such Fundamental Change, of the Company's voting securities.

(iv) Notwithstanding the foregoing, to the extent that this Award constitutes a deferral of compensation subject to Code Section 409A, then no Change in Control shall be deemed to have occurred upon an event described in this Section 3(c) unless the event would also constitute a change in ownership or effective control of, or a change in the ownership of a substantial portion of the assets of, the Company under Code Section 409A.

(d) Employment Termination Event. An "*Employment Termination Event*" will be deemed to have occurred upon either: (i) the involuntary termination of your employment for reasons other than Cause (as defined in Section 3(e)), or (ii) the voluntary termination of your employment for Good Reason (as defined in Section 3(f)).

(e) Cause. "*Cause*" means only the following: (i) your indictment or conviction of, or a plea of nolo contendere to, (A) any felony (other than any felony arising out of negligence), or any misdemeanor involving moral turpitude with respect to the Company, or (B) your commission any crime or offense involving dishonesty with respect to the Company; (ii) theft or embezzlement by you of Company property or commission of similar acts involving dishonesty or moral turpitude; (iii) repeated material negligence in the performance of your duties after you have received written notice of the same; (iv) your failure to devote substantially all of your working time and efforts during normal business hours to the Company's business; (v) your knowing engagement in conduct that is materially injurious to the Company; or (vi) your knowingly providing materially misleading information concerning the Company to the Company's Board of Directors, any governmental body or regulatory agency or to any lender or other financing source or proposed financing source of the Company.

(f) Good Reason. "*Good Reason*" means only the following: (i) the failure of the Company to pay any material amount due to you under a prevailing Employment Agreement; (ii) a meaningful diminution, without Cause, as defined above, in your responsibilities or job functions unless approved by you; (iii) a material reduction in your total compensation potential as defined by annual base salary and cash compensation targets; or (iv) your relocation to an office location greater than 50 miles from your office location at the time of a Change in Control.

4. **Effect of Termination of Employment**. Except as otherwise provided in accordance with Section 3(b)(3), if you cease to be employed by the Company or any of its Affiliates prior to the Vesting Date(s) specified on the cover page of this Agreement, you will forfeit all unvested Units.

5. **Settlement of Units**. After any Units vest pursuant to Section 3, the Company shall, as soon as practicable (but no later than March 15 of the year following the calendar year in which such Units vest), cause to be issued and delivered to you, or to your designated beneficiary or estate in the event of your death, one Share in payment and settlement of each vested Unit. Delivery of the Shares shall be effected by an appropriate entry in the stock register maintained by the Company's transfer agent with a notice of issuance provided to you, or by the electronic delivery of the Shares to a brokerage account you designate, and shall be subject to the tax withholding provisions of Section 6 and compliance with all applicable legal requirements, including compliance with the requirements of applicable federal and state securities laws, and shall be in complete satisfaction and settlement of such vested Units.

6. **Tax Consequences and Withholding**. As a condition precedent to the delivery of Shares in settlement of the Units, you are required to make arrangements acceptable to the Company for payment of any federal, state, local or foreign withholding taxes that may be due as a result of the settlement of vested Units. The Company will retain a portion of the Shares that would otherwise be delivered to you in settlement of vested Units, which retained Shares shall have a Fair Market Value equal to the amount required to be withheld, unless you provide notice to the Company prior to the vesting date of the Units that you desire to pay cash or direct the Company (or any Affiliate) to withhold from payroll or other amounts payable to you any sums required to satisfy such withholding tax obligations, and otherwise agree to satisfy such obligations in accordance with the provisions of Section 15 of the Plan. Delivery of Shares upon the vesting of Units is subject to the satisfaction of applicable withholding tax obligations.

7. **No Stockholder Rights**. The Units subject to this Award do not entitle you to any rights of a holder of the Company's Stock. You will not have any of the rights of a stockholder of the Company in connection with the grant of Units subject to this Agreement unless and until Shares are issued to you in settlement of the Units as provided in Section 5.

8. **Plan Document**. This Agreement and the Award are subject to all the provisions of the Plan, and to all interpretations, rules and regulations that may, from time to time, be adopted and promulgated by the Committee pursuant to the Plan. If there is any conflict between the provisions of this Agreement and the Plan, the provisions of the Plan will govern.

9. **Choice of Law**. This Agreement will be interpreted and enforced under the laws of the state of Minnesota (without to its conflicts or choice of law principles).

10. **Effect**. This Agreement will be binding in all respects on your heirs, representatives, successors and assigns, and on the successors and assigns of the Company.

11. **Discontinuance of Employment**. This Agreement does not give you a right to continued employment with the Company or Affiliate, and the Company or any such Affiliate may terminate your employment at any time and otherwise deal with you without regard to the effect it may have upon you under this Agreement.

12. **Section 409A of the Code**. The award of Units as provided in this Agreement and any issuance of Shares pursuant to this Agreement are intended to be exempt from Section 409A of the Code under the short-term deferral specified in Treas. Reg. § 1.409A-l(b)(4).

***By signing the cover page of this Agreement or otherwise accepting this Award in a manner approved by the Company, you agree to all the terms and conditions contained in this Agreement and in the Plan document.***

**Digi International Inc.**

**2017 Omnibus Incentive Plan**

**Restricted Stock Unit Award Agreement**

Digi International, Inc. (the "*Company*"), pursuant to its 2017 Omnibus Incentive Plan (the "*Plan*"), hereby grants an Award of restricted Stock Units to you, the Participant named below. The terms and conditions of this Award are set forth in this Restricted Stock Unit Award Agreement (the "*Agreement*"), consisting of this cover page and the Terms and Conditions on the following pages, and in the Plan document, which has been provided to you. To the extent any capitalized term used in this Agreement is not defined, it shall have the meaning assigned to it in the Plan as it currently exists or as it is amended in the future.

| | |
|---|---|
| Name of Participant: | |
| Number of Restricted Stock Units: | Grant Date:__________, 20__ |
| Vesting Schedule:<br>Vesting Date(s) | <br>Number of Stock Units that Vest |

By signing below, you agree to all of the terms and conditions contained in this Agreement and in the Plan document. You acknowledge that you have reviewed these documents and that they set forth the entire agreement between you and the Company regarding the grant to you of the number of Restricted Stock Units specified in the table above.

PARTICIPANT:

DIGI INTERNATIONAL INC.

By:

Title:

**Digi International Inc.**

**2017 Omnibus Incentive Plan**

**Restricted Stock Unit Award Agreement**

**Terms and Conditions**

1. **Grant of Restricted Stock Units**. The Company hereby grants to you, subject to the terms and conditions in this Agreement and the Plan, an Award of the number of restricted Stock Units ("*Units*") specified on the cover page of this Agreement, each representing the right to receive one Share of the Company's Stock. The Units granted to you will be credited to an account in your name maintained by the Company. This account shall be unfunded and maintained for book-keeping purposes only, with the Units simply representing an unfunded and unsecured obligation of the Company.

2. **Restrictions on Units**. Neither this Award nor the Units subject to this Award may be sold, assigned, transferred, exchanged or encumbered other than by will or the laws of descent and distribution. Any attempted transfer in violation of this Section 2 shall be of no effect and shall result in the forfeiture of all Units. The Units and your right to receive shares in settlement of the Units under this Agreement shall be subject to forfeiture as provided in Section 4 until satisfaction of the vesting conditions set forth in Section 3.

3. **Vesting of Units**.

(a) Scheduled Vesting. If you remain employed (which includes other service relationships described in Section 5 of the Plan) by the Company or any of its Affiliates continuously from the Grant Date specified on the cover page of this Agreement, then the Units will vest in the numbers and on the dates specified in the Vesting Schedule on the cover page of this Agreement.

(b) Effect of Change in Control. The following provisions shall apply if a Change in Control (as defined in Section 3(c)) occurs while Units remain outstanding pursuant to this Award.:

(1) If the surviving or successor entity (which may include the Company), or such entity's parent corporation, continues, assumes or replaces this Award (with such adjustments as may be required or permitted by Section 17 of the Plan), this Award or its replacement shall remain outstanding and be governed by its terms. For these purposes, this Award shall be considered assumed or replaced if, in connection with the Change in Control, either (i) the contractual obligations represented by the Award are expressly assumed by the surviving or successor entity (or its parent corporation) with appropriate adjustments to the number and type of securities subject to the Award that preserves the intrinsic value of the Award existing at the time of the Change in Control, or (ii) you have received a comparable equity-based award that preserves the intrinsic value of this Award existing at the time of the Change in Control and contains terms and conditions that are substantially similar to those of this Award.

(2) If and to the extent that this Award is not continued, assumed or replaced in connection with a Change in Control, then all outstanding Units shall fully vest at or immediately prior to the effective time of the Change in Control. The Committee may alternatively provide that this Award shall be canceled at or immediately prior to the effective time of the Change in Control in exchange for a payment to you in an amount equal to the fair market value (as determined in good faith by the Committee) of the consideration that would otherwise be received in the Change in Control transaction by a Company stockholder for the number of Shares for which outstanding Units could then be settled (or, if no consideration would be received by the Company's stockholders in the Change of Control transaction, the fair market value (as determined in good faith by the Committee) of such number of Shares immediately prior to the Change in Control). Payment of any such amount may be made in such form, on such terms and subject to such conditions as the Committee determines in its discretion,

which may or may not be the same as the form, terms and conditions applicable to payments to the Company's stockholders in connection with the Change in Control, and may, in the Committee's discretion, include subjecting such payments to escrow or holdback terms comparable to those imposed upon the Company's stockholders under the Change in Control, or calculating and paying the present value of payments that would otherwise be subject to escrow or holdback terms.

(c) Change in Control. "*Change in Control*" means one of the following:

(i) any individual, entity or Group (a "*Person*") becomes a "beneficial owner" (as defined in Rule 13d-3 or any successor rule under the Exchange Act), directly or indirectly, of 30% or more of the combined voting power of the Company's voting securities, except that the following shall not constitute a Change in Control: (A) any acquisition or beneficial ownership by the Company or a Subsidiary; (B) any acquisition or beneficial ownership by any employee benefit plan (or related trust) sponsored or maintained by the Company or one or more Subsidiary; (C) any formation of a Group consisting solely of beneficial owners of the Company's voting securities as of the effective date of the Plan, or any repurchase or other acquisition by the Company of its voting securities that causes any Person to become the beneficial owner of 30% or more of the Company's voting securities, in either case so long as such Person does not acquire beneficial ownership of additional Company voting securities after the Person initially became the beneficial owner of 30% or more of the Company's voting securities by one of the means described in this clause (C); or (D) any acquisition of beneficial ownership by any entity with respect to which, immediately following such acquisition, more than 50% of the combined voting power of such entity's then outstanding voting securities is beneficially owned, directly or indirectly, by all or substantially all of the Persons who beneficially owned the Company's voting securities immediately prior to such acquisition in substantially the same proportions as their ownership of the Company's voting securities immediately prior to such acquisition;

(ii) individuals (A) who are, as of the effective date of the Plan, directors of the Company, or (B) who are elected as directors of the Company subsequent to the Grant Date and whose initial election, or nomination for initial election by the Company's stockholders, was approved by at least a majority of the then Continuing Directors (collectively, "*Continuing Directors*") cease for any reason to constitute a majority of the members of the Board; or

(iii) the consummation of a Fundamental Change unless, immediately following such Fundamental Change, all or substantially all of the Persons who were the beneficial owners of the Company's voting securities immediately prior to such Fundamental Change beneficially own, directly or indirectly, more than 50% of the combined voting power of the then outstanding voting securities of the surviving or acquiring entity (or its Parent) resulting from such Fundamental Change in substantially the same proportions as their ownership, immediately prior to such Fundamental Change, of the Company's voting securities.

(iv) Notwithstanding the foregoing, to the extent that this Award constitutes a deferral of compensation subject to Code Section 409A, then no Change in Control shall be deemed to have occurred upon an event described in this Section 3(c) unless the event would also constitute a change in ownership or effective control of, or a change in the ownership of a substantial portion of the assets of, the Company under Code Section 409A.

4. **Effect of Termination of Employment**. If you cease to be employed by the Company or any of its Affiliates prior to the Vesting Date(s) specified on the cover page of this Agreement, you will forfeit all unvested Units.

5. **Settlement of Units**. After any Units vest pursuant to Section 3, the Company shall, as soon as practicable (but no later than March 15 of the year following the calendar year in which such Units vest), cause to be issued and delivered to you, or to your designated beneficiary or estate in the event of your death, one Share in payment

and settlement of each vested Unit. Delivery of the Shares shall be effected by an appropriate entry in the stock register maintained by the Company's transfer agent with a notice of issuance provided to you, or by the electronic delivery of the Shares to a brokerage account you designate, and shall be subject to the tax withholding provisions of Section 6 and compliance with all applicable legal requirements, including compliance with the requirements of applicable federal and state securities laws, and shall be in complete satisfaction and settlement of such vested Units.

6. **Tax Consequences and Withholding**. As a condition precedent to the delivery of Shares in settlement of the Units, you are required to make arrangements acceptable to the Company for payment of any federal, state, local or foreign withholding taxes that may be due as a result of the settlement of vested Units. The Company will retain a portion of the Shares that would otherwise be delivered to you in settlement of vested Units, which retained Shares shall have a Fair Market Value equal to the amount required to be withheld, unless you provide notice to the Company prior to the vesting date of the Units that you desire to pay cash or direct the Company (or any Affiliate) to withhold from payroll or other amounts payable to you any sums required to satisfy such withholding tax obligations, and otherwise agree to satisfy such obligations in accordance with the provisions of Section 15 of the Plan. Delivery of Shares upon the vesting of Units is subject to the satisfaction of applicable withholding tax obligations.

7. **No Stockholder Rights**. The Units subject to this Award do not entitle you to any rights of a holder of the Company's Stock. You will not have any of the rights of a stockholder of the Company in connection with the grant of Units subject to this Agreement unless and until Shares are issued to you in settlement of the Units as provided in Section 5.

8. **Plan Document**. This Agreement and the Award are subject to all the provisions of the Plan, and to all interpretations, rules and regulations that may, from time to time, be adopted and promulgated by the Committee pursuant to the Plan. If there is any conflict between the provisions of this Agreement and the Plan, the provisions of the Plan will govern.

9. **Choice of Law**. This Agreement will be interpreted and enforced under the laws of the state of Minnesota (without to its conflicts or choice of law principles).

10. **Effect**. This Agreement will be binding in all respects on your heirs, representatives, successors and assigns, and on the successors and assigns of the Company.

11. **Discontinuance of Employment**. This Agreement does not give you a right to continued employment with the Company or Affiliate, and the Company or any such Affiliate may terminate your employment at any time and otherwise deal with you without regard to the effect it may have upon you under this Agreement.

12. **Section 409A of the Code**. The award of Units as provided in this Agreement and any issuance of Shares pursuant to this Agreement are intended to be exempt from Section 409A of the Code under the short-term deferral specified in Treas. Reg. § 1.409A-l(b)(4).

***By signing the cover page of this Agreement or otherwise accepting this Award in a manner approved by the Company, you agree to all the terms and conditions contained in this Agreement and in the Plan document.***

Exhibit 10(b)(iv)

| Notice of Grant of Stock Options and Option Agreement | **Digi International Inc.**<br>**ID:** 41-1532464<br>11001 Bren Road East<br>Minnetonka, MN 55343 |
|---|---|
| **[Optionee]**<br>**[Address]**<br>**[City, State, County, Zip Code]** | **Option Number:**<br>**Plan: 2017 Omnibus Incentive Plan**<br>**ID:** |

Effective [date], you have been granted a Non-Qualified Stock Option to buy [number of shares] shares of Digi International Inc. (the Company) stock at $[per share exercise price] per share.

The total option price of the shares granted is $[aggregate exercise price]

Shares in each period will become fully vested on the date shown.

| Shares | Vest Type | Full Vest | Expiration |
|---|---|---|---|

By your signature and the Company's signature below, you and the Company agree that these options are granted under and governed by the terms and conditions of the Company's Stock Option Plan as amended and the Option Agreement, all of which are attached and made a part of this document.

| | |
|---|---|
| Digi International Inc. | Date |
| [Optionee] | Date |

**DIGI INTERNATIONAL INC.**

**2017 OMNIBUS INCENTIVE PLAN**

Terms and Conditions of an Award

These are the terms and conditions applicable to the INCENTIVE PLAN AWARD AGREEMENT between Digi International Inc., a Delaware corporation (the "Company"), and the participant (the "Participant") listed on the cover page hereof (the "Cover Page") effective as of the date of award. The Cover Page together with these terms and conditions of Incentive Plan Award Agreement constitute the "Incentive Plan Award Agreement."

WHEREAS, the Company desires to carry out the purposes of its Digi International Inc. 2017 Omnibus Incentive Plan as amended from time to time (the "Plan"), by affording the Participant an opportunity to purchase Stock of the Company, par value $.01 per share (the " Shares"), according to the terms set forth herein and on the Cover Page;

NOW THEREFORE, the Company hereby awards this Option to the Participant under the terms and conditions as follows:

1. **Award of Option.** Subject to the terms of the Plan, the Company hereby awards to the Participant the right and option (the "Option") to purchase the number of Shares specified on the Cover Page, on the terms and conditions hereinafter set forth. The Option is not intended by the Company to be an "incentive stock option" within the meaning of Section 422 of the Internal Revenue Code of 1986, as amended (the "Code").

2. **Purchase Price.** The purchase price of each of the Shares subject to the Option shall be the exercise price per share specified on the Cover Page, which price has been specified in accordance with the Plan and shall not be less than the Fair Market Value (as defined in paragraph 2.1(1) of the Plan) of a Share as of the date of grant.

3. **Option Period.**

(a) Subject to the provisions of paragraphs 5(a), 6(a) and 6(b) hereof, the Option shall become exercisable as to the number of Shares and on the dates specified in the exercise schedule on the Cover Page. The exercise schedule shall be cumulative; thus, to the extent the Option has not already been exercised and has not expired, terminated or been canceled, the Participant may at any time, and from time to time, purchase all or any portion of the Shares then purchasable under the exercise schedule.

(b) The Option and all rights to purchase Shares thereunder shall cease on the earliest of:

(i) the expiration date specified on the Cover Page (which date shall not be more than seven years after the date of grant);

(ii) the expiration of the period after the termination of the Participant's employment (as defined in paragraph 6.4 of the Plan) within which the Option is exercisable as specified in paragraph 5(a); or

(iii) the date, if any, fixed for cancellation pursuant to paragraph 6(b) hereof.

Notwithstanding any other provision in this Incentive Plan Award Agreement, in no event may anyone exercise the Option, in whole or in part, after its original expiration date.

**4. Manner of Exercising Option.** Subject to the terms and conditions of this Incentive Plan Award Agreement, the Option may be exercised online with E*Trade at www.etrade.com/stockplans or by such other means as the Committee shall approve. In accordance with present practice, when your Option is awarded, a letter or email will be sent to you from E*Trade with instructions on how to activate your account with E*Trade so that you can view and exercise your Option online. If you are a director or officer of the Company, then you must contact E*Trade Executive Support at 1-800-775-2793 in order to exercise your Option.

**5. Exercisability of Option After Termination of Employment.**

(a) During the lifetime of the Participant, the Option may be exercised only while the Participant is employed (as defined in paragraph 5 of the Plan) by the Company or a parent or subsidiary thereof, and only if the Participant has been continuously so employed since the date of this Incentive Plan Award Agreement, except that:

(i) if the Participant is not a Non-Employee Director (as defined in paragraph 2.1(q) of the Plan), the Option shall continue to be exercisable for three months after termination of the Participant's employment for any reason other than death, disability or cause, but only to the extent that the Option was exercisable immediately prior to the Participant's termination of employment;

(ii) if the Participant is not a Non-Employee Director, in the event the Participant's employment terminates because the Participant is disabled (within the meaning of Section 22(e)(3) of the Code), the Participant or his or her legal representative may exercise the Option (to the extent specified in paragraph 6(a) of this Incentive Plan Award Agreement) within one year after the termination of the Participant's employment because of such disability;

(iii) if the Participant is not a Non-Employee Director and if the Participant dies while employed, or within three months after his or her termination of employment, the heirs or legatees of the Participant's estate or the person who acquired the right to exercise the Option by bequest or inheritance may exercise the Option (to the extent specified in paragraph 6(a)) within one year after the death of the Participant;

(iv) if the Participant is a Non-Employee Director, the Option shall continue to be exercisable after the Participant's employment ends for the remaining term of the Option, but shall be exercisable only to the extent that the Option was exercisable immediately prior to the end of Participant's employment, except that if the Participant's employment ends because of death or disability, or the Participant dies within three months of his or her employment ending, the Option, whether or not previously exercisable, shall become exercisable to the extent specified in paragraph 6(a) of this Incentive Plan Award Agreement and shall continue to be exercisable after the Participant's employment ends for the remaining term of the Option;

(v) if the Participant's employment terminates due to cause (as defined in paragraph 20.1 of the Plan), the Option and all rights of the Participant hereunder shall terminate immediately; and

(vi) if the Participant's employment terminates after a declaration pursuant to paragraph 6(b) of this Incentive Plan Award Agreement, the Participant may exercise the Option at any time permitted by such declaration.

If, during the term of the Option, the Participant's status changes to or from that of a Non-Employee Director, the provisions of this paragraph 5(a) shall be applied to the Participant based on the Participant's status as of the date the Option was awarded.

(b) Neither the transfer of the Participant between any combination of the Company and any Affiliate, nor a leave of absence awarded to the Participant and approved by the Committee, shall be deemed a termination of employment.

**6. Acceleration of Option.**

(a) Disability or Death. If paragraph 5(a)(ii), 5(a)(iii) or the exception clause of paragraph 5(a)(iv) of this Incentive Plan Award Agreement is applicable, the Option, whether or not previously exercisable, shall become immediately exercisable in full if the Participant shall have been employed continuously by the Company or an Affiliate between the date the Option was granted and the date of such disability or, in the event of death, the date of such Participant's death.

(b) Dissolution, Liquidation, Merger. In the event of (i) a proposed merger or consolidation of the Company with or into any other corporation, regardless of whether the Company is the surviving corporation, unless appropriate provision shall have been made for the protection of the Option by the substitution, in lieu of the Option, of an option to purchase appropriate voting stock (the "Survivor's Stock") of the corporation surviving any such merger or consolidation or, if appropriate, the parent corporation of the Company or such surviving corporation, or, alternatively, by the delivery of a number of shares of the Survivor's Stock that has a Fair Market Value as of the effective date of such merger or consolidation equal to the product of (A) the excess of (x) the Event Proceeds per Share (as hereinafter defined) covered by the Option as of such effective date, over (y) the Option exercise price per Share, times (B) the number of Shares covered by the Option, or (ii) the proposed dissolution or liquidation of the Company (such merger, consolidation, dissolution or liquidation being herein called an "Event"), the Committee shall declare, at least ten days prior to the actual effective date of an Event, and provide written notice to the Participant of the declaration, that the Option, whether or not then exercisable, shall be canceled at the time of, or immediately prior to the occurrence of, the Event (unless it shall have been exercised prior to the occurrence of the Event) in exchange for payment to the Participant, within ten days after the Event, of cash equal to the amount (if any), for each Share covered by the canceled Option, by which the Event Proceeds per Share (as hereinafter defined) exceeds the exercise price per Share covered by the Option. At the time of the declaration provided for in the immediately preceding sentence, the Option shall immediately become exercisable in full and the Participant shall have the right, during the period preceding the time of cancellation of the Option, to exercise the Option as to all or any part of the Shares covered thereby. The Option, to the extent it shall not have been exercised prior to the Event, shall be canceled at the time of, or immediately prior to, the Event, as provided in the declaration, and this Plan shall terminate at the time of such cancellation, subject to the payment obligations of the Company provided in this paragraph 6(b). For purposes of this paragraph, "Event Proceeds per Share" shall mean the cash plus the fair market value, as determined in good faith by the Committee, of the non-cash consideration to be received per Share by the stockholders of the Company upon the occurrence of the Event.

**7. Limitation on Transfer.** During the lifetime of the Participant, only the Participant or his or her guardian or legal representative may exercise the Option. The Participant shall not assign or transfer the Option otherwise than by will or the laws of descent and distribution, and the Option shall not be subject to pledge, hypothecation, execution, attachment or similar process. Any attempt to assign, transfer, pledge, hypothecate or otherwise dispose of the Option contrary to the provisions hereof, and the levy of any attachment or similar process upon the Option, shall be null and void.

**8. Stockholder Rights Before Exercise.** The Participant shall have none of the rights of a stockholder of the Company with respect to any share subject to the Option until the share is actually issued to him or her upon exercise of the Option.

**9. Adjustment For Changes in Capitalization.** The Option is subject to adjustment for changes in capitalization as provided in paragraph 17 of the Plan.

**10. Tax Withholding.** The parties hereto recognize that the Company or a parent or subsidiary thereof may be obligated to withhold federal and state income taxes and social security or other taxes upon the Participant's exercise of the Option. The Participant agrees that, at the time he or she exercises the Option, if the Company or a parent or subsidiary thereof is required to withhold such taxes, he or she will promptly pay in cash upon demand to the Company, or the parent or subsidiary having such obligation, such amounts as shall be necessary to satisfy such obligation; provided, however, that in lieu of all or any part of such a cash payment, the Committee may, but shall not be required to (or, in the case of an Participant who is a Non-Employee Director (as defined in the Plan), the Committee shall) permit the Participant to elect to cover all or any part of the required withholdings (up to the Participant's minimum required tax withholding rate) through a reduction of the number of Shares delivered to the Participant or through a subsequent return to the Company of shares delivered to the Participant.

**11. Interpretation of this Incentive Plan Award Agreement.** All decisions and interpretations made by the Committee with regard to any question arising hereunder or under the Plan shall be binding and conclusive upon the Company and the Participant. In the event that there is any inconsistency between the provisions of this Incentive Plan Award Agreement and the Plan, the provisions of the Plan shall govern.

**12. Discontinuance of Employment.** This Incentive Plan Award Agreement shall not give the Participant a right to continued employment with the Company or any parent or subsidiary thereof, and the Company or any such parent or subsidiary thereof employing the Participant may terminate his or her employment and otherwise deal with the Participant without regard to the effect it may have upon him or her under this Incentive Plan Award Agreement.

**13. General.** The Company shall at all times during the term of this Option reserve and keep available such number of Shares as will be sufficient to satisfy the requirements of this Incentive Plan Award Agreement. This Incentive Plan Award Agreement shall be binding in all respects on the Participant's heirs, representatives, successors and assigns. This Incentive Plan Award Agreement is entered into under the laws of the State of Minnesota and shall be construed and interpreted thereunder.

**DIGI INTERNATIONAL INC.**

**2017 OMNIBUS INCENTIVE PLAN**

**Addendum I**

**to**

**Terms and Conditions of Nonstatutory Stock Option Agreement**

Paragraph 6, entitled "Acceleration of Option," is amended to add new subparagraph (c), which provides as follows:

(c) Change in Control and Employment Termination Event. The Option, whether or not previously exercisable, shall become immediately exercisable in full upon the occurrence of any "Change in Control" that occurs contemporaneously with, or is followed within 12 months of the Change in Control by, an "Employment Termination Event".

A "*Change in Control*" will be deemed to have occurred upon the occurrence of either of the following events:

(i) any person, as defined in Sections 3(a)(9) and 13(d)(3) of the Securities Exchange Act of 1934 (the "Exchange Act"), becomes the "beneficial owner" (as defined in Rule 13d-3 promulgated pursuant to the Exchange Act), directly or indirectly, of securities of the Company having 25% or more of the voting power in the election of directors of the Company, excluding, however, Participant (or a group of persons, including Participant, acting in concert); or

(ii) the occurrence within any period, commencing immediately after an Annual Meeting of Stockholders and continuing to and including the Annual Meeting of Stockholders occurring on or about the third anniversary date of the commencement of such period, of a change in the Board of Directors of the Company with the result that the Incumbent Members (as defined below) do not constitute a majority of the Company's Board of Directors. The term "Incumbent Members" shall mean the members of the Board on the date of the commencement of such period, provided that any person becoming a director during such period whose election or nomination for election was approved by a majority of the directors who, on the date of such election or nomination for election, comprised the Incumbent Members shall be considered one of the Incumbent Members in respect of such period.

An "*Employment Termination Event*" will be deemed to have occurred upon either:

For purposes of this subparagraph (c), "*Cause*" means only the following:

(i) indictment or conviction of, or a plea of nolo contendere to, (A) any felony (other than any felony arising out of negligence), or any misdemeanor involving moral turpitude with respect to the Company, or (B) any crime or offense involving dishonesty with respect to the Company;

(ii) theft or embezzlement of Company property or commission of similar acts involving dishonesty or moral turpitude;

(iii) repeated material negligence in the performance of Participant's duties after the Participant has received written notice of the same;

(iv) Participant's failure to devote substantially all of his working time and efforts during normal business hours to the Company's business;

(v) knowing engagement in conduct that is materially injurious to the Company; or

(vi) knowingly providing materially misleading information concerning the Company to the Company's Board of Directors, any governmental body or regulatory agency or to any lender or other financing source or proposed financing source of the Company.

For purposes of this subparagraph (c), "*Good Reason*" means only the following:

(i) the failure of the Company to pay any material amount due to Participant under a prevailing Employment Agreement;

(ii) a meaningful diminution, without Cause, as defined above, in the responsibilities or job functions of the Participant unless approved by the Participant;

(iii) a material reduction in total compensation potential as defined by annual base salary and cash compensation targets; or

(iv) the relocation of Participant to an office location greater than 50 miles from his/her office location at the time of a Change in Control.

**Exhibit No. 31(a)**

**CERTIFICATION PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Ronald E. Konezny, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Digi International Inc.;

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 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 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.

| | |
|---|---|
| May 5, 2017 | /s/ Ronald E. Konezny |
| | Ronald E. Konezny |
| | President and Chief Executive Officer |

**Exhibit No. 31(b)**

**CERTIFICATION PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Michael C. Goergen, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Digi International Inc.;

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 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 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.

| | |
|---|---|
| May 5, 2017 | /s/ Michael C. Goergen |
| | Michael C. Goergen |
| | Senior Vice President, Chief Financial Officer and Treasurer |

**Exhibit No. 32**

**CERTIFICATION PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Digi International Inc. (the Registrant) on Form 10-Q for the fiscal quarter ended March 31, 2017 as filed with the Securities and Exchange Commission on the date hereof, each of the undersigned certifies, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Quarterly Report on Form 10-Q complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Quarterly Report on Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Registrant.

May 5, 2017

/s/ Ronald E. Konezny

Ronald E. Konezny
President and Chief Executive Officer

/s/ Michael C. Goergen

Michael C. Goergen
Senior Vice President, Chief Financial Officer and Treasurer