UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended March 31, 2005

OR

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

For the transition period from to

Commission file number 001-08762

ITERIS, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**95-2588496**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

1515 South Manchester Avenue, Anaheim, California 92802
(Address of Principal Executive Offices) (Zip Code)

Registrant's Telephone Number, Including Area Code: **(714) 774-5000**

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

Title of each class	**Name of each exchange on which registered**
Common Stock, $0.10 par value	American Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: **None**

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

Indicate by a check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K ☒

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

Based on the closing sale price on the OTC Bulletin Board on September 30, 2004, the last business day of the registrant's most recently completed second fiscal quarter, the aggregate market value of the voting common stock held by nonaffiliates of the registrant was $44,496,650. For the purposes of this calculation, shares owned by officers, directors and 10% stockholders known to the registrant have been deemed to be owned by affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

As of June 22, 2005, there were 28,409,905 shares of common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Information required by Items 10 through 14 of Part III of this report is incorporated herein by reference to portions of the registrant's definitive proxy statement for its 2005 Annual Meeting of Stockholders, which will be filed with the Securities and Exchange Commission not later than 120 days after the end of the fiscal year ended March 31, 2005. Except with respect to information specifically incorporated by reference in this report, the registrant's proxy statement is not deemed to be filed as part hereof.

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ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

Unless otherwise indicated in this report, the "registrant," "we," "us" and "our" collectively refers to Iteris, Inc. (formerly known as Iteris Holdings, Inc. and Odetics, Inc.) and its subsidiary, Meyer, Mohaddes Associates, Inc.

Autovue™, Iteris™ and Vantage™ are among the trademarks of Iteris, Inc. Any other trademarks or trade names mentioned herein are the property of their respective owners.

Cautionary Statement

This report, including the following discussion and analysis, contains forward-looking statements (within the meaning of the Private Securities Litigation Reform Act of 1995) that are based on our current expectations, estimates and projections about our business and our industry, and reflect management's beliefs and certain assumptions made by us based upon information available to us as of the date of this report. When used in this report and the information incorporated herein by reference, the words "expect(s)," "feel(s)," "believe(s)," "should," "will," "may," "anticipate(s)," "estimate(s)" and similar expressions or variations of these words are intended to identify forward-looking statements. These forward-looking statements include but are not limited to statements regarding our anticipated sales, revenue, expenses, profits, capital needs, competition, backlog and manufacturing capabilities, the practical market applications, future applications and acceptance of our products and services, and the status of our facilities, product development and renegotiations with our lender. These statements are not guarantees of future performance and are subject to certain risks and uncertainties which could cause actual results to differ materially from those projected. You should not place undue reliance on these forward-looking statements that speak only as of the date hereof. We undertake no obligation to republish revised forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events. We encourage you to carefully review and consider the various disclosures made by us which describe certain factors which could affect our business, including those "Risk Factors" at the end of Item 7 of this report, before deciding to invest in our company or to maintain or increase your investment. We undertake no obligation to revise or update publicly any forward-looking statement for any reason.

PART I

ITEM 1. BUSINESS

Overview

Iteris, Inc., formerly known as Iteris Holdings, Inc., is a leading provider of outdoor machine vision systems and sensors that optimize the flow of traffic and enhance driver safety. Using proprietary software and Intelligent Transportation Systems ("ITS") industry expertise, we provide video sensor systems, transportation management and traveler information systems and other engineering consulting services to the ITS industry. The ITS industry is comprised of companies applying a variety of technologies to enable the safe and efficient movement of people and goods. We use our outdoor image recognition software expertise to develop proprietary algorithms for video sensor systems that improve vehicle safety and the flow of traffic. Using our knowledge of the ITS industry, we design and implement transportation management systems that help public agencies reduce traffic congestion and provide greater access to traveler information. On October 22, 2004, we completed a merger with our majority-owned subsidiary, Iteris, Inc. (the "Iteris Subsidiary"), and officially changed our corporate name from Iteris Holdings, Inc. to Iteris, Inc. We were originally incorporated in Delaware in 1987 as Odetics, Inc. and in September 2003 changed our name to Iteris Holdings, Inc. to reflect our focus on the ITS industry and our capital structure at that time.

Our proprietary image recognition systems include AutoVue and Vantage. AutoVue is a small windshield mounted sensor that uses proprietary software to detect and warn drivers of unintended lane departures. We have sold approximately 13,000 production AutoVue Lane Departure Warning ("LDW") systems for use on truck platforms in the European and North American markets, and our AutoVue LDW system is currently offered as an option on certain Mercedes, MAN, Freightliner and International trucks. We believe that our AutoVue LDW technology is a broad sensor platform that, through additional software development, may be expanded to incorporate additional safety and convenience features. Vantage is a video-based vehicle sensing system that detects vehicles on roadways, enabling more efficient traffic management. Applications include traffic signal operations, incident detection and data collection.

Our transportation management systems include the design, development and implementation of our software-based systems that integrate sensors, video surveillance, computers and advanced communications equipment to enable public agencies to monitor, control and direct traffic flow, assist in the quick dispatch of emergency crews and distribute real-time information about traffic conditions. We also offer related services that include planning and other engineering for the implementation of transportation related communications systems, analysis and studies related to goods movement and commercial vehicle operations, and parking systems designs.

We currently operate in three reportable segments: Roadway Sensors, Automotive Sensors and Systems. The Roadway Sensors segment includes our Vantage vehicle detection systems. The Automotive Sensors segment includes our AutoVue LDW systems for vehicle safety. The Systems segment includes transportation engineering and consulting services, and the development of transportation management and traveler information systems for the ITS industry.

Sales, Marketing and Principal Customers

We sell our Vantage vehicle detection systems primarily through indirect sales channels comprised of independent dealers in the United States and Canada who sell integrated systems and related products to the traffic management market. Our independent dealers are primarily responsible for sales, installation and support of Vantage systems. These dealers maintain an inventory of demonstration traffic products from various manufacturers including our Vantage vehicle detection systems and sell directly to government agencies and installation contractors. These dealers often have long-term arrangements with the government agencies in their territory for the supply of various products for the construction and renovation of traffic intersections. We hold technical training classes for dealers and end users and maintain a full-time staff of customer support technicians to provide technical assistance when needed.

Our marketing strategy for AutoVue is to establish it as the leading platform for in-vehicle video sensing for heavy trucks and passenger cars. We sell AutoVue directly to heavy truck manufacturers and to U.S. truck fleets. We also market to the manufacturers of passenger automobiles through a strategic relationship with Valeo Schalter and Sensuren GmbH ("Valeo"), an independent automotive supplier.

We market and sell our transportation management systems and traveler information services directly to government agencies pursuant to negotiated contracts that involve competitive bidding and specific qualification requirements. Most of our contracts with federal, state and municipal customers provide for cancellation or renegotiation at the option of the customer upon reasonable notice and fees paid for modification. We use selected members of our engineering team divided on a regional basis to serve in sales and business development functions. We do not engage in sales of transportation management systems and traveler information services outside of the U.S. Sales of our transportation management systems contracts generally involve long lead times and require extensive specification development, evaluation and price negotiations.

Our largest customer accounted for 12.8% of total net sales and contract revenues in the fiscal year ended March 31, 2005 ("Fiscal 2005").

Manufacturing and Materials

We use contract manufacturers to build subassemblies that are used in our Vantage products. Additionally, we procure certain components from qualified suppliers, both globally and locally, and use multi-sourcing strategies when technically and economically feasible to mitigate supply risk. These subassemblies and components are delivered to our Anaheim facility where they go through final assembly and testing prior to shipment to our customers. Our manufacturing activities are conducted in approximately 8,000 square feet of space at our Anaheim facility. Production volume at our subcontractors is based upon quarterly forecasts that we adjust on a monthly basis to control inventory. For sales of Autovue LDW systems to the truck market, we subcontract the manufacture of our AutoVue LDW systems to one manufacturer, and our internal processes are limited primarily to testing and final verification. We are currently in the process of qualifying an additional subcontractor for the manufacture of LDW systems to mitigate production risk and handle increased demand. For Autovue LDW sales to the passenger car market, we anticipate that all manufacturing will be done by Valeo; however, we plan to continue to provide engineering support to Valeo. We currently do not manufacture any of the hardware used in the transportation management and traveler information systems that we design and implement. Our production facility is currently ISO 9001 certified.

Customer Support and Services

We provide warranty service and support for our Vantage and AutoVue products as well as follow-up service and support for which we charge separately. Service revenue accounted for less than 1.0% of total net sales and contract revenues for Fiscal 2005. We believe customer support is a key competitive factor.

Backlog

Our backlog of unfulfilled firm orders was approximately $18.9 million as of March 31, 2005, which was comprised of $1.7 million related to Roadway Sensors, $3.4 million related to Automotive Sensors and $13.8 million related to Systems. All backlog for Roadway Sensors and Automotive Sensors is expected to be recognized as revenue in the fiscal year ending March 31, 2006 ("Fiscal 2006") while approximately 60.0% of Systems backlog is expected to be recognized as revenue in Fiscal 2006. At March 31, 2004, we had backlog of approximately $21.6 million, which was comprised of $4.7 million related to Roadway Sensors, $3.9 million related to Automotive Sensors and $13.0 million related to Systems. At March 31,

2004, backlog for Roadway Sensors and Automotive Sensors was recognized as revenue in Fiscal 2005 while 63.8% of Systems March 31, 2004, backlog was recognized as revenue in Fiscal 2005. Pursuant to the customary terms of our agreements with government contractors and other customers, customers can generally cancel or reschedule orders with little or no penalties. Lead times for the release of purchase orders often depend upon the scheduling and forecasting practices of our individual customers, which also can affect the timing of the conversion of our backlog into revenues. For these reasons, among others, our backlog at a particular date may not be indicative of our future revenues.

Product Development

Most of our development activities are conducted at our principal facilities in Anaheim, California. Our company-sponsored research and development costs and expenses were approximately $4.2 million for Fiscal 2005, $3.9 million for the fiscal year ended March 31, 2004 ("Fiscal 2004"), and $3.9 million for the fiscal year ended March 31, 2003 ("Fiscal 2003"). We expect to continue to pursue significant product development programs and incur significant research and development expenditures.

Competition

We generally face significant competition in each of our target markets. Increased competition may result in price reductions, reduced gross margins and loss of market share, any of which could have a material adverse effect on our business, financial condition and results of operations. We believe that AutoVue is the only commercially-available lane departure warning system used in the U.S. and in Europe in the heavy truck market. Potential competitors of AutoVue include Delphi Automotive Systems Corporation domestically, NEC Corporation and Hitachi Ltd. in Japan and Robert Bosch GmbH in Europe, as well as Siemens, Continental Tavis and Visteon, which could be currently developing video sensor technologies for the vehicle industry that could be used for lane departure warning systems. In the market for our Vantage vehicle detection systems, we compete with manufacturers of other "above ground" video camera detection systems such as Econolite Control Products, Inc., Traficon, N.V., Quixote, and other non-intrusive detection devices including microwave, infrared, ultrasonic and magnetic detectors, as well as manufacturers and installers of in-pavement inductive loop products.

The transportation management and traveler information systems market is highly fragmented and is subject to evolving national and regional quality and safety standards. Our competitors vary in number, scope and breadth of the products and services they offer. Our competitors in advanced transportation management and traveler information systems include large multi-national corporations such as Transcore, Lockheed Martin Corporation, PB Farradyne, Inc., Kimley-Horn and Associates, Inc. and National Engineering Technology, Inc. Our competitors in transportation engineering, planning and design include major firms such as Parsons Brinkerhoff, Inc. and Parsons Transportation Group, Inc., as well as many smaller regional engineering firms.

In general, the markets for the products and services offered by our businesses are highly competitive and are characterized by rapidly changing technology and evolving standards. Many of our current and prospective competitors have longer operating histories, greater name recognition, access to larger customer bases and significantly greater financial, technical, manufacturing, distribution and marketing resources than us. As a result, they may be able to adapt more quickly to new or emerging standards or technologies or to devote greater resources to the promotion and sale of their products. It is also possible that new competitors or alliances among competitors could emerge and rapidly acquire significant market share. We believe that our ability to compete effectively in our target markets will depend on a number of factors, including the success and timing of our new product development, the compatibility of our products with a broad range of computing systems, product quality and performance, reliability, functionality, price, and service and technical support. Our failure to provide services and develop and market products that compete successfully with those of other suppliers and consultants in our target markets would have a material adverse effect on our business, financial condition and results of operations.

Intellectual Property and Proprietary Rights

Our ability to compete effectively depends in part on our ability to develop and maintain the proprietary aspects of our technology. Our policy is to obtain appropriate proprietary rights protection for any potentially significant new technology acquired or developed by us. We currently hold ten U.S. patents, which expire commencing in 2012, and have three U.S. patent applications pending, mostly relating to our outdoor image processing techniques used in our AutoVue systems. Two of our patents relate specifically to our AutoVue technology and provide a basis for enhanced functionality for rain sensing and improved performance. We believe that our other patents, while important for our technology platforms, are less critical to our near term product strategy. We cannot assure you that any new patents will be granted pursuant to any outstanding or subsequent applications.

In addition to patent laws, we rely on copyright and trade secret laws to protect our proprietary rights. We attempt to protect our trade secrets and other proprietary information through agreements with customers and suppliers, proprietary

information agreements with our employees and consultants, and other similar measures. We do not have any material licenses or trademarks other than those relating to product names. We cannot be certain that we will be successful in protecting our proprietary rights. While we believe our patents, patent applications, software and other proprietary know-how have value, changing technology makes our future success dependent principally upon our employees' technical competence and creative skills for continuing innovation.

Litigation has been necessary in the past and may be necessary in the future to enforce our proprietary rights, to determine the validity and scope of the proprietary rights of others, or to defend us against claims of infringement or invalidity by others. An adverse outcome in such litigation or similar proceedings could subject us to significant liabilities to third parties, require disputed rights to be licensed from others or require us to cease marketing or using certain products, any of which could have a material adverse effect on our business, financial condition and results of operations. In addition, the cost of addressing any intellectual property litigation claim, both in legal fees and expenses, as well as from the diversion of management's resources, regardless of whether the claim is valid, could be significant and could have a material adverse effect on our business, financial condition and results of operations.

Employees

We refer to our employees as associates. As of June 8, 2005, we employed an aggregate of 215 associates, including 48 associates in general management, administration and finance; 20 associates in sales and marketing; 113 associates in engineering and product development; 26 associates in operations, manufacturing and quality; and 8 associates in customer service. None of our associates are represented by a labor union, and we have never experienced a work stoppage.

Government Regulation

Our manufacturing operations are subject to various federal, state and local laws and regulations, including those restricting the discharge of materials into the environment. We are not involved in any pending or, to our knowledge, threatened governmental proceedings, which would require curtailment of our operations because of such laws and regulations. We continue to expend funds in connection with our compliance with applicable environmental regulations. These expenditures have not, however, been significant in the past, and we do not expect any significant expenditure in the near future. Currently, compliance with foreign laws has not had a material impact on our business and is not expected to have a material impact in the near future.

ITEM 2. PROPERTIES

Our headquarters and principal operations consist of 88,000 square feet of space located at 1515 South Manchester Boulevard in Anaheim, California. The Anaheim facility is leased by us under three separate agreements and houses our operations and administrative offices (approximately 78,000 dedicated square feet) and the operations of our former subsidiary, MAXxess Systems, Inc. (approximately 10,000 dedicated square feet). Two of the three Anaheim leases representing 82,000 of the 88,000 square feet commenced on July 1, 2003 and have four year terms at a monthly lease rate of $60,000 for 65,000 square feet and $14,000 per month for 17,000 square feet. Approximately 10,000 square feet is subleased to MAXxess at a rate of $10,000 per month. On March 1, 2004, we entered into a third lease in Anaheim for 6,000 additional square feet at a rate of $3,000 per month. All three Anaheim leases expire on October 31, 2007.

ITEM 3. LEGAL PROCEEDINGS

The information set forth under Note 7 of Notes to Consolidated Financial Statements, included in Part IV, Item 15 of this report, is incorporated herein by reference.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of our security holders during the three months ended March 31, 2005.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

In October 2004, we amended our certificate of incorporation to (a) change the voting rights of our Class A common stock from one-tenth to one vote per share, (b) remove the ability to issue any further shares of Class B common stock, and (c) rename our Class A common stock as common stock. As a result, we currently have only one class of common stock outstanding, the common stock. Our Class A common stock and Class B common stock were delisted from the Nasdaq SmallCap Market in August 2003 and April 2003, respectively, and were quoted on the OTC Bulletin Board thereafter until December 9, 2004, when our common stock began trading on the American Stock Exchange ("AMEX") under the symbol "ITI."

	Class A Common Stock		Class B Common Stock	
	High	Low	High	Low
Fiscal 2004				
Quarter Ended June 30, 2003	$ .89	$ .45	$ .53	$ .20
Quarter Ended September 30, 2003	1.75	.51	.20	.20
Quarter Ended December 31, 2003	2.60	1.36	.40	.20
Quarter Ended March 31, 2004	4.15	1.91	3.00	.40
Fiscal 2005				
Quarter Ended June 30, 2004	$ 4.10	$ 2.60	$ 3.00	$ 3.00
Quarter Ended September 30, 2004	3.60	2.85	3.00	3.00
Quarter Ended December 31, 2004	3.87	2.90	3.00	3.00
Quarter Ended March 31, 2005	3.43	2.30	N/A	N/A

On July 13, 2005, the last reported sale price of our common stock on the AMEX was $2.78. As of July 13, 2005, we had 599 holders of record of our common stock according to information furnished by our transfer agent.

Dividend Policy

We have never paid or declared cash dividends on our common stock, and have no current plans to pay such dividends in the foreseeable future. We currently intend to retain any earnings for working capital and general corporate purposes. The payment of any future dividends will be at the discretion of our Board of Directors and will depend upon a number of factors, including, but not limited to, future earnings, the success of our business, our capital requirements, our general financial condition and future prospects, general business conditions, the consent of our lender and such other factors as the Board of Directors may deem relevant.

ITEM 6. SELECTED CONSOLIDATED FINANCIAL DATA

The following table sets forth selected consolidated financial data for each of the five fiscal years ended March 31, 2005. The statement of operations and balance sheet data for the years ended and as of March 31, 2005, 2004, 2003, 2002 and 2001 are derived from our audited consolidated financial statements. The accompanying consolidated financial statements have been restated to reflect the classification and presentation of our former subsidiaries, Broadcast, Inc., Zyfer Inc., Mariner Networks, Inc., Gyyr, Inc. and MAXxess Systems, Inc., as discontinued operations for all periods presented. See Note 1 to the accompanying consolidated financial statements. The following information should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and with our consolidated financial statements and the related notes thereto included elsewhere in this report.

The financial information for the year ended March 31, 2004 has been restated for the impact of adjustments discussed in Note 1 to the consolidated financial statements.

	Fiscal Year Ended March 31,				
	2005	2004	2003	2002	2001
	(in thousands, except per share data)				
		(Restated)			
Consolidated Statement of Operations Data:					
Net sales and contract revenues:					
Net sales	$ 29,062	$ 23,470	$ 19,112	$ 17,104	$ 10,626
Contract revenues	17,335	21,813	22,283	20,205	17,430
Total net sales and contract revenues	46,397	45,283	41,395	37,309	28,056
Costs and expenses:					
Cost of net sales	15,645	12,758	9,366	8,401	5,558
Cost of contract revenues	11,398	14,712	15,110	12,043	11,463
Selling, general and administrative expenses	13,964	12,844	14,105	14,627	15,882
Research and development expenses	4,193	3,923	3,908	3,434	5,526
Stock-based compensation	11,777	—	—	—	—
Deferred compensation expense (benefit)	(484)	868	—	—	—
Disposal of fixed assets	422	—	—	—	—
Acquired in-process research and development	140	—	—	—	—
Amortization of intangible assets	114	—	—	—	—
Restructuring charges	—	—	—	1,142	367
Total costs and expenses	57,169	45,105	42,489	39,647	38,796
Income (loss) from operations	(10,772)	178	(1,094)	(2,338)	(10,740)
Non-operating income (expense):					
Royalty income	—	—	—	—	17,825
Other income (expense), net	1,054	1,003	417	(1,365)	188
Interest expense, net	(1,178)	(123)	(761)	(4,190)	(1,762)
Income (loss) from continuing operations before income taxes and minority interest	(10,896)	1,058	(1,438)	(7,893)	5,511
Income tax benefit (provision)	94	(100)	—	785	—
Minority interest in earnings of subsidiary	(526)	(2,813)	(3,818)	(1,910)	—
Income (loss) from continuing operations	(11,328)	(1,855)	(5,256)	(9,018)	5,511
Income (loss) from discontinued operations, net of taxes	—	1,215	(7,892)	(17,120)	(38,051)
Extraordinary loss from early extinguishment of debt, net of taxes	—	—	—	(450)	—
Net loss	$ (11,328)	$ (640)	$ (13,148)	$ (26,588)	$ (32,540)
Basic earnings (loss) per share:					
Continuing operations	$ (0.45)	$ (0.09)	$ (0.37)	$ (0.80)	$ 0.55
Discontinued operations	—	0.06	(0.55)	(1.52)	(3.81)
Extraordinary loss	—	—	—	(0.04)	—
Basic loss per share	$ (0.45)	$ (0.03)	$ (0.92)	$ (2.36)	$ (3.26)
Diluted earnings (loss) per share:					
Continuing operations	$ (0.45)	$ (0.09)	$ (0.37)	$ (0.80)	$ 0.54
Discontinued operations	—	0.06	(0.55)	(1.52)	(3.73)
Extraordinary loss	—	—	—	(0.04)	—
Diluted loss per share	$ (0.45)	$ (0.03)	$ (0.92)	$ (2.36)	$ (3.19)
Shares used in calculating basic earnings (loss) per share	25,284	19,454	14,276	11,267	9,977
Shares used in calculating diluted earnings (loss) per share	25,284	19,454	14,276	11,267	10,209

	At March 31,				
	2005	2004	2003	2002	2001
			(in thousands)		
		(Restated)			
Consolidated Balance Sheet Data:					
Working capital (deficit)	$ 2,197	$ 9,369	$ 3,368	$ (7,349)	$ 2,114
Total assets	46,656	30,065	34,842	52,238	68,061
Long-term debt (less current portion)	10,315	891	1,265	2,042	4,791
Accumulated deficit	(110,436)	(99,108)	(98,468)	(85,320)	(58,732)
Total stockholders' equity (deficit)	17,462	(1,076)	(5,340)	4,203	20,378

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion and analysis in conjunction with our Consolidated Financial Statements and related Notes thereto included in Part IV, Item 15 of this report and the "Risk Factors" section at the end of this Item 7, as well as other cautionary statements and risks described elsewhere in this report, before deciding to purchase, hold or sell our common stock.

Overview

We are a leading provider of outdoor machine vision systems and sensors that optimize the flow of traffic and enhance driver safety. Using our proprietary software and ITS industry expertise, we provide video sensor systems and transportation management systems and traveler information and other engineering services to the ITS industry. We use our outdoor image recognition software expertise to develop proprietary algorithms for video sensor systems that improve vehicle safety and the flow of traffic. Using our knowledge of the ITS industry, we design and implement transportation management systems that help public agencies reduce traffic congestion and provide greater access to traveler information.

Our Vantage product is a video vehicle sensing system that detects the presence of vehicles at signalized intersections enabling a more efficient allocation of green signal time and has certain incident detection and highway traffic data collection applications. We sell and distribute our Vantage products primarily to commercial customers and municipal agencies.

Our AutoVue LDW systems consist of a small windshield mounted sensor that uses proprietary software to detect and warn drivers of unintended lane departures. Approximately 13,000 production AutoVue units have been sold for truck platforms in the North American and European markets. Our AutoVue LDW systems are currently offered as an option on certain Mercedes, MAN, Freightliner and International trucks. In September 2003, we entered into an agreement with Valeo, which granted Valeo the exclusive right to sell and manufacture our AutoVue LDW systems to the worldwide passenger car market in exchange for royalty payments for each AutoVue unit sold. We provided specific contract engineering services, technical marketing and sales support to Valeo to enable the launch of our LDW technology on the Infiniti FX45 platform in October 2004. Additionally, our LDW system is offered on the 2006 Infiniti M35 and M45 luxury sedans as part of Infiniti's Technology Package. Valeo is currently in negotiations to provide our LDW system to other passenger car original equipment manufacturers ("OEMs"); however, we cannot assure you that such negotiations will be successful. We plan to provide technical marketing and sales support to Valeo in our efforts to win new OEM customers for the passenger car market as well as contract engineering services related to the possible launch of new Infiniti platforms that include our LDW system. We believe that AutoVue is a broad sensor platform that, through additional software development, may be expanded to incorporate additional safety and convenience features.

Our transportation management systems business includes transposition engineering and consulting services focused on the design, development, and implementation of software-based systems that integrate sensors, video surveillance, computers and advanced communications equipment to enable public agencies to monitor, control, and direct traffic flow, assist in the quick dispatch of emergency crews and distribute real-time information about traffic conditions. Our services include planning and other engineering for the implementation of transportation related communications systems, analysis and study related to goods movement and commercial vehicle operations, and parking systems designs. These services and systems are sold to local, state, and national transportation agencies in the United States. Our transportation management systems business is largely dependent upon governmental funding and budgetary issues. The adoption of the Federal Highway Bill has been delayed, which adversely impacted our transportation management systems business in Fiscal 2005. Further delays in this bill or other governmental funding could materially and adversely affect our business in Fiscal 2006 as well.

We have historically operated multiple business units. During Fiscal 2003, we operated in three business segments consisting of ITS, video products, and telecom products. The ITS segment consisted of our current operations, the ITS business, which was previously conducted by the Iteris Subsidiary. The video products segment consisted of our former wholly-owned subsidiaries, MAXxess Systems, Inc. ("MAXxess," previously known as Gyyr Incorporated), which designed and manufactured security management systems, and Broadcast, Inc. ("Broadcast"), which developed and supplied software based systems to automate and control the multiple classes of equipment used in broadcast studios and satellite uplink facilities. Our telecom segment consisted of our wholly-owned subsidiary, Zyfer, Inc. ("Zyfer"), which developed and manufactured timing and synchronization products and which, prior to its incorporation, was operated as our Communications division.

Beginning in Fiscal 2003, we began divesting certain of our business units in order to reduce our operating expenses and to focus on the operations of our Iteris Subsidiary. These divestitures and related restructuring activities included the following transactions:

• In March 2003, we ceased the development and sale of any new Broadcast products and in September 2003, we sold the balance of our Broadcast business.

• In May 2003, we sold the assets of Zyfer for a purchase price of $2.3 million in cash and the assumption of liabilities, plus future incentive payments of up to $1.0 million in each of the twelve months ended April 30, 2004 and 2005. The amount of these future incentive payments was to be based on the revenues generated by the sale of Zyfer's products or the license of its technologies. In October 2004, we received an incentive payment of $135,000 related to the twelve month period ended April 30, 2004. We expect to receive information related to the incentive payment for the twelve month period ended April 30, 2005, by the end of July 2005.

• In September 2003, we sold substantially all of the assets of MAXxess to an investor group that included certain members of the MAXxess management group. The consideration for the sale consisted of the assumption of $2.7 million of liabilities, resulting in a net gain of $2.3 million on this sale.

• In May 2004, we repurchased all of the outstanding shares of Series A preferred stock of the Iteris Subsidiary for an aggregate purchase price of approximately $17.5 million in cash and we purchased 547,893 shares of the Iteris Subsidiary common stock from DaimlerChrysler Ventures GmbH ("DCV") in consideration for the issuance of 1,219,445 shares of our common stock. We financed the purchase price for the Iteris Subsidiary Series A preferred stock through the issuance of convertible debentures in the original principal amount of $10.1 million, a $5.0 million term note payable to our bank and $2.4 million in cash.

• In June 2004, we issued 2,639,082 shares of our common stock valued at $8.6 million at the date of issuance in exchange for an aggregate of 1,319,541 shares of common stock of the Iteris Subsidiary, which had the effect of reducing the residual minority interest in our Iteris Subsidiary to 8.1%.

• In October 2004, we merged the Iteris Subsidiary into us and the remaining minority interest in the Iteris Subsidiary (consisting of 1,228,981 shares of common stock of the Iteris Subsidiary) was converted to 2,457,962 shares of our common stock valued at $7.6 million at the merger date. Immediately following the merger, we converted all of our outstanding Class B common stock (921,917 shares) into 1,014,108 shares of our common stock (formerly designated as Class A common stock). In connection with this merger, we also assumed all of the outstanding options and warrants to purchase common stock of the Iteris Subsidiary, which now represent options and warrants to purchase an aggregate of 6,039,556 and 654,718 shares, respectively, of our common stock.

• In October 2004, we amended our certificate of incorporation to (a) change the voting rights of our Class A common stock from one-tenth to one vote per share, (b) remove the ability to issue any further shares of Class B common stock, and (c) rename our Class A common stock to common stock. As a result, we currently have only one class of common stock outstanding, the common stock.

Our financial statements for all periods presented in this report have been restated to reflect the discontinuation of the operations of Broadcast, Zyfer and MAXxess and the financial information for the year ended March 31, 2004 has also been restated for the impact of adjustments discussed in Note 1 of the consolidated financial statements.

We currently operate in three reportable segments: Roadway Sensors, Automotive Sensors and Systems. The Roadway Sensors segment includes our Vantage vehicle detection systems for traffic intersection control, incident detection and certain highway traffic data collection applications. The Automotive Sensors segment includes our AutoVue LDW systems for vehicle safety. The Systems segment includes transportation engineering and consulting services and the development of transportation management and traveler information systems for the ITS industry.

Critical Accounting Policies and Estimates

Management's Discussion and Analysis of Financial Condition and Results of Operations is based on our consolidated financial statements included herein, which have been prepared in accordance with generally accepted accounting principles in the United States ("GAAP"). The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and related disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. On an ongoing basis, we evaluate these estimates and assumptions, including those related to the collectibility of

accounts receivable, the valuation of inventories, the recoverability of long-lived assets and goodwill and warranty reserves. We base these estimates on historical experience and on various other factors that we believe 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. These estimates and assumptions by their nature involve risks and uncertainties, and may prove to be inaccurate. In the event that any of our estimates or assumptions are inaccurate in any material respect, it could have a material adverse effect on our reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period.

The following critical accounting policies affect our more significant judgments and estimates used in the preparation of our consolidated financial statements.

Revenue Recognition. We record product revenues and related costs of sales upon transfer of title, which is generally upon shipment or, if required, upon acceptance by the customer, provided that we believe collectibility of the net sales amount is reasonably assured. Accordingly, at the date revenue is recognized, the significant uncertainties concerning the sale have been resolved.

Contract revenue is derived primarily from long-term contracts with governmental agencies. Contract revenues include costs incurred plus a portion of estimated fees or profits determined using the percentage of completion method of accounting based on the relationship of costs incurred to total estimated costs. Any anticipated losses on contracts are charged to earnings when identified. Changes in job performance and estimated profitability, including those arising from contract penalty provisions and final contract settlements, may result in revisions to recognized costs and revenues and are recognized in the period in which the revisions are determined. Profit incentives are included in revenue when their realization is reasonably assured.

In addition to product and contract revenue, we derive revenue from technology access fees, the provision of specific non-recurring contract engineering services related to our AutoVue LDW system, and royalties related to unit sales of our AutoVue LDW systems by our strategic partner Valeo to the passenger car market. Combined technology access fees and contract engineering revenues are recognized on the percentage of completion method of accounting based on the relationship of hours incurred to total estimated hours. Royalty revenue is recorded based on unit sales of our products by Valeo and is recognized in the period in which such sales occur. Technology access fee revenues, contract engineering revenues and royalty revenues are included in net sales in the accompanying consolidated statements of operations.

Revenues from follow-on service and support, for which we charge separately, are recorded in the period in which the services are performed.

Accounts Receivable. We estimate the collectibility of customer receivables on an ongoing basis by periodically reviewing invoices outstanding greater than a certain period of time. We have recorded reserves for receivables deemed to be at risk for collection as well as a general reserve based on our historical collections experience. A considerable amount of judgment is required in assessing the ultimate realization of trade receivables, including the current credit-worthiness of each customer. If the financial condition of our customers deteriorates, resulting in an impairment of their ability to make required payments, additional allowances may be required that could adversely affect our operating results.

Inventory. Inventories consist of finished goods, work-in-process and raw materials and are stated at the lower of cost or market. We provide reserves for potentially excess and obsolete inventory. In assessing the ultimate realization of inventories, we make judgments as to future demand requirements and compare that with the current or committed inventory levels. Reserves are established for inventory levels that exceed future demand. It is possible that reserves over and above those already established may be required in the future if market conditions for our products deteriorate.

Goodwill. Goodwill is tested for impairment annually in the fourth fiscal quarter at the reporting unit level unless a change in circumstances indicates that more frequent impairment analysis is required. Impairment, if any, is measured based on the estimated fair value of the reporting units with the recorded goodwill. Fair value is determined by using the income approach methodology of valuation which utilizes discounted cash flows. Significant management judgment is required in the forecasts of future operating results that are used in the discounted cash flow method of valuation. In estimating future cash flows, we generally use the financial assumptions in our current budget and our current strategic plan, subject to modification as considered necessary, including sales and expense growth rates and the discount rates we estimate to represent our cost of funds. It is possible, however, that the plans and estimates used may be incorrect. If our actual results, or the plans and estimates used in future impairment analyses, are lower than the original estimates used to assess the recoverability of goodwill, we could incur impairment charges.

Warranty. Unless otherwise stated, we provide a one to three year warranty from the original invoice date on all products, materials and workmanship. Defective products are either repaired or replaced, at our option, upon meeting certain criteria. We accrue a provision for the estimated costs that may be incurred for product warranties relating to a product as a component of cost of sales at the time revenue for that product is recognized. The accrued warranty provision is included within accrued expenses on the accompanying consolidated balance sheets. Should our actual experience of warranty returns be higher than anticipated, additional warranty reserves may be required, which may adversely affect our operating results.

Taxes. We recorded a valuation allowance to reduce our deferred tax assets to amounts that we believe are more likely than not to be realized. Realization of deferred tax assets (such as net operating loss carryforwards) is dependent on future taxable earnings and is therefore uncertain. On a quarterly basis, we assess the likelihood that our deferred tax asset balance will be recovered from future taxable income. To the extent we believe that recovery is not likely, we establish a valuation allowance against our deferred tax asset, increasing our income tax expense in the period such determination is made.

On an interim basis, we estimate what our anticipated annual effective tax rate will be and record a quarterly income tax provision in accordance with this anticipated rate. As the fiscal year progresses, we refine our estimates based upon actual events and earnings during the year. This estimation process can result in significant changes to our expected effective tax rate. When this occurs, we adjust the income tax provision during the quarter in which the change in estimate occurs so that the year-to-date provision reflects the expected annual rate. The changes described in the preceding sentence and the recording of valuation allowances may create fluctuations in our overall effective tax rate from quarter to quarter.

Results of Operations

The following table sets forth certain statement of operations data as a percentage of total net sales and contract revenues for the periods indicated. The following table should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations.

	Fiscal Year Ended March 31,		
	2005	2004 (Restated)	2003
Net sales and contract revenues:			
Net sales	62.6%	51.8%	46.2%
Contract revenues	37.4	48.2	53.8
Total net sales and contract revenues	100.0%	100.0%	100.0%
Costs and expenses:			
Cost of net sales	33.7	28.2	22.6
Cost of contract revenues	24.6	32.5	36.5
Selling, general and administrative expenses	30.1	28.4	34.1
Research and development expenses	9.0	8.6	9.4
Stock-based compensation expense (benefit)	25.4	—	—
Deferred compensation	(1.0)	1.9	—
Disposal of fixed assets	0.9	—	—
Acquired in-process research and development	0.3	—	—
Amortization of intangible assets	0.2	—	—
Total costs and expenses	123.2	99.6	102.6
Income (loss) from operations	(23.2)	0.4	(2.6)
Non-operating income (expense):			
Other income net	2.2	2.2	1.0
Interest expense, net	(2.5)	(0.3)	(1.8)
Income (loss) from continuing operations before income taxes and minority interest	(23.5)	2.3	(3.4)
Income tax benefit (provision)	0.2	(0.2)	—
Minority interest in earnings of subsidiary	(1.1)	(6.2)	(9.2)
Loss from continuing operations	(24.4)	(4.1)	(12.6)
Income (loss) from discontinued operations, net of income taxes	0.0	2.7	(19.1)
Net loss	(24.4)%	(1.4)%	(31.7)%

Years Ended March 31, 2005, 2004, and 2003

Net Sales and Contract Revenues. Net sales consist principally of sales of our Vantage video detection systems and AutoVue LDW systems, as well as technology access fees, contract engineering revenue and royalty revenue generated from AutoVue related activities. Contract revenue consists principally of revenue derived from systems integration and ITS consulting services with state, county and municipal agencies. We currently have a diverse customer base with our largest customer constituting 12.8% of total net sales and contract revenues in Fiscal 2005. Total net sales and contract revenues increased 2.5% to $46.4 million in Fiscal 2005 compared to $45.3 million in Fiscal 2004, and increased 9.4% in Fiscal 2004 compared to $41.4 million in Fiscal 2003. The increases were a result of increased net sales offset by decreased contract revenues, as discussed below.

Net sales increased 23.8% to $29.1 million in Fiscal 2005 compared to $23.5 million in Fiscal 2004, and increased 22.8% in Fiscal 2004 compared to $19.1 million in Fiscal 2003. The increase in net sales in each of the periods primarily reflected an increase in the unit sales of our Vantage vehicle detection systems and increased unit sales of our AutoVue LDW systems. Net sales from AutoVue products increased 70.2% in Fiscal 2005 compared to Fiscal 2004, and represented 24.6% of our total net sales in Fiscal 2005 versus 17.9% of total our net sales in Fiscal 2004. The increase in sales of AutoVue products was principally related to increased unit sales of LDW systems in the European and North American commercial heavy truck markets, and to a lesser extent, increased license fee revenue and fees for non-recurring engineering services derived from Valeo, our strategic partner for the passenger car OEM customer base. AutoVue sales in Fiscal 2006 may be adversely impacted due to potential supply issues as a new production unit for the heavy truck market is being redesigned and qualified. Vantage sales comprised 75.4%, 82.1% and 92.0% of net sales in Fiscal 2005, Fiscal 2004 and Fiscal 2003, respectively. The majority of Vantage revenues were derived from sales within North America. The Vantage sales growth was primarily due to increased market adoption of video-based detection technologies for traffic intersection management and our ability to obtain additional contracts with state departments of transportation.

Contract revenues decreased 20.5% to $17.3 million in Fiscal 2005 compared to $21.8 million in Fiscal 2004, and decreased 2.1% in Fiscal 2004 compared to $22.3 million in Fiscal 2003. Contract revenues reflect a broad range of fixed price and cost plus fixed fee contracts for engineering study and design, systems integration and system implementation. Contract revenues are dependent upon the continued availability of funding on both the state and federal levels from the various departments of transportation. We believe the decrease in Fiscal 2005 revenues compared to Fiscal 2004 and Fiscal 2003 principally reflects budget constraints in both the federal and California markets, where a significant portion of our contract revenues have been derived during the last several years, which constraints have been exacerbated by the continued delay in the adoption of the Federal Highway Bill. All of our contract revenue is currently derived from work performed in North America.

Gross Profit. Total gross profit increased 8.7% to $19.4 million in Fiscal 2005 compared to $17.8 million in Fiscal 2004, and increased 5.3% from $16.9 million in Fiscal 2003 compared to Fiscal 2004. Total gross profit as a percent of net sales and contract revenues increased to 41.7% in Fiscal 2005 compared to 39.3% in Fiscal 2004 and 40.9% in Fiscal 2003.

Gross profit as a percentage of net sales was 46.2% in Fiscal 2005 compared to 45.6% in Fiscal 2004 and 51.0% in Fiscal 2003. The 0.6% increase in gross profit in Fiscal 2005 compared to Fiscal 2004 was primarily a result of increased margins on AutoVue activities due to better overhead absorption on higher unit sales of LDW systems to the heavy truck market as well as the recognition of technology access fee revenue and royalty revenue from Valeo, both of which provide a 100% gross margin, which was somewhat offset by declining margins related to the sales of Vantage products due to lower unit pricing on large, high volume state contracts and increased price pressure in the industry.

The decrease in gross profit as a percent of net sales in Fiscal 2004 compared to 2003 primarily reflected lower unit pricing on large, high volume state contracts for Vantage products, in addition to lower gross profits realized on AutoVue products and services principally related to fewer sales of sample LDW systems which generated higher gross profits in Fiscal 2004 compared to Fiscal 2003. We expect that price pressure will continue into the foreseeable future for both our Vantage and AutoVue product lines and we are constantly analyzing various strategies to reduce the impact of further price pressure on gross profits.

Gross profit as a percent of contract revenues increased to 34.2% in Fiscal 2005 compared to 32.6% in Fiscal 2004 and 32.2% in Fiscal 2003. We recognize contract revenues and related gross profit using percentage of completion contract accounting and the underlying mix of contract activity affects the related gross profit recognized in any given year. The increase in Fiscal 2005 reflects a mix of higher margin contracts in Fiscal 2005 as compared to Fiscal 2004 and Fiscal 2003.

Selling, General and Administrative Expense. Selling, general and administrative expense increased 8.7% to $14.0 million (or 30.1% of total net sales and contract revenues) in Fiscal 2005 compared to $12.8 million (or 28.4% of total net sales and contract revenues) in Fiscal 2004, and decreased 8.9% in Fiscal 2004 compared to $14.1 million (or 34.1% of total net sales and contract revenues) in Fiscal 2003. The increase in Fiscal 2005 compared to Fiscal 2004 was principally related to $807,000 of severance charges recorded in connection with the merger and acquisition of the Iteris Subsidiary in October 2004, as well as increased costs to support expanded sales and marketing efforts for our Vantage and AutoVue products in Fiscal 2005. The decrease in Fiscal 2004 compared to Fiscal 2003 principally reflected decreased facilities lease expense related to the restructuring of lease commitments for our Anaheim facilities in June 2003, reduced further by salary expense for corporate support personnel related to the divestiture of our Broadcast, Zyfer and MAXxess Systems businesses in Fiscal 2004.

Research and Development Expense. Research and development expense increased 6.9% to $4.2 million (or 9.0% of total net sales and contract revenues) in Fiscal 2005 compared to $3.9 million (or 8.6% of total net sales and contract revenues) in Fiscal 2004, and increased 0.4% in Fiscal 2004 compared to $3.9 million (or 9.4% of total net sales and contract revenues) in Fiscal 2003. The increase in research and development expense in Fiscal 2005 compared to Fiscal 2004 reflects increased spending to support the development of AutoVue products, which was partially offset by decreased spending to support the development of Vantage products. AutoVue product development primarily related to the development of the next generation LDW unit for the heavy truck market, particularly for the re-engineering and qualification for a new imager. The increases were primarily in the areas of personnel costs and related benefits and overhead, prototype material costs, and consulting fees. Vantage product development primarily reflects activities for product line extensions to support new communications platforms and to accommodate new camera designs. The modest increase in research and development expense in Fiscal 2004 compared to Fiscal 2003 primarily reflects software algorithm development and new hardware designs for enhancements to our existing product family of Vantage video detection systems.

For competitive reasons, we closely guard the confidentiality of specific development projects.

Stock-Based Compensation. On October 22, 2004, we recorded an $11.3 million charge for stock-based compensation in connection with the assumption and exchange of vested Iteris Subsidiary stock options for stock options immediately exercisable into our common stock. This charge was based on the differences between the fair market value of our common stock on the merger date and the exercise prices of the modified stock options. Additionally, we recorded approximately $1.4 million in deferred compensation expense related to the unvested Iteris Subsidiary stock options also assumed as part of the merger, which will be amortized to stock-based compensation expense as the options vest. We amortized $508,000 of the $1.4 million of deferred compensation to stock-based compensation expense in Fiscal 2005.

Deferred Compensation Expense (Benefit): The $868,000 non-cash charge for the change in value of common stock held in trust by our deferred compensation savings plan in Fiscal 2004 related to the estimated appreciation in value of the Iteris Subsidiary common stock held in the plan for the period ending March 31, 2004. In Fiscal 2005, the Iteris Subsidiary was merged into the Company and shares of Iteris Subsidiary common stock held in the plan were exchanged for shares of common stock of the Company. The $484,000 non-cash benefit for deferred compensation plan expenses related to the decline in value of the Company's common stock during Fiscal 2005. Non-cash charges or benefits for deferred compensation plan expenses will be recorded in future periods based on increases or decreases in the fair value of the Company's common stock at the end of each reporting period. "We intend to amend this plan in the near future to prohibit diversification of any shares of our common stock held in the plan, which we believe will prevent any future deferred compensation charges or other impact on the Company's financial statements as a result of changes in the value of our common stock held in this plan."

Disposal of Fixed Assets. After the October 22, 2004, merger of the Iteris Subsidiary into us, we conducted a review of our property and equipment and determined that certain corporate property and equipment would not provide value to our on-going operations. These assets primarily consisted of furniture and fixtures and computer equipment. Accordingly, we recorded a $422,000 loss on disposal of fixed assets in Fiscal 2005.

Other Income, Net. Other income, net reflects the following:

	Year Ended March 31,		
	2005	2004	2003
	(In thousands)		
Gain on sale of real estate	$ —	$ 970	$ 640
Loss on sale of Iteris common stock	—	—	(310)
Gain on settlement of lawsuit	949	—	—
Other	105	33	87
Other income, net	$ 1,054	$ 1,003	$ 417

Other income, net in Fiscal 2005 primarily reflects a $949,000 gain recognized on the settlement of litigation. We were a beneficiary of, but not a party to, litigation between Rockwell International and the Michigan Department of Transportation. Other income, net in Fiscal 2004 and 2003 includes a gain of $970,000 and $640,000, respectively, recognized on the sale and leaseback of our Anaheim, California facility, which was consummated in May 2002.

Interest Expense, Net. Interest expense, net reflects the net of interest expense and interest income as follows:

	Year Ended March 31,		
	2005	2004	2003
	(In thousands)		
Interest expense	$ 1,180	$ 125	$ 761
Interest income	(2)	(2)	—
Interest expense, net	$ 1,178	$ 123	$ 761

Interest expense increased 844.0% in Fiscal 2005 compared to Fiscal 2004 and decreased 83.8% in Fiscal 2004 compared to Fiscal 2003. The increase in Fiscal 2005 is due to additional interest expense incurred related to the $5.0 million term debt entered into by the Iteris Subsidiary on May 28, 2004 (which was assumed by us in October 2004), interest expense related to the $10.1 million convertible debentures issued by us on May 19, 2004, the amortization of debt discounts

associated with the issuance of the convertible debentures and related warrants, and increased borrowings on our line of credit. The decrease in Fiscal 2004 compared to Fiscal 2003 reflected the sale and leaseback of our Anaheim, California facilities, and our subsequent repayment in May 2002 of a $16.4 million promissory note.

Income Taxes. During Fiscal 2005, we recognized an income tax benefit of $94,000, and at March 31, 2005, we recorded a net deferred tax asset of $660,000. The ability to record the deferred tax asset was based on the more likely than not criteria of Statement of Financial Accounting Standards ("SFAS") No. 109, *Accounting for Income Taxes*, since the Iteris Subsidiary had historically been profitable and had utilized all its federal net operating loss carryovers and could thus carryback and realize the reversal of future tax deductions. During Fiscal 2004, we recognized an income tax expense of $100,000 and at March 31, 2004, we recorded a net deferred tax asset of $821,000 directly related to the profitable operations of the Iteris Subsidiary. No income tax benefit for losses incurred in Fiscal 2003 was recorded due to uncertainty as to the ultimate realization of the related benefit.

At March 31, 2005, we had $50.5 million of federal net operating loss carryforwards and $33.0 million of state net operating loss carryforwards that begin to expire in 2019 and 2005, respectively. As a result of these net operating loss carryforwards and the valuation allowance, we have recorded against the related net deferred tax assets in our consolidated balance sheet, we believe that future income tax payments and income tax expense will be substantially lower than the income tax liability and income tax expense calculated using statutory tax rates.

Minority Interest in Earnings of Subsidiary. Minority interest in earnings of subsidiary represents the minority stockholders' share of the Iteris Subsidiary's net income or loss combined with the accretion of the redemption preference of the Iteris Subsidiary's Series A preferred stock. The decrease in minority interest from $2.8 million in Fiscal 2004 to $526,000 in Fiscal 2005 was the result of the merger and acquisition of the Iteris Subsidiary by us. On October 22, 2004, we fully completed the merger and acquisition of the Iteris Subsidiary, and as a result, we do not anticipate incurring any further charges for minority interest.

Income (Loss) from Discontinued Operations, net of income taxes . As discussed in the Overview to Management's Discussion and Analysis of Financial Condition and Results of Operations, the results of operations related to certain businesses discontinued by us in Fiscal 2004 and Fiscal 2003 are reflected as discontinued operations in our consolidated financial statements. As of the end of Fiscal 2004, we had completed all such restructuring activities so that we could focus our efforts in the ITS marketplace.

Restatement of Consolidated Financial Statements for the year ended March 31, 2004

As further discussed in Note 1 to the consolidated financial statements, we have restated our consolidated financial statements for the year ended March 31, 2004. This restatement was necessary in order to reflect the consolidation of our deferred compensation savings plan, the principal effects of which were to increase operating expenses by a non-cash charge of $868,000 for the year ended March 31, 2004, and decrease minority interest in the earnings of the Iteris Subsidiary by $221,000 for the year ended March 31, 2004. This restatement had no impact on our consolidated cash flows.

Liquidity and Capital Resources

During Fiscal 2005, we generated $858,000 in cash from operating activities and used this cash to partially fund our investing and financing activities. Net cash provided by operating activities principally reflected our net loss of $11.3 million increased for non-cash charges of $11.8 million related to stock-based compensation, $1.2 million for depreciation and amortization, $296,000 in charges related to the minority interest in the Iteris Subsidiary and $422,000 related to the disposal of fixed assets, offset by a decrease of $609,000 for non-cash gains related to amortization of the deferred gain on real-estate sales and $914,000 related to the usage of cash to fund changes in operating assets and liabilities. Most of the cash requirements for operating assets and liabilities during Fiscal 2005 related to $746,000 in cash used to purchase inventory and $485,000 used to pay income taxes.

In May 2002, we completed the sale and leaseback of our Anaheim, California facility for an aggregate sale price of $22.6 million. Under the terms of the sale and leaseback agreement, we agreed to lease one of the two buildings located on the property for an initial ten-year period at a rate of $152,150 per month and the other building for a period of 30 months at a rate of approximately $57,553 per month. Approximately $16.4 million of the proceeds from the sale was used to repay the outstanding indebtedness and accrued interest under a promissory note that was secured by a first deed of trust on the Anaheim facility. The balance of the proceeds was available for general working capital purposes. The gain on the sale of the facility was approximately $8.2 million, of which $640,000 was recognized immediately and the remainder was deferred and is being amortized against rent expenses over the term of the leases.

In May 2003, we completed the sale of substantially all the assets of our wholly-owned subsidiary, Zyfer, for $2.3 million in cash plus the assumption of certain liabilities. The cash proceeds were used to fund working capital requirements and pay short-term liabilities. The asset purchase agreement provides for incentive payments to us of up to $1.0 million in each of the twelve months ended April 30, 2004 and 2005. The amount of these incentive payments are based on the revenues generated by the sale of Zyfer's products or the license of its technologies. Based on the terms of the sale agreement, Zyfer has 60 days to provide us with support for the incentive payments. In October 2004, we received a payment of approximately $135,000 related to the twelve month period ended April 30, 2004. We expect to receive information for the twelve month period ended April 30, 2005 by the end of July 2005.

In July 2003, we renegotiated the terms of our existing lease for our Anaheim facilities whereby the initial lease term of ten years was reduced to four years and we were relieved of our obligation to lease both buildings. In consideration for the restructured agreement, we paid approximately $2.5 million in cash that had been previously pledged as collateral on the lease, in addition to issuing to the lessor 425,000 shares of our common stock valued at $255,000 and a note payable for $811,000. Under the terms of the new lease, we are only responsible for 88,000 square feet at a rate of $77,000 per month. In addition, are subleasing 10,000 of the 88,000 square feet at our Anaheim facility for a period of four years at a rate of $10,000 per month. The aggregate future rental payments under this sublease are $120,000 for the year ending March 31, 2006 and $70,000 for the year ending March 31, 2007. Also, as a result of the new lease, the deferred gain on the sale of the building was adjusted to reflect the changes in the lease term. The remaining deferred gain was $733,000 at March 31, 2005.

Also, in July 2003, we completed a private placement of 3,666,666 of our common stock to seven accredited investors for net proceeds of $1.9 million in cash. In connection with this offering, we also issued warrants to the investors to purchase up to another 366,666 shares in the aggregate at an exercise price of $1.50 per share. The fair value of these warrants was $55,000 calculated using the Black Scholes Model. The warrants are considered a cost of raising capital and were recorded in equity as an offset to additional paid-in capital. The warrants expire in July 2006 and became exercisable in January 2003. The proceeds from this transaction were used to fund our general working capital requirements.

In September 2003, we completed the sale of the assets of our MAXxess subsidiary to an investor group that included certain members of the MAXxess management group. The consideration for the sale consisted of the assumption by the buyer of $2.7 million of liabilities, resulting in a net gain to the Company of approximately $2.3 million. We did not receive any cash in this transaction.

In May 2004, we issued convertible debentures in the original principal amount of $10.1 million and entered into a $5.0 million term note with our bank. We purchased the outstanding Series A preferred stock of the Iteris Subsidiary from DCV and Hockenheim Investment Pte. Ltd. for $17.5 million, which was comprised of $2.4 million of available cash and the proceeds from the debenture financing and the bank term note. DCV also exchanged its outstanding Iteris Subsidiary common stock for 1,219,445 shares of our common stock (the "Exchange Shares"). Beginning on May 28, 2005 , DCV has the right to request registration of all 1,219,445 shares of our common stock held as part of this exchange. In the event we decide not to file a registration statement to register all such shares, DCV may require us to repurchase any or all of DCV's shares of our common stock at a purchase price of $1.438 per share. On February 1, 2005, DCV announced that it was sold to European-based Cipio Partners for an undisclosed sum. All repurchase and registration rights associated with the DCV shares have inured to the benefit of Cipio Partners.

The debentures are due in full in May 2009, provide for 6.0% annual interest, payable quarterly, and are convertible into our common stock at an initial conversion price of $3.61 per share, subject to certain adjustments, including adjustments for dilutive issuances. From May 19, 2007 until May 18, 2008, the debentures may be redeemed by us, at our option, at 120% of the principal amount being redeemed; and from May 19, 2008, until the maturity date, the debentures may be redeemed at 110% of the principal amount being redeemed.

Each individual investor in the debenture financing also received two warrants to purchase shares of our common stock. For every dollar of debenture purchased, each investor received one warrant to purchase approximately 0.03235 shares of common stock at an exercise price of $3.86 per share and a second warrant to purchase approximately 0.03100 shares of common stock at an exercise price of $4.03 per share. The exercise prices are subject to certain adjustments, including adjustments for dilutive issuances. The warrants to purchase 639,347 shares of common stock issued to these investors expire on May 18, 2009, and none of the warrants had been exercised at March 31, 2005.

In conjunction with the debenture financing, we also issued warrants to purchase 34,036 shares of our common stock at an exercise price of $3.61 per share as commissions related to the transaction. These warrants also expire on May 18, 2009.

Concurrent with the issuance of the debentures, our Iteris Subsidiary entered into a $5.0 million term note payable with a bank. Proceeds from the debentures and note payable were used to purchase the Series A preferred stock of our Iteris Subsidiary as described above. The four year bank note is due and payable on May 27, 2008, and provides for monthly principal payments of $104,167. Interest accrues at the current stated prime rate plus 0.25%.

Also in May 2004, our Iteris Subsidiary renegotiated its existing line of credit agreement and entered into a new line

of credit agreement with the same bank. The new agreement has a one year term that expires on August 1, 2005 and a maximum available credit line of $5.0 million. We assumed this line of credit and the $5.0 million term note described above in October 2004 in connection with our merger with the Iteris Subsidiary. Under the terms of this agreement, we may borrow against our eligible accounts receivable and the value of our eligible inventory, as defined in such agreement. Interest on borrowed amounts is payable monthly at the prime rate (5.50% at March 31, 2005). Additionally, we are obligated to pay an unused line fee of 0.25% per annum applied to the amount by which the maximum credit amount exceeds the average daily principal balance during the preceding month. There are no monthly collateral management fees associated with our line of credit and no pre-payment or early termination fees. Both the term note payable and the line of credit are secured by substantially all of our assets.

In November 2004, we amended our existing lease for our Anaheim facility and increased the $860,000 note payable to the landlord by $432,000 resulting in a total payable of $1.3 million. This increase was recorded as a decrease to the deferred gain on the sale of the building. The increase was negotiated as a settlement to release us from obligations under the existing lease related to the separation of buildings located at 1515 and 1585 S. Manchester Avenue in Anaheim, California, and other facility improvements to be made at the Anaheim location. This note is payable in quarterly installments of principal and interest beginning on October 1, 2006 and accrues interest at the current stated prime rate plus 2.0%.

We had a cash balance of $46,000 as of March 31, 2005, and generally do not have a substantial amount of cash on hand at any given time. In order to minimize interest expense on our line of credit, available funds are swept from our cash accounts to pay down the line of credit if a balance due exists.

Our contractual obligations are as follows at March 31, 2005:

	Payments Due by Period						
	2006	2007	2008	2009	2010	Thereafter	Total
	(In thousands)						
Lines of credit	$ 945	$ —	$ —	$ —	$ —	$ —	$ 945
Notes payable and capital leases	4,008	670	649	—	—	—	5,327
Convertible debentures	—	—	—	—	9,850	—	9,850
Operating leases	1,116	1,005	601	3	—	—	2,725
Total	$ 6,069	$ 1,675	$ 1,250	$ 3	$ 9,850	$ —	$ 18,847

At March 31, 2005, we had firm commitments to purchase inventory in the amount of $271,000 during the first quarter of Fiscal 2006.

Although we incurred a net loss of $11.3 million in Fiscal 2005, our operations generated positive cash of $858,000 for such fiscal year. However, we used $625,000 of cash in investing activities and $2.8 million of available cash in financing activities and ended the year with a cash balance of $46,000. At March 31, 2005, we had a revolving line of credit with our principal bank, which expires in August 2005 and provides for available borrowings up to $5.0 million subject to a borrowing formula based upon qualified accounts receivable and inventories as defined in the credit agreement. At March 31, 2005, $4.4 million was available for borrowing subject to the borrowing base in the credit agreement, of which $3.4 million was unused. Due to covenant violations as of March 31, 2005, we are re-negotiating the line of credit facility as well as the term loan with the bank. We believe these negotiations will be successful and that the combination of available borrowings on our line of credit and our internally generated cash flows will be sufficient to enable us to execute our operating plans and meet our obligations on a timely basis. As discussed in Note 5 to the consolidated financial statements, the entire balance of the bank term loan is presented as a current liability in our March 31, 2005, consolidated balance sheet.

Recent Accounting Pronouncements

In November 2004, the FASB issued SFAS No. 151, *Inventory Costs*, which clarifies the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material. SFAS No. 151 will be effective for inventory costs incurred during fiscal years beginning after June 15, 2005. We do not believe the adoption of SFAS No. 151 will have a material impact on our financial statements.

On December 16, 2004, the FASB issued SFAS No. 123 (revised 2004), *Share-Based Payment* ("SFAS 123R"), which replaced SFAS No. 123, *Accounting for Stock-Based Compensation*, supersedes Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees*, and amends SFAS No. 95, *Statement of Cash Flows*. Generally, the

approach in SFAS 123R is similar to the approach described in SFAS 123. However, SFAS 123R requires all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their fair values (i.e., pro forma disclosure is no longer an alternative to financial statement recognition). In accordance with SEC Release No. 33-8568, SFAS 123R will become effective for us beginning April 1, 2006. We are currently assessing the impact of SFAS 123R. As of the date of this filing, no decisions have been made as to whether we will apply the modified prospective or retrospective transition method of application.

RISK FACTORS

Our business is subject to a number of risks, some of which are discussed below. Other risks are presented elsewhere in this report and in the information incorporated by reference into this report. You should consider the following risks carefully in addition to the other information contained in this report and our other filings with the SEC, including our subsequent reports on Forms 10-Q and 8-K, before deciding to buy, sell or hold our common stock. The risks and uncertainties described below are not the only ones facing our company. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also affect our business operations. If any of these risks actually occurs, our business, financial condition or results of operations could be seriously harmed. In that event, the market price for our common stock could decline and you may lose all or part of your investment.

We Have Experienced Substantial Losses And May Continue To Experience Losses For The Foreseeable Future. We experienced net losses from continuing operations of $11.3 million, $1.9 million and $5.3 million in the years ended March 31, 2005, 2004, and 2003, respectively. While we have divested all of our other business units and merged with our Iteris Subsidiary, we cannot assure you that our efforts to downsize our operations or reduce our operating expenses will improve our financial performance, or that we will be able to achieve profitability on a quarterly or annual basis in the future. Most of our expenses are fixed in advance. As such, we generally are unable to reduce our expenses significantly in the short-term to compensate for any unexpected delay or decrease in anticipated revenues. As a result, we may continue to experience operating losses and net losses, which would make it difficult to fund our operations and achieve our business plan, and could cause the market price of our common stock to decline.

We May Need To Raise Additional Capital In The Future, But We May Not Be Able To Secure Adequate Funds On Terms Acceptable To Us, Or At All. We have generated significant net losses and operating losses in recent periods, and have experienced volatility in our cash flows from operations ranging from positive cash flows from operations of $858,000 in the year ended March 31, 2005, to negative cash flows from operations of $718,000 and $4.8 million in the years ended March 31, 2004, and 2003, respectively. While we completed a $10.1 million convertible debenture financing and our Iteris Subsidiary closed a $5.0 million term loan in May 2004, the majority of the proceeds from such financings were used to purchase the Series A preferred stock of our Iteris Subsidiary held by outside investors.

As further described in Note 5 to the consolidated financial statements, we failed to meet some of our debt covenants under our current credit agreement with our bank. At March 31, 2005, we had $4.0 million in term debt and $945,000 in revolving credit outstanding in connection with this credit agreement. Although we are currently in negotiations to restructure this credit facility, we cannot assure you that we will be able to complete this restructuring under acceptable terms, or at all.

We may raise additional capital in the near future to fund our operations or to repay indebtedness. Such additional capital may be raised through bank borrowings, or other debt or equity financings. We cannot assure you that any additional capital will be available on a timely basis, on acceptable terms, or at all.

Our capital requirements will depend on many factors, including, but not limited to:

- our ability to successfully renegotiate a new credit arrangement with our bank;
- our ability to control costs;
- market acceptance of our products and the overall level of sales of our products;
- our ability to generate operating income;
- increased research and development funding;
- increased sales and marketing expenses;
- technological advancements and our competitors' response to our products;
- capital improvements to new and existing facilities;

- potential acquisitions of businesses and product lines;
- our relationships with customers and suppliers; and
- general economic conditions, including the effects of the current economic slowdown and international conflicts.

If our capital requirements are materially different from those currently planned, we may need additional capital sooner than anticipated. If additional funds are raised through the issuance of equity or convertible debt securities, the percentage ownership of our stockholders will be reduced and such securities may have rights, preferences and privileges senior to our common stock. Additional financing may not be available on favorable terms or at all. If adequate funds are not available or are not available on acceptable terms, we may be unable to continue our operations as planned, develop or enhance our products, expand our sales and marketing programs, take advantage of future opportunities or respond to competitive pressures.

If Our Internal Controls Over Financial Reporting Do Not Comply With The Requirements Of The Sarbanes-Oxley Act, Our Business And Stock Price Could Be Adversely Affected. We and our independent registered public accounting firm are evaluating the effectiveness of our internal controls over financial reporting to comply with Section 404 of the Sarbanes-Oxley Act of 2002. Section 404 requires us to evaluate the effectiveness of our internal controls over financial reporting as the end of each fiscal year beginning in Fiscal 2006, and to include a management report assessing the effectiveness of our internal controls over financial reporting in all annual reports beginning with our Annual Report on Form 10-K for the fiscal year ending March 31, 2006. Section 404 also requires our independent accountant to attest to, and report on, management's assessment of our internal controls over financial reporting.

Our management, including our CEO and CFO, does not expect that our internal controls over financial reporting will prevent all error and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the company have been, or will be detected. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple error or mistake. Controls can also be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part on certain assumptions about the likelihood of future events, and we cannot assure you that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

As of March 31, 2005 we became aware of a material weakness in our internal controls related to the accounting for the consolidation of our deferred compensation savings plan. We cannot assure you that we or our independent registered public accounting firm will not identify another material weakness in our internal controls. A material weakness is a control deficiency, or combination of control deficiencies, that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected. Based on our evaluation under the framework in *Internal Control—Integrated Framework*, our management has concluded that, as of March 31, 2004, our internal control over financial reporting was not effective due to the existence of one material weakness. If our internal controls over financial reporting are not considered adequate, we may experience a loss of public confidence, which could have an adverse effect on our business and our stock price.

We Rely On A Single Manufacturer For Our AutoVue LDW Systems And May Experience Supply Issues For This Product Which Could Materially And Adversely Impact Our Sales And Ultimate Market Acceptance Of AutoVue. We outsource the manufacture of our AutoVue product line to a single manufacturer. We are currently negotiating with a second supplier for the AutoVue product line. This manufacturer may not be able to produce sufficient quantities of this product in a timely manner or at a reasonable cost, which could materially and adversely affect our ability to launch or gain market acceptance of AutoVue. We are currently experiencing shortages on certain components used in the manufacture of AutoVue LDW units sold to the heavy truck market and must design and qualify a next generation system before our existing supplies are exhausted. AutoVue production availability may also be impacted by long lead times on replacement components or an inability to design these new components into production units. Based on current sales and unit forecasts, we believe we currently have a four month supply of these components on hand. We are searching world-wide supply sources to acquire additional components, but we cannot assure you that we will be able to obtain sufficient quantities of these components or that such components will be available on a timely basis. Should we not be able to procure these components before our current inventory is depleted or we engineer and qualify a next generation system, we could experience a shortfall in revenues for a brief period of time until such components can be located or the qualification of a new component is complete.

We Depend On Government Contracts And Subcontracts, And Because Many Of Our Government Contracts Are Fixed Price Contracts, Higher Than Anticipated Costs Will Reduce Our Profit And Could Adversely Impact Our Operating Results. A significant portion of our sales were derived from contracts with governmental agencies, either as a general contractor, subcontractor or supplier. Government contracts represented approximately 37.4%, 48.2% and 53.8% of our total net sales and contract revenues for the years ended March 31, 2005, 2004 and 2003, respectively. We anticipate that revenue from government contracts will continue to increase in the near future. Government business is, in general, subject to special risks and challenges, including:

- long purchase cycles or approval processes;
- competitive bidding and qualification requirements;
- the impact of international conflicts;
- performance bond requirements;
- changes in government policies and political agendas;
- delays in funding, budgetary constraints and cut-backs; and
- milestone requirements and liquidated damage provisions for failure to meet contract milestones

In addition, a large number of our government contracts are fixed price contracts. As a result, we may not be able to recover any cost overruns we may incur. These fixed price contracts require us to estimate the total project cost based on preliminary projections of the project's requirements. The financial viability of any given project depends in large part on our ability to estimate these costs accurately and complete the project on a timely basis. In the event our costs on these projects exceed the fixed contractual amount, we will be required to bear the excess costs. Such additional costs would adversely affect our financial condition and results of operations. Moreover, certain of our government contracts are subject to termination or renegotiation at the convenience of the government, which could result in a large decline in our net sales in any given quarter. Our inability to address any of the foregoing concerns or the loss or renegotiation of any material government contract could seriously harm our business, financial condition and results of operations.

If We Are Unable To Develop And Introduce New Products And Product Enhancements Successfully And In A Cost-Effective And Timely Manner, Or Are Unable To Achieve Market Acceptance Of Our New Products, Our Operating Results Would Be Adversely Affected. We believe our revenue growth and future operating results will depend on our ability to complete development of new products and enhancements, introduce these products in a timely, cost-effective manner, achieve broad market acceptance of these products and enhancements, and reduce our product costs. We may not be able to introduce any new products or any enhancements to our existing products on a timely basis, or at all. In addition, the introduction of any new products could adversely affect the sales of certain of our existing products. Our future success will also depend in part on the success of several products including our AutoVue LDW system.

We believe that we must continue to make substantial investments to support ongoing research and development in order to remain competitive. We need to continue to develop and introduce new products that incorporate the latest technological advancements in outdoor image processing hardware, software and camera technologies in response to evolving customer requirements. Our business and results of operations could be adversely affected if we do not anticipate or respond adequately to technological developments or changing customer requirements. We cannot assure you that any such investments in research and development will lead to any corresponding increase in revenue.

Market acceptance of our new products depends upon many factors, including our ability to accurately predict market requirements and evolving industry standards, our ability to resolve technical challenges in a timely and cost-effective manner and achieve manufacturing efficiencies, the perceived advantages of our new products over traditional products and the marketing capabilities of our independent distributors and strategic partners. In particular, we have granted Valeo the exclusive right to sell and manufacture our AutoVue lane departure warning system to the worldwide passenger market in exchange for royalty payments for each AutoVue unit sold. As such, the future success and broad market acceptance of our AutoVue technologies will depend upon Valeo's ability to manufacture, market and sell our technologies, and to convince more OEM passenger car manufacturers to adopt our technologies. The success of our AutoVue system will also depend in part on the success of the automotive vehicles that incorporate our technology, as well as the success of optional equipment that OEMs bundle with our technologies.

Our business and results of operations could also be seriously harmed by any significant delays in our new product development. Certain of our new products could contain undetected design faults and software errors or "bugs" when first released by us, despite our testing. We may not discover these faults or errors until after a product has been installed and used by our customers. Any faults or errors in our existing products or in any new products may cause delays in product introduction and shipments, require design modifications or harm customer relationships, any of which could adversely affect our business and competitive position.

An Economic Slowdown And Related Uncertainties Could Adversely Impact The Demand For Our Products. Concerns about inflation, decreased consumer confidence, reduced corporate profits and capital spending, and recent international conflicts and terrorist and military actions have resulted in a downturn in worldwide economic conditions, particularly in the United States. These unfavorable economic conditions may have a negative impact on customer orders, cancellations and rescheduling of backlog. In addition, recent political and social turmoil related to international conflicts and terrorist acts can be expected to put further pressure on economic conditions in the U.S. and worldwide. These political, social and economic conditions make it extremely difficult for our customers, our suppliers and us to accurately forecast and plan future business activities. If such conditions continue or worsen, our business, financial condition and results of operations will likely be materially and adversely affected.

Our Quarterly Operating Results Fluctuate As A Result Of Many Factors. Therefore, We May Fail To Meet Or Exceed The Expectations Of Securities Analysts And Investors, Which Could Cause Our Stock Price To Decline. Our quarterly revenues and operating results have fluctuated and are likely to continue to vary from quarter to quarter due to a number of factors, many of which are not within our control. Factors that could affect our revenues include, among others, the following:

- our ability to raise additional capital;
- our ability to control costs;
- international conflicts and acts of terrorism;
- our ability to develop, introduce, patent, market and gain market acceptance of new products, applications and product enhancements in a timely manner, or at all;
- the size, timing, rescheduling or cancellation of significant customer orders;
- the introduction of new products by competitors;
- the availability of components used in the manufacture of our products;
- changes in our pricing policies and the pricing policies of our suppliers and competitors, pricing concessions on volume sales, as well as increased price competition in general;
- the long lead times associated with government contracts or required by vehicle manufacturers;
- continued delays in the passage of the six year transportation bill by the U.S. government;
- our success in expanding and implementing our sales and marketing programs;
- the effects of technological changes in our target markets;
- our relatively small level of backlog at any given time;
- seasonality due to winter weather conditions;
- the mix of our sales;
- deferrals of customer orders in anticipation of new products, applications or product enhancements;

- risks and uncertainties associated with our international business;
- currency fluctuations and our ability to get currency out of certain foreign countries; and
- general economic and political conditions.

Due to all of the factors listed above as well as other unforeseen factors, our future operating results could be below the expectations of securities analysts or investors. If that happens, the trading price of our common stock could decline. As a result of these quarterly variations, you should not rely on quarter-to-quarter comparisons of our operating results as an indication of our future performance.

If We Do Not Keep Pace With Rapid Technological Changes And Evolving Industry Standards, We Will Not Be Able To Remain Competitive And There Will Be No Demand For Our Products. Our markets are in general characterized by the following factors:

- rapid technological advances;
- downward price pressure in the marketplace as technologies mature;
- changes in customer requirements;
- frequent new product introductions and enhancements; and
- evolving industry standards and changes in the regulatory environment.

Our future success will depend upon our ability to anticipate and adapt to changes in technology and industry standards, and to effectively develop, introduce, market and gain broad acceptance of new products and product enhancements incorporating the latest technological advancements.

We Have Adopted A New Operating Strategy, Which Is Untried And Exposes Us To New Risks. We recently divested ourselves of all of our other business units and merged with our Iteris Subsidiary and significantly scaled back our operations in order to focus on the ITS business. We have abandoned our strategy of incubating emerging companies, which historically required us to make significant investments in new business units. Our current business strategy is narrow and untried, and we cannot assure you that our new business strategy or the continued execution of this business will be successful.

The Markets In Which We Operate Are Highly Competitive And Have Many More Established Competitors, Which Could Adversely Affect Our Sales Or The Market Acceptance Of Our Products. We compete with numerous other companies in our target markets including, but not limited to, large, multinational corporations and many smaller regional engineering firms. We expect such competition to increase due to technological advancements, industry consolidations and reduced barriers to entry. Increased competition is likely to result in price reductions, reduced gross margins and loss of market share, any of which could seriously harm our business, financial condition and results of operations. Many of our competitors have far greater name recognition and greater financial, technological, marketing and customer service resources than we do. This may allow them to respond more quickly to new or emerging technologies and changes in customer requirements. It may also allow them to devote greater resources to the development, promotion, sale and support of their products than we can. Recent consolidations of end users, distributors and manufacturers in our target markets have exacerbated this problem. As a result of the foregoing factors, we may not be able to compete effectively in our target markets and competitive pressures could adversely affect our business, financial condition and results of operations.

We May Be Unable To Attract And Retain Key Personnel, Which Could Seriously Harm Our Business. Due to the specialized nature of our business, we are highly dependent on the continued service of our executive officers and other key management, engineering and technical personnel, particularly Jack Johnson. In connection with the roll-up merger of the Iteris Subsidiary, Mr. Johnson became our Chief Executive Officer and Mr. James Miele, the former Controller of our Iteris Subsidiary, was promoted to serve as our Chief Financial Officer. The loss of either of these individuals or of any of our executive officers or key members of management could adversely affect our business, financial condition or results of operations. Our success will also depend in large part upon our ability to continue to attract, retain and motivate qualified engineering and other highly skilled technical personnel. Competition for employees, particularly development engineers, is intense. We may not be able to continue to attract and retain sufficient numbers of such highly skilled employees. Our inability to attract and retain additional key employees or the loss of one or more of our current key employees could adversely affect our business, financial condition and results of operations.

We May Not Be Able To Adequately Protect Or Enforce Our Intellectual Property Rights, Which Could Harm Our Competitive Position. If we are not able to adequately protect or enforce the proprietary aspects of our technology, competitors could be able to access our proprietary technology and our business, financial condition and results of operations will likely be seriously harmed. We currently attempt to protect our technology through a combination of patent, copyright, trademark and trade secret laws, employee and third party nondisclosure agreements and similar means. Despite our efforts, other parties may attempt to disclose, obtain or use our technologies or systems. Our competitors may also be able to independently develop products that are substantially equivalent or superior to our products or design around our patents. In addition, the laws of some foreign countries do not protect our proprietary rights as fully as do the laws of the United States. As a result, we may not be able to protect our proprietary rights adequately in the United States or abroad.

From time to time, we have received notices that claim we have infringed upon the intellectual property of others. Even if these claims are not valid, they could subject us to significant costs. We have engaged in litigation in the past, and litigation may be necessary in the future to enforce our intellectual property rights or to determine the validity and scope of the proprietary rights of others. Litigation may also be necessary to defend against claims of infringement or invalidity by others. An adverse outcome in litigation or any similar proceedings could subject us to significant liabilities to third parties, require us to license disputed rights from others or require us to cease marketing or using certain products or technologies. We may not be able to obtain any licenses on terms acceptable to us, or at all. We also may have to indemnify certain customers or strategic partners if it is determined that we have infringed upon or misappropriated another party's intellectual property. Any of these results could adversely affect our business, financial condition and results of operations. In addition, the cost of addressing any intellectual property litigation claim, both in legal fees and expenses, and the diversion of management's attention and resources, regardless of whether the claim is valid, could be significant and could seriously harm our business, financial condition and results of operations.

The Trading Price Of Our Common Stock Is Highly Volatile. The trading price of our common stock has been subject to wide fluctuations in the past. Since January 2000, our Class A common stock (now known as our common stock) has traded at prices as low as $0.45 per share and as high as $29.44 per share. The market price of our common stock could continue to fluctuate in the future in response to various factors, including, but not limited to:

- quarterly variations in operating results;
- our ability to control costs and improve cash flow;
- our ability to raise additional capital;
- shortages announced by suppliers;
- announcements of technological innovations or new products or applications by our competitors, customers or us;
- acquisitions of businesses, products or technologies;
- the impact of any litigation;
- changes in investor perceptions;
- changes in earnings estimates or investment recommendations by securities analysts; and
- international conflicts, political unrest and acts of terrorism.

The stock market in general has recently experienced volatility, which has particularly affected the market prices of equity securities of many technology companies. This volatility has often been unrelated to the operating performance of these companies. These broad market fluctuations may adversely affect the market price of our common stock. In the past, companies that have experienced volatility in the market price of their securities have been the subject of securities class action litigation. If we were to become the subject of a class action lawsuit, it could result in substantial losses and divert management's attention and resources from other matters.

We May Engage In Acquisitions Of Companies or Technologies That May Require Us To Undertake Significant Capital Infusions And Could Result In Disruptions Of Our Business And Diversion Of Resources And Management Attention. We have historically, and may in the future, acquire complementary businesses, products and technologies. Acquisitions may require significant capital infusions and, in general, acquisitions also involve a number of special risks, including:

- potential disruption of our ongoing business and the diversion of our resources and management's attention;
- the failure to retain or integrate key acquired personnel;
- the challenge of assimilating diverse business cultures, and the difficulties in integrating the operations, technologies and information system of the acquired companies;

- increased costs to improve managerial, operational, financial and administrative systems and to eliminate duplicative services;
- the incurrence of unforeseen obligations or liabilities;
- potential impairment of relationships with employees or customers as a result of changes in management; and
- increased interest expense and amortization of acquired intangible assets.

Our competitors are also soliciting potential acquisition candidates, which could both increase the price of any acquisition targets and decrease the number of attractive companies available for acquisition. Acquisitions may also materially and adversely affect our operating results due to large write-offs, contingent liabilities, substantial depreciation, deferred compensation charges or intangible asset amortization, or other adverse tax or accounting consequences. We cannot assure you that we will be able to identify or consummate any additional acquisitions, successfully integrate any acquisitions or realize the benefits anticipated from any acquisition.

Our International Business Operations May Be Threatened By Many Factors That Are Outside Of Our Control. We currently market our AutoVue and Vantage products internationally and we anticipate that our international operations will expand in the near future. International business operations are subject to various inherent risks including, among others:

- currency fluctuations and restrictions;
- political, social and economic instability;
- reduced protection for intellectual property rights in some countries;
- unexpected changes in regulatory requirements, tariffs and other trade barriers or restrictions;
- the burdens of compliance with a wide variety of foreign laws and more restrictive labor laws and obligations;
- longer accounts receivable payment cycles;
- difficulties in managing and staffing international operations;
- potentially adverse tax consequences; and
- import and export license requirements and restrictions of the United States and each other country in which we operate.

All of our international sales from this point on are denominated in U.S. dollars. As a result, an increase in the relative value of the dollar could make our products more expensive and potentially less price competitive in international markets. We do not engage in any transactions as a hedge against risks of loss due to foreign currency fluctuations.

Any of the factors mentioned above may adversely affect our future international sales and, consequently, affect our business, financial condition and operating results. Furthermore, as we increase our international sales, our total revenues may also be affected to a greater extent by seasonal fluctuations resulting from lower sales that typically occur during the summer months in Europe and other parts of the world.

Some Of Our Directors, Officers And Their Affiliates Can Control The Outcome Of Matters That Require The Approval Of Our Stockholders, And Accordingly We Will Not Be Able To Engage In Certain Transactions Without Their Approval. As of March 31, 2005, our officers and directors owned approximately 16% of the outstanding shares of our common stock (and approximately 25% of our common stock when including options, warrants and other convertible securities held by them which are currently exercisable or convertible or will become exercisable or convertible within 60 days after March 31, 2005). As a result of their stock ownership, our management will be able to significantly influence the election of our directors and the outcome of corporate actions requiring stockholder approval, such as mergers and acquisitions, regardless of how our other stockholders may vote. This concentration of voting control may have a significant effect in delaying, deferring or preventing a change in our management or change in control and may adversely affect the voting or other rights of other holders of common stock.

Certain Anti-Takeover Provisions May Affect The Price Of Our Common Stock And Discourage A Third Party From Acquiring Us. Certain provisions of our certificate of incorporation and our stockholder rights plan could make it difficult for a third party to acquire us, even though an acquisition might be beneficial to our stockholders. Such provisions could limit the price that investors might be willing to pay in the future for shares of our common stock. Under the terms of our certificate of incorporation, our Board of Directors is authorized to issue, without stockholder approval, up to 2,000,000 shares of preferred stock with voting, conversion and other rights and preferences superior to those of our common stock. Our future issuance of preferred stock could be used to discourage an unsolicited acquisition proposal. In addition, in March 1998, we adopted a stockholder rights plan and declared a dividend of preferred stock purchase rights to our stockholders. We amended this plan in May 2004. In the event a third party acquires more than 15% of the outstanding voting control of our company or 15% of our outstanding common stock, the holders of these rights will be able to purchase the junior participating preferred stock at a substantial discount off of the then current market price. The exercise of these rights and purchase of a significant amount of stock at below market prices could cause substantial dilution to a particular acquirer and discourage the acquirer from pursuing our company. The mere existence of a stockholder rights plan often delays or makes a merger, tender offer or proxy contest more difficult.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our exposure to interest rate risk is limited to our lines of credit. Our lines of credit bear interest based on the prevailing prime rate (5.50% at March 31, 2005). A 10% increase in the interest rate on our line of credit (from 5.50% to 6.05%) would not have a material impact on our financial position, operating results, or cash flows. In addition, we believe that the carrying value of our outstanding debt approximates fair value.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The financial statements and supplementary data required by Regulation S-X are included in Part IV, Item 15 of this report.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

On a Form 8-K filed with the Securities and Exchange Commission on October 12, 2004, as amended on November 12, 2004, we previously reported our decision to dismiss our former independent registered public accounting firm, Ernst & Young LLP, effective October 5, 2004 and appoint McGladrey & Pullen, LLP as its new independent registered public accounting firm, to perform auditing services beginning with the second fiscal quarter ended September 30, 2004.

ITEM 9A. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rule 13a-15(f). Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting and concluded that our disclosure controls and procedures were ineffective in timely alerting them to the material information involving transactions occurring in the normal course of business relating to us required to be included in the reports we file or submit under the Securities Exchange Act of 1934. The Company concluded that it has a material weakness related to the administration and proper accounting for certain types of its contracts and agreements.

A material weakness is a control deficiency, or combination of control deficiencies, that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected. The material weakness described above resulted in improper accounting treatment for the Iteris Subsidiary's Deferred Compensation Savings Plan. The material weakness resulted in restatement to our 2004 financial statements with respect to deferred compensation expense and compensation saving plan liabilities.

Management's Response and Plan for Improvement

Management has responded to the identification of the material weakness related to the consolidation and proper accounting for the Plan in the 2004 financial statements by performing additional accounting, financial analysis and managerial review of procedures in order to ensure that the financial information contained in our Annual Report on Form 10-K is reliable. Additionally, we intend to amend the Plan to clarify its original intent and prohibit diversification of any shares of Company common stock held in the plan, which we believe will prevent any compensation charges or other impact on our financial statements as a result of changes in the value of the Company's common stock held in the Plan.

Changes in Internal Controls

Except as set forth above, during the most recent completed fiscal quarter covered by this report, there has been no change in our internal controls over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934) that has materially affected, or is reasonably likely to materially affect, our internal controls over financial reporting.

ITEM 9B. OTHER INFORMATION

None.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

(a) *Identification of Directors.* The information under the caption "Election of Directors," appearing in our proxy statement for the 2005 Annual Meeting of Stockholders, is incorporated herein by reference.

(b) *Identification of Executive Officers.* The information under the caption "Executive Officers," appearing in our proxy statement for the 2005 Annual Meeting of Stockholders, is incorporated herein by reference.

(c) *Compliance with Section 16(a) of the Exchange Act.* The information under the caption Section 16(a) Beneficial Ownership Reporting Compliance appearing in our proxy statement for the 2005 Annual Meeting of Stockholders is incorporated herein by reference.

(d) *Code of Ethics*. The information under the caption "Corporate Governance," appearing in our proxy statement for the 2005 Annual Meeting of Stockholders, is incorporated herein by reference.

ITEM 11. EXECUTIVE COMPENSATION

The information under the caption "Executive Compensation and Other Information," appearing in our proxy statement for the 2005 Annual Meeting of Stockholders, is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information under the captions "Equity Compensation Plans" and "Principal Stockholders and Common Stock Ownership of Certain Beneficial Owners and Management," appearing in our proxy statement for the 2005 Annual Meeting of Stockholders, is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The information under the caption "Certain Transactions," appearing in our proxy statement for the 2005 Annual Meeting of Stockholders, is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

The information under the caption "Fees Paid to Independent Auditors," appearing in our proxy statement for the 2005 Annual Meeting of Stockholders, is incorporated herein by reference.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a) Documents filed as part of this report:

1. *Financial Statements.* The following financial statements of Iteris, Inc. are included in a separate section of this Annual Report on Form 10-K commencing on the pages referenced below:

Report of Independent Registered Public Accounting Firm, McGladrey & Pullen, LLP	F-2
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2. *Financial Statement Schedules*.

Schedule II— Valuation and Qualifying Accounts

All other schedules have been omitted because they are not required or the required information is included in our consolidated financial statements and notes thereto.

3. *Exhibits*.

The following exhibits are filed herewith or incorporated by reference to the location indicated below:

Exhibit Number	Description	Where Located
3.1	Amended and Restated Certificate of Incorporation of the registrant	*Exhibit 3.1 to the registrant's current Report on Form 8-K as filed with the SEC on October 28, 2004*
3.2	Bylaws of the registrant, as amended	*Exhibit 4.2 to the registrant's Registration Statement on Form S-1 (Reg. No. 033-67932) as filed with the SEC on July 6, 1993*
3.3	Certificates of Amendment to Bylaws of the registrant dated April 24, 1998 and August 10, 2001	*Exhibit 3.4 to the registrant's Annual Report on Form 10-K/A for the year ended March 31, 2003 as filed with the SEC on July 29, 2003*

Exhibit Number	Description	Where Located
4.1	Specimen of common stock certificate	*Exhibit 4.1 to registrant's Amendment No. 1 to the Registration Statement on Form 8-A as filed with the SEC on December 8, 2004*
4.2	Form of rights certificate for preferred stock purchase rights	*Exhibit A of Exhibit 4 to the registrant's Current Report on Form 8-K as filed with the SEC on May 1, 1998*
10.1*	Profit Sharing Plan and Trust	*Exhibit 10.3 to the registrant's Amendment No. 2 to the Registration Statement on Form S-8 (Reg. No. 002-98656) as filed with the SEC on May 5, 1988*
10.2*	Amendment Nos. 3 and 4 to the Profit Sharing Plan and Trust	*Exhibits 4.3.1 and 4.3.2, respectively, to Amendment No. 3 to Iteris Holdings' Registration Statement on Form S-3 (Reg. No. 002-86220) as filed with the SEC on June 13, 1990*
10.3 *	Form of Executive Deferral Plan between the registrant and certain employees of the registrant).	*Exhibit 10.4 to the registrant's Annual Report on Form 10-K for the year ended March 31, 1988*
10.4	Form of Indemnity Agreement entered into by the registrant and certain of its officers and directors	*Exhibit 19.4 to the registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 1988*
10.5	Form of Indemnification Agreement entered into by the registrant and certain of its officers and directors	*Exhibit 10.5 to the registrant's Annual Report on Form 10-K for the year ended March 31, 2004 as filed with the SEC on June 29, 2004*
10.6 *	1997 Stock Incentive Plan (as amended on May 3, 2002)	*Exhibit 10.5 to the registrant's Annual Report on Form 10-K for the year ended March 31, 2003 as filed with the SEC on June 30, 2003*
107 *	Form of Notice of Grant of Stock Option	*Exhibit 99.2 to the registrant's Registration Statement on Form S-8 (File No. 333-30396) as filed with the SEC on February 14, 2000*
10.8 *	Form of Stock Option Agreement	*Exhibit 99.3 to the registrant's Registration Statement on Form S-8 (File No. 333-30396) as filed with the SEC on February 14, 2000*
10.9 *	Form of Addendum to Stock Option Agreement—Involuntary Termination Following Corporate Transaction or Change in Control	*Exhibit 99.4 to the registrant's Registration Statement on Form S-8 (File No. 333-30396) as filed with the SEC on February 14, 2000*
10.10 *	Form of Addendum to Stock Option Agreement—Limited Stock Appreciation Rights	*Exhibit 99.5 to the registrant's Registration Statement on Form S-8 (File No. 333-30396) as filed with the SEC on February 14, 2000*
10.11 *	Form of Stock Issuance Agreement	*Exhibit 99.6 to the registrant's Registration Statement on Form S-8 (File No. 333-30396) as filed with the SEC on February 14, 2000*

Exhibit Number	Description	Where Located
10.12 *	Form of Addendum to Stock Issuance Agreement—Involuntary Termination Following Corporate Transaction/Change in Control	*Exhibit 99.7 to the registrant's Registration Statement on Form S-8 (File No. 333-30396) as filed with the SEC on February 14, 2000*
10.13 *	Form of Notice of Grant of Automatic Stock Option—Initial Grant	*Exhibit 99.8 to Exhibit 99.8 to registrant's Registration Statement on Form S-8 (File No. 333-30396) as filed with the SEC on February 14, 2000*
10.14 *	Form of Notice of Grant of Automatic Stock Option—Annual Grant	*Exhibit 99.9 to the registrant's Registration Statement on Form S-8 (File No. 333-30396) as filed with the SEC on February 14, 2000*
10.15 *	Form of Automatic Stock Option Agreement.	*Exhibit 99.10 to the registrant's Registration Statement on Form S-8 (File No. 333-30396) as filed with the SEC on February 19, 2000*
10.16	Amended and Restated Rights Agreement, dated as of May 10, 2004, by and between the registrant and U.S. Stock Transfer Corporation, including the exhibits thereto.	*Exhibit 99.1 to the registrant's Registration Statement on Form 8-A/A as filed with the SEC on June 18, 2004.*
10.17 *	1994 Long-Term Equity Plan Exhibit 4.3 to the registrant's Registration Statement on Form S-8 (File No. 333-05735) as filed with the SEC on June 11, 1996).	*Exhibit 4.3 to the registrant's Registration Statement on Form S-8 (File No. 333-05735) as filed with the SEC on June 11, 1996*
10.18	Amended and Restated Agreement of Purchase and Sale and Escrow Instructions, dated February 19, 2002, by and between Iteris, Inc. and 1515 South Manchester, LLC	*Exhibit 2.1 to the registrant's Current Report on Form 8-K as filed with the SEC on June 12, 2002*
10.19	Sublease Agreement dated May 7, 2003 by and between Iteris, Inc. and FEI-Zyfer, Inc.	*Exhibit 10.19 to registrant's Annual Report on Form 10-K for the year ended March 31, 2003 as filed with the SEC on June 30, 2003*
10.20	Loan and Security Agreement dated February 22, 2002 by and between the registrant and Technology Lending Partners, L.L.C.	*Exhibit 10.20 to the registrant's Annual Report on Form 10-K/A for the year ended March 31, 2003 as filed with the SEC on July 29, 2003*
10.21	Receivables Purchase Agreement dated October 18, 2002 by and between the registrant and Technology Lending Partners, L.L.C., as amended by Amendment Number One dated November 27, 2002 and Amendment Number Two dated January 7, 2003	*Exhibit 10.21 to the registrant's Annual Report on Form 10-K/A for the year ended March 31, 2003 as filed with the SEC on July 29, 2003*
10.22 *	Change in Control Agreement dated May 8, 2003 by and between the registrant and Gregory A. Miner	*Exhibit 10.1 to the registrant's Annual Report on Form 10-Q for the quarter ended June 30, 2003 as filed with the SEC on August 14, 2003*
10.23 *	Change in Control Agreement dated May 20, 2003 by and between the registrant and Jack E. Johnson	*Exhibit 10.23 to Amendment No. 1 to the registrant's Registration Statement on Form S-1 as filed with the SEC on February 17, 2004*

Exhibit Number	Description	Where Located
10.24 *	1998 Stock Incentive Plan (as amended on February 7, 2000)	*Filed Herewith*
10.25	Wells Fargo Bank Credit Agreement dated May 27, 2004	*Filed Herewith*
10.26	Wells Fargo Bank Assumption and Amendment Agreement dated October 20, 2004	*Filed Herewith*
10.27	Wells Fargo Bank Revolving Line of Credit Note dated May 27, 2004	*Filed Herewith*
10.28	Wells Fargo Bank Term Note dated May 27, 2004	*Filed Herewith*
10.29	Wells Fargo Bank Continuing Security Agreement Rights to Payment and Inventory dated May 27, 2004	*Filed Herewith*
10.30	Wells Fargo Bank Security Agreement Equipment dated May 27, 2004	*Filed Herewith*
10.31*	Iteris, Inc. Deferred Compensation Savings Plan and Grantor Trust	*Filed Herewith*
10.32*	1997 Stock Incentive Plan (as amended on May 3, 2003, as further amended on December 15, 2004)	*Filed Herewith*
21	Subsidiaries of the registrant	*Filed Herewith*
23.1	Consent of Independent Registered Public Accounting Firm, McGladrey & Pullen, LLP	*Filed Herewith*
23.2	Consent of Independent Registered Public Accounting Firm, Ernst & Young, LLP	*Filed Herewith*
31.1	Certification of the Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	*Filed Herewith*
31.2	Certification of the Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	*Filed Herewith*
32.1	Certification of the Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	*Filed Herewith*
32.2	Certification of the Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	*Filed Herewith*

* Indicates a management contract or compensatory plan or arrangement

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized.

ITERIS, INC.
(Registrant)

By /s/ JACK JOHNSON
Jack Johnson
President and Chief Executive Officer

POWER OF ATTORNEY

We, the undersigned officers and directors of Iteris, Inc., do hereby constitute and appoint James S. Miele and Jack Johnson, and each of them, our true and lawful attorneys-in-fact and agents, each with full power of substitution and resubstitution, for him and in his name, place and stead, in any and all capacities, to sign any and all amendments to this report, and to file the same, with exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite or necessary to be done in and about the premises, as fully to all intents and purposes as he might or could do in person, hereby, ratifying and confirming all that each of said attorneys-in-fact and agents, or his substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant in the capacities and on the dates indicated:

Signature	Title	Date
/s/ JACK JOHNSON Jack Johnson	Director, President and Chief Executive Officer (principal executive officer)	July 12, 2005
/s/ JAMES S. MIELE James S. Miele	Chief Financial Officer (principal financial and accounting officer)	July 12, 2005
/s/ GREGORY A. MINER Gregory A. Miner	Chairman of the Board	July 12, 2005
/s/ KEVIN C. DALY Kevin C. Daly, Ph.D.	Director	July 12, 2005

/s/ GARY HERNANDEZ Gary Hernandez	Director	July 12, 2005
/s/ HARTMUT MARWITZ Hartmut Marwitz, Ph.D.	Director	July 12, 2005
/s/ JOHN SEAZHOLTZ John Seazholtz	Director	July 12, 2005
/s/ JOEL SLUTZKY Joel Slutzky	Director	July 12, 2005
/s/ THOMAS L. THOMAS Thomas L. Thomas	Director	July 12, 2005
/s/ PAUL E. WRIGHT Paul E. Wright	Director	July 12, 2005

Iteris, Inc.

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Report of Independent Registered Public Accounting Firm

To the Board of Directors
Iteris, Inc.
Anaheim, California

We have audited the consolidated balance sheet of Iteris, Inc. as of March 31, 2005, and the related consolidated statements of operations, stockholders' equity and cash flows for the year then ended. Our audit also included the 2005 financial statement schedule listed at Item 15. These financial statements and the schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provided a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Iteris, Inc. as of March 31, 2005, and the results of its operations and its cash flows for the year then ended, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

/s/ McGladrey & Pullen, LLP

Irvine, California
June 1, 2005, except for the four paragraphs under the caption "Deferred Compensation Plan" in Note 7 as to which the date is July 12, 2005

Report of Independent Registered Public Accounting Firm

Stockholders and Board of Directors
Iteris, Inc.

We have audited the accompanying consolidated balance sheet of Iteris, Inc. as of March 31, 2004, and the related consolidated statements of operations, stockholders' equity (deficit), and cash flows for each of the two years in the period ended March 31, 2004. Our audits also included the financial statement schedule listed in the index at Item 15(a). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1, the accompanying financial statements as of and for the year ended March 31, 2004 have been restated to reflect the consolidation of the Company's Subsidiary's deferred compensation plan.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Iteris, Inc. at March 31, 2004, and the consolidated results of its operations and its cash flows for each of the two years in the period ended March 31, 2004, in conformity with accounting principles generally accepted in the United States. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set-forth therein.

/s/ Ernst & Young LLP

Orange County, California
June 8, 2004,
except for Note 1 - Restatement of Consolidated Financial Statements for the Year Ended March 31, 2004, and Note 7 - Deferred Compensation Plan, as to which the date is July 13, 2005.

Iteris, Inc.

Consolidated Balance Sheets

(In thousands)

	March 31,	
	2005	2004 (Restated)
Assets		
Current assets:		
Cash and cash equivalents	$ 46	$ 2,612
Trade accounts receivable, net of allowance for doubtful accounts of $239 and $204 at March 31, 2005, and 2004, respectively.	8,866	8,255
Costs and estimated earnings in excess of billings on uncompleted contracts	2,086	2,653
Notes receivable	—	125
Deferred income taxes	101	821
Inventories, net of reserve for inventory obsolescence of $514 and $399 at March 31, 2005, and 2004 respectively	4,344	3,598
Prepaid expenses and other current assets	384	323
Total current assets	15,827	18,387
Property and equipment:		
Leasehold improvements	105	97
Equipment	5,281	7,724
Accumulated depreciation	(4,283)	(6,179)
	1,103	1,642
Deferred income taxes	559	—
Intangible assets, net of accumulated amortization of $114 at March 31, 2005	698	—
Goodwill	27,774	9,807
Other assets	695	229
Total assets	$ 46,656	$ 30,065

See accompanying notes.

Iteris, Inc.

Consolidated Balance Sheets

(In thousands, except share and per share amounts)

	March 31,	
	2005	2004 (Restated)
Liabilities and stockholders' equity (deficit)		
Current liabilities:		
Trade accounts payable	$ 3,936	$ 3,560
Accrued payroll and related expenses	3,007	3,218
Accrued liabilities	790	1,064
Revolving line of credit	945	—
Billings in excess of costs and estimated earnings on uncompleted contracts	944	549
Income taxes payable	—	485
Revolving line of credit with related party	—	100
Current portion of long-term debt	4,008	42
Total current liabilities	13,630	9,018
Non-current payroll related liability	330	—
Deferred compensation plan liability	772	1,256
Deferred gain on sale of building	733	1,774
Long-term debt and capital lease obligation	1,319	891
Convertible debentures, net	8,996	—
Minority interest	—	18,202
Commitments and contingencies		
Redeemable common stock		
Issued and outstanding shares – 1,219,445 and none at March 31, 2005, and 2004, respectively	3,414	—
Stockholders' equity (deficit):		
Preferred stock:		
Authorized shares – 2,000,000		
Issued and outstanding – none	—	—
Common stock, $.10 par value:		
Authorized shares – 50,000,000 at March 31, 2005, and 50,000,000 of Class A and 2,600,000 of Class B at March 31, 2004		
Issued and outstanding shares – 27,089,661 at March 31, 2005; 20,476,568 of Class A and 928,317 of Class B at March 31, 2004	2,709	2,141
Additional paid-in capital	126,534	95,937
Deferred stock-based compensation	(925)	—
Common stock held in trust – 310,510 shares at March 31, 2005 and none at March 31, 2004	(374)	—
Treasury stock – 93 shares at March 31, 2005, and 2004	(1)	(1)
Notes receivable from employees	(45)	(45)
Accumulated deficit	(110,436)	(99,108)
Total stockholders' equity (deficit)	17,462	(1,076)
Total liabilities and stockholders' equity (deficit)	$ 46,656	$ 30,065

See accompanying notes.

Iteris, Inc.

Consolidated Statements of Operations

(In thousands, except per share amounts)

	Year Ended March 31,		
	2005	2004 (Restated)	2003
Net sales and contract revenues:			
Net sales	$ 29,062	$ 23,470	$ 19,112
Contract revenues	17,335	21,813	22,283
Total net sales and contract revenues	46,397	45,283	41,395
Costs and expenses:			
Cost of net sales	15,645	12,758	9,366
Cost of contract revenues	11,398	14,712	15,110
Selling, general and administrative expenses	13,964	12,844	14,105
Research and development expenses	4,193	3,923	3,908
Stock-based compensation	11,777	—	—
Deferred compensation expense (benefit)	(484)	868	—
Disposal of fixed assets	422	—	—
Acquired in-process research and development	140	—	—
Amortization of intangible assets	114	—	—
Total costs and expenses	57,169	45,105	42,489
Income (loss) from operations	(10,772)	178	(1,094)
Non-operating income (expense):			
Other income, net	1,054	1,003	417
Interest expense, net	(1,178)	(123)	(761)
Income (loss) from continuing operations before income taxes and minority interest	(10,896)	1,058	(1,438)
Income tax benefit (provision)	94	(100)	—
Minority interest in earnings of subsidiary	(526)	(2,813)	(3,818)
Loss from continuing operations	(11,328)	(1,855)	(5,256)
Income (loss) from discontinued operations, net of taxes of $0	—	1,215	(7,892)
Net loss	$ (11,328)	$ (640)	$ (13,148)
Basic and diluted earnings (loss) per share:			
Continuing operations	$ (0.45)	$ (0.09)	$ (0.37)
Discontinued operations	—	0.06	(0.55)
Basic earnings (loss) per share	$ (0.45)	$ (0.03)	$ (0.92)
Shares used in computing basic earnings (loss) per share	25,284	19,454	14,276
Shares used in computing diluted earnings (loss) per share	25,284	19,454	14,276

See accompanying notes.

Iteris, Inc.

Consolidated Statements of and Stockholders' Equity (Deficit)

(In thousands)

	Common Stock Shares outstanding											
	Class A common stock	Class B common stock	Amount	Additional paid-in capital	Treasury stock	Notes receivable from employees	Accumulated other comprehensive income	Deferred stock-based compensation	Common Stock held in trust	Accumulated deficit	Total Stockholder's equity (deficit)	Comprehensive income (loss)
Balance at March 31, 2002	11,491	1,036	$ 1,252	$ 88,082	$ (1)	$ (51)	$ 241	$ —	$ —	$ (85,320)	$ 4,203	
Issuances of Class A common stock	2,590	—	260	3,685	—	—	—	—	—	—	3,945	—
Foreign currency translation adjustments	—	—	—	—	—	—	(340)	—	—	—	(340)	$ (340)
Net loss	—	—	—	—	—	—	—	—	—	(13,148)	(13,148)	(13,148)
Balance at March 31, 2003	14,081	1,036	1,512	91,767	(1)	(51)	(99)	—	—	(98,468)	(5,340)	$ (13,488)
Issuance of Class A common stock and warrants	6,288	—	629	4,170	—	—	—	—	—	—	4,799	—
Conversion of Class B common stock	108	(108)	—	—	—	—	—	—	—	—	—	—
Payments on notes receivable	—	—	—	—	—	6	—	—	—	—	6	—
Foreign currency translation adjustments	—	—	—	—	—	—	99	—	—	—	99	$ 99
Net loss (Restated)	—	—	—	—	—	—	—	—	—	(640)	(640)	(640)
Balance at March 31, 2004 (Restated)	20,477	928	2,141	95,937	(1)	(45)	—	—	—	(99,108)	(1,076)	$ (541)
Warrant exercises	402	—	40	344	—	—	—	—	—	—	384	—
Stock option exercises	25	—	2	49	—	—	—	—	—	—	51	—
Issuance of warrants in connection with convertible debentures	—	—	—	1,101	—	—	—	—	—	—	1,101	—
Conversion of Class B common stock	1,020	(928)	9	(9)	—	—	—	—	—	—	—	—
Convertible debenture conversion to common stock	69	—	7	205	—	—	—	—	—	—	212	—
Issuance of common stock in connection with merger of Iteris Subsidiary	4,787	—	479	14,722	—	—	—	—	—	—	15,201	—
Issuance of warrants	—	—	—	26	—	—	—	—	—	—	26	—
Assumption of Iteris subsidiary stock options and warrants	—	—	—	13,816	—	—	—	(1,433)	—	—	12,383	—
Common stock held in trust	310	—	31	343	—	—	—	—	(374)	—	—	—
Amortization of deferred stock-based compensation	—	—	—	—	—	—	—	508	—	—	508	—
Net loss	—	—	—	—	—	—	—	—	—	(11,328)	(11,328)	$ (11,328)
Balance at March 31, 2005	27,090	—	$ 2,709	$ 126,534	$ (1)	$ (45)	$ —	$ (925)	$ (374)	$ (110,436)	$ 17,462	$ (11,328)

See accompanying notes.

Iteris, Inc.

Consolidated Statements of Cash Flows
(In thousands)

	Year Ended March 31,		
	2005	2004 (Restated)	2003
Operating activities			
Net loss from continuing operations	$ (11,328)	$ (1,855)	$ (5,256)
Net income (loss) from discontinued operations	—	1,215	(7,892)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Depreciation and amortization	787	857	816
Write-off of acquired in-process research and development	140	—	—
Minority interest in earnings of subsidiary	526	2,813	3,818
Amortization of warrants	—	—	246
Amortization of deferred gain on sale-leaseback	(609)	(855)	(1,665)
Amortization of intangible assets	114	—	—
Amortization of debt discounts	184	—	—
Amortization of deferred financing costs	121	—	—
Fair value of warrants issued for services	26	—	—
Stock-based compensation	11,777	—	—
Loss on sale of Iteris subsidiary common stock	—	—	310
Loss on disposal of assets	422	—	2
Change in deferred tax assets	(200)	—	—
Changes in operating assets and liabilities:			
Accounts receivable	(611)	(88)	(518)
Net costs and estimated earnings in excess of billings	961	(10)	187
Inventories	(746)	305	(741)
Prepaid expenses and other assets	41	1,454	(1,388)
Deferred gain on sale of building	—	(3,396)	7,690
Accounts payable and accrued expenses	(521)	(1,625)	3,790
Deferred revenue	(226)	226	—
Net assets (liabilities) of discontinued operations	—	241	(4,188)
Net cash provided by (used in) operating activities	858	(718)	(4,789)
Investing activities			
Purchases of property and equipment net	(670)	(558)	(518)
Proceeds from sale of building	—	—	18,951
Notes receivable	125	—	—
Acquistion costs	(80)	—	—
Other	—	99	(340)
Net cash provided by (used in) investing activities	(625)	(459)	18,093
Financing activities			
Proceeds (payments) from borrowings on lines of credit, net	845	(1,385)	(767)
Proceeds from long-term debt	5,000	918	—
Payments on long-term debt and capital lease obligations	(1,038)	—	(16,145)
Proceeds from issuance of common stock and related warrants	—	3,813	2,766
Proceeds from issuance of convertible debentures	9,436	—	—
Purchase of Iteris subsidiary Series A preferred stock	(17,543)	—	—
Proceeds from stock option and warrant exercises	501	—	—
Proceeds from sale of common and preferred stock	—	—	871
Payments on notes receivable from employees	—	6	—
Net cash provided by (used in) financing activities	(2,799)	3,352	(13,275)
Increase (decrease) in cash	(2,566)	2,175	29
Cash and cash equivalents at beginning of year	2,612	437	408
Cash and cash equivalents at end of year	$ 46	$ 2,612	$ 437

Supplemental cash flow information:			
Cash paid during the period:			
Interest	$ 747	$ 123	$ 507
Income taxes	624	320	—
Supplemental schedule of non-cash investing and financing activities:			
Proceeds from sale-leaseback held in escrow	$ —	$ —	$ 2,516
Issuance of Common Stock to settle liabilities	—	416	—
Increase in promissory note to landlord to settle lease obligation	432	—	—
Acquistion of minority interest of the Iteris subsidiary			
Intangible assets	812	—	—
Deferred tax liabilities	360	—	—
Goodwill	17,887	—	—
Reduction of minority interest	1,253	—	—
Issuance of warrants in connection with Debenture and Warrant Purchase Agreement	1,101	—	—
Conversion of convertible debt to equity	250	—	—
Contribution of common stock to 401(k) plan to settle employer match	—	578	141

See accompanying notes.

Iteris, Inc.
Notes to Consolidated Financial Statements
March 31, 2005

1. Description of Business and Summary of Significant Accounting Policies

Description of Business

Iteris, Inc., formerly known as Iteris Holdings, Inc. (the "Company"), is a leading provider of outdoor machine vision systems and sensors that optimize the flow of traffic and enhance driver safety. Using proprietary software and Intelligent Transportation Systems ("ITS") industry expertise, the Company provides video sensor systems and transportation management and traveler information systems to the ITS industry. The ITS industry is comprised of companies applying a variety of technologies to enable the safe and efficient movement of people and goods. The Company uses its outdoor image recognition software expertise to develop proprietary algorithms for video sensor systems that improve vehicle safety and the flow of traffic. Using its knowledge of the ITS industry, the Company designs and implements transportation management systems that help public agencies reduce traffic congestion and provide greater access to traveler information. On October 22, 2004, the Company completed the merger with its majority-owned subsidiary, Iteris, Inc. (the "Iteris Subsidiary"), and officially changed the Company's corporate name from Iteris Holdings, Inc. to Iteris, Inc. (Note 3). The Company was originally incorporated in Delaware in 1987 as Odetics, Inc. and in September 2003 changed its name to Iteris Holdings, Inc. to reflect its focus on the ITS industry and its capital structure at that time.

The Company has incurred losses from continuing operations of $11.3 million, $1.9 million and $5.3 million during the fiscal years ended March 31, 2005, 2004 and 2003, respectively. Operating activities generated cash of $858,000 in the fiscal year ended March 31, 2005; and utilized cash of $718,000 and $4.8 million in the fiscal years ended March 31, 2004, and 2003, respectively. As of March 31, 2005, the Company had an accumulated deficit of $110.4 million, cash and cash equivalents on hand of $46,000, and borrowings of $945,000 against its $5.0 million line of credit. As discussed further in Note 5, at March 31, 2005, the Company was in violation of certain covenants associated with its line of credit and term debt facility and is currently in the process of restructuring this facility. The Company believes that cash generated from operations and the restructuring of its credit facility will provide sufficient funding to meet working capital requirements, capital expenditures, debt and other obligations through the next 12 months. The Company may face significant risks associated with the successful execution of its business strategy and may need to raise additional capital in order to fund more rapid expansion, to expand its marketing activities, to develop new or enhance existing services or products, and to respond to competitive pressures or to acquire complementary services, businesses, or technologies. If the Company is not successful in generating sufficient cash flow from operations or is unable to restructure its credit facility, it may need to raise additional capital through public or private financing, strategic relationships or other arrangements. However, there are no assurances that any additional capital will be available at a cost or in an amount sufficient to execute the Company's business strategy.

Restatement of Consolidated Financial Statements for the Year Ended March 31, 2004

The Company has restated its consolidated financial statements for the year ended March 31, 2004 as previously reported on Form 10-K. The restatement was necessary in order to reflect the consolidation of the Iteris Deferred Compensation Savings Plan (the "Deferred Compensation Plan" – Note 7), the principal effects of which were to increase operating expenses by a non-cash charge of $868,000 for the year ended March 31, 2004 and decrease minority interest in the earnings of the Iteris Subsidiary by $221,000 for the year ended March 31, 2004. This restatement had no impact on the Company's consolidated cash flows.

The effect of the restatement had the following impact on the Company's net income (loss) and net income (loss) per share for the year ended March 31, 2004 (in thousands, except share data):

	As previously reported	Restatement	As restated
Loss from continuing operations	$ (1,208)	$ (647)	$ (1,855)
Loss from discontinued operations	1,215	—	1,215
Net income (loss)	$ 7	$ (647)	$ (640)
Basic and diluted loss per share:			
Loss from continuing operations	(0.06)	(0.03)	(0.09)
Loss from discontinued operations	0.06	—	0.06
Net income (loss)	$ 0.00	$ (0.03)	$ (0.03)

Basis of Presentation

The accompanying consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation. The consolidated financial statements have been restated to reflect the discontinuation of all operations except those of the Company and its remaining subsidiary, Meyer Mohaddes Associates, Inc.. The Company also consolidated the Deferred Compensation Plan (Note 7).

As discussed further in Note 11, the Company previously discontinued the operations of its Broadcast, Inc. subsidiary ("Broadcast"), its Zyfer, Inc. subsidiary ("Zyfer"), and its MAXxess Systems, Inc. subsidiary ("MAXxess"), so that the Company could focus on its ITS business. The results of operations for these businesses are presented as discontinued operations in the accompanying consolidated financial statements.

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the U.S. requires management to

make certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements, and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates made in the preparation of the consolidated financial statements include the allowance for doubtful accounts, deferred tax assets, inventory and warranty reserves, costs to complete long-term contracts, overhead rates used in cost-plus contracts, contract reserves and estimates of future cash flows used to assess the recoverability of long-lived assets, the valuation of equity instruments and the realization of goodwill.

Reclassifications

Certain reclassifications have been made to the prior years financial statements to conform with the current year presentation.

Revenue Recognition

Product revenues and related costs of sales are recognized upon the transfer of title, which generally occurs upon shipment or, if required, upon acceptance by the customer, provided that the Company believes collectibility of the net sales amount is probable. Accordingly, at the date revenue is recognized, the significant uncertainties concerning the sale have been resolved.

Contract revenues are derived primarily from long-term contracts with governmental agencies. Contract revenues include costs incurred plus a portion of estimated fees or profits determined on the percentage of completion method of accounting based on the relationship of costs incurred to total estimated costs. Any anticipated losses on contracts are charged to earnings when identified. Changes in job performance and estimated profitability, including those arising from contract penalty provisions and final contract settlements, may result in revisions to costs and revenues and are recognized in the period in which the revisions are determined. Profit incentives are included in revenue when their realization is reasonably assured.

In addition to product and contract revenue, the Company derives revenue from technology access fees, the provision of specific non-recurring contract engineering services and royalties. Technology access fees and contract engineering revenues are recognized on the percentage of completion method of accounting based on the relationship of hours incurred to total estimated hours. Royalty revenue is recorded in the period in which the royalty is earned, based on unit sales of the Company's products. Technology access fee revenues, contract engineering revenues and royalty revenues are included in net sales in the accompanying consolidated statements of operations.

Revenues from follow-on service and support, for which the Company charges separately, are recorded in the period in which the services are performed.

Concentration of Credit Risk

Accounts receivable are derived from revenues earned from customers located throughout North America and Europe. The Company generally does not require collateral or other security from customers. Collectibility of receivable balances is estimated through review of invoices outstanding greater than a certain period of time and ongoing credit evaluations of customers' financial condition. Reserves are maintained for potential credit losses, and such losses have historically been within management's expectations.

At March 31, 2005, and 2004, accounts receivable from governmental agencies and prime government contractors were approximately $3.5 million. No customer or government agency had a receivable balance greater than 10% of our total net sales or contract revenues at March 31, 2005 and 2004.

Fair Values of Financial Instruments

The fair values of cash and cash equivalents, receivables, inventories, accounts payable and accrued expenses approximate carrying value because of the short period of time to maturity. The fair values of line of credit agreements and long-term debt approximate carrying value because the related rates of interest approximate current market rates. The fair value of convertible debentures approximates carrying value because the effective interest rate, taking into account recorded debt discounts, approximates current market rates. The fair value of redeemable common stock approximates carrying value since these shares are not tradable in any public equity markets. If the redeemable shares become registered, the fair value of such shares may differ from the carrying value based on the value of the shares as determined in the public equity markets.

Cash and Cash Equivalents

Cash and cash equivalents consist of cash and short-term investments with initial maturities of ninety days or less.

Inventories

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

Property and Equipment

Property and equipment are recorded at cost and are depreciated principally by the double declining balance method over the estimated useful life ranging from three to eight years. Leasehold improvements are depreciated over the term of the related lease.

Goodwill and Long-Lived Assets

In accordance with Statement of Financial Accounting Standards ("SFAS") No. 142, *Goodwill and Intangible Assets* ("SFAS 142"), goodwill is tested for impairment at the reporting unit level (operating segment or one level below an operating segment) on an annual basis in the Company's fourth fiscal quarter or more frequently if indicators of impairment exist. The performance of the test involves a two-step process. The first step of the impairment test involves comparing the fair value of the Company's reporting units with the reporting unit's carrying amount, including goodwill. The fair value of reporting units is generally determined using the income approach. If the carrying amount of a reporting unit exceeds the reporting unit's fair value, the second step of the goodwill impairment test is performed to determine the amount of any impairment loss. The second step of the goodwill impairment test involves comparing the implied fair value of the reporting unit's goodwill with the carrying amount of that goodwill.

The Company evaluates long-lived assets for impairment in accordance with SFAS No. 144, *"Accounting for the Impairment or Disposal of Long-Lived Assets,"* which requires impairment evaluation on long-lived assets used in operations when indicators of impairment are present. Reviews are performed to determine whether the carrying value of assets is impaired, based on comparison to undiscounted expected future cash flows. If this comparison indicates that there is impairment, the impaired asset is written down to fair value, which is typically calculated using discounted expected future cash flows using a discount rate based upon the Company's weighted average cost of capital adjusted for risks associated with the related operations. Impairment is based on the excess of the carrying amount over the fair value of those assets.

Income Taxes

The Company utilizes the liability method of accounting for income taxes as set forth in SFAS No. 109, *Accounting for Income Taxes* ("SFAS 109"). Under the liability method, deferred taxes are determined based on the temporary differences between the financial statement and tax bases of assets and liabilities using enacted tax rates. A valuation allowance is recorded when it is more likely than not that some of the deferred tax assets will not be realized. See Note 6.

Stock-Based Compensation

The Company accounts for stock-based employee compensation arrangements in accordance with Accounting Principles Board Opinion No. 25, *Accounting for Stock-Issued to Employees* ("APB 25") and related interpretations, and complies with the disclosure-only provisions of SFAS No. 123, *Accounting for Stock-Based Compensation* ("SFAS 123") and SFAS 148, *Accounting for Stock-Based Compensation – Transition and Disclosure* ("SFAS 148"). Under APB 25, compensation cost is recognized based on the difference, if any, on the date of the grant between the fair value of the Company's stock and the amount the employee must pay to acquire the stock.

In accordance with the requirements of the disclosure-only alternative of SFAS 123 and SFAS 148, set forth below are the assumptions used and the pro forma statement of operations data of the Company giving effect to valuing stock-based awards to employees using the Black-Scholes option pricing model instead of the guidelines provided by APB 25. Among other factors, the Black-Scholes model considers the expected life of the option and the expected volatility of the Company's stock price in arriving at an option valuation.

The per share fair value of stock options granted in connection with stock option plans has been estimated with the following weighted average assumptions:

	Years Ended March 31,		
	2005	2004	2003
Dividend rate	0.0	0.0	0.0
Expected life – years	7.0	7.0	7.0
Risk-free interest rate	4.5	2.0	2.0
Volatility of common stock	0.5	0.4	0.4

For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the options' vesting period. The Company's pro forma information follows:

	Year Ended March 31,		
	2005	2004	2003
	(In thousands, except per share amounts)		
		(Restated)	
Net loss — as reported	$ (11,328)	$ (640)	$ (13,148)
Add: Stock-based compensation expense included in net loss – as reported	11,777	—	—
Deduct: Stock-based compensation expense determined under fair value method	(12,806)	(385)	(637)
Net loss — pro forma	$ (12,357)	$ (1,025)	$ (13,785)
Basic and diluted loss per share — as reported	$ (0.45)	$ (0.03)	$ (0.92)
Basic and diluted loss per share — pro forma	$ (0.49)	$ (0.05)	$ (0.97)

Research and Development Expenditures

Research and development expenditures are charged to expense in the period incurred.

Shipping and Handling Costs

Shipping and handling costs are included as cost of sales in the period during which the products ship.

Advertising Expenses

Advertising costs are expensed in the period incurred and totaled $112,000, $127,000 and $77,000 in the years ended March 31, 2005, 2004 and 2003, respectively.

Warranty

Unless otherwise stated, the Company provides a one to three year warranty from the original invoice date on all products, materials, and workmanship. Products sold to certain original equipment manufacturer ("OEM") customers sometimes carry longer warranties. Defective products will be either repaired or replaced, generally at the Company's option, upon meeting certain criteria. The Company accrues a provision for the estimated costs that may be incurred for product warranties relating to a product as a component of cost of sales at the time revenue for that product is recognized. The accrued warranty provision is included within accrued expenses on the accompanying condensed consolidated balance sheets.

Repair and Maintenance Costs

The Company incurs repair and maintenance costs in the normal course of business. Should the activity result in a permanent improvement to one of the Company's leased facilities, the cost is capitalized as a leasehold improvement and amortized over its useful life or the remainder of the lease period, whichever is shorter. Non-permanent repair and maintenance costs are charged to expense as incurred.

Comprehensive Income

The only component of accumulated other comprehensive income is the cumulative foreign currency translation adjustment recorded in stockholders' equity (deficit), which was eliminated through transactions that occurred during the year ended March 31, 2004.

Recent Accounting Pronouncements

In November 2004, the FASB issued SFAS No. 151, *Inventory Costs* ("SFAS 151"), which clarifies the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material. SFAS 151 will be effective for inventory costs incurred during fiscal years beginning after June 15, 2005. Management does not believe the adoption of SFAS 151 will have a material impact on the Company's consolidated financial statements.

On December 16, 2004, the FASB issued SFAS No. 123 (revised 2004), *Share-Based Payment* ("SFAS 123R") which replaces SFAS 123, supersedes APB 25 and amends SFAS No. 95, *Statement of Cash Flows*. Generally, the approach in SFAS 123R is similar to the approach described in SFAS 123. However, SFAS 123R requires all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their fair values (i.e., pro forma disclosure is no longer an alternative to financial statement recognition). In accordance with SEC Release No. 33-8568, SFAS 123R will be effective for the Company beginning April 1, 2006. The Company is currently assessing the impact of SFAS 123R. As of the date of this filing, no decisions have been made as to whether the Company will apply the modified prospective or retrospective transition method of application.

Reclassifications

Certain prior year amounts have been reclassified to conform to the current year presentation.

2. Supplementary Financial Information

Inventories

The following table presents details of the Company's inventories:

	March 31,	
	2005	2004
	(In thousands)	
Materials and supplies	$ 3,204	$ 2,762
Work in process	558	294
Finished goods	582	542
	$ 4,344	$ 3,598

Goodwill and Identifiable Intangible Assets

	March 31, 2005		March 31, 2004	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
	(In thousands)			
Intangible assets subject to amortization:				
Developed Technology	$ 495	$ (78)	$ —	$ —
Patents	317	(36)	—	—
Total	$ 812	$ (114)	$ —	$ —

Amortization expense for intangible assets subject to amortization was $114,000 for the year ended March 31, 2005. Future estimated amortization expense for the next five years and thereafter is as follows (in thousands):

Year ending March 31:	
(In thousands)	
2006	$ 147
2007	147
2008	147
2009	147
2010	58
Thereafter	52
	$ 698

At March 31, 2005, goodwill was comprised of $18.0 million associated with the October 2004 merger of the Iteris Subsidiary (Note 3); $9.6 million associated with the acquisitions of the Rockwell International Transportation Systems Group, Meyer Mohaddes Associates and the Viggen Systems Consulting Group; and $200,000 associated with the purchase of the assets of Mil-Lektron, a complimentary product to the Company's Vantage video detection business.

Warranty Reserve Activity

The following table presents activity in accrued warranty obligations:

	March 31,		
	2005	2004	2003
	(In thousands)		
Balance at beginning of year	$ 192	$ 256	$ 249
Additions charged to cost of sales	614	161	323
Warranty claims	(480)	(225)	(316)
Balance at end of year	$ 326	$ 192	$ 256

Earnings (Loss) Per Share

The following table sets forth the computation of basic and diluted income (loss) per share:

	Year Ended March 31,		
	2005	2004	2003
		(Restated)	
	(In thousands, except per share amounts)		
Numerator:			
Loss from continuing operations	$ (11,328)	$ (1,855)	$ (5,256)
Income (loss) from discontinued operations	—	1,215	(7,892)
Net loss	$ (11,328)	$ (640)	$ (13,148)
Denominator:			
Denominator for basic and diluted loss per share	25,284	19,454	14,276
Basic and diluted earnings (loss) per share:			
Loss from continuing operations	$ (0.45)	$ (0.09)	$ (0.37)
Income (loss) from discontinued operations	—	0.06	(0.55)
Net loss	$ (0.45)	$ (0.03)	$ (0.92)

The following shares were excluded from the computation of diluted earnings (loss) per share as their effect would have been anti-dilutive:

	Year Ended March 31,		
	2005	2004	2003
	(In thousands)		
Stock options	4,560	162	61
Warrants	1,095	64	—

3. Merger of the Company and the Iteris Subsidiary

On May 28, 2004 (the "Closing Date"), in order to simplify the Company's capital structure and facilitate the merger of the Iteris Subsidiary into the Company, the Company completed the purchase of all of the outstanding shares of the Series A preferred stock of the Iteris Subsidiary (the "Series A preferred stock"), which were held by DaimlerChrysler Ventures GmbH ("DCV") and Hockenheim Investment Pte. Ltd. ("Hockenheim"), in exchange for approximately $17.5 million in cash. In addition, the Company acquired all of the 547,893 shares of common stock of the Iteris Subsidiary held by DCV in exchange for the issuance of 1,219,445 shares (the "Exchange Shares") of the Company's Class A common stock (now known as the Company's common stock) which was valued at $3.4 million at the date of issuance. The fair value of the Company's common stock issued in the transaction was based on the quoted market price of the Company's stock on the OTC Bulletin Board averaged over a five-day period. The purchase and exchange of the shares were made pursuant to a Stock Purchase and Exchange Agreement dated March 31, 2004, by and among the Company, the Iteris Subsidiary, DCV and Hockenheim (the "Purchase and Exchange Agreement").

Pursuant to the Purchase and Exchange Agreement, the Company purchased 3,124,913 shares of the Series A preferred stock of the Iteris Subsidiary from DCV and Hockenheim for a purchase price of $5.61 per share. The purchase price represented the stated redemption value of the Series A preferred stock. The purchase of the shares was financed primarily with a $10.1 million convertible debenture financing completed in May 2004 with a group of accredited investors, in addition to a $5.0 million senior credit facility arranged through a bank and $2.4 million in cash (Note 5).

On June 30, 2004, the Company and certain minority stockholders of the Iteris Subsidiary (including certain officers and directors) entered into an exchange agreement whereby an aggregate of 1,319,541 shares of common stock of the Iteris Subsidiary were exchanged for 2,639,082 shares of the Company's newly issued common stock valued at $8.6 million at the date of issuance. The fair value of the Company's stock issued in the transaction was based on the quoted market price of the Company's common stock on the OTC Bulletin Board averaged over a five-day period. The effect of this exchange was to reduce the residual minority interest in the Iteris Subsidiary to 8.1%.

On October 22, 2004, the Iteris Subsidiary was merged into the Company. The remaining 8.1% minority interest in the Iteris Subsidiary (consisting of 1,228,981 shares of common stock of the Iteris Subsidiary) was converted to 2,457,962 shares of the Company's common stock valued at $7.6 million at the merger date. Immediately following the merger, the Company converted all of its outstanding Class B common stock (921,917 shares) into 1,014,108 shares of its common stock (formerly designated as Class A common stock). The exchange ratio used in conversion was determined by the Company's Board of Directors. The fair value of the Company's common stock issued in the transaction was based on the quoted market price of the Company's common stock on the OTC Bulletin Board averaged over a five-day period. In October 2004, the Company also amended its certificate of incorporation to (a) change the voting rights of its common stock from one-tenth to one vote per share, (b) remove the ability to issue any further shares of Class B common stock, and (c) rename its Class A common stock to common stock. As a result, the Company currently has only one class of common stock outstanding, the common stock.

In connection with the merger, the Company assumed all outstanding options and warrants to purchase shares of common stock of the Iteris Subsidiary that were outstanding immediately prior to the merger, whether vested or unvested, together with the Iteris Subsidiary's 1998 Stock Incentive Plan (the "Option Plan"). Each such option and warrant assumed by the Company shall continue to have, and be subject to, the same terms and conditions as were applicable immediately prior to the merger, provided that (A) such option or warrant shall be exercisable for that number of whole shares of the Company's common stock equal to the product of the number of shares of the Company's common stock that were issuable upon exercise of such assumed option or warrant immediately prior to the merger multiplied by two (2) (the "Exchange Ratio") rounded down to the nearest whole number of shares and (B) the per share exercise price for the shares of the Company's common stock issuable upon exercise of such assumed option or warrant is equal to the quotient determined by dividing the exercise price per share at which such option or warrant was exercisable immediately prior to the merger by the Exchange Ratio (rounded up to the nearest whole cent). As a result, options and warrants to purchase approximately 3.1 million shares and 327,000 shares, respectively, of common stock of the Iteris Subsidiary assumed in the merger became options and warrants to purchase approximately 6.1 million and 654,000 shares of common stock of the Company, respectively. The weighted-average exercise prices of the assumed options and warrants were $1.09 and $2.32, respectively. Stock-based compensation expense of $11.3 million was recorded in connection with the assumption and exchange of vested Iteris Subsidiary stock options for stock options immediately exercisable into the Company's common stock based on the difference between the fair market value of the Company's common stock on the October 22, 2004, merger date and the exercise price of the modified stock option. Additionally, the Company recorded approximately $1.4 million in deferred compensation related to the assumption of unvested stock options to purchase common stock of the Iteris Subsidiary. Deferred compensation is being amortized to stock-based compensation expense as the options vest. The Company also recorded $1.1 million of goodwill and additional paid-in-capital in connection with the 654,000 vested warrants assumed in the merger and acquisition of the Iteris Subsidiary. The $1.1 million value was based on the difference between the fair market value of the Company's common stock on the October 22, 2004, merger date and modified exercise price of the assumed warrant awards.

The excess of the purchase price over the proportionate amount of minority interest acquired was allocated to acquired intangible assets based on the estimated fair values with the residual allocated to goodwill. Accordingly, the Company recorded goodwill of $18.0 million, which represents the excess of the purchase price over the fair value of the proportionate identifiable net assets acquired. The estimated fair value of the intangible assets was determined using the income method and discounting future expected returns. The estimated useful life for each of the acquired intangible assets is provided below:

Patents	7 years
Developed technology	5 years

The following table summarizes fair values of the assets acquired and liabilities assumed and the allocation of the purchase price at the date of acquisition (in thousands):

Acquisition costs:		
Issuance of common stock	$	18,617
Assumption of Iteris Subsidiary warrants		1,114
Purchase of Iteris Subsidiary Series A preferred stock		17,543
Acquisition costs		80
Total acquisition costs	$	37,354
Purchase price allocation:		
Fair value of 41% of Iteris Subsidiary		
Patents	$	318
Developed technology		495
Acquired in-process research and development		140
Deferred tax liabilities		(360)
Reduction of minority interest		18,794
Goodwill (not deductable for tax purposes)		17,967
Total purchase price allocation	$	37,354

On October 22, 2004, in connection with the Company's merger with the Iteris Subsidiary, the Chief Executive Officer of the Iteris Subsidiary, Mr. Jack Johnson, was promoted to President and Chief Executive Officer of the Company, replacing Mr. Gregory Miner. This merger triggered certain obligations under the Company's change-in-control agreement with Mr. Miner. Accordingly, the Company recorded approximately $807,000 in severance expense, which included $57,000 for related payroll taxes, as a charge to operations for the year ended March 31, 2005. The severance amount will be paid to Mr. Miner in bi-weekly installments over the next 30 months. Mr. Miner is not required to render any services to the Company in connection with this agreement.

4. Costs and Estimated Earnings on Uncompleted Contracts

Costs incurred, estimated earnings and billings on uncompleted long-term contracts are as follows:

	March 31,	
	2005	2004
	(In thousands)	
Total estimated contract value	$ 71,835	$ 64,434
Costs incurred on uncompleted contracts	$ 16,553	$ 20,840
Estimated earnings	1,655	2,084
	18,208	22,924
Less billings to date	(17,066)	(20,820)
	$ 1,142	$ 2,104
Included in accompanying consolidated balance sheets:		
Costs and estimated earnings in excess of billings on uncompleted contracts	$ 2,086	$ 2,653
Billings in excess of costs and estimated earnings on uncompleted contracts	(944)	(549)
	$ 1,142	$ 2,104

Costs and estimated earnings in excess of billings at March 31, 2005, and 2004 include $481,000 and $534,000, respectively, that were not billable as certain milestone objectives specified in the contracts had not been attained. Substantially all costs and estimated earnings in excess of billings at March 31, 2005, are expected to be billed and collected during the year ending March 31, 2006.

5. Revolving Lines of Credit and Long-Term Debt

Revolving Lines of Credit

On May 28, 2004, Iteris Subsidiary entered into a line of credit agreement with a bank, which expires on August 1, 2005, and provides for a maximum available credit line of $5.0 million. This line of credit was assumed by the Company in October 2004. Under the terms of this agreement, the Company may borrow against its eligible accounts receivable and the value of its eligible inventory, as defined in the credit agreement. Interest on borrowed amounts is payable monthly at the current stated prime rate. Additionally, the Company is obligated to pay an unused line fee of 0.25% per annum applied to the amount by which the maximum credit amount exceeds the average daily principal balance during the preceding month.

There are no monthly collateral management fees and no pre-payment or early termination fees. On March 31, 2005, the available credit under this line of credit agreement was $4.4 million, of which $3.4 million was unused.

At March 31, 2004, the Company had $100,000 outstanding under a $1.25 million line of credit with a partnership controlled by the Company's then Chairman of the Board. This line of credit agreement was cancelled during the year ended March 31, 2005, and all amounts were repaid.

Long-Term Debt

Long-term debt consists of the following:

	March 31,	
	2005	2004
	(In thousands)	
Convertible debentures, net	$ 8,996	$ —
Bank term note	3,958	—
Promissory note to landlord	1,292	811
4% note payable	67	109
Capital lease obligation	$ 10	$ 13
	14,323	933
Less current portion	(4,008)	(42)
	$ 10,315	$ 891

Convertible Debentures, Net. In order to finance the purchase of the Iteris Subsidiary Series A preferred stock (Note 3), the Company entered into a Debenture and Warrant Purchase Agreement dated May 19, 2004 (the "Debenture and Warrant Purchase Agreement"), with a group of accredited investors, which included certain officers of the Company, pursuant to which the Company sold and issued subordinated convertible debentures in the aggregate original principal amount of $10.1 million. In connection with the issuance of the convertible debentures, the Company issued detachable warrants to purchase an aggregate of 639,847 shares of its common stock (Note 9), the value of which was recorded as a debt discount against the face amount of the debentures on the date of issuance and is being amortized to interest expense over the term of the convertible debentures.

The debentures are due in full on May 19, 2009, provide for 6.0% annual interest, payable quarterly, and are convertible into the Company's common stock at an initial conversion price of $3.61 per share, subject to certain adjustments, including adjustments for dilutive issuances. From May 19, 2007, until May 18, 2008, the debentures may be redeemed by the Company, at its option, at 120% of the principal amount being redeemed; and from May 19, 2008, until the maturity date, the debentures may be redeemed at 110% of the principal amount being redeemed. As of March 31, 2005, $250,000 of convertible debentures had been converted into 69,252 shares of common stock leaving $9.9 million of the originally issued convertible debentures outstanding at March 31, 2005.

Bank Term Note. Concurrent with the issuance of the convertible debentures, Iteris Subsidiary entered into a $5.0 million term note payable with a bank. This note was assumed by the Company in October 2004.The proceeds from the note were used to purchase the Series A preferred stock of the Iteris Subsidiary (Note 3). The note is due on May 27, 2008, and provides for monthly principal payments of approximately $104,000. Interest accrues at the current stated prime rate plus 0.25% (5.75% at March 31, 2005).

Both the term note payable and the line of credit are held by one bank under the same credit agreement and are secured by substantially all of the assets of the Company. At March 31, 2005, the Company failed to meet certain financial covenants under the credit agreement. On May 12, 2005, the bank waived its right of default regarding the covenant violations for the quarter ended March 31, 2005, only. The Company is currently renegotiating the entire credit facility to modify the covenant requirements to allow the Company to meet its future covenants and also provide sufficient financing to fund future working capital requirements. Because the bank has not waived its default rights for a period of at least twelve months and because the Company has not entered into a definitive agreement for a modified credit agreement, the entire balance of the bank term note is presented as a current liability in the accompanying March 31, 2005, consolidated balance sheet.

Promissory Note to Landlord. As discussed further in Note 7, on July 1, 2003, the Company amended the terms of its lease for its headquarters and entered into a $811,000 unsecured promissory note payable to its landlord. On November 1, 2004, $432,000 was added to the principal balance of this note to settle prior lease obligations, bringing the total principal

balance to $1.3 million. Under the terms of the note agreement, interest is payable quarterly and accrues at a rate of prime plus 2.0% (7.5% at March 31, 2005). Beginning on October 1, 2006, the Company is required to make four equal quarterly payments of principal and accrued interest. All outstanding accrued interest and principal shall be payable in full on July 2, 2007.

4% Note Payable. On October 9, 2003, the Company entered into a $126,000 unsecured note payable agreement to settle trade payables. The note is secured by the equipment related to the payable. The note bears interest at 4.0%, is payable in monthly installments of $4,000 for 36 months and is payable in full on October 20, 2006.

Scheduled aggregate maturities of long-term debt principal as of March 31, 2005, were as follows:

Year ending March 31, (In thousands)	
2006	$ 4,008
2007	670
2008	649
2009	—
2010	9,850
	$ 15,177

6. Income Taxes

The reconciliation of the income tax provision (benefit) from continuing operations to taxes computed at U.S. federal statutory rates is as follows:

	Year Ended March 31,		
	2005	2004	2003
		(In thousands) (Restated)	
Income tax (benefit) provision at statutory rates	$ (3,705)	$ 360	$ (489)
State income taxes net of federal benefit	(72)	20	4
Change in valuation allowance associated with federal deferred tax assets	(755)	(316)	330
Compensation charges	3,692	—	—
Adjustment to prior year deferred taxes	229	—	—
Expiration of unused credits	266	—	—
Other permanent differences	251	36	155
	$ (94)	$ 100	$ —

The components of deferred tax assets and liabilities are as follows:

	March 31,	
	2005	2004
	(In thousands)	
Deferred tax assets:		
Net operating losses	$ 19,880	$ 20,244
Property and equipment	1,695	5,323
Credit carry forwards	1,914	2,420
Deferred compensation and payroll	1,626	977
Bad debt allowances and other reserves	422	209
Other, net	204	202
Total deferred tax assets	25,741	29,375
Valuation allowance	(24,417)	(28,119)
Net deferred tax assets	1,324	1,256
Deferred tax liabilities:		
Capitalized interest and taxes	(369)	(404)
Acquired intangibles	(295)	—
Other, net	—	(31)
Total deferred tax liabilities	(664)	(435)
Net deferred tax assets	$ 660	821
Current portion of net deferred taxes	101	821
Long-term portion of net deferred taxes	559	—
Net deferred tax assets	$ 660	$ 821

The components of current and deferred federal and state income tax benefits and provisions are as follows:

	Year Ended March 31,		
	2005	2004	2003
	(In thousands)		
Current income tax (benefit) provision			
Federal	$ 91	$ 891	$ 35
State	14	30	—
Deferred income tax (benefit) provision			
Federal	(75)	(821)	(35)
State	(124)	—	—
Net income tax (benefit) provision	$ (94)	$ 100	$ —

At March 31, 2005, the Company had approximately $1.4 million in federal general business credit carryforwards that begin to expire in 2006 and $700,000 in state general business credit carryforwards that can be carried forward indefinitely. The Company had $54.5 million of federal net operating loss carryforwards at March 31, 2005, that begin to expire in 2019 and $35.0 million of state net operating loss carryforwards that begin to expire in 2005. For financial reporting purposes, a valuation allowance has been recorded to offset the deferred tax asset related to these credits and net operating losses. Any future benefits recognized from the reduction of the valuation allowance related to these carryforwards will result in a reduction of income tax expense.

Prior to May 28, 2004, the Iteris Subsidiary was required to file a separate federal income tax return. On May 28, 2004, the Company acquired a greater than 80% ownership interest in the Iteris Subsidiary. From that date forward, income taxes are provided on a consolidated basis for federal income tax purposes. Due to changes in stock ownership, the prior year $49.8 million federal net operating loss carryforwards and other federal tax attributes of the Company are subject to a Section 382 limitation estimated at approximately $2.9 million annually which can be utilized to offset federal consolidated taxable income. To the extent such limitation is not exceeded in a particular year, the excess limitation accumulates and adds to subsequent years' limitations. As a result of the annual limitation, a portion of the Company's carryforwards will expire before ultimately becoming available to reduce future income tax liabilities.

At March 31, 2005, the Company recorded a valuation allowance against its net deferred tax assets of approximately $24.0 million for that portion of deferred tax assets that it is more likely than not will not be realized. In making such determination, a review of all available positive and negative evidence was considered, including scheduled reversal of deferred tax liabilities potential carryback, projected future taxable income, tax planning strategies, and recent financial performance. At March 31, 2005, the Company has established a partial valuation allowance against its existing net deferred tax assets, and recorded a net deferred tax asset of $660,000 related to the consolidated group.

7. Commitments and Contingencies

Litigation

On June 29, 2004, a supplier to Mariner Networks, Inc., the Company's former subsidiary, filed a complaint in Orange County Superior Court against the Company alleging various breaches of written contract claims arising out of alleged purchase orders. The plaintiff in this lawsuit seeks monetary damages aggregating approximately $850,000 plus attorney fees and related costs. Discovery has commenced with respect to this matter, and no trial date has been set. Settlement discussions are currently pending at this time, but there can be no assurance that this lawsuit will be settled in a timely manner or for a reasonable amount.
The Company believes that the ultimate resolution of this claim will not have a material impact on the Company's financial position, results of operations or cash flows, and, accordingly, has not recorded any amounts in the accompanying consolidated financial statements in connection with this matter.

In June 2004, the Company received $949,000 as part of a settlement between Rockwell International and the Michigan Department of Transportation, pursuant to which the Company was a third party beneficiary. This amount was recorded in other income in the consolidated statement of operations for the year ended March 31, 2005.

From time to time, the Company has been involved in litigation relating to claims arising out of its operations in the normal course of business. The Company currently is not a party to any legal proceedings except as described above, the adverse outcome of which, in management's opinion, individually or in the aggregate, would have a material adverse effect on its consolidated results of operations, financial position or cash flows.

Operating Leases

In May 2002, the Company completed the sale and leaseback of its headquarters in Anaheim, California whereby the Company entered into a lease with an initial term of ten years. In connection with the sale leaseback transaction, the Company originally recorded a deferred gain of approximately $7.6 million that was being amortized against operating expenses over the term of the initial lease. On July 1, 2003, the Company renegotiated the terms of this lease whereby the square footage under lease was reduced and the initial lease term of ten years was reduced to four years. As a result of the new lease agreement, $2.5 million of restricted cash was released to the Company and paid to the landlord, the Company entered into a promissory note agreement with the landlord for $811,000 (Note 5), and the deferred gain on the sale of the building was adjusted. On November 1, 2004, the Company again amended this lease and increased the note payable to the landlord by $432,000 as a settlement to release the Company from its obligations under the existing lease related to the separation of buildings located at the Anaheim facility and other facility improvements to be made at the location. The $432,000 was recorded as a reduction of the deferred gain on the sale of the building. The remaining deferred gain was $733,000 at March 31, 2005 which will be amortized through October 2007.

The Company has lease commitments for facilities in various locations throughout the United States. Future minimum rental payments under noncancelable operating leases are as follows at March 31, 2005:

Year ending March 31, (In thousands)		
2006	$	1,116
2007		1,005
2008		601
2009		3
	$	2,725

Rent expense under operating leases totaled $1,722,000, $2,241,000 and $2,597,000, respectively, for the years ending March 31, 2005, 2004 and 2003.

The Company subleases 10,000 of the 88,000 square feet that it leases in Anaheim, California at a monthly rate of $10,000. Aggregate future minimum rental income from this sublease agreement is $120,000 and $70,000 for the years ending March 31, 2006, and 2007, respectively.

Inventory Purchase Commitments

At March 31, 2005, the Company had firm commitments to purchase inventory in the amount of $271,000 during the first quarter of its fiscal year ending March 31, 2006.

Deferred Compensation Plan

In 1986, the Company adopted the Executive Deferral Plan (the "1986 Plan") under which certain executives were able to defer a portion of their annual compensation into the 1986 Plan. All deferred amounts earned interest, generally with no guaranteed rate of return.

During the year ended March 31, 2003, the Iteris Subsidiary adopted the Deferred Compensation Plan for the sole purpose of transferring Iteris Subsidiary common stock and cash out of the 1986 Plan. All assets of the 1986 Plan were distributed prior to March 31, 2003. Certain of these assets, consisting of 133,333 shares of the Iteris Subsidiary's common stock and $14,000 in cash, were transferred to the Deferred Compensation Plan during the year ended March 31, 2003. Compensation withholdings deferred under the 1986 Plan and the Deferred Compensation Plan aggregated $0, $0 and $43,000 for the years ended March 31, 2005, 2004 and 2003, respectively.

During the year ended March 31, 2005, the Company assumed the Deferred Compensation Plan as part of the October 2004 merger and acquisition of the Iteris Subsidiary. In accordance with the merger (Note 3) the Company exchanged the original 133,333 shares of Iteris Subsidiary common stock held in the Deferred Compensation Plan and an additional 21,922 shares of the Iteris Subsidiary's common stock subsequently purchased with deferred wages for 310,510 shares of the Company's common stock. All shares of Iteris Subsidiary stock held in the plan were purchased with funds earned by the executives and deferred to the plan at the estimated fair value and the same price that was paid by outside investors at that time, or approximately $374,000.

At March 31, 2005, the Deferred Compensation Plan held 310,510 shares of the Company's common stock and $14,000 in cash, which the Company has presented as an aggregated $772,000 deferred compensation plan liability in the accompanying consolidated balance sheet. Changes in the value of Company common stock held by the Deferred Compensation Plan are determined based on changes in the quoted market price of the Company's common stock at the close of each reporting period and presented within operating expenses in the accompanying consolidated statements of operations. The original $374,000 cost basis of shares of Company common stock held in the Deferred Compensation Plan has been recorded as a contra-equity account in the accompanying consolidated financial statements.

8. Redeemable Common Stock

As discussed in Note 3, the Company issued 1,219,445 Exchange Shares in connection with the merger of the Iteris Subsidiary into the Company. Subject to certain exceptions, DCV agreed not to sell or otherwise transfer the Exchange Shares during the year following the Closing Date. However, beginning on November 28, 2005, DCV may require the Company to repurchase up to 50% of the Exchange Shares at a purchase price of $1.438 per share; and beginning on May 28, 2007, DCV may require the Company to repurchase up to 100% of the Exchange Shares at a purchase price of $1.438 per

share. All such rights to require the repurchase of the Exchange Shares expire on September 28, 2007. Because this right is outside the control of the Company, the Company has classified the $3.4 million value of the 1,219,445 shares as redeemable common stock on the accompanying March 31, 2005, consolidated balance sheet. In addition, beginning on May 28, 2005, DCV had the right to request registration of all 1,219,445 shares of the Company's common stock held as part of this exchange. In the event the Company decides not to file a registration statement to register all such shares, DCV may require the Company to repurchase any or all of its shares of the Company's common stock at a purchase price of $1.438 per share. On February 1, 2005, DCV announced that its investment portfolio, which included its ownership in Iteris, Inc., was sold to European-based Cipio Partners for an undisclosed sum. All repurchase and registration rights associated with the DCV shares inured to the benefit of Cipio Partners.

9. Stockholders' Equity

Preferred Stock

The Company's certificate of incorporation provides for the issuance of up to 2,000,000 shares of preferred stock. As of March 31, 2005, and 2004, there were no outstanding shares of preferred stock, and the Company does not have any plans to issue any shares of preferred stock. The Company's Board of Directors is authorized to issue from time to time such authorized but unissued shares of preferred stock in one or more series and to fix or alter the designations, preferences, rights and any qualifications, limitations or restrictions of the shares of each such series, including the dividend, conversion, voting, redemption and liquidation rights.

Common Stock and Common Stock Warrants

As discussed in Note 3, on October 22, 2004, the Iteris Subsidiary was merged into the Company. Also in October 2004, the Company amended its certificate of incorporation to (a) change the voting rights of its common stock from one-tenth to one vote per share, (b) remove the ability to issue any further shares of Class B common stock, and (c) rename its Class A common stock to common stock. As a result, the Company currently has only one class of common stock outstanding, the common stock. Previously, the Company had two classes of common stock outstanding – the Class A common stock and the Class B common stock.

Subject to the rights specifically granted to holders of any then outstanding shares of the Company's preferred stock, the Company's common stockholders are entitled to any dividends that may be declared by the Board of Directors. Upon dissolution, liquidation or winding up, holders of common stock are entitled to share ratably in net assets after payment or provision for all liabilities and any preferential liquidation rights of preferred stock then outstanding. Common stockholders generally do not have preemptive or redemption rights, except for the Exchange Shares issued to DCV in the merger of the Company and the Iteris Subsidiary (Notes 3 and 8). The rights, preferences and privileges of holders of common stock will be subject to those of the holders of any shares of common stock and preferred stock the Company may issue in the future.

Pursuant to the Debenture and Warrant Purchase Agreement discussed in Note 5, each individual investor also received two warrants to purchase shares of the Company's common stock. For every dollar of debenture purchased, each investor received one warrant to purchase approximately 0.03235 shares of the Company's common stock at an exercise price of $3.86 per share and a second warrant to purchase approximately 0.03100 shares of the Company's common stock at an exercise price of $4.03 per share. The exercise prices are subject to certain adjustments, including adjustments for dilutive issuances. The warrants to purchase 639,347 shares of common stock were immediately exercisable and expire on May 18, 2009. Debt discount costs related to the fair value of the warrants issued in connection with the convertible debentures were calculated based on the fair value of the warrants determined using the Black-Scholes valuation model, and were approximately $854,000 at March 31, 2005. Significant valuation estimates used in the determination of the value of the warrants include an expected life of five years, no dividends, a risk-free interest rate of 4.5% and a stock volatility factor of 0.5.

Also in connection with the Debenture and Warrant Purchase Agreement, the Company issued warrants to the investment bankers, as a commission, to purchase 34,036 shares of its common stock at an exercise price of $3.86 per share. The warrants were immediately exercisable and expire on May 18, 2009. The estimated fair value of these warrants of $40,000 was recorded as a deferred financing cost and is being amortized to interest expense over the five-year life of the debentures. Additionally, the Company incurred $621,000 in transaction costs associated with the debenture offering, which have also been capitalized as deferred financing costs and are being amortized to interest expense over the five-year term of the debentures. Unamortized deferred financing costs aggregated $568,000 at March 31, 2005, and are presented within other assets on the accompanying consolidated balance sheet.

During the year ended March 31, 2004, the Company issued 657,132 shares of its Class A common stock valued at $578,000 and 89,332 shares of its Class A common stock valued at $151,000 to settle 401(k) match liabilities and prior trade liabilities in Company stock, respectively.

In September 2003, the Company issued 425,000 shares of its Class A common stock, valued at $255,000, and 75,000 warrants to purchase common stock at an exercise price of $5.00 per share, to settle liabilities related to the sale lease-back of the Anaheim facility and the renegotiation of the related lease. The warrants are immediately exercisable and expire in July 2010. The fair value of these warrants was $5,000 calculated using the Black Scholes Model. The value of the warrants was recorded as a reduction of the deferred gain on the sale of the building.

In July 2003, the Company completed a private placement of 3,666,666 shares of its Class A common stock to seven accredited investors for net proceeds of $1.9 million in cash. In connection with this offering, the Company also issued warrants to purchase an additional 366,666 shares of common stock at an exercise price of $1.50 per share. The fair value of these warrants was $55,000 calculated using the Black Scholes Model. The warrants are considered a cost of raising capital and were recorded in equity as an offset to additional paid-in capital. The warrants expire in July 2006 and became exercisable in January 2003.

In April 2002 and February 2003, the Company sold 322,581 shares of the Iteris Subsidiary common stock that it held at an aggregate purchase price of $900,000 to a group of investors, which included certain members of management of the Company and the Iteris Subsidiary. In connection with this transaction, the Company realized a loss of $300,000 that is reflected in other income net in the accompanying consolidated statements of operations. In February 2003, the Iteris Subsidiary purchased back from the Company 288,500 shares of Iteris Subsidiary common stock that the Company held. The Company realized a loss of $310,000 on this transaction, which is reflected in other income, net in the accompanying consolidated statements of operations.

In September 2002, the Company issued 75,000, 50,000 and 62,500 warrants at exercise prices of $1.44, $1.68 and $1.95, respectively, in connection with prior year fund raising activities. The warrants were immediately exercisable and expire in August 2007. The fair value of these warrants was $130,000 calculated using the Black Scholes Model. The warrants were considered a cost of raising capital and were recorded in equity as an offset to additional paid-in capital.

On August 16, 2002, the Company completed a private placement of 2,500,000 of its Class A common stock to an institutional investor for $3.0 million in cash. The transaction, net of expenses, raised net proceeds of approximately $2.7 million. In connection with this offering, the Company also issued warrants to the investor to purchase up to another 1,250,000 shares at an exercise price of $1.50 per share, and up to 1,250,000 shares at an exercise price of $1.80 per share. The warrants are exercisable at any time by the investor, are callable by the Company if the market price of the Company's common stock trades for 20 consecutive days at a price equal or greater than two times the exercise price of the warrants, and expire in August 2007. The fair value of these warrants was $713,000 calculated using the Black Scholes Model. The warrants were considered a cost of raising capital and were recorded in equity as an offset to additional paid-in capital. The proceeds from the August 2002 transaction were used to fund general working capital requirements. In March 2004, 1,250,000 warrants at $1.50 per share become callable and were exercised by the holder.

The following table summarizes information regarding outstanding warrants to purchase the Company's common stock as of March 31, 2005:

Range of Exercise Prices	Warrants Outstanding at March 31, 2005	Weighted Avg. Remaining Contractual Life	Weighted Avg. Exercise Price
	(In thousands, except per share amounts)		
$1.40 to $1.95	2,229	2.02	$ 1.66
$3.00 to $4.03	1,150	2.94	$ 3.56
$5.00 to $5.26	230	4.66	$ 5.18
	3,609	2.48	$ 2.49

All of the warrants were exercisable at March 31, 2005.

Common stock reserved for future issuance at March 31, 2005:

	(In thousands)
Issuable under stock options plans	7,679
Issuable upon the exercise of warrants	3,609
	11,288

10. Associate Benefit Plans

Stock Option Plan

The Company has adopted the 1997 Stock Incentive Plan (the "Plan"), which provides that options for shares of the Company's unissued common stock may be granted to directors, associates and consultants to the Company. Options granted enable the option holder to purchase one share of common stock at prices which are equal to or greater than the fair market value of the shares at the date of grant. Options expire ten years after the date of grant or 90 days after termination of employment and generally vest ratably at the rate of 25% on each of the first four anniversaries of the grant date. In connection with the merger of the Company and the Iteris Subsidiary, the Company assumed the outstanding options of the Iteris Subsidiary (Note 3).

A summary of all Company stock option activity is as follows:

	Year Ended March 31,					
	2005		2004		2003	
	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price
	(In thousands, except per share amounts)					
Options outstanding at beginning of year	1,132	$ 2.98	962	$ 3.73	329	$ 8.37
Granted	163	3.34	230	0.78	659	1.38
Assumed in merger (Note 3)	6,133	1.09	—	—	—	—
Exercised	(25)	2.10	—	—	—	—
Cancelled	(80)	1.29	(60)	6.76	(26)	4.29
Options outstanding at end of year	7,323	$ 1.42	1,132	$ 2.98	962	$ 3.73
Exercisable at end of year	6,446		778		879	
Available for grant at end of year	356		519		689	
Weighted average fair value of options granted		$ 1.83		$ 0.55		$ 0.68

The following table summarizes information regarding the Company's stock options at March 31, 2005:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Options Outstanding at March 31, 2005	Weighted Avg. Remaining Contractual Life	Weighted Avg. Exercise Price	Options Exercisable At March 31, 2005	Weighted Avg. Exercise Price
	(In thousands, except per share amounts)				
$0.53 to $0.80	1,861	3.31	$ 0.57	1,861	$ 0.57
$0.95 to $1.40	4,851	5.39	1.25	4,077	1.24
$1.50 to $1.88	171	4.59	1.74	171	1.74
$2.28 to $3.20	70	8.22	2.77	70	2.77
$3.60 to $4.63	202	6.63	4.09	99	4.59
$5.69 to $8.00	26	3.55	6.13	26	6.13
$10.31 to $15.63	142	4.96	12.64	142	12.64
	7,323	4.89	$ 1.42	6,446	$ 1.40

Associate Incentive Programs

Under the terms of a Profit Sharing Plan, the Company contributes to a trust fund such amounts as are determined annually by the Board of Directors. No contributions were made during the years ended March 31, 2005, 2004 and 2003.

In May 1990, the Company adopted a 401(k) Plan as an amendment and replacement of the former Associate Stock Purchase Plan that was an additional feature of the Profit Sharing Plan. Under the 401(k) Plan, eligible associates voluntarily

contribute to the plan up to 15% of their salary through payroll deductions. The Company matches 50% of contributions up to a stated limit. Under the provisions of the 401(k) Plan, associates have thirteen investment choices, one of which is the purchase of Iteris, Inc. common stock at market price. Company matching contributions were approximately $409,000, $403,000, and $544,000 for the years ended March 31, 2005, 2004, and 2003, respectively.

11. Discontinued Operations

In September 2003, the Company sold substantially all of the assets of MAXxess to an investor group that included certain members of the MAXxess management group. The consideration for the assets consisted of the assumption of $2.7 million of liabilities, resulting in a net gain of $2.4 million from the sale.

On May 9, 2003, the Company completed the sale of substantially all of the assets of Zyfer for $2.3 million in cash plus the assumption of certain liabilities. The asset purchase agreement provided for future incentive payments of up to $1.0 million in each of the twelve month periods ended April 30, 2004 and 2005, based on the achievement of certain revenue goals related to the sale of Zyfer products or the licensing of its technologies. Based on the terms of the sale agreement, Zyfer has 60 days to provide the Company with support for the incentive payments. In October 2004 the Company received a payment of approximately $135,000 related to the twelve month period ended April 30, 2004. The Company expects to receive information for the twelve month period ended April 30, 2005, by the end of July 2005.

In March 2003, the Company ceased the development and sale of products of Broadcast and reduced the headcount in Broadcast to only support the existing customer contracts for service and support through their expiration dates. The aggregate losses recognized to write down the assets of Broadcast to their fair value less cost to sell were approximately $3.4 million. In addition, the Company accrued $400,000 for employees severed in March 2003 and other direct costs to wind down the operation.

Asset write-downs and accrued costs are included in income (loss) from discontinued operations in the years ended March 31, 2004, and 2003. The results of operations of Broadcast, Zyfer and MAXxess for all periods presented have been reclassified and presented as discontinued operations in the accompanying consolidated statements of operations. Interest expense was not reclassified to discontinued operations because the discontinuances did not eliminate any of the Company's debt.

The net sales and income (loss) from discontinued operations are as follows:

	Year Ended March 31,		
	2005	2004	2003
		(In thousands)	
Net sales and contract revenues:			
MAXxess	$ —	$ 1,747	$ 6,232
Zyfer	—	—	6,487
Broadcast	—	385	3,599
Total net sales and contract revenues	$ —	$ 2,132	$ 16,318
Net income (loss) from discontinued operations:			
MAXxess	$ —	$ 199	$ 862
Zyfer	—	—	(1,718)
Broadcast	—	(122)	(2,468)
	—	77	(3,324)
Loss recognized upon discontinuance of operations	—	(1,226)	(4,909)
Gain on sale of assets of discontinued operations	—	2,364	341
Income (loss) from discontinued operations	$ —	$ 1,215	$ (7,892)

The Company had no assets or liabilities of discontinued operations at March 31, 2005.

12. Disposal of Fixed Assets

After the merger of the Iteris Subsidiary into the Company on October 2004, the Company reviewed and determined certain corporate property and equipment would not provide value to its on-going operations. These assets primarily consisted of furniture and fixtures and computer equipment. Accordingly, the Company recorded a $422,000 loss on disposal of fixed assets in the year ended March 31, 2005.

13. Business Segment and Geographic Information

The Company currently operates in three reportable segments: Roadway Sensors, Automotive Sensors and Systems. The Roadway Sensors segment includes Vantage vehicle detection systems for traffic intersection control and certain highway traffic data collection applications. The Automotive Sensors segment includes AutoVue and is comprised of all activities related to lane departure warning systems for vehicle safety. The Systems segment includes transportation engineering and consulting services and the development of transportation management and traveler information systems for the ITS industry. The accounting policies of the reportable segments are the same as those described in the summary of significant accounting policies except that certain expenses, such as interest, amortization of certain intangibles and certain corporate expenses are not allocated to the segments. In addition, certain assets including cash and cash equivalents, deferred taxes and certain long-lived and intangible assets are not allocated to the segments. The reportable segments are each managed separately because they manufacture and distribute distinct products or provide services with different processes. All segment revenues are derived from external customers.

Selected financial information for the Company's reportable segments as of and for the years ended March 31, 2005, 2004, and 2003 is as follows:

	Roadway Sensors	Automotive Sensors	Systems	Total
		(In thousands)		
Year Ended March 31, 2005				
Product revenue from external customers	$ 21,920	$ 4,326	$ —	$ 26,246
Service and other revenue from external customers	—	2,816	17,335	20,151
Depreciation and amortization	117	116	415	648
Allocated goodwill	8,197	4,671	14,906	27,774
Segment income	3,544	(1,695)	2,313	4,162
Year Ended March 31, 2004				
Product revenue from external customers	$ 19,273	$ 2,308	$ —	$ 21,581
Service and other revenue from external customers	—	1,889	21,813	23,702
Depreciation and amortization	117	116	440	673
Allocated goodwill	200	—	9,607	9,807
Segment income	2,629	(2,343)	2,207	2,493
Year Ended March 31, 2003				
Product revenue from external customers	$ 17,575	$ 1,417	$ —	$ 18,992
Service and other revenue from external customers	—	120	22,283	22,403
Depreciation and amortization	133	120	452	705
Allocated goodwill	200	—	9,607	9,807
Segment income (loss)	3,873	(4,063)	2,302	2,112

The Roadway Sensors segment had two customers with combined revenue representing 38.0% of total segment revenue for the year ended March 31, 2005; four customers with combined revenue representing 59.5% of total segment revenue for the year ended March 31, 2004; and four customers with combined revenue representing 49.0% of total segment revenue for the year ended March 31, 2003. The Automotive Sensors segment had two customers with combined revenue representing 85.2% of total segment revenue for the year ended March 31, 2005; two customers with combined revenue representing 85.3% of total segment revenue for the year ended March 31, 2004; and one customer with revenue representing 60.6% of total segment revenue for the year ended March 31, 2003. The Systems segment had one customer with revenue representing 14.9% of total segment revenue for the year ended March 31, 2005, and one customer with revenue representing 20.0% of total segment revenue for the year ended March 31, 2004.

In connection with the October 2004 merger of the Iteris Subsidiary into the Company (Note 3), goodwill of $8.0 million, $4.7 million and $5.3 million was allocated to the Roadway Sensors, Automotive Sensors and Systems segments, respectively. This allocation was determined based on the respective fair value of each segment as calculated using the income approach.

The following reconciles segment income (loss) to consolidated income (loss) from continuing operations before income taxes and minority interest and segment assets to consolidated assets:

	March 31,		
	2005	2004 (Restated)	2003
		(In thousands)	
Segment income			
Total income for reportable segments	$ 4,162	$ 2,493	$ 2,112
Unallocated amounts:			
Corporate and other expenses	(1,911)	(444)	(2,789)
Deferred compensation	484	(868)	—
Stock-based compensation	(11,777)	—	—
Disposal of fixed assets	(422)	—	—
Acquired in-process research and development	(140)	—	—
Amortization of intangible assets	(114)	—	—
Interest expense, net	(1,178)	(123)	(761)
Income (loss) from continuing operations before income taxes and minority interest	$ (10,896)	$ 1,058	$ (1,438)
Assets			
Total assets for reportable segments	$ 44,833	$ 28,856	$ 26,005
Assets held at Corporate	1,823	1,209	8,837
Total assets	$ 46,656	$ 30,065	$ 34,842

The Company's revenues from continuing operations are generated and the Company's assets are held substantially in the United States.

14. Quarterly Financial Data (Unaudited)

All quarters presented in the following schedule have been restated for the discontinuance of MAXxess, Zyfer, and Broadcast:

	Net Sales	Gross Profit	Income (Loss) from Continuing Operations	Net Income (loss)	Income (Loss) per Share from Continuing Operations
		(In thousands, except per share amounts)			
June 30, 2004	$ 11,441	4,949	$ 966	$ 966	0.04
September 30, 2004	11,760	4,695	(4)	(4)	0.00
December 31, 2004	11,714	5,044	(12,233)	(12,233)	(0.44)
March 31, 2005	11,482	4,666	(57)	(57)	(0.00)
	$ 46,397	$ 19,354	$ (11,328)	$ (11,328)	$ (0.45)*
June 30, 2003	$ 11,530	$ 4,547	$ (1,259)	$ (1,954)	$ (0.08)
September 30, 2003	11,250	4,441	207	2,584	0.01
December 31, 2003	11,128	4,402	(740)	(740)	(0.04)
March 31, 2004 (restated see Note 1)	11,375	4,423	(63)	(530)	0.00
	$ 45,283	$ 17,813	$ (1,855)	$ (640)	$ (0.09)*

* Annual per share amounts may not agree to the sum of the quarterly per share amounts due to differences between average shares outstanding during the periods.

Schedule II

Valuation and Qualifying Accounts (In thousands)

Description	Balance at Beginning of Period	Charged to Costs and Expenses	Charged to Accounts	Balance at End of Period
Year Ended March 31, 2005				
Deducted from asset accounts:				
Allowance for doubtful accounts	$ 204	$ 37	$ (2)	$ 239
Reserve for inventory obsolescence	399	367	(252)	514
Year Ended March 31, 2004				
Deducted from asset accounts:				
Allowance for doubtful accounts	$ 156	$ 87	$ (39)	$ 204
Reserve for inventory obsolescence	248	251	(100)	399
Year Ended March 31, 2003				
Deducted from asset accounts:				
Allowance for doubtful accounts	$ 115	$ 78	$ (37)	$ 156
Reserve for inventory obsolescence	378	—	(130)	248

Exhibit 10.24

ITERIS, INC.
1998 STOCK INCENTIVE PLAN
(as amended February 7, 2000)

ARTICLE ONE

GENERAL PROVISIONS

I. PURPOSE OF THE PLAN

This 1998 Stock Incentive Plan is intended to promote the interests of Iteris, Inc. (formerly known as Odetics ITS, Inc.), a California corporation, by providing eligible persons with the opportunity to acquire a proprietary interest, or otherwise increase their proprietary interest, in the Corporation as an incentive for them to remain in the service of the Corporation.

Capitalized terms shall have the meanings assigned to such terms in the attached Appendix.

II. STRUCTURE OF THE PLAN

A. The Plan shall be divided into three separate equity programs:

- the Discretionary Option Grant Program under which eligible persons may, at the discretion of the Plan Administrator, be granted options to purchase shares of Common Stock,

- the Stock Issuance Program under which eligible persons may, at the discretion of the Plan Administrator, be issued shares of Common Stock directly, either through the immediate purchase of such shares or as a bonus for services rendered the Corporation (or any Parent or Subsidiary), and

- the Automatic Option Grant Program under which eligible non-employee Board members shall automatically receive option grants at periodic intervals to purchase shares of Common Stock.

B. The provisions of Articles One and Five shall apply to all equity programs under the Plan and shall govern the interests of all persons under the Plan.

III. ADMINISTRATION OF THE PLAN

A. Prior to the Section 12 Registration Date, the Discretionary Option Grant and Stock Issuance Programs shall be administered by the Board. Beginning with the Section 12 Registration Date, the Primary Committee shall have sole and exclusive authority to administer the Discretionary Option Grant and Stock Issuance Programs with respect to Section 16 Insiders. Administration of the Discretionary Option Grant and Stock Issuance Programs with respect to all other persons eligible to participate in those programs may, at the Board's discretion, be vested in the Primary Committee or a Secondary Committee, or the Board may retain the power to administer those programs with respect to all such persons.

B. Members of the Primary Committee or any Secondary Committee shall serve for such period of time as the Board may determine and may be removed by the Board at any time. The Board may also at any time terminate the functions of any Secondary Committee and reassume all powers and authority previously delegated to such committee.

C. Each Plan Administrator shall, within the scope of its administrative functions under the Plan, have full power and authority (subject to the provisions of the Plan) to establish such rules and regulations as it may deem appropriate for proper administration of the Discretionary Option Grant and Stock Issuance Programs and to make such determinations under, and issue such interpretations of, the provisions of such programs and any outstanding options or stock issuances thereunder as it may deem necessary or advisable. Decisions of the Plan Administrator within the scope of its administrative functions under the Plan shall be final and binding on all parties who have an interest in the Discretionary Option Grant and Stock Issuance Programs under its jurisdiction or any option or stock issuance thereunder.

D. Service on the Primary Committee or the Secondary Committee shall constitute service as a Board member, and members of each such committee shall accordingly be entitled to full indemnification and reimbursement as Board members for their service on such committee. No member of the Primary Committee or the Secondary Committee shall be liable for any act or omission made in good faith with respect to the Plan or any option grants or stock issuances under the Plan.

E. Administration of the Automatic Option Grant Program shall be self executing in accordance with the terms of that program, and no Plan Administrator shall exercise any discretionary functions with respect to any option grants or stock issuances made under such program.

IV. ELIGIBILITY

A. The persons eligible to participate in the Discretionary Option Grant and Stock Issuance Programs are as follows:

(i) Employees,

(ii) non-employee members of the Board or the board of directors of any Parent or Subsidiary, and

(iii) consultants and other independent advisors who provide services to the Corporation (or any Parent or Subsidiary).

B. Each Plan Administrator shall, within the scope of its administrative jurisdiction under the Plan, have full authority to determine, (i) with respect to the option grants under the Discretionary Option Grant Program, which eligible persons are to receive option grants, the time or times when such option grants are to be made, the number of shares to be covered by each such grant, the status of the granted option as either an Incentive Option or a Nonstatutory Option, the time or times when each option is to become exercisable, the vesting schedule (if any) applicable to the option shares and the maximum term for which the option is to remain outstanding and (ii) with respect to stock issuances under the Stock Issuance Program, which eligible persons are to receive stock issuances, the time or times when such issuances are to be made, the number of shares to be issued to each Participant, the vesting schedule (if any) applicable to the issued shares and the consideration to be paid for such shares.

C. The Plan Administrator shall have the absolute discretion either to grant options in accordance with the Discretionary Option Grant Program or to effect stock issuances in accordance with the Stock Issuance Program.

D. The individuals who shall be eligible to participate in the Automatic Option Grant Program shall be limited to (i) those individuals who first become non-employee Board members on or after the Underwriting Date, whether through appointment by the Board or election by the Corporation's shareholders, and (ii) those individuals who continue to serve as non-employee Board members at one or more Annual Shareholders Meetings held after the Underwriting Date, whether or not they commenced such Board service prior to the Underwriting Date.

V. STOCK SUBJECT TO THE PLAN

A. The stock issuable under the Plan shall be shares of authorized but unissued or reacquired Common Stock, including shares repurchased by the Corporation on the open market. The maximum number of shares of Common Stock reserved for issuance over the term of the Plan shall not exceed 3,000,000(1) shares, subject to certain changes in the Corporation's capital structure.

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(1) Such share reserve is comprised of (i) 1,500,000 shares originally authorized under the Plan (or 2,812,374 shares after giving effect to the 1.874916-for-1 stock split effected in February 2000), and (ii) an additional 187,626 shares approved by the Corporation's shareholders in February 2000.

B. No one person participating in the Plan may receive options, separately exercisable stock appreciation rights and direct stock issuances for more than 250,000 shares of Common Stock in the aggregate per calendar year, beginning with the 1998 calendar year.

C. Shares of Common Stock subject to outstanding options shall be available for subsequent issuance under the Plan to the extent (i) those options expire or terminate for any reason prior to exercise in full or (ii) those options are cancelled in accordance with the option cancellation/regrant provisions of Section IV of Article Two. Unvested shares issued under the Plan and subsequently cancelled or repurchased by the Corporation, at the original exercise or direct issue price paid per share, pursuant to the Corporation's repurchase rights under the Plan shall be added back to the number of shares of Common Stock reserved for issuance under the Plan and shall accordingly be available for reissuance through one or more subsequent option grants or direct stock issuances under the Plan. However, shares subject to any options surrendered in connection with the stock appreciation right provisions of the Plan shall not be available for reissuance. Should the exercise price of an option under the Plan be paid with shares of Common Stock or should shares of Common Stock otherwise issuable under the Plan be withheld by the Corporation in satisfaction of the withholding taxes incurred in connection with the exercise of an option or the vesting of a stock issuance under the Plan, then the number of shares of Common Stock available for issuance under the Plan shall be reduced by the gross number of shares for which the option is exercised or which vest under the stock issuance, and not by the net number of shares of Common Stock issued to the holder of such option or stock issuance.

D. If any change is made to the Common Stock by reason of any stock split, stock dividend, recapitalization, combination of shares, exchange of shares or other change affecting the outstanding Common Stock as a class without the Corporation's receipt of consideration, appropriate adjustments shall be made to (i) the maximum number and/or class of securities issuable under the Plan, (ii) the number and/or class of securities for which any one person may be granted stock options, separately exercisable stock appreciation rights and direct stock issuances under the Plan per calendar year, (iii) the number and/or class of securities for which grants are subsequently to be made under the Automatic Option Grant Program to new and continuing non-employee Board members, and (iv) the number and/or class of securities and the exercise price per share in effect under each outstanding option under the Plan. Such adjustments to the outstanding options are to be effected in a manner which shall preclude the enlargement or dilution of rights and benefits under such options. The adjustments determined by the Plan Administrator shall be final, binding and conclusive.

ARTICLE TWO

DISCRETIONARY OPTION GRANT PROGRAM

I. OPTION TERMS

Each option shall be evidenced by one or more documents in the form approved by the Plan Administrator; provided, however, that each such document shall comply with the terms specified below. Each document evidencing an Incentive Option shall, in addition, be subject to the provisions of the Plan applicable to such options.

A. **Exercise Price**.

1. The exercise price per share shall be fixed by the Plan Administrator in accordance with the following provisions:

(i) The exercise price shall not be less than eighty-five percent (85%) of the Fair Market Value per share of Common Stock on the option grant date.

(ii) If the person to whom the option is granted is a 10% Stockholder, then the exercise price shall not be less than one hundred ten percent (110%) of the Fair Market Value per share of Common Stock on the option grant date.

2. The exercise price shall become immediately due upon exercise of the option and shall, subject to the provisions of Section I of Article Five and the documents evidencing the option, be payable in cash or check made payable to the Corporation. Should the Common Stock be registered under Section 12 of the 1934 Act at the time the option is exercised, then the exercise price may also be paid as follows:

(i) in shares of Common Stock held for the requisite period necessary to avoid a charge to the Corporation's earnings for financial reporting purposes and valued at Fair Market Value on the Exercise Date, or

(ii) to the extent the option is exercised for vested shares, through a special sale and remittance procedure pursuant to which the Optionee shall concurrently provide irrevocable instructions (A) to a Corporation-designated brokerage firm to effect the immediate sale of the purchased shares and remit to the Corporation, out of the sale proceeds available on the settlement date, sufficient funds to cover the aggregate exercise price payable for the purchased shares plus all applicable Federal, state and local income and employment taxes required to be withheld by the Corporation by reason of such exercise and (B) to the Corporation to deliver the certificates for the purchased shares directly to such brokerage firm in order to complete the sale.

Except to the extent such sale and remittance procedure is utilized, payment of the exercise price for the purchased shares must be made on the Exercise Date.

B. **Exercise and Term of Options.** Each option shall be exercisable at such time or times, during such period and for such number of shares as shall be determined by the Plan Administrator and set forth in the documents evidencing the option. However, no option shall have a term in excess of ten (10) years measured from the option grant date.

C. **Effect of Termination of Service**.

1. The following provisions shall govern the exercise of any options held by the Optionee at the time of cessation of Service or death:

(i) Should the Optionee cease to remain in Service for any reason other than death, Disability or Misconduct, then the Optionee shall have a period of three (3) months following the date of such cessation of Service during which to exercise each outstanding option held by such Optionee.

(ii) Should Optionee's Service terminate by reason of Disability, then the Optionee shall have a period of twelve (12) months following the date of such cessation of Service during which to exercise each outstanding option held by such Optionee.

(iii) If the Optionee dies while holding an outstanding option, then the personal representative of his or her estate or the person or persons to whom the option is transferred pursuant to the Optionee's will or the laws of inheritance or the Optionee's designated beneficiary or beneficiaries of that option shall have a twelve (12)-month period following the date of the Optionee's death to exercise such option.

(iv) Under no circumstances, however, shall any such option be exercisable after the specified expiration of the option term.

(v) During the applicable post-Service exercise period, the option may not be exercised in the aggregate for more than the number of vested shares for which the option is exercisable on the date of the Optionee's cessation of Service. Upon the expiration of the applicable exercise period or (if earlier) upon the expiration of the option term, the option shall terminate and cease to be outstanding for any vested shares for which the option has not been exercised. However, the option shall, immediately upon the Optionee's cessation of Service, terminate and cease to be outstanding with respect to any and all option shares for which the option is not otherwise at the time exercisable or in which the Optionee is not otherwise at that time vested.

(vi) Should Optionee's Service be terminated for Misconduct or should Optionee otherwise engage in Misconduct while holding one or more outstanding options under the Plan, then all those options shall terminate immediately and cease to remain outstanding.

2. The Plan Administrator shall have complete discretion, exercisable either at the time an option is granted or at any time while the option remains outstanding, to:

(i) extend the period of time for which the option is to remain exercisable following the Optionee's cessation of Service from the limited exercise period otherwise in effect for that option to such greater period of time as the Plan Administrator shall deem appropriate, but in no event beyond the expiration of the option term, and/or

(ii) permit the option to be exercised, during the applicable post-Service exercise period, not only with respect to the number of vested shares of Common Stock for which such option is exercisable at the time of the Optionee's cessation of Service but also with respect to one or more additional installments in which the Optionee would have vested had the Optionee continued in Service.

D. **Shareholder Rights.** The holder of an option shall have no shareholder rights with respect to the shares subject to the option until such person shall have exercised the option, paid the exercise price and become a holder of record of the purchased shares.

E. **Repurchase Rights.** The Plan Administrator shall have the discretion to grant options which are exercisable for unvested shares of Common Stock. Should the Optionee cease Service while holding such unvested shares, the Corporation shall have the right to repurchase, at the exercise price paid per share, any or all of those unvested shares. The terms upon which such repurchase right shall be exercisable (including the period and procedure for exercise and the appropriate vesting schedule for the purchased shares) shall be established by the Plan Administrator and set forth in the document evidencing such repurchase right. However, with respect to any option grant made prior to the Section 12 Registration Date, the Plan Administrator may not impose a vesting schedule upon that grant or any shares of Common Stock subject to that option which is more restrictive than twenty percent (20%) per year vesting, with the initial vesting to occur not later than one (1) year after the option grant date. Such limitation shall not be applicable to any option grants made to individuals who are officers of the Corporation, non-employee Board members or independent consultants and shall not be in effect for any options granted after the Section 12 Registration Date.

F. **First Refusal Rights**. Until such time as the Common Stock is first registered under Section 12 of the 1934 Act, the Corporation shall have the right of first refusal with respect to any proposed disposition by the Optionee (or any successor in interest) of any shares of Common Stock issued under the Plan. Such right of first refusal shall be exercisable in accordance with the terms established by the Plan Administrator and set forth in the document evidencing such right.

G. **Limited Transferability of Options**. During the lifetime of the Optionee, Incentive Options shall be exercisable only by the Optionee and shall not be assignable or transferable other than by will or by the laws of inheritance following the Optionee's death. However, a Nonstatutory Option may, in connection with the Optionee's estate plan, be assigned in whole or in part during the Optionee's lifetime to one or more members of the Optionee's immediate family or to a trust established exclusively for one or more such family members.

The assigned portion may only be exercised by the person or persons who acquire a proprietary interest in the option pursuant to the assignment. The terms applicable to the assigned portion shall be the same as those in effect for the option immediately prior to such assignment and shall be set forth in such documents issued to the assignee as the Plan Administrator may deem appropriate. Notwithstanding the foregoing, the Optionee may also designate one or more persons as the beneficiary or beneficiaries of his or her outstanding options under the Plan, and those options shall, in accordance with such designation, automatically be transferred to such beneficiary or beneficiaries upon the Optionee's death while holding those options. Such beneficiary or beneficiaries shall take the transferred options subject to all the terms and conditions of the applicable agreement evidencing each such transferred option, including (without limitation) the limited time period during which the option may be exercised following the Optionee's death.

II. INCENTIVE OPTIONS

The terms specified below shall be applicable to all Incentive Options. Except as modified by the provisions of this Section II, all the provisions of Articles One, Two and Five shall be applicable to Incentive Options. Options which are specifically designated as Nonstatutory Options when issued under the Plan shall not be subject to the terms of this Section II.

A. **Eligibility.** Incentive Options may only be granted to Employees.

B. **Exercise Price**. The exercise price per share shall not be less than one hundred percent (100%) of the Fair Market Value per share of Common Stock on the option grant date.

C. **Dollar Limitation.** The aggregate Fair Market Value of the shares of Common Stock (determined as of the respective date or dates of grant) for which one or more options granted to any Employee under the Plan (or any other option plan of the Corporation or any Parent or Subsidiary) may for the first time become exercisable as Incentive Options during any one calendar year shall not exceed the sum of One Hundred Thousand Dollars ($100,000). To the extent the Employee holds two (2) or more such options which become exercisable for the first time in the same calendar year, the foregoing limitation on the exercisability of such options as Incentive Options shall be applied on the basis of the order in which such options are granted.

D. **10% Shareholder.** If any Employee to whom an Incentive Option is granted is a 10% Shareholder, then the exercise price per share shall not be less than one hundred ten percent (110%) of the Fair Market Value per share of Common Stock on the option grant date, and the option term shall not exceed five (5) years measured from the option grant date.

III. CORPORATE TRANSACTION/CHANGE IN CONTROL

A. In the event of any Corporate Transaction, each outstanding option shall automatically vest on an accelerated basis so that each such option shall, immediately prior to the effective date of the Corporate Transaction, become exercisable for all of the shares of Common Stock at the time subject to such option and may be exercised for any or all of those shares as fully vested shares of Common Stock. However, an outstanding option shall not vest on such an accelerated basis if and to the extent: (i) such option is, in connection with the Corporate Transaction, to be assumed by the successor corporation (or parent thereof) or (ii) such option is to be replaced with a cash incentive program of the successor corporation which preserves the spread existing at the time of the Corporate Transaction on any shares for which the option is not otherwise at that time vested and exercisable and provides for subsequent payout in accordance with the same exercise/vesting schedule applicable to those option shares or (iii) the acceleration of such option is subject to other limitations imposed by the Plan Administrator at the time of the option grant.

B. All outstanding repurchase rights under the Discretionary Option Grant Program shall automatically terminate, and the shares of Common Stock subject to those terminated rights shall immediately vest in full, in the event of any Corporate Transaction, except to the extent: (i) those repurchase rights are to be assigned to the successor corporation (or parent thereof) in connection with such Corporate Transaction or (ii) such accelerated vesting is precluded by other limitations imposed by the Plan Administrator at the time the repurchase right is issued.

C. Immediately following the consummation of the Corporate Transaction, all outstanding options shall terminate and cease to be outstanding, except to the extent assumed by the successor corporation (or parent thereof).

D. Each option which is assumed in connection with a Corporate Transaction shall be appropriately adjusted, immediately after such Corporate Transaction, to apply to the number and class of securities which would have been issuable to the Optionee in consummation of such Corporate Transaction had the option been exercised immediately prior to such Corporate Transaction. Appropriate adjustments to reflect such Corporate Transaction shall also be made to (i) the exercise price payable per share under each outstanding option, provided the aggregate exercise price payable for such securities shall remain the same, (ii) the maximum number and/or class of securities available for issuance over the remaining term of the Plan and (iii) the maximum number and/or class of securities for which any one person may be granted stock options, separately exercisable stock appreciation rights and direct stock issuances under the Plan per calendar year. To the extent the actual holders of the Corporation's outstanding Common Stock receive cash consideration for their Common Stock in consummation of the Corporate Transaction, the successor corporation may, in connection with the assumption of the outstanding options under this Plan, substitute one or more shares of its own common stock with a fair market value equivalent to the cash consideration paid per share of Common Stock in such Corporate Transaction.

E. The Plan Administrator shall have the discretionary authority to provide for the automatic acceleration of one or more outstanding options under the Discretionary Option Grant Program upon the occurrence of a Corporate Transaction, whether or not those options are to be assumed in the Corporate Transaction, so that each such option shall, immediately prior to the effect date of such Corporate Transaction, become fully exercisable for all of the shares of Common Stock at the time subject to that option and may be exercised for any or all of those shares as fully vested shares of Common Stock. In addition, the Plan Administrator shall have the discretionary authority to structure one or more of the Corporation's repurchase rights under the Discretionary Option Grant Program so that those rights shall not be assignable in connection with such Corporate Transaction and shall accordingly terminate upon the consummation of such Corporate Transaction, and the shares subject to those terminated rights shall thereupon vest in full.

F. The Plan Administrator shall have full power and authority, exercisable either at the time the option is granted or at any time while the option remains outstanding, to provide for the full and immediate acceleration of one or more outstanding options under the Discretionary Option Grant Program in the event the Optionee's Service is subsequently terminated by reason of an Involuntary Termination within a designated period (not to exceed eighteen (18) months) following the effective date of any Corporate Transaction in which those options are assumed and do not otherwise accelerate. Any options so accelerated shall remain exercisable for fully vested shares until the earlier of (i) the expiration of the option term or (ii) the expiration of the one (1) year period measured from the effective date of the Involuntary Termination. In addition, the Plan Administrator may provide that one or more of the Corporation's outstanding repurchase rights with respect to shares held by the Optionee at the time of such Involuntary Termination shall immediately terminate, and the shares subject to those terminated repurchase rights shall accordingly vest in full.

G. The Plan Administrator shall have the discretionary authority to provide for the full and immediate acceleration of one or more outstanding options under the Discretionary Option Grant Program upon the occurrence of a Change in Control so that each such option shall, immediately prior to the effect date of such Change in Control, become fully exercisable for all of the shares of Common Stock at the time subject to that option and may be exercised for any or all of those shares as fully vested shares of Common Stock. Each such accelerated option shall remain exercisable until the expiration or sooner termination of the option term. In addition, the Plan Administrator shall have the discretionary authority to structure one or more of the Corporation's repurchase rights under the Discretionary Option Grant Program so that those rights shall terminate automatically upon the consummation of such Change in Control, and the shares subject to those terminated rights shall thereupon vest in full. Alternatively, the Plan Administrator may condition the automatic acceleration of one or more outstanding options under the Discretionary Option Grant Program and the termination of one or more of the Corporation's outstanding repurchase rights under such program upon the subsequent termination of the Optionee's Service by reason of an Involuntary Termination within a designated period (not to exceed eighteen (18) months) following the effective date of such Change in Control. Each option so accelerated shall remain exercisable for fully vested shares until the earlier of (i) the expiration of the option term or (ii) the expiration of the one (1) year period measured from the effective date of such Involuntary Termination.

H. The portion of any Incentive Option accelerated in connection with a Corporate Transaction or Change in Control shall remain exercisable as an Incentive Option only to the extent the applicable One Hundred Thousand Dollar ($100,000) limitation is not exceeded. To the extent such dollar limitation is exceeded, the accelerated portion of such option shall be exercisable as a Nonstatutory Option under the Federal tax laws.

I. The outstanding options shall in no way affect the right of the Corporation to adjust, reclassify, reorganize or otherwise change its capital or business structure or to merge, consolidate, dissolve, liquidate or sell or transfer all or any part of its business or assets.

IV. CANCELLATION AND REGRANT OF OPTIONS

The Plan Administrator shall have the authority to effect, at any time and from time to time, with the consent of the affected option holders, the cancellation of any or all outstanding options under the Discretionary Option Grant Program and to grant in substitution new options covering the same or different number of shares of Common Stock but with an exercise price per share equal to the Fair Market Value per share of Common Stock on the new grant date.

V. STOCK APPRECIATION RIGHTS

A. The Plan Administrator shall have the authority to grant to selected Optionees tandem stock appreciation rights and/or limited stock appreciation rights.

B. The following terms shall govern the grant and exercise of tandem stock appreciation rights:

(i) One or more Optionees may be granted the right, exercisable upon such terms as the Plan Administrator may establish, to elect between the exercise of the underlying option for shares Common Stock and the surrender of that option in exchange for a distribution from the Corporation in an amount equal to the excess of (a) the Fair Market Value (on the option surrender date) of the number of shares in which the Optionee is at the time vested under the surrendered option (or surrendered portion) over (b) the aggregate exercise price payable for those shares.

(ii) No such option surrender shall be effective unless it is approved by the Plan Administrator, either at the time of the actual option surrender or at any earlier time. If the surrender is so approved, then the distribution to which the Optionee shall be entitled may be made in shares of Common Stock valued at Fair Market Value on the option surrender date, in cash, or partly in shares and partly in cash, as the Plan Administrator shall in its sole discretion deem appropriate.

(iii) If the surrender of an option is not approved by the Plan Administrator, then the Optionee shall retain whatever rights the Optionee had under the surrendered option (or surrendered portion) on the option surrender date and may exercise such rights at any time prior to the later of (a) five (5) business days after the receipt of the rejection notice or (b) the last day on which the option is otherwise exercisable in accordance with the terms of the documents evidencing such option, but in no event may such rights be exercised more than ten (10) years after the option grant date.

C. The following terms shall govern the grant and exercise of limited stock appreciation rights:

(i) One or more Section 16 Insiders may, at any time following the Section 12 Registration Date, be granted limited stock appreciation rights with respect to their outstanding options.

(ii) Upon the occurrence of a Hostile Takeover, each individual holding one or more options with such a limited stock appreciation right shall have the unconditional right (exercisable for a thirty (30) day period following such Hostile Takeover) to surrender each such option to the Corporation. In return for the surrendered option, the Optionee shall receive a cash distribution from the Corporation in an amount equal to the excess of (A) the Takeover Price of the shares of Common Stock which are at the time subject to each surrendered option (whether or not the option is otherwise vested or exercisable as to those shares) over (B) the aggregate exercise price payable for those shares. Such cash distribution shall be paid within five (5) days following the option surrender date.

(iii) The Plan Administrator shall pre-approve, at the time the limited right is granted, the subsequent exercise of that right in accordance with the terms of the grant and the provisions of this Section V. No additional approval of the Plan Administrator or the Board shall be required at the time of the actual option surrender and cash distribution.

(iv) The balance of the option (if any) shall remain outstanding and exercisable in accordance with the documents evidencing such option.

ARTICLE THREE

STOCK ISSUANCE PROGRAM

I. STOCK ISSUANCE TERMS

Shares of Common Stock may be issued under the Stock Issuance Program through direct and immediate issuances without any intervening option grants. Each such stock issuance shall be evidenced by a Stock Issuance Agreement which complies with the terms specified below.

A. **Purchase Price.**

1. The purchase price per share shall be fixed by the Plan Administrator, but shall not be less than eighty-five percent (85%) of the Fair Market Value per share of Common Stock on the issuance date. However, the purchase price per share of Common Stock issued to a 10% Stockholder shall not be less than one hundred and ten percent (110%) of such Fair Market Value.

2. Subject to the provisions of Section I of Article Five, shares of Common Stock may be issued under the Stock Issuance Program for any combination of the following items of consideration which the Plan Administrator may deem appropriate in each individual instance:

(i) cash or check made payable to the Corporation, or

(ii) past services rendered to the Corporation (or any Parent or Subsidiary).

B. **Vesting Provisions.**

1. Shares of Common Stock issued under the Stock Issuance Program may, in the discretion of the Plan Administrator, be fully and immediately vested upon issuance or may vest in one or more installments over the Participant's period of Service or upon attainment of specified performance objectives. However, with respect to any stock issuance effected under the Stock Issuance Program prior to the Section 12 Registration Date, the Plan Administrator may not impose a vesting schedule which is more restrictive than twenty percent (20%) per year vesting, with initial vesting to occur not later than one (1) year after the issuance date. Such limitation shall not apply to any Common Stock issuances made to the officers of the Corporation, non-employee Board members or independent consultants and shall not be in effect for any stock issuances effected after the Section 12 Registration Date.

2. Any new, substituted or additional securities or other property (including money paid other than as a regular cash dividend) which the Participant may have the right to receive with respect to the Participant's unvested shares of Common Stock by reason of any stock dividend, stock split, recapitalization, combination of shares, exchange of shares or other change affecting the outstanding Common Stock as a class without the Corporation's receipt of consideration shall be issued subject to (i) the same vesting requirements applicable to the Participant's unvested shares of Common Stock and (ii) such escrow arrangements as the Plan Administrator shall deem appropriate.

3. The Participant shall have full shareholder rights with respect to any shares of Common Stock issued to the Participant under the Stock Issuance Program, whether or not the Participant's interest in those shares is vested. Accordingly, the Participant shall have the right to vote such shares and to receive any regular cash dividends paid on such shares.

4. Should the Participant cease to remain in Service while holding one or more unvested shares of Common Stock issued under the Stock Issuance Program or should the performance objectives not be attained with respect to one or more such unvested shares of Common Stock, then those shares shall be immediately surrendered to the Corporation for cancellation, and the Participant shall have no further shareholder rights with respect to those shares. To the extent the surrendered shares were previously issued to the Participant for consideration paid in cash or cash equivalent (including the Participant's purchase money indebtedness), the Corporation shall repay to the Participant the cash consideration paid for the surrendered shares and shall cancel the unpaid principal balance of any outstanding purchase money note of the Participant attributable to the surrendered shares.

5. The Plan Administrator may in its discretion waive the surrender and cancellation of one or more unvested shares of Common Stock which would otherwise occur upon the cessation of the Participant's Service or the non attainment of the performance objectives applicable to those shares. Such waiver shall result in the immediate vesting of the Participant's interest in the shares of Common Stock as to which the waiver applies. Such waiver may be effected at any time, whether before or after the Participant's cessation of Service or the attainment or non attainment of the applicable performance objectives.

C. **First Refusal Rights**. Until such time as the Common Stock is first registered under Section 12 of the 1934 Act, the Corporation shall have the right of first refusal with respect to any proposed disposition by the Participant (or any successor in interest) of any shares of Common Stock issued under the Stock Issuance Program. Such right of first refusal shall be exercisable in accordance with the terms established by the Plan Administrator and set forth in the document evidencing such right.

II. CORPORATE TRANSACTION/CHANGE IN CONTROL

A. All of the Corporation's outstanding repurchase rights under the Stock Issuance Program shall terminate automatically, and all the shares of Common Stock subject to those terminated rights shall immediately vest in full, in the event of any Corporate Transaction, except to the extent (i) those repurchase rights are to be assigned to the successor corporation (or parent thereof) in connection with such Corporate Transaction or (ii) such accelerated vesting is

B. The Plan Administrator shall have the discretionary authority, exercisable either at the time the unvested shares are issued under the Stock Issuance Program or any time while the Corporation's repurchase rights with respect to those shares remain outstanding, to structure one or more of those repurchase rights so that such rights shall not be assignable in connection with a Corporate Transaction and shall accordingly terminate upon the consummation of such Corporate Transaction, and the shares subject to those terminated repurchase rights shall thereupon vest in full.

C. The Plan Administrator shall have the discretionary authority, exercisable either at the time the unvested shares are issued or any time while the Corporation's repurchase rights remain outstanding under the Stock Issuance Program, to provide that those rights shall automatically terminate in whole or in part, and the shares of Common Stock subject to those terminated rights shall immediately vest, in the event the Participant's Service should subsequently terminate by reason of an Involuntary Termination within a designated period (not to exceed eighteen (18) months) following the effective date of any Corporate Transaction in which those repurchase rights are assigned to the successor corporation (or parent thereof).

D. The Plan Administrator shall have the discretionary authority, exercisable either at the time the unvested shares are issued or any time while the Corporation's repurchase rights with respect to those shares remain outstanding under the Stock Issuance Program, to structure one or more of those repurchase rights so that such rights shall automatically terminate in whole or in part, and the shares of Common Stock subject to those terminated rights shall immediately vest, upon (i) a Change in Control or (ii) the subsequent termination of the Participant's Service by reason of an Involuntary Termination within a designated period (not to exceed eighteen (18) months) following the effective date of such Change in Control or Involuntary Termination.

III. SHARE ESCROW/LEGENDS

Unvested shares may, in the Plan Administrator's discretion, be held in escrow by the Corporation until the Participant's interest in such shares vests or may be issued directly to the Participant with restrictive legends on the certificates evidencing those unvested shares.

ARTICLE FOUR

AUTOMATIC OPTION GRANT PROGRAM

I. OPTION TERMS

A. **Grant Dates.** Option grants shall be made on the dates specified below:

1. Each individual who is first elected or appointed as a non-employee Board member at any time on or after the Underwriting Date shall automatically be granted, on the date of such initial election or appointment, a Nonstatutory Option to purchase 20,000(2) shares of Common Stock, provided that individual has not previously been in the employ of the Corporation or any Parent or Subsidiary.

2. On the date of each Annual Shareholders Meeting, beginning with the first Annual Shareholders Meeting held after the Underwriting Date, each individual who is to continue to serve as a non-employee Board member, whether or not that individual is standing for reelection to the Board at that particular Annual Meeting, shall automatically be granted a Nonstatutory Option to purchase 10,000(3) shares of Common Stock, provided such individual has served as a non-employee Board member for at least six (6) months. There shall be no limit on the number of such 10,000(3) share option grants any one non-employee Board member may receive over his or her period of Board service, and non-employee Board members who have previously been in the employ of the Corporation (or any Parent or Subsidiary) or who have previously received stock options in connection with their Board service prior to the Plan Effective Date shall be eligible to receive one or more such annual option grants over their period of continued Board service.

B. **Exercise Price**.

1. The exercise price per share shall be equal to one hundred percent (100%) of the Fair Market Value per share of Common Stock on the option grant date.

2. The exercise price shall be payable in one or more of the alternative forms authorized under the Discretionary Option Grant Program. Except to the extent the sale and remittance procedure specified thereunder is utilized, payment of the exercise price for the purchased shares must be made on the Exercise Date.

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(2) Such shares include (i) 10,000 shares originally authorized under the Plan (or 18,749 shares after giving effect to the 1.874916-for-1 stock split effected in February 2000), and (ii) an additional 1,251 shares increase approved by the shareholders in February 2000.

(3) Such shares include (i) 5,000 shares originally authorized under the Plan (or 9,374 shares after giving effect to the 1.874916-for-1 stock split effected in February 2000), and (ii) an additional 626 shares approved by the shareholders in February 2000.

C. **Option Term.** Each option shall have a term of ten (10) years measured from the option grant date.

D. **Exercise and Vesting of Options.** Each initial 20,000 share option grant shall be immediately exercisable for any or all of the option shares. However, the shares of Common Stock purchased under each initial 20,000 share grant shall be subject to repurchase by the Corporation, at the exercise price paid per share, upon the Optionee's cessation of Board service prior to vesting in those shares. Each initial 20,000 share grant shall vest, and the Corporation's repurchase right shall lapse, in a series of three (3) successive equal annual installments upon the optionee's completion of each year of Board service over the three (3) year period measured from the option grant date. Each annual 10,000 share grant shall be immediately exercisable for any or all of the option shares as fully vested shares of Common Stock and shall remain so exercisable until the expiration or sooner termination of the option term.

E. **Termination of Board Service.** The following provisions shall govern the exercise of any options held by the Optionee at the time the Optionee ceases to serve as a Board member:

(i) The Optionee (or, in the event of Optionee's death, the personal representative of the Optionee's estate or the person or persons to whom the option is transferred pursuant to the Optionee's will or in accordance with the laws of inheritance) shall have a twelve (12) month period following the date of such cessation of Board service in which to exercise each such option.

(ii) During the twelve (12) month exercise period, the option may not be exercised in the aggregate for more than the number of vested shares of Common Stock for which the option is exercisable at the time of the Optionee's cessation of Board service.

(iii) Should the Optionee cease to serve as a Board member by reason of death or Permanent Disability, then all shares at the time subject to the option shall immediately vest so that such option may, during the twelve (12) month exercise period following such cessation of Board service, be exercised for all or any portion of those shares as fully vested shares of Common Stock.

(iv) In no event shall the option remain exercisable after the expiration of the option term. Upon the expiration of the twelve (12) month exercise period or (if earlier) upon the expiration of the option term, the option shall terminate and cease to be outstanding for any vested shares for which the option has not been exercised. However, the option shall, immediately upon the Optionee's cessation of Board service for any reason other than death or Permanent Disability, terminate and cease to be outstanding to the extent the option is not otherwise at that time exercisable for vested shares.

II. CORPORATE TRANSACTION/CHANGE IN CONTROL/HOSTILE TAKEOVER

A. The shares of Common Stock subject to each option outstanding under this Article Four at the time of a Corporate Transaction but not otherwise vested shall automatically vest in full so that each such option shall, immediately prior to the effective date of the Corporate Transaction, become fully exercisable for all of the shares of Common Stock at the time subject to such option and may be exercised for all or any portion of those shares as fully vested shares of Common Stock. Immediately following the consummation of the Corporate Transaction, each automatic option grant shall terminate and cease to be outstanding, except to the extent assumed by the successor corporation (or parent thereof).

B. The shares of Common Stock subject to each option outstanding under this Article Four at the time of a Change in Control but not otherwise vested shall automatically vest in full so that each such option shall, immediately prior to the effective date of the Change in Control, become fully exercisable for all of the shares of Common Stock at the time subject to such option and may be exercised for all or any portion of those shares as fully vested shares of Common Stock. Each such option shall remain exercisable for such fully vested option shares until the expiration or sooner termination of the option term or the surrender of the option in connection with a Hostile Takeover.

C. All outstanding repurchase rights under the Automatic Option Grant Program shall automatically terminate, and the unvested shares of Common Stock subject to those terminated rights shall thereupon vest in full, immediately prior to any Corporate Transaction or Change in Control.

D. Upon the occurrence of a Hostile Takeover at any time after the Section 12 Registration Date, the Optionee shall have a thirty (30) day period in which to surrender to the Corporation each of his or her outstanding automatic option grants. The Optionee shall in return be entitled to a cash distribution from the Corporation in an amount equal to the excess of (i) the Takeover Price of the shares of Common Stock at the time subject to each surrendered option (whether or not the Optionee is otherwise at the time vested in those shares) over (ii) the aggregate exercise price payable for such shares. Such cash distribution shall be paid within five (5) days following the surrender of the option to the Corporation. No approval or consent of the Plan Administrator or the Board shall be required at the time of the actual option surrender and cash distribution.

E. Each option which is assumed in connection with a Corporate Transaction shall be appropriately adjusted, immediately after such Corporate Transaction, to apply to the number and class of securities which would have been issuable to the Optionee in consummation of such Corporate Transaction had the option been exercised immediately prior to such Corporate Transaction. Appropriate adjustments shall also be made to the exercise price payable per share under each outstanding option, provided the aggregate exercise price payable for such securities shall remain the same.

F. The grant of options under the Automatic Option Grant Program shall in no way affect the right of the Corporation to adjust, reclassify, reorganize or otherwise change its capital or business structure or to merge, consolidate, dissolve, liquidate or sell or transfer all or any part of its business or assets.

III. REMAINING TERMS

The remaining terms of each option granted under the Automatic Option Grant Program shall be the same as the terms in effect for option grants made under the Discretionary Option Grant Program.

ARTICLE FIVE

MISCELLANEOUS

I. FINANCING

The Plan Administrator may permit any Optionee or Participant to pay the option exercise price under the Discretionary Option Grant Program or the purchase price of shares issued under the Stock Issuance Program by delivering a full recourse, interest bearing promissory note payable in one or more installments and secured by the purchased shares. However, any promissory note delivered by a consultant must be secured by collateral in addition to the purchased shares of Common Stock. All other terms of any such promissory note (including the interest rate and the terms of repayment) shall be established by the Plan Administrator in its sole discretion. In no event may the maximum credit available to the Optionee or Participant exceed the sum of (i) the aggregate option exercise price or purchase price payable for the purchased shares plus (ii) any Federal, state and local income and employment tax liability incurred by the Optionee or the Participant in connection with the option exercise or share purchase.

II. TAX WITHHOLDING

A. The Corporation's obligation to deliver shares of Common Stock upon the exercise of options or the issuance or vesting of such shares under the Plan shall be subject to the satisfaction of all applicable Federal, state and local income and employment tax withholding requirements.

B. At any time after the Section 12 Registration Date, the Plan Administrator may, in its discretion, provide one or more all holders of Nonstatutory Options or unvested shares of Common Stock under the Plan (other than the options granted or the shares issued under the Automatic Option Grant Program) with the right to use shares of Common Stock in satisfaction of all or part of the Withholding Taxes to which such holders may become subject in connection with the exercise of their options or the vesting of their shares. Such right may be provided to any such holder in either or both of the following formats:

Stock Withholding: The election to have the Corporation withhold, from the shares of Common Stock otherwise issuable upon the exercise of such Nonstatutory Option or the vesting of such shares, a portion of those shares with an aggregate Fair Market Value equal to the percentage of the Withholding Taxes (not to exceed one hundred percent (100%)) designated by the holder.

Stock Delivery: The election to deliver to the Corporation, at the time the Nonstatutory Option is exercised or the shares vest, one or more shares of Common Stock previously acquired by such holder (other than in connection with the option exercise or share vesting triggering the Withholding Taxes) with an aggregate Fair Market Value equal to the percentage of the Withholding Taxes (not to exceed one hundred percent (100%)) designated by the holder.

III. EFFECTIVE DATE AND TERM OF THE PLAN

A. The Plan was adopted by the Board and the shareholders of the Corporation on April 14, 1998l and the Plan became effective on such Plan Effective Date. However, the Automatic Option Grant Program in effect under the Plan shall not become effective until the Underwriting Date, and no option grants shall be made under that program prior to such date. The Plan was amended by the Board and the shareholders in February 2000 (i) to increase the maximum number of shares of Common Stock authorized for issuance under the Plan by an additional 187,626 shares to a total of 3,000,000 shares and (ii) to amend the number of the shares issuable to non-employee members of the Board under the Automatic Option Grant Program.

B. The Plan shall terminate upon the earliest to occur of (i) April 13, 2008, (ii) the date on which all shares available for issuance under the Plan shall have been issued as fully vested shares or (iii) the termination of all outstanding options in connection with a Corporate Transaction. Upon such plan termination, all outstanding option grants and unvested stock issuances shall thereafter continue to have force and effect in accordance with the provisions of the documents evidencing those grants or issuances.

IV. AMENDMENT OF THE PLAN

A. The Board shall have complete and exclusive power and authority to amend or modify the Plan in any or all respects. However, no such amendment or modification shall adversely affect the rights and obligations with respect to stock options or unvested stock issuances at the time outstanding under the Plan unless the Optionee or the Participant consents to such amendment or modification. In addition, certain amendments may require shareholder approval pursuant to applicable laws or regulations.

B. Options to purchase shares of Common Stock may be granted under the Discretionary Option Grant Program and shares of Common Stock may be issued under the Stock Issuance Program that are in each instance in excess of the number of shares then available for issuance under the Plan, provided any excess shares actually issued under those programs shall be held in escrow until there is obtained shareholder approval of an amendment sufficiently increasing the number of shares of Common Stock available for issuance under the Plan. If such shareholder approval is not obtained within twelve (12) months after the date the first such excess issuances are made, then (i) any unexercised options granted on the basis of such excess shares shall terminate and cease to be outstanding and (ii) the Corporation shall promptly refund to the Optionees and the Participants the exercise or purchase price paid for any excess shares issued under the Plan and held in escrow, together with interest (at the applicable Short Term Federal Rate) for the period the shares were held in escrow, and such shares shall thereupon be automatically cancelled and cease to be outstanding.

V. USE OF PROCEEDS

Any cash proceeds received by the Corporation from the sale of shares of Common Stock under the Plan shall be used for general corporate purposes.

VI. REGULATORY APPROVALS

A. The implementation of the Plan, the granting of any stock option under the Plan and the issuance of any shares of Common Stock (i) upon the exercise of any granted option or (ii) under the Stock Issuance Program shall be subject to the Corporation's procurement of all approvals and permits required by regulatory authorities having jurisdiction over the Plan, the stock options granted under it and the shares of Common Stock issued pursuant to it.

B. No shares of Common Stock or other assets shall be issued or delivered under the Plan unless and until there shall have been compliance with all applicable requirements of Federal and state securities laws, including the filing and effectiveness of the Form S-8 registration statement for the shares of Common Stock issuable under the Plan, and all applicable listing requirements of any stock exchange (or the Nasdaq National Market, if applicable) on which Common Stock is then listed for trading.

VII. NO EMPLOYMENT/SERVICE RIGHTS

Nothing in the Plan shall confer upon the Optionee or the Participant any right to continue in Service for any period of specific duration or interfere with or otherwise restrict in any way the rights of the Corporation (or any Parent or Subsidiary employing or retaining such person) or of the Optionee or the Participant, which rights are hereby expressly reserved by each, to terminate such person's Service at any time for any reason, with or without cause.

VIII. FINANCIAL REPORTS

Prior to the Section 12 Registration Date, the Corporation shall deliver a balance sheet and an income statement at least annually to each individual holding an outstanding option under the Plan, unless such individual is a key Employee whose duties in connection with the Corporation (or any Parent or Subsidiary) assure such individual access to equivalent information. The requirement to deliver financial statements under this Section VIII shall terminate on the Section 12 Registration Date.

APPENDIX

The following definitions shall be in effect under the Plan:

A. **Automatic Option Grant Program** shall mean the automatic option grant program in effect under the Plan.

B. **Board** shall mean the Corporation's Board of Directors.

C. **Change in Control** shall mean a change in ownership or control of the Corporation effected through either of the following transactions:

(i) the acquisition, directly or indirectly by any person or related group of persons (other than the Corporation or a person that directly or indirectly controls, is controlled by, or is under common control with, the Corporation), of beneficial ownership (within the meaning of Rule 13d-3 of the 1934 Act) of securities possessing more than fifty percent (50%) of the total combined voting power of the Corporation's outstanding securities pursuant to a tender or exchange offer made directly to the Corporation's shareholders, or

(ii) a change in the composition of the Board over a period of thirty-six (36) consecutive months or less such that a majority of the Board members ceases, by reason of one or more contested elections for Board membership, to be comprised of individuals who either (A) have been Board members continuously since the beginning of such period or (B) have been elected or nominated for election as Board members during such period by at least a majority of the Board members described in clause (A) who were still in office at the time the Board approved such election or nomination.

D. **Common Stock** shall mean the Corporation's common stock.

E. **Code** shall mean the Internal Revenue Code of 1986, as amended.

F. **Corporate Transaction** shall mean either of the following shareholder approved transactions to which the Corporation is a party:

(i) a merger or consolidation in which securities possessing more than fifty percent (50%) of the total combined voting power of the Corporation's outstanding securities are transferred to a person or persons different from the persons holding those securities immediately prior to such transaction, or

(ii) the sale, transfer or other disposition of all or substantially all of the Corporation's assets in complete liquidation or dissolution of the Corporation.

G. **Corporation** shall mean Iteris, Inc. (formerly known as Odetics ITS, Inc.), a California corporation, and any successor corporation to all or substantially all of the assets or voting stock of Iteris, Inc. which shall by appropriate action adopt the Plan.

H. **Discretionary Option Grant Program** shall mean the discretionary option grant program in effect under the Plan.

I. **Employee** shall mean an individual who is in the employ of the Corporation (or any Parent or Subsidiary), subject to the control and direction of the employer entity as to both the work to be performed and the manner and method of performance.

J. **Exercise Date** shall mean the date on which the Corporation shall have received written notice of the option exercise.

K. **Fair Market Value** per share of Common Stock on any relevant date shall be determined in accordance with the following provisions:

(i) If the Common Stock is at the time traded on the Nasdaq National Market, then the Fair Market Value shall be deemed equal to the closing selling price per share of Common Stock on the date in question, as such price is reported on the Nasdaq National Market. If there is no closing selling price for the Common Stock on the date in question, then the Fair Market Value shall be the closing selling price on the last preceding date for which such quotation exists.

(ii) If the Common Stock is at the time listed on any Stock Exchange, then the Fair Market Value shall be deemed equal to the closing selling price per share of Common Stock on the date in question on the Stock Exchange determined by the Plan Administrator to be the primary market for the Common Stock, as such price is officially quoted in the composite tape of transactions on such exchange. If there is no closing selling price for the Common Stock on the date in question, then the Fair Market Value shall be the closing selling price on the last preceding date for which such quotation exists.

(iii) If the Common Stock is at the time neither listed on any Stock Exchange nor traded on the Nasdaq National Market, then the Fair Market Value shall be determined by the Plan Administrator after taking into account such factors as the Plan Administrator shall deem appropriate.

L. **Hostile Takeover** shall mean the acquisition, directly or indirectly, by any person or related group of persons (other than the Corporation or a person that directly or indirectly controls, is controlled by, or is under common control with, the Corporation) of beneficial ownership (within the meaning of Rule 13d-3 of the 1934 Act) of securities possessing more than fifty percent (50%) of the total combined voting power of the Corporation's outstanding securities pursuant to a tender or exchange offer made directly to the Corporation's shareholders which the Board does not recommend such shareholders to accept.

M. **Incentive Option** shall mean an option which satisfies the requirements of Code Section 422.

N. **Involuntary Termination** shall mean the termination of the Service of any individual which occurs by reason of:

(i) such individual's involuntary dismissal or discharge by the Corporation for reasons other than Misconduct, or

(ii) such individual's voluntary resignation following (A) a change in his or her position with the Corporation which materially reduces his or her duties and responsibilities or the level of management to which he or she reports, (B) a reduction in his or her level of compensation (including base salary, fringe benefits and target bonus under any corporate performance based bonus or incentive programs) by more than fifteen percent (15%) or (C) a relocation of such individual's place of employment by more than fifty (50) miles, provided and only if such change, reduction or relocation is effected by the Corporation without the individual's consent.

O. **Misconduct** shall mean the commission of any act of fraud, embezzlement or dishonesty by the Optionee or Participant, any unauthorized use or disclosure by such person of confidential information or trade secrets of the Corporation (or any Parent or Subsidiary), or any other intentional misconduct by such person adversely affecting the business or affairs of the Corporation (or any Parent or Subsidiary) in a material manner. The foregoing definition shall not in any way preclude or restrict the right of the Corporation (or any Parent or Subsidiary) to discharge or dismiss any Optionee or Participant or other person in the Service of the Corporation (or any Parent or Subsidiary) for any other acts or omissions, but such other acts or omissions shall not be deemed, for purposes of the Plan, to constitute grounds for termination for Misconduct.

P. **1934 Act** shall mean the Securities Exchange Act of 1934, as amended.

Q. **Nonstatutory Option** shall mean an option not intended to satisfy the requirements of Code Section 422.

R. **Optionee** shall mean any person to whom an option is granted under the Discretionary Option Grant or Automatic Option Grant Program.

S. **Parent** shall mean any corporation (other than the Corporation) in an unbroken chain of corporations ending with the Corporation, provided each corporation in the unbroken chain (other than the Corporation) owns, at the time of the determination, stock possessing fifty percent (50%) or more of the total combined voting power of all classes of stock in one of the other corporations in such chain.

T. **Participant** shall mean any person who is issued shares of Common Stock under the Stock Issuance Program.

U. **Permanent Disability or Permanently Disabled** shall mean the inability of the Optionee or the Participant to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment expected to result in death or to be of continuous duration of twelve (12) months or more. However, solely for purposes of the

Automatic Option Grant Program, Permanent Disability or Permanently Disabled shall mean the inability of the non-employee Board member to perform his or her usual duties as a Board member by reason of any medically determinable physical or mental impairment expected to result in death or to be of continuous duration of twelve (12) months or more.

V. **Plan** shall mean the Corporation's 1998 Stock Incentive Plan, as set forth in this document.

W. **Plan Administrator** shall mean the particular entity, whether the Primary Committee, the Board or the Secondary Committee, which is authorized to administer the Discretionary Option Grant and Stock Issuance Programs with respect to one or more classes of eligible persons, to the extent such entity is carrying out its administrative functions under those programs with respect to the persons under its jurisdiction.

X. **Plan Effective Date** shall mean April 14, 1998, the date the Plan was adopted by the Board.

Y. **Primary Committee** shall mean the committee of two (2) or more non-employee Board members appointed by the Board to administer the Discretionary Option Grant and Stock Issuance Programs with respect to Section 16 Insiders.

Z. **Secondary Committee** shall mean a committee of two (2) or more Board members appointed by the Board to administer the Discretionary Option Grant and Stock Issuance Programs with respect to eligible persons other than Section 16 Insiders.

AA. **Section 12 Registration Date** shall mean the date on which the Common Stock is first registered under Section 12 of the 1934 Act.

BB. **Section 16 Insider** shall mean an officer or director of the Corporation subject to the short swing profit liabilities of Section 16 of the 1934 Act.

CC. **Service** shall mean the performance of services for the Corporation (or any Parent or Subsidiary) by a person in the capacity of an Employee, a non-employee member of the board of directors or a consultant or independent advisor, except to the extent otherwise specifically provided in the documents evidencing the option grant or stock issuance.

DD. **Stock Exchange** shall mean either the American Stock Exchange or the New York Stock Exchange.

EE. **Stock Issuance Agreement** shall mean the agreement entered into by the Corporation and the Participant at the time of issuance of shares of Common Stock under the Stock Issuance Program.

FF. **Stock Issuance Program** shall mean the stock issuance program in effect under the Plan.

GG. **Subsidiary** shall mean any corporation (other than the Corporation) in an unbroken chain of corporations beginning with the Corporation, provided each corporation (other than the last corporation) in the unbroken chain owns, at the time of the determination, stock possessing fifty percent (50%) or more of the total combined voting power of all classes of stock in one of the other corporations in such chain.

HH. **Takeover Price** shall mean the greater of (i) the Fair Market Value per share of Common Stock on the date the option is surrendered to the Corporation in connection with a Hostile Takeover or (ii) the highest reported price per share of Common Stock paid by the tender offeror in effecting such Hostile Takeover. However, if the surrendered option is an Incentive Option, the Takeover Price shall not exceed the clause (i) price per share.

II. **10% Shareholder** shall mean the owner of stock (as determined under Code Section 424(d)) possessing more than ten percent (10%) of the total combined voting power of all classes of stock of the Corporation (or any Parent or Subsidiary).

JJ. **Underwriting Agreement** shall mean the agreement between the Corporation and the underwriter or underwriters managing the initial public offering of the Common Stock.

KK. **Underwriting Date** shall mean the date on which the Underwriting Agreement is executed and priced in connection with an initial public offering of the Common Stock.

LL. **Withholding Taxes** shall mean the Federal, state and local income and employment withholding taxes to which the holder of Nonstatutory Options or unvested shares of Common Stock may become subject in connection with the exercise of those options or the vesting of those shares.

Exhibit 10.25

CREDIT AGREEMENT

THIS AGREEMENT is entered into as of May 27, 2004, by and between ITERIS, INC., a Delaware corporation ("Borrower'), and WELLS FARGO BANK, NATIONAL ASSOCIATION ("Bank").

RECITALS

Borrower has requested that Bank extend or continue credit to Borrower as described below, and Bank has agreed to provide such credit to Borrower on the terms and conditions contained herein.

NOW, THEREFORE, for valuable consideration, the receipt and sufficiency of which are hereby acknowledged, Bank and Borrower hereby agree as follows;

ARTICLE I
CREDIT TERMS

SECTION 1.1 LINE OF CREDIT.

(a) Line of Credit. Subject to the terms and conditions of this Agreement, Bank hereby agrees to make advances to Borrower from time to time up to and including August 1, 2005, not to exceed at any time the aggregate principal amount of Five Million and 00/100 Dollars ($5,000,000.00) ("Line of Credit"), the proceeds of which shall be used for working capital requirements. Borrowers obligation to repay advances under the Line of Credit shall be evidenced by a promissory note dated as of May 27, 2004 ("Line of Credit Note"), all terms of which are incorporated herein by this reference.

(b) Limitation on Borrowings. Outstanding borrowings under the Line of Credit, to a maximum of the principal amount set forth above, shall not at any time exceed an aggregate of (i) eighty percent 80% of Borrower's eligible accounts receivable (Non-Gov't/Non-Consulting) (ii) Forty percent (40%) of Borrower's eligible accounts receivable (Gov't/Consulting) provided that outstanding borrowings against such accounts receivable shall not exceed Seven Hundred Fifty Thousand and 00/100 Dollars ($750,000.00), and (iii) fifty percent (50%) of the value of Borrowers eligible inventory, (exclusive of work in process and inventory which is obsolete, unsaleable or damaged), with value defined as the lower of cost or market value, provided however, that outstanding borrowing against inventory shall not at any time exceed an aggregate of One Million and 00/100 Dollars ($1,000,000). All of the foregoing shall be determined by Bank upon receipt and review of all collateral reports required hereunder and such other documents and collateral information as Bank may from time to time require. Borrower acknowledges that said borrowing base was established by Bank with the understanding that, among other items, the aggregate of all returns, rebates, discounts, credits and allowances for the immediately preceding three (3) months at all times shall be less than five percent (5%) of Borrower's gross sales for said period. If such dilution of Borrower's accounts for the immediately preceding three (3) months at any time exceeds five percent (5%) of Borrower's gross sales for said period, or if there at any time exists any other matters, events, conditions or contingencies which Bank reasonably believes may affect payment of any portion of Borrower's accounts, Bank, in its sole discretion, may reduce the foregoing advance rate against eligible accounts receivable to a percentage appropriate to reflect such additional dilution and/or establish additional reserves against Borrowers eligible accounts receivable.

As used herein, "eligible accounts receivable" shall consist solely of trade accounts created in the ordinary course of Borrower's business, upon which Borrower's right to receive payment is absolute and not contingent upon the fulfillment of any condition whatsoever, and in which Bank has a perfected security interest of first priority, and shall not include:

(i) any Non-Gov't/Non-Consulting account which is past due more than ninety (90) days, except with respect to any account for which Borrower has provided extended payment terms not to exceed one hundred eighty (180) days, any such account is more than thirty (30) days past due;

(ii) any Gov't/Consulting account which is past due more than sixty (60) days;

(iii) that portion of any account for which there exists any right of setoff, defense or discount (except regular discounts allowed in the ordinary course of business to promote prompt payment) or for which any defense or counterclaim has been asserted;

(iv) any account which represents an obligation of an account debtor located in a foreign country except (A) to the extent any such account, in Bank's determination, is supported by a letter of credit or insured under a policy of foreign credit insurance, in each case in form, substance and issued by a party acceptable to Bank and (B) accounts of Daimler Chrysler and Valeo to the extent that the accounts of Daimler Chrysler and Valeo, in the aggregate, do not exceed 10% of the total eligible accounts receivable and such accounts otherwise qualify as eligible accounts receivable;

(v) any account which arises from the sale or lease to or performance of services for, or represents an obligation of, an employee, affiliate, partner, member, parent or subsidiary of Borrower;

(vi) that portion of any account, which represents interim or progress billings or retention rights on the part of the account debtor;

(vii) any account which represents an obligation of any account debtor when twenty percent (20%) or more of Borrowers accounts from such account debtor are not eligible pursuant to (i) and (ii) above;

(viii) that portion of any account from an account debtor which represents the amount by which Borrower's total accounts from said account debtor exceeds twenty-five percent (25%) of Borrower's total accounts;

(ix) any account deemed ineligible by Bank when Bank, in its reasonable discretion from the standpoint of a secured creditor, deems the creditworthiness or financial condition of the account debtor, or the industry in which the account debtor is engaged, to be unsatisfactory.

(c) Borrowing and Repayment. Borrower may from time to time during the term of the Line of Credit borrow, partially or wholly repay its outstanding borrowings, and reborrow, subject to all of the limitations, terms and conditions contained herein or in the Line of Credit Note; provided however, that the total outstanding borrowings under the Line of Credit shall not at any time exceed the maximum principal amount available thereunder, as set forth above.

SECTION 1.2 TERM LOAN.

(a) Term Loan. Subject to the terms and conditions of this Agreement, Bank hereby agrees to make a loan to Borrower in the principal amount of Five Million and 00/100 Dollars ($5,000,000.00) ("Term Loan"), the proceeds of which shall be used to repurchase preferred stock of Borrower, directly or indirectly, by distribution of proceeds to Iteris Holdings, Inc. ("Guarantor") and causing Guarantor to purchase such shares. Borrowers obligation to repay the Term Loan shall be evidenced by a promissory note dated as of May 27, 2004 ("Term Note"), all terms of which are incorporated herein by this reference. Bank's Commitment to grant the Term Loan shall terminate on June 27, 2004.

(b) Repayment. The principal amount of the Term Loan shall be repaid in accordance with the provisions of the Term Note.

(c) Prepayment. Borrower may prepay principal on the Term Loan solely in accordance with the provisions of the Term Note.

SECTION 1.3 INTEREST/FEES.

(a) Interest. The outstanding principal balance of each credit subject hereto shall beer interest at the rate of interest set forth in each promissory note or other instrument or document executed in connection therewith.

(b) Computation and Payment. Interest shall be computed on the basis of a 360-day year, actual days elapsed. Interest shall be payable at the times and place set forth in each promissory note or other instrument or document required hereby.

(c) Commitment Fee. Borrower shall pay to Bank a non-refundable commitment fee for the Term Loan equal to Six Thousand Two Hundred Fifty Dollars ($6,250.00), which fee shall be due and payable in full upon execution of this Agreement.

(d) Unused Commitment Fee. Borrower shall pay to Bank a fee equal to one quarter percent (0.25%) per annum (computed on the basis of a 360-day year, actual days elapsed) on the average daily unused amount of the Line of Credit, which fee shall be calculated on a quarterly basis by Bank and shall be due and payable by Borrower in arrears on the last day of each quarter.

SECTION 1.4 COLLATERAL.

As security for all indebtedness of Borrower to Bank subject hereto, Borrower hereby grants to Bank security interests of first priority in all Borrower's accounts receivables and other rights to payment, general intangibles, inventory and equipment.

All of the foregoing shall be evidenced by and subject to the terms of such security agreements, financing statements, deeds of trust and other documents as Bank shall reasonably require, all in form and substance satisfactory to Bank. Borrower shall reimburse Bank immediately upon demand for all costs and expenses incurred by Bank in connection with any of the foregoing security, including without limitation, filing and recording fees and costs of appraisals, audits and title insurance.

SECTION 1.5 GUARANTIES. All indebtedness of Borrower to Bank shall be guaranteed jointly and severally by Guarantor in the principal amount of Ten Million Dollars ($10,000,000.00), as evidenced by and subject to the terms of guaranties in form and substance satisfactory to Bank.

ARTICLE II
REPRESENTATIONS AND WARRANTIES

Borrower makes the following representations and warranties to Bank, which representations and warranties shall survive the execution of this Agreement and shall continue in full force and effect until the full and final payment, and satisfaction and discharge, of all obligations of Borrower to Bank subject to this Agreement.

SECTION 2.1 LEGAL STATUS. Borrower is a **corporation**, duly organized and existing and in good standing under the laws of the State of **Delaware**, and is qualified or licensed to do business (and is in good standing as a foreign corporation, if applicable) in all jurisdictions in which such qualification or licensing is required or in which the failure to so qualify or to be so licensed could have a material adverse effect on Borrower.

SECTION 2.2 AUTHORIZATION AND VALIDITY. This Agreement and each promissory note, contract, instrument and other document required hereby or at any time hereafter delivered to Bank in connection herewith (collectively, the "Loan Documents") have been duly authorized, and upon their execution and delivery in accordance with the provisions hereof will constitute legal, valid and binding agreements and obligations of Borrower or the party which executes the same, enforceable in accordance with their respective terms, except as enforceability may be limited by applicable bankruptcy, insolvency or similar laws affecting creditors' rights generally.

SECTION 2.3 NO VIOLATION. The execution, delivery and performance by Borrower of each of the Loan Documents do not violate any provision of any law or regulation, or contravene any provision of the Articles of Incorporation or By-Laws of Borrower, or result in any breach of or default under any contract, obligation, indenture or other instrument to which Borrower is a party or by which Borrower may be bound.

SECTION 2.4 LITIGATION. There are no pending, or to the best of Borrower's knowledge threatened, actions, claims, investigations, suits or proceedings by or before any governmental authority, arbitrator, court or administrative agency which could have a material adverse effect on the financial condition or operation of Borrower other then those disclosed by Borrower to Bank in writing prior to the date hereof.

SECTION 2.5 CORRECTNESS OF FINANCIAL STATEMENT. The financial statement of Borrower dated March 31, 2004, a true copy of which has been delivered by Borrower to Bank prior to the date hereof, (a) is complete and correct in all material respects and presents fairly the financial condition of Borrower, (b) discloses all liabilities of Borrower that are required to be reflected or reserved against under generally accepted accounting principles, whether liquidated or unliquidated, fixed or contingent, and (c) has been prepared in accordance with generally accepted accounting principles consistently applied subject to normal year-end adjustments made by outside auditors. Since the date of such financial statement there has been no material adverse change In the financial condition of Borrower, nor has Borrower mortgaged, pledged, granted a security interest in or otherwise encumbered any of its assets or properties except in favor of Bank or as otherwise permitted by Bank in writing.

SECTION 2.6 INCOME TAX RETURNS. Borrower has no knowledge of any pending assessments or adjustments of its income tax payable with respect to any year.

SECTION 2.7 NO SUBORDINATION. There is no agreement, indenture, contract or instrument to which Borrower is a party or by which Borrower may be bound that requires the subordination in right of payment of any of Borrower's obligations subject to this Agreement to any other obligation of Borrower.

SECTION 2.8 PERMITS, FRANCHISES. Borrower possesses, and will hereafter possess, all permits, consents, approvals, franchises and licenses required and rights to all trademarks, trade names, patents, and fictitious names, if any, necessary to enable it to conduct the business in which it is now engaged in compliance with applicable law.

SECTION 2.9 ERISA. Borrower is in compliance in all material respects with all applicable provisions of the Employee Retirement Income Security Act of 1974, as amended or recodified from time to time ("ERISA"); Borrower has not violated any provision of any defined employee pension benefit plan (as defined in ERISA) maintained or contributed to by Borrower (each, a "Plan"); no Reportable Event as defined in ERISA has occurred and is continuing with respect to any Plan initiated by Borrower; Borrower has met its minimum funding requirements under ERISA with respect to each Plan; and each Plan will be able to fulfill its benefit obligations as they come due in accordance with the Plan documents and under generally accepted accounting principles.

SECTION 2.10 OTHER OBLIGATIONS. Borrower is not in default on any obligation for borrowed money, any purchase money obligation or any other material lease, commitment, contract, instrument or obligation other than late payments to trade creditors in the ordinary course of business and consistent with past practices, provided that the average payment time for any individual trade creditor shall not be more than 30 days longer than the average payment terms for such trade creditor.

SECTION 2.11 ENVIRONMENTAL MATTERS. Except as disclosed by Borrower to Bank in writing prior to the date hereof, Borrower is in compliance in all material respects with all applicable federal or state environmental, hazardous waste, health and safety statutes, and any rules or regulations adopted

pursuant thereto, which govern or effect any of Borrower's operations and/or properties, including without limitation, the Comprehensive Environmental Response, Compensation and Liability Act of 1980, the Superfund Amendments and Reauthorization Act of 1986, the Federal Resource Conservation and Recovery Act of 1976, and the Federal Toxic Substances Control Act, as any of the same may to amended, modified or supplemented from time to time. None of the operations of Borrower is the subject of any federal or state investigation evaluating whether any remedial action involving a material expenditure is needed to respond to a release of any toxic or hazardous waste or substance into the environment. Borrower has no material contingent liability in connection with any release of any toxic or hazardous waste or substance into the environment.

ARTICLE III
CONDITIONS

SECTION 3.1 CONDITIONS OF INITIAL EXTENSION OF CREDIT. The obligation of Bank to extend any credit contemplated by this Agreement is subject to the fulfillment to Bank's satisfaction of all of the following conditions:

(a) Approval of Bank Counsel. All legal matters incidental to the extension of credit by Bank shall be satisfactory to Bank's counsel.

(b) Documentation. Bank shall have received, in form and substance satisfactory to Bank, each of the following, duly executed:

(i) This Agreement and each promissory note or other instrument or document required hereby.
(ii) Certificate of Incumbency of Borrower.
(iii) Certificate of Incumbency of Guarantor.
(iv) Corporate Resolution: Borrowing.
(v) Corporate Resolution: Continuing Guaranty.
(vi) Continuing Guaranty.
(vii) Disbursement Order for revolving loan.
(viii) Disbursement Order for term loan.
(ix) Security Agreement: Continuing-Rights to Payment and Inventory.
(x) Insurance Information Request.
(xi) Such other documents as Bank may require under any other Section of this Agreement.

(c) Financial Condition. There shall have been no material adverse change, as determined by Bank, in the financial condition or business of Borrower or any guarantor hereunder, nor any material decline, as determined by Bank, in the market value of any collateral required hereunder or a substantial or material portion of the assets of Borrower or any such guarantor.

(d) Insurance. Borrower shall have delivered to Bank evidence of insurance coverage on all Borrower's property, in form, substance, amounts, covering risks and issued by companies satisfactory to Bank, and where required by Bank, with loss payable endorsements in favor of Bank.

SECTION 3.2 CONDITIONS OF EACH EXTENSION OF CREDIT. The obligation of Bank to make each extension of credit requested by Borrower hereunder shall be subject to the fulfillment to Bank's satisfaction of each of the following conditions:

(a) Compliance. The representations and warranties contained herein and in each of the other Loan Documents shall be true on and as of the date of the signing of this Agreement and on the date of each extension of credit by Bank pursuant hereto, with the same effect as though such representations and warranties had been made on and as of each such date, and on each such date, no Event of Default as defined herein, and no condition, event or act which with the giving of notice or the passage of time or both would constitute such an Event of Default, shall have occurred and be continuing or shall exist.

(b) Documentation. Bank shall have received all additional documents which may be required in connection with such extension of credit.

ARTICLE IV
AFFIRMATIVE COVENANTS

Borrower covenants that so long as Bank remains committed to extend credit to Borrower pursuant hereto, or any liabilities (whether direct or contingent, liquidated or unliquidated) of Borrower to Bank under any of the Loan Documents remain outstanding, and until payment in full of all obligations of Borrower subject hereto, Borrower shall, unless Bank otherwise consents in writing:

SECTION 4.1 PUNCTUAL PAYMENTS. Punctually pay all principal, interest, fees or other liabilities due under any of the Loan Documents at the times and place and in the manner specified therein, and immediately upon demand by Bank, the amount by which the outstanding principal balance of any credit subject hereto at any time exceeds any limitation on borrowings applicable thereto.

SECTION 4.2 ACCOUNTING RECORDS. Maintain adequate books and records in accordance with generally accepted accounting principles consistently applied, and permit any representative of Bank, at any reasonable time, to inspect, audit and examine such books and records, to make copies of the same, and to inspect the properties of Borrower.

SECTION 4.3 FINANCIAL STATEMENTS. Provide to Bank all of the following, in form and detail satisfactory to Bank:

(a) not later than 120 days after and as of the end of each fiscal year, a Borrower prepared financial statement of Borrower, prepared by Borrower, to include a balance sheet, statement of income and statement of cash flows;

(b) not later than 45 days after and as of the end of each fiscal quarter, a consolidating financial statement of Borrower, prepared by Borrower, to include a balance sheet, statement of income and statement of cash flows;

(c) not later than 120 days after and as of the end of each fiscal year, an audited financial statement of each guarantor hereunder, prepared by a certified public accountant acceptable to Bank, to include a balance sheet, statement of income, statement of cash flows and to include a consolidating schedule;

(d) not later than 45 days after and as of the end of each fiscal quarter, a consolidating financial statement of Guarantor, prepared by such Guarantor, to include a balance sheet, statement of income and statement of cash flows;

(e) not later than 15 days after and as of the end of each month, a borrowing base certificate, an inventory collateral report, an aged listing of accounts receivable and accounts payable and a reconciliation of accounts, and not later than each June 30 and December 31, a list of the names and addresses of all Borrower's account debtors.

(f) from time to time such other information as Bank may reasonably request.

SECTION 4.4 COMPLIANCE. Preserve and maintain all licenses, permits, governmental approvals, rights, privileges and franchises necessary for the conduct of its business; and comply with the provisions of all documents pursuant to which Borrower is organized and/or which govern Borrower's continued existence and with the requirements of all laws, rules, regulations and orders of any governmental authority applicable to Borrower and/or its business.

SECTION 4.5 INSURANCE. Maintain and keep in force insurance of the types and in amounts customarily carried in lines of business similar to that of Borrower, including but not limited to fire, extended coverage, public liability, flood, property damage and workers' compensation, with all such insurance carried with companies and in amounts satisfactory to Bank, and deliver to Bank from time to time at Bank's request schedules setting forth all insurance then in effect.

SECTION 4.6 FACILITIES. Keep all properties necessary to Borrower's business in good repair and condition, and from time to time make necessary repairs, renewals and replacements thereto so that such properties shall be fully and efficiently preserved and maintained.

SECTION 4.7 TAXES AND OTHER LIABILITIES. Pay and discharge when due any and all indebtedness (except indebtedness to trade creditors in the ordinary course of business and consistent with past practices, provided that the average payment time for any individual trade creditor shall not be more than 30 days longer than the average payment terms for such trade creditor), obligations, assessments and taxes, both real or personal, including without limitation federal and state income taxes and state and local property taxes and assessments, except such (a) as Borrower may in good faith contest or as to which a bona fide dispute may arise, and (b) for which Borrower has made provision, to Bank's satisfaction, for eventual payment thereof in the event Borrower is obligated to make such payment.

SECTION 4.8 LITIGATION. Promptly give notice in writing to Bank of any litigation pending or threatened against Borrower.

SECTION 4.9 FINANCIAL CONDITION. Maintain Borrower's financial condition, as follows using generally accepted accounting principles consistently applied and used consistently with prior practices (except to the extent modified by the definitions herein), with compliance determined commencing with Borrower's financial statements for the period ending December 31, 2003:

(a) Net income after taxes not less than $1.00 on a year-to-date basis, determined as of each fiscal quarter end.

(b) Senior Funded Debt to EBITDA not more than 4.00 to 1.0 as of June 30, 2004, not more than 3.50 to 1.0 as of September 30, 2004, not more than 3.00 to 1.0 as of December 31, 2004, and not more than 2.75 to 1.0 quarterly thereafter, with "Senior Funded Debt" defined as the sum of all obligations for borrowed money plus all capital lease obligations less subordinated debt, and with "EBITDA" defined as net profit before tax plus interest expense (net of capital interest expense), depreciation expense and amortization expense.

(c) Fixed Charge Coverage Ratio not at any time less than 1.00 to 1.0, through September 30, 2004, not less than 1.15 to 1.0 as of December 31, 2004 and not less than 1.35 to 1.0 quarterly thereafter, determined on a rolling 4-quarter basis, "Fixed Charge Coverage Ratio" shall mean consolidated EBITDA minus non-financed capital expenditures divided by the aggregate sum of (i) all interest paid or payable on the Funded Debt (ii) all installments of scheduled principal during the period (iii) all income taxes paid or payable plus (iv) the amount of dividends declared or paid in cash. "Funded Debt" shall mean the sum of all obligations for borrowed money plus all capital lease obligations.

SECTION 4.10 NOTICE TO BANK. Promptly (but in no event more than five (5) days after the occurrence of each such event or matter) give written notice to Bank in reasonable detail of: (a) the occurrence of any Event of Default, or any condition, event or act which with the giving of notice or the passage of time or both would constitute an Event of Default; (b) any change in the name or the organizational structure of Borrower; (c) the occurrence and nature of any Reportable Event or Prohibited Transaction, each as defined in ERISA, or any funding deficiency with respect to any Plan; or (d) any termination or cancellation of any insurance policy which Borrower is required to maintain, or any uninsured or partially uninsured loss through liability or property damage, or through fire, theft or any other cause affecting Borrower's property.

ARTICLE V
NEGATIVE COVENANTS

Borrower further covenants that so long as Bank remains committed to extend credit to Borrower pursuant hereto, or any liabilities (whether direct or contingent, liquidated or unliquidated) of Borrower to Bank under any of the Loan Documents remain outstanding, and until payment in full of all obligations of Borrower subject hereto, Borrower will not without Bank's prior written consent:

SECTION 5.1 USE OF FUNDS. Use any of the proceeds of any credit extended hereunder except for the purposes stated in Article I hereof.

SECTION 5.2 CAPITAL EXPENDITURES. Make any additional investment in fixed assets in any fiscal year in excess of an aggregate of $750,000.00.

SECTION 5.3 OTHER INDEBTEDNESS. Create, incur, assume or permit to exist any indebtedness or liabilities resulting from borrowings, loans or advances, whether secured or unsecured, matured or unmatured, liquidated or unliquidated, joint or several, except (a) the liabilities of Borrower to Bank, (b) any other liabilities of Borrower existing as of, and disclosed to Bank prior to, the date hereof, (c) indebtedness incurred in connection with lease obligations, not to exceed $100,000 in the aggregate in any fiscal year, and any extensions or renewals thereof, (d) renewals or extensions of operating leases existing on the date hereof, provided that the outstanding principal amount does not increase, and (e) liabilities to trade creditors incurred in the ordinary course of the Borrower's business and consistent with past practices.

SECTION 5.4 MERGER, CONSOLIDATION, TRANSFER OF ASSETS. Merge into or consolidate with any other entity; make any substantial change in the nature of Borrower's business as conducted as of the date hereof; acquire all or substantially all of the assets of any other entity; nor sell, lease, transfer or otherwise dispose of all or a substantial or material portion of Borrower's assets except in the ordinary course of its business.

SECTION 5.5 GUARANTIES. Guarantee or become liable in any way as surety, endorser (other than as endorser of negotiable instruments for deposit or collection in the ordinary course of business), accommodation endorser or otherwise for, nor pledge or hypothecate any assets of Borrower as security for, any liabilities or obligations of any other person or entity, except any of the foregoing in favor of Bank.

SECTION 5.6 LOANS, ADVANCES, INVESTMENTS. Make any loans or advances to or investments (other than investments in cash equivalents) in any person or entity, except (i) any of the foregoing existing as of, and disclosed to Bank prior to, the date hereof and (ii) in an aggregate amount outstanding at any time not to exceed $50,000.

SECTION 5.7 DIVIDENDS, DISTRIBUTIONS. Declare or pay any dividend or distribution either in cash, stock or any other property on Borrower's stock now or hereafter outstanding, nor redeem, retire, repurchase or otherwise acquire any shares of any class of Borrowers stock now or hereafter outstanding, except (a) annual divided distributions and inter-company transactions limited to $1,000,000.00 to Guarantor (b) the distributions to Guarantor and repurchases of preferred stock of Borrower from Guarantor referenced in Section 1.2(a) hereof and (c) repurchases of stock pursuant to the terms of incentive equity compensation arrangements with employees, directors or consultants of Borrower in an aggregate amount not to exceed $75,000 in any fiscal year.

SECTION 5.8 PLEDGE OF ASSETS. Mortgage, pledge, grant or permit to exist a security interest in, or lien upon, all or any portion of Borrower's assets now owned or hereafter acquired, except any of the foregoing in favor of Bank or which is existing as of, and disclosed to Bank in writing prior to, the date hereof and security interests under any lease agreement permitted under Section 5.3, provided that the security interest is limited to the leased equipment.

ARTICLE VI
EVENTS OF DEFAULT

SECTION 6.1 The occurrence of any of the following shall constitute an "Event of Default" under this Agreement:

(a) Borrower shall fail to pay when due any principal, interest, fees or other amounts payable under any of the Loan Documents.

(b) Any financial statement or certificate furnished to Bank in connection with, or any representation or warranty made by Borrower or any other party under this Agreement or any other Loan Document shall prove to be incorrect, false or misleading in any material respect when furnished or made.

(c) Any default in the performance of or compliance with any obligation, agreement or other provision contained herein or in any other Loan Document (other than those referred to in subsections (a) and (b) above), and with respect to any such default which by its nature can be cured, such default shall continue for a period of thirty (30) days from its occurrence.

(d) Any default in the payment or performance of any obligation or obligations, or any defined event of default, under the terms of any contract, contracts, instrument, or instruments (other than any of the Loan Documents) pursuant to which Borrower, any guarantor hereunder, or any general partner or joint venturer in any Borrower which is a partnership or a joint venture (with each such guarantor, general partner and/or joint venturer referred to herein as a "Third Party Obligor) has incurred any debt or other liability to any person, persons, entity or entities, excluding Bank, in excess of $50,000 in the aggregate.

(e) The filing of a notice of judgment lien against Borrower or any Third Party Obligor, or the recording of any abstract of judgment against Borrower or any Third Party Obligor in any county in which Borrower or any Third Party Obligor has an interest in real property; or the service of a notice of levy and/or of a writ of attachment or execution, or other like process, against the assets of Borrower or any Third Party Obligor; or the entry of a judgment against Borrower or any Third Party Obligor, provided, that (1) a judgment or judgments not in excess of $50,000 in the aggregate shall not constitute an Event of Default, and (2) a judgment or judgments not in excess of $500,000 in the aggregate each of which is (i) stayed pending appeal and (ii) bonded (or insured against) in a manner satisfactory to Bank shall not constitute an Event of Default.

(f) Borrower or any Third Party Obligor shall become insolvent, or shall suffer or consent to or apply for the appointment of a receiver, trustee, custodian or liquidator of itself or any of its property, or shall generally fail to pay its debts as they become due, or shall make a general assignment for the benefit of creditors; Borrower or any Third Party Obligor shall file a voluntary petition in bankruptcy, or seeking reorganization, in order to effect a plan or other arrangement with creditors or any other relief under the Bankruptcy Reform Act, Title 11 of the United States Code, as amended or recodified from time to time ("Bankruptcy Code"), or under any state or federal law granting relief to debtors, whether now or hereafter in effect; or any involuntary petition or proceeding pursuant to the Bankruptcy Code or any other applicable state or federal law relating to bankruptcy, reorganization or other relief for debtors is filed or commenced against Borrower or any Third Party Obligor which is not dismissed within sixty (60) days; or Borrower or any Third Party Obligor shall file an answer admitting the jurisdiction of the court and the material allegations of any involuntary petition; or Borrower or any Third Party Obligor shall be adjudicated a bankrupt, or an order for relief shall be entered against Borrower or any Third Party Obligor by any court of competent jurisdiction under the Bankruptcy Code or any other applicable state or federal law relating to bankruptcy, reorganization or other relief for debtors.

(g) There shall exist or occur any event or condition which Bank in good faith believes impairs, or is substantially likely to impair, the prospect of payment or performance by Borrower of its obligations under any of the Loan Documents.

(h) The dissolution or liquidation of any Borrower or Third Party Obligor which is a corporation, partnership, joint venture or other type of entity; or any such Borrower or Third Party Obligor, or any of its directors, stockholders or members, shall take action seeking to effect the dissolution or liquidation of such Borrower or Third Party Obligor.

(i) Any change in ownership of an aggregate of twenty-five percent (25%) or more of the common stock in Borrower.

SECTION 6.2 REMEDIES. Upon the occurrence of any Event of Default: (a) all indebtedness of Borrower under each of the Loan Documents, any term thereof to the contrary notwithstanding, shall at Bank's option and without notice become immediately due and payable without presentment, demand, protest or notice of dishonor, all of which are hereby expressly waived by each Borrower; (b) the obligation, if any, of Bank to extend any further credit under any of the Loan Documents shall immediately cease and terminate; and (c) Bank shall have all rights, powers and remedies available under each of the Loan Documents, or accorded by law, including without limitation the right to resort to any or all security for any credit Subject hereto and to exercise any or all of the rights of a beneficiary or secured party pursuant to applicable law. All rights, powers and remedies of Bank may be exercised at any, time by Bank and from time to time after the occurrence of an Event of Default, are cumulative and not exclusive, and shall be in addition to any other rights, powers or remedies provided by law or equity.

ARTICLE VII
MISCELLANEOUS

SECTION 7.1 NO WAIVER. No delay, failure or discontinuance of Bank in exercising any right, power or remedy under any of the Loan Documents shall affect or operate as a waiver of such right, power or remedy; nor shall any single or partial exercise of any such right, power or remedy preclude, waive or otherwise affect any other or further exercise thereof or the exercise of any other right, power or remedy. Any waiver, permit, consent or approval of any kind by Bank of any breach of or default under any of the Loan Documents must be in writing and shall be effective only to the extent set forth in such writing.

SECTION 7.2 NOTICES. All notices, requests and demands which any party is required or may desire to give to any other party under any provision of this Agreement must be in writing delivered to each party at the following address:

BORROWER: Iteris, Inc.
1515 S. Manchester
Anaheim, CA 92802

BANK: WELLS FARGO BANK, NATIONAL ASSOCIATION
Orange County RCBO
2030 Main Street, Suite #900
Irvine, CA 92614

or to such other address as any party may designate by written notice to all other parties. Each such notice, request and demand shall be deemed given or made as follows: (a) if sent by hand delivery, upon delivery; (b) if sent by mail, upon the earlier of the date of receipt or three (3) days after deposit in the U.S. mail, first class and postage prepaid; and (c) if sent by telecopy, upon receipt.

SECTION 7.3 COSTS, EXPENSES AND ATTORNEYS' FEES. Borrower shall pay to Bank immediately upon demand the full amount of all payments, advances, charges, costs and expenses, including reasonable attorneys' fees (to include outside counsel fees and all allocated costs of Bank's in-house counsel), expended or incurred by Bank in connection with (a) the negotiation and preparation of this Agreement and the other Loan Documents, Bank's continued administration hereof and thereof, and the preparation of any amendments and waivers hereto and thereto, (b) the enforcement of Bank's rights and/or the collection of any amounts which become due to Bank under any of the Loan Documents, and

(c) the prosecution or defense of any action in any way related to any of the Loan Documents, including without limitation, any action for declaratory relief, whether incurred at the trial or appellate level, in an arbitration proceeding or otherwise, and including any of the foregoing incurred in connection with any bankruptcy proceeding (including without limitation, any adversary proceeding, contested matter or motion brought by Bank or any other person) relating to any Borrower or any other person or entity.

SECTION 7.4 SUCCESSORS, ASSIGNMENT. This Agreement shall be binding upon and inure to the benefit of the heirs, executors, administrators, legal representatives, successors and assigns of the parties; provided however, that Borrower may not assign or transfer its interest hereunder without Bank's prior written consent. Bank reserves the right to sell, assign, transfer, negotiate or grant participations in all or any part of, or any interest in, Bank's rights and benefits under each of the Loan Documents. In connection therewith, Bank may disclose all documents and information which Bank now has or may hereafter acquire relating to any credit subject hereto, Borrower or its business, any guarantor hereunder or the business of such guarantor, or any collateral required hereunder.

SECTION 7.5 ENTIRE AGREEMENT; AMENDMENT. This Agreement and the other Loan Documents constitute the entire agreement between Borrower and Bank with respect to each credit subject hereto and supersede all prior negotiations, communications, discussions and correspondence concerning the subject matter hereof. This Agreement may be amended or modified only in writing signed by each party hereto.

SECTION 7.6 NO THIRD-PARTY BENEFICIARIES. This Agreement is made and entered into for the sole protection and benefit of the parties hereto and their respective permitted successors and assigns, and no other person or entity shall be a third party beneficiary of, or have any direct or indirect cause of action or claim in connection with, this Agreement or any other of the Loan Documents to which it is not a party.

SECTION 7.7 TIME. Time is of the essence of each and every provision of this Agreement and each other of the Loan Documents.

SECTION 7.8 SEVERABILITY OF PROVISIONS. If any provision of this Agreement shall be prohibited by or invalid under applicable law, such provision shall be ineffective only to the extent of such prohibition or invalidity without invalidating the remainder of such provision or any remaining provisions of this Agreement.

SECTION 7.9 COUNTERPARTS. This Agreement may be executed in any number of counterparts, each of which when executed and delivered shall be deemed to be an original, and all of which when taken together shall constitute one and the same Agreement.

SECTION 7.10 GOVERNING LAW. This Agreement shall be governed by and construed in accordance with the laws of the State of California.

SECTION 7.11 ARBITRATION.

(a) Arbitration. The parties hereto agree, upon demand by any party, to submit to binding arbitration all claims, disputes and controversies between or among them (and their respective employees, officers, directors, attorneys, and other agents), whether in tort, contract or otherwise arising out of or relating to in any way (i) the loan and related Loan Documents which ore the subject of this Agreement and its negotiation, execution, collateralization, administration, repayment, modification, extension, substitution, formation, inducement, enforcement, default or termination; or (ii) requests for additional credit.

(b) Governing Rules. Any arbitration proceeding will (i) proceed in a location in California selected by the American Arbitration Association ("AAA"); (ii) be governed by the Federal Arbitration Act (Title 9 of the United States Code), notwithstanding any conflicting choice of law provision in any of the documents between the parties; and (iii) be conducted by the AAA, or such other administrator as the parties shall

mutually agree upon, in accordance with the AAA's commercial dispute resolution procedures, unless the claim or counterclaim is at least $1,000,000.00 exclusive of claimed interest, arbitration fees and costs in which case the arbitration shall be conducted in accordance with the AAA's optional procedures for large, complex commercial disputes (the commercial dispute resolution procedures or the optional procedures for large, complex commercial disputes to be referred to, as applicable, as the "Rules"). If there is any inconsistency between the terms hereof and the Rules, the terms and procedures set forth herein shall control. Any party who fails or refuses to submit to arbitration following a demand by any other party shall bear all costs and expenses incurred by such other party in compelling arbitration of any dispute. Nothing contained herein shall be deemed to be a waiver by any party that is a bank of the protections afforded to it under 12 U.S.C. §91 or any similar applicable state law.

(c) No Waiver of Provisional Remedies, Self-Help and Foreclosure. The arbitration requirement does not limit the right of any party to (i) foreclose against real or personal property collateral; (ii) exercise self-help remedies relating to collateral or proceeds of collateral such as setoff or repossession; or (iii) obtain provisional or ancillary remedies such as replevin, injunctive relief, attachment or the appointment of a receiver, before during or after the pendency of any arbitration proceeding. This exclusion does not constitute a waiver of the right or obligation of any party to submit any dispute to arbitration or reference hereunder, including those arising from the exercise of the actions detailed in sections (i), (ii) and (iii) of this paragraph.

(d) Arbitrator Qualifications and Powers. Any arbitration proceeding in which the amount in controversy is $5,000,000.00 or less will be decided by a single arbitrator selected according to the Rules, and who shall not render an award of greater than $5,000,000.00. Any dispute in which the amount in controversy exceeds $5,000,000.00 shall be decided by majority vote of a panel of three arbitrators; provided however, that all three arbitrators must actively participate in all hearings and deliberations. The arbitrator will be a neutral attorney licensed in the State of California or a neutral retired judge of the state or federal judiciary of California, in either case with a minimum of ten years experience in the substantive law applicable to the subject matter of the dispute to be arbitrated. The arbitrator will determine whether or not an issue is arbitratable and will give effect to the statutes of limitation in determining any claim. In any arbitration proceeding the arbitrator will decide (by documents only or with a hearing at the arbitrator's discretion) any pre-hearing motions which are similar to motions to dismiss for failure to state a claim or motions for summary adjudication. The arbitrator shall resolve all disputes in accordance with the substantive law of California and may grant any remedy or relief that a court of such state could order or grant within the scope hereof and such ancillary relief as is necessary to make effective any award. The arbitrator shall also have the power to award recovery of all costs and fees, to impose sanctions and to take such other action as the arbitrator deems necessary to the same extent a judge could pursuant to the Federal Rules of Civil Procedure, the California Rules of Civil Procedure or other applicable law. Judgment upon the award rendered by the arbitrator may be entered in any court having jurisdiction. The institution and maintenance of an action for judicial relief or pursuit of a provisional or ancillary remedy shall not constitute a waiver of the right of any party, including the plaintiff, to submit the controversy or claim to arbitration if any other party contests such action for judicial relief.

(e) Discovery. In any arbitration proceeding discovery will be permitted in accordance with the Rules. All discovery shall be expressly limited to matters directly relevant to the dispute being arbitrated and must be completed no later than 20 days before the hearing date and within 180 days of the filing of the dispute with the AAA. Any requests for an extension of the discovery periods, or any discovery disputes, will be subject to final determination by the arbitrator upon a showing that the request for discovery is essential for the party's presentation and that no alternative means for obtaining information is available.

(f) Class Proceedings and Consolidations. The resolution of any dispute arising pursuant to the terms of this Agreement shall be determined by a separate arbitration proceeding and such dispute shall not be consolidated with other disputes or included in any class proceeding.

(g) Payment of Arbitration Costs and Fees. The arbitrator shall award all costs and expenses of the arbitration proceeding.

(h) Real Property Collateral; Judicial Reference. Notwithstanding anything herein to the contrary, no dispute shall be submitted to arbitration if the dispute concerns indebtedness secured directly or indirectly, in whole or in pert, by any real property unless (i) the holder of the mortgage, lien or security interest specifically elects in writing to proceed with the arbitration, or (ii) all parties to the arbitration waive any rights or benefits that might accrue to them by virtue of the single action rule statute of California, thereby agreeing that all indebtedness and obligations of the parties, and all mortgages, liens and security interests securing such indebtedness and obligations, shall remain fully valid and enforceable. If any such dispute is not submitted to arbitration, the dispute shall be referred to a referee in accordance with California Code of Civil Procedure Section 638 et seq., and this general reference agreement is intended to be specifically enforceable in accordance with said Section 638. A referee with the qualifications required herein for arbitrators shall be selected pursuant to the AAAs selection procedures. Judgment upon the decision rendered by a referee shall be entered in the court in which such proceeding was commenced in accordance with California Code of Civil Procedure Sections 644 and 645.

(i) Miscellaneous. To the maximum extent practicable, the AAA, the arbitrators and the parties shall take all action required to conclude any arbitration proceeding within 180 days of the filing of the dispute with the AAA. No arbitrator or other party to an arbitration proceeding may disclose the existence, content or results thereof, except for disclosures of information by a party required in the ordinary course of its business or by applicable law or regulation. If more than one agreement for arbitration by or between the parties potentially applies to a dispute, the arbitration provision most directly related to the Loan Documents or the subject matter of the dispute shall control. This arbitration provision shall survive termination, amendment or expiration of any of the Loan Documents or any relationship between the parties.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed as of the day and year first written above.

Iteris, Inc.

By: /s/ Jack Johnson

Title: CEO

By: /s/ Abbas Mohaddes

Title: Secretary

WELLS FARGO BANK, NATIONAL ASSOCIATION

By: /s/ Elisa Angeles
Elisa Angeles, Relationship Manager

Exhibit 10.26

ASSUMPTION AND AMENDMENT AGREEMENT

This Assumption Agreement ("Agreement"), dated as of October 20, 2004, is made by and between Wells Fargo Bank, National Association ("Bank") and Iteris Holdings, Inc., a Delaware corporation ("Holdings"), successor by merger to Iteris, Inc., a Delaware corporation ("Original Borrower").

R E C I T A L S

A. Reference is made to that certain Credit Agreement dated as of May 27, 2004 between Bank and Original Borrower, as "Borrower" (as amended, supplemented or otherwise modified from time to time, the " Credit Agreement"). Capitalized terms used and not otherwise defined herein shall have the meanings given such terms in the Credit Agreement

B. In addition, to the Credit Agreement, Original Borrower is a party to the certain other Loan Documents, including without limitation each of the documents set forth on Schedule I attacked hereto.

C. Pursuant to a merger (the "Merger") described in a Certificate of Ownership and Merger Merging Iteris, Inc. into Iteris Holdings, Inc. dated as of 10/22/2004, 2004 between Original Borrower and Holdings (the "Merger Agreement"; collectively with other related documents, the ("Merger Documents"), the existence of Original Borrower as a separate legal entity will be terminated and Holdings, as the surviving corporation of the Merger, will, by operation of law, succeeded to the liabilities and assets of Original Borrower.

D. Bank is agreeable to continuing the Loan Documents in effect with Holdings pursuant to and in accordance with the terms and conditions set forth below and, in connection therewith, Bank and Holdings have agreed to certain modifications to the Loan Documents as set forth herein.

AGREEMENT

NOW, THEREFORE, in consideration of the terms and conditions herein, and for other good and valuable consideration, the receipt and adequacy of which are acknowledged, the parties hereto agree to the following covenants, agreements, amendments and modifications:

1. Merger and Assumption.

(a) Holdings hereby (i) acknowledges and affirms that it will perform and discharge any and all of the obligations of Original Borrower under the Loan Documents, and (ii) agrees to be bound by all the terms, provisions and conditions of the Loan Documents with the same force and effect as though Holdings were an original party thereto.

(b) The execution of this Agreement by Holdings shall be deemed its execution of the Credit Agreement and the other Loan Documents. This Agreement does not (i) constitute the creation of a new obligation or the extinguishment of the obligations evidenced by the Credit Agreement or the other Loan Documents, or (ii) in any way affect or impair the liens of the Loan Documents granted by Original Borrower, each of which Holdings acknowledges to be valid first liens on the property described therein (except as otherwise set forth in the Loan Documents). Holdings agrees that the liens of the Loan Documents granted by Original Borrower shall continue in full force and effect, unimpaired and unaffected by this Agreement or by the Merger.

2. Representations and Warranties. Holdings makes the following representations and warranties to Bank:

(a) Holdings makes all of the representations and warranties made by Borrower in the Loan Documents, other than representations and warranties that expressly speak as of a particular date;

(b) The execution, delivery and performance of this Agreement are within Holdings' powers, have been duly authorized by all necessary action, have received all necessary approvals and do not contravene any law or any contractual restrictions binding on Holdings;

(c) This Agreement and, pursuant to the assumption described herein, the Loan Documents, are the legal, valid and binding obligations of Holdings, enforceable against Holdings in accordance with their respective terms, except as enforcement may be limited by bankruptcy, insolvency, reorganization, arrangement, moratorium or other similar laws relating to or affecting creditors' rights generally or equitable principles relating to the granting of specific performance and other equitable remedies as a matter of judicial discretion;

(d) There are no pending or, to the best of Holdings' knowledge, threatened actions, suits, proceedings or investigations before any Governmental Authority, arbitrator or administrative agency which could have a material adverse effect on the financial condition or operation of Holdings other than those disclosed by Holdings, to Bank in writing prior to the date hereof; and

(e) The Merger has become effective pursuant to the terms of the Merger Documents and all applicable laws. All assets of Original Borrower existing immediately prior to the Merger have become vested in Holdings, subject to all the liabilities of Original Borrower immediately prior to the Merger. All consents and approvals of any governmental agency and any other entity necessary to effect the Merger have been obtained and the Merger has been effected in compliance with all applicable laws.

3. Knowledge of Loan Documents. Holdings warrants that it has full knowledge of all terms of the Loan Documents. Holdings understands and acknowledges that except as expressly provided herein or In the Loan Documents, Bank has not waived any right of Bank or obligation of Holdings under the Loan Documents, and Bank has not agreed to any modification or extension of any provision of any Loan Document.

4. Security Interest. Holdings hereby confirms the grant to Bank by Original Borrower of a security interest in all presently existing and hereafter acquired Collateral (as defined in the Continuing Security Agreement Rights to Payment and Inventory and the Security Agreement Equipment). Holdings irrevocably authorizes Bank at any time and from time to time to file in any applicable jurisdiction any financing statements (including fixture filings) and amendments thereto that contain information required by Article 9 of the Uniform Commercial Code of each applicable jurisdiction for the filing of any such financing statement or amendment, including (a) whether Holdings is an organization, the type of organization and any organizational identification number issued to Holdings and (b) in the case of a financing statement filed as a fixture filing, a sufficient description of the real property to which such Article 9 collateral relates. Holdings agrees to provide any necessary information in connection therewith to Bank promptly upon request.

5. Indemnity. Holdings indemnifies Bank and its directors, officers, agents, attorneys and employees (collectively, the "Indemnitees") from and against any and all claims, demands, actions or causes of action (and liabilities, losses and reasonable costs or expenses that any Indemnitee suffers or incurs as a result of the assertion of any such claim, demand, action or cause of action) relating to the Merger or Holdings' assumption of the Loan Documents and the obligations evidenced thereby; provided that no Indemnitee shall be entitled to indemnification for any liability, loss, cost or expense caused by its own gross negligence or willful misconduct or for any liability, loss, cost or expense asserted against it by another Indemnitee. Any obligation or liability of Holdings to any Indemnitee under this Section 5 shall survive the expiration or termination of the Credit Agreement and the repayment of all Advances and the payment and performance of all other Obligations owed to Bank.

6. Confirmation of Liens. Nothing contained herein shall affect or be construed to affect any lien, security interest, charge or encumbrance created by any Loan Document or the priority of that lien, security interest, charge or encumbrance over other liens, security interests, charges or encumbrances.

7. Integration; Interpretation. This Agreement is a "Loan Document" as defined in the Credit Agreement. The Loan Documents, including this Agreement, contain or expressly incorporate by reference the entire agreement of the parties with respect to the matters contemplated herein and supersede all prior negotiations. The Loan Documents shall not be modified except as set forth therein. Any reference herein to the Loan Documents includes any amendments, renewals or extensions thereof approved by Bank and otherwise done in accordance with the terms thereof. Except as expressly modified hereby, all terms and conditions of the Loan Documents shall continue in full force and effect without waiver or modification, and Lenders reserves all of their rights, privileges and remedies in connection therewith.

8. Amendments to Credit Agreement.

(a) Section 1.5 of the Credit Agreement is amended to read in its entirety as follows: "[Intentionally Omitted]".

(b) Section 4.3 is amended to read in its entirety as follows:

SECTION 4.3 FINANCIAL STATEMENTS. Provide to Bank all of the following, in form and detail satisfactory to Bank:

(a) not later than 120 days after and as of the end of each fiscal year, audited financial statements of Borrower, prepared by an outside accounting firm acceptable to Bank, to include a balance sheet, statement of income and statement of cash flows;

(b) not later than 45 days after and as of the end of each fiscal quarter, financial statements of Borrower, prepared by Borrower, to include a balance sheet, statement of income and statement of cash flows;

(c) not later than 15 days after and as of the end of each month, a borrowing base certificate, an inventory collateral report, an aged listing of accounts receivable and accounts payable and a reconciliation of accounts, and not later than each June 30 and December 31, a list of the names and addresses of all Borrower's account debtors; and

(d) from time to time such other information as Bank may reasonably request.

(c) Section 5.7 is amended to read in its entirety as follows:

SECTION 5.7 DIVIDENDS, DISTRIBUTIONS. Declare or pay any dividend or distribution either in cash, stock or any other property on Borrower's stock now or hereafter outstanding, nor redeem, retire, repurchase or otherwise acquire any shares of any class of Borrowers stock now or hereafter outstanding, except repurchases of stock pursuant to the terms of incentive equity compensation arrangements with employees, directors or consultants of Borrower in an aggregate amount not to exceed $75,000 in any fiscal year.

9. Successors and Assigns. This Agreement is binding upon and shall inure to the benefit of the successors and assigns of the parties, subject to all prohibitions of transfers contained in any Loan Document.

10. Miscellaneous. This Agreement shall be governed by and interpreted in accordance with the laws of the State of California. This Agreement may be executed in counterparts, which counterparts, when so executed and delivered shall together constitute but one original. Execution of any such counterpart may be evidenced by a telecopier transmission of the signature of such party.

11. Address for Notices. Holdings' address for notices pursuant to the Credit Agreement and the other Loan Documents shall be the address for notices provided for Borrower in the Credit Agreement or as Holdings may otherwise designate by written notice to the other parties to the Loan Documents.

[signature page follows]

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the date first set forth above.

"Holdings"

ITERIS HOLDINGS, INC.,
a Delaware corporation

By: /s/ Gregory A. Miner

Gregory A. Miner CEO
[Printed Name and Title]

"Bank"

WELLS FARGO BANK, NATIONAL ASSOCIATION

By: /s/ Elisa Angeles

Elisa Angeles Assistant Vice President
[Printed Name and Title]

SCHEDULE I

SELECTED LOAN DOCUMENTS

In addition to the Credit Agreement, Original Borrower executed and delivered to Bank each of the following Loan Documents:

1. Revolving Line of Credit Note
2. Term Note
3. Addendum to Promissory Note (Prime Rate Pricing Adjustments)
4. Continuing Security Agreement Rights to Payments and Inventory
5. Security Agreement Equipment

Exhibit 10.27

WELLS FARGO ***REVOLVING LINE OF CREDIT NOTE***

$5,000,000.00 **Irvine, California**
May 27, 2004

FOR VALUE RECEIVED, the undersigned Iteris, Inc. ("Borrower") promises to pay to the order of WELLS FARGO BANK, NATIONAL ASSOCIATION ("Bank") at its office at Orange County RCBO, 2030 Main Street, Suite #900, Irvine, CA 92614, or at such other place as the holder hereof may designate, in lawful money of the United States of America and in immediately available funds, the principal sum of $5,000,000.00, or so much thereof as may be advanced and be outstanding, with interest thereon, to be computed on each advance from the date of its disbursement as set forth herein.

1. DEFINITIONS:

As used herein, the following terms shall have the meanings set forth after each, and any other term defined in this Note shall have the meaning set forth at the place defined:

1.1 "Business Day" means any day except a Saturday, Sunday or any other day on which commercial banks in California are authorized or required by law to close.

1.2 "Fixed Rate Term" means a period commencing on a Business Day and continuing for 1, 2 or 3 months, as designated by Borrower, during which all or a portion of the outstanding principal balance of this Note bears interest determined in relation to LIBOR; provided however, that no Fixed Rate Term may be selected for a principal amount less than $100,000.00; and provided further, that no Fixed Rate Term shall extend beyond the scheduled maturity date hereof. If any Fixed Rate Term would end on a day which is not a Business Day, then such Fixed Rate Term shall be extended to the next succeeding Business Day.

1.3 "LIBOR" means the rate per annum (rounded upward, if necessary, to the nearest whole 1/8 of 1%) determined by dividing Base LIBOR by a percentage equal to 100% less any LIBOR Reserve Percentage.

(a) "Base LIBOR" means the rate per annum for United States dollar deposits quoted by Bank as the Inter-Bank Market Offered Rate, with the understanding that such rate is quoted by Bank for the purpose of calculating effective rates of interest for loans making reference thereto, on the first day of a Fixed Rate Term for delivery of funds on said date for a period of time approximately equal to the number of days in such Fixed Rate Term and in an amount approximately equal to the principal amount to which such Fixed Rate Term applies. Borrower understands and agrees that Bank may base its quotation of the Inter-Bank Market Offered Rate upon such offers or other market indicators of the Inter-Bank Market as Bank in its discretion deems appropriate including, but not limited to, the rate offered for U.S. dollar deposits on the London Inter-Bank Market.

(b) "LIBOR Reserve Percentage" means the reserve percentage prescribed by the Board of Governors of the Federal Reserve System (or any successor) for "Eurocurrency Liabilities" (as defined in Regulation D of the Federal Reserve Board, as amended), adjusted by Bank for expected changes in such reserve percentage during the applicable Fixed Rate Term.

1.4 "Prime Rate" means at any time the rate of interest most recently announced within Bank at its principal office as its Prime Rate, with the understanding that the Prime Rate is one of Bank's base rates and serves as the basis upon which effective rates of interest are calculated for those loans making reference thereto, and is evidenced by the recording thereof after its announcement in such internal publication or publications as Bank may designate.

2. INTEREST:

2.1 Interest. The outstanding principal balance of this Note shall bear interest (computed on the basis of a 360-day year, actual days elapsed) either (a) at a fluctuating rate per annum equal to the Prime Rate in effect from time to time, or (b) at a fixed rate per annum determined by Bank to be 2.75000% above LIBOR in effect on the first day of the applicable Fixed Rate Term. When interest is determined in relation to the Prime Rate, each change in the rate of interest hereunder shall become effective on the date each Prime Rate change is announced within Bank. With respect to each LIBOR selection option selected hereunder, Bank is hereby authorized to note the date, principal amount, interest rate and Fixed Rate Term applicable thereto and any payments made thereon on Bank's books and records (either manually or by electronic entry) and/or on any schedule attached to this Note, which notations shall be prima facie evidence of the accuracy of the information noted.

2.2 Selection of Interest Rate Options. At any time any portion of this Note bears interest determined in relation to LIBOR, it may be continued by Borrower at the end of the Fixed Rate Term applicable thereto so that all or a portion thereof bears interest determined in relation to the Prime Rate or to LIBOR for a new Fixed Rate Term, designated by Borrower. At any time any portion of this Note bears interest determined in relation to the Prime Rate. Borrower may convert all or a portion thereof so that it bears interest determined in relation to LIBOR for a Fixed Rate Term designated by Borrower. At such time as Borrower requests an advance hereunder or wishes to select a LIBOR option for all or a portion of the outstanding principal balance hereof, and at the end of each Fixed Rate Term, Borrower shall give Bank notice specifying: (a) the interest rate option selected by Borrower; (b) the principal amount subject thereto; and (c) for each LIBOR selection, the length of the applicable Fixed Rate Term. Any such notice may be given by telephone (or such other electronic method as Bank may permit) so long as, with respect to each LIBOR selection, (i) if requested by Bank, Borrower provides to Bank written confirmation thereof not later than 3 Business Days after such notice is given, and (ii) such notice is given to Bank prior to 10:00 a.m. on the first day of the Fixed Rate Term, or at a later time during any Business Day if Bank, at it's sole option but without obligation to do so, accepts Borrower's notice and quotes a fixed rate to Borrower. If Borrower does not immediately accept a fixed rate when quoted by Bank, the quoted rate shall expire and any subsequent LIBOR request from Borrower shall be subject to a redetermination by Bank of the applicable fixed rate. If no specific designation of interest is made at the time any advance is requested hereunder or at the end of any Fixed Rate Term, Borrower shall be deemed to have made a Prime Rate interest selection for such advance or the principal amount to which such Fixed Rate Term applied.

2.3 Taxes and Regulatory Costs. Borrower shall pay to Bank immediately upon demand, in addition to any other amounts due or to become due hereunder, as applicable during any Fixed Rate Term selection, any and all (a) withholdings, interest equalization taxes, stamp taxes or other taxes (except income and franchise taxes) imposed by any domestic or foreign governmental authority and related in any manner to LIBOR, and (b) future, supplemental, emergency or other changes in the LIBOR Reserve Percentage, assessment rates imposed by the Federal Deposit Insurance Corporation, or similar requirements or costs imposed by any domestic or foreign governmental authority or resulting from compliance by Bank with any request or directive (whether or not having the force of law) from any central bank or other governmental authority and related in any manner to LIBOR to the extent they are not included in the calculation of LIBOR. In determining which of the foregoing are attributable to any LIBOR option available to Borrower hereunder, any reasonable allocation made by Bank among its operations shall be conclusive and binding upon Borrower.

2.4 Payment of Interest. Interest accrued on this Note shall be payable on the 1 st day of each month, commencing June 1, 2004.

2.5 Default Interest. From and after the maturity date of this Note, or such earlier date as all principal owing hereunder becomes due and payable by acceleration or otherwise, the outstanding principal balance of this Note shall bear interest until paid in full at an increased rate per annum (computed on the basis of a 360-day year, actual days elapsed) equal to 4% above the rate of interest from time to time applicable to this Note.

3. BORROWING AND REPAYMENT:

3.1 Borrowing and Repayment. Borrower may from time to time during the term of this Note borrow, partially or wholly repay its outstanding borrowings, and reborrow, subject to all of the limitations; terms and conditions of this Note end of the Credit Agreement between Borrower and Bank defined below; provided however, that the total outstanding borrowings under this Note shall not at any time exceed the principal amount stated above. The unpaid principal balance of this obligation at any time shall be the total amounts advanced hereunder by the holder hereof less the amount of principal payments made hereon by or for any Borrower, which balance may be endorsed hereon from time to time by the holder. The outstanding principal balance of this Note shall be due and payable in full on August 1, 2005.

3.2 Advances. Advances hereunder, to the total amount of the principal sum available hereunder, may be made by the holder at the oral or written request of (a) Jack Johnson or Abbas Mohaddes or James S. Miele, any one acting alone, who are authorized to request advances and direct the disposition of any advances until written notice of the revocation of such authority is received by the holder at the office designated above, or (b) any person, with respect to advances deposited to the credit of any deposit account of any Borrower which advances, when so deposited, shall be conclusively presumed to have been made to or for the benefit of each Borrower regardless of the fact that persons other than those authorized to request advances may have authority to draw against such account. The holder shall have no obligation to determine whether any person requesting an advance is or has been authorized by any Borrower.

3.3 Application of Payments. Each payment made on this Note shall be credited first, to any interest then due and second, to the outstanding principal balance hereof. All payments credited to principal shall be applied first, to the outstanding principal balance of this Note which bears interest determined in relation to the Prime Rate, if any, and second, to the outstanding principal balance of this Note which bears interest determined in relation to LIBOR, with such payments applied to the oldest Fixed Rate Term first.

4. PREPAYMENT:

4.1 Prime Rate. Borrower may prepay principal on any portion of this Note which bears interest determined in relation to the Prime Rate at any time, in any amount and without penalty.

4.2 LIBOR. Borrower may prepay principal on any portion of this Note which bears interest determined in relation to LIBOR at any time and in the minimum amount of $100,000.00; provided however, that if the outstanding principal balance of such portion of this Note is less than said amount, the minimum prepayment amount shall be the entire outstanding principal balance thereof. In consideration of Bank providing this prepayment option to Borrower, or if any such portion of this Note shall become due and payable at any time prior to the last day of the Fixed Rate Term applicable thereto by acceleration or otherwise, Borrower shall pay to Bank immediately upon demand a fee which is the sum of the discounted monthly differences for each month from the month of prepayment through the month in which such Fixed Rate Term matures, calculated as follows for each such month:

(a) Determine the amount of interest which would have accrued each month on the amount prepaid at the interest rate applicable to such amount had it remained outstanding until the last day of the Fixed Rate Term applicable thereto.

(b) Subtract from the amount determined in (a) above the amount of interest which would have accrued for the same month on the amount prepaid for the remaining term of such Fixed Rate Term at LIBOR in effect on the date of prepayment for new loans made for such term and in a principal amount equal to the, amount prepaid.

(c) If the result obtained in (b) for any month is greater than zero, discount that difference by LIBOR used in (b) above.

Each Borrower acknowledges that prepayment of such amount may result in Bank incurring additional costs, expenses and/or liabilities, and that it is difficult to ascertain the full extent of such costs, expenses and/or liabilities. Each Borrower, therefore, agrees to pay the above-described prepayment fee and agrees that said amount represents a reasonable estimate of the prepayment costs, expenses, and/or liabilities of Bank. If Borrower fails to pay any prepayment fee when due, the amount of such prepayment fee shall thereafter bear interest until paid at a rate per annum 2.000% above the Prime Rate in effect from time to time (computed on the basis of a 360-day year actual days elapsed). Each change in the rate of interest on any such past due prepayment fee shall become effective on the date each Prime Rate change is announced within Bank.

5. EVENTS OF DEFAULT:

This Note is made pursuant to and is subject to the terms and conditions of that certain Credit Agreement between Borrower and Bank dated as of May 27, 2004, as amended from time to time (the "Credit Agreement"). Any default in the payment or performance of any obligation under this Note, or any defined event of default under the Credit Agreement, shall constitute an "Event of Default" under this Note.

6. MISCELLANEOUS:

6.1 Remedies. Upon the occurrence of any Event of Default, the holder of this Note, at the holder's option, may declare all sums of principal and interest outstanding hereunder to be immediately due and payable without presentment, demand, notice of nonperformance, notice of protest, protest or notice of dishonor, all of which are expressly waived by each Borrower, and the obligation, if any, of the holder to extend any further credit hereunder shall immediately cease and terminate. Each Borrower shall pay to the holder immediately upon demand the full amount of all payments, advances, charges, costs and expenses, including reasonable attorneys' fees (to include outside counsel fees and all allocated costs of the holder's in-house counsel), expended or incurred by the holder in connection with the enforcement of the holder's rights and/or the collection of any amounts which become due to the holder under this Note, and the prosecution or defense of any action in any way related to this Note, including without limitation, any action for declaratory relief, whether incurred at the trial or appellate level, in an arbitration proceeding or otherwise, and including any of the foregoing incurred in connection with any bankruptcy proceeding (including without limitation, any adversary proceeding, contested matter or motion brought by Bank or any other person) relating to any Borrower or any other person or entity.

6.2 Obligations Joint and Several. Should more than one person or entity sign this Note as a Borrower, the obligations of each such Borrower shall be joint and several.

6.3 Governing Law. This Note shall be governed by and construed in accordance with the laws of the State of California.

IN WITNESS WHEREOF, the undersigned has executed this Note as of the date first written above.

Iteris, Inc.

By: /s/ Jack Johnson

Title: CEO

By: /s/ Abbas Mohaddes

Title: Secretary

Exhibit 10.28

WELLS FARGO ***TERM NOTE***

$5,000,000.00 **Irvine, California**
May 27, 2004

FOR VALUE RECEIVED, the undersigned Iteris, Inc. ("Borrower") promises to pay to the order of WELLS FARGO BANK, NATIONAL ASSOCIATION ("Bank") at its office at **Orange County RCBO, 2030 Main Street, Suite #900, Irvine, CA 92614** , or at such other place as the holder hereof may designate, in lawful money of the United States of America and in immediately available funds, the principal sum of **$5,000,000.00**, with interest thereon as set forth herein.

1. **INTEREST**:

1.1 Interest. The outstanding principal balance of this Note shall bear interest (computed on the basis of a **360-**day year, actual days elapsed) at a rate per annum **.50000%** above the Prime Rate in effect from time to time. The "Prime Rate" is a base rate that Bank from time to time establishes and which serves as the basis upon which effective rates of interest are calculated for those loans making reference thereto. Each change in the rate of interest hereunder shall become effective on the date each Prime Rate change is announced within Bank.

1.2 Payment of Interest. Interest accrued on this Note shall be payable on the **27th** day of each month, commencing **June 27, 2004**.

1.3 Default Interest. From and after the maturity date of this Note, or such earlier date as all principal owing hereunder becomes due and payable by acceleration or otherwise, the outstanding principal balance of this Note shall bear interest until paid in full at an increased rate per annum (computed on the basis of a **360-**day year, actual days elapsed) equal to 4% above the rate of interest from time to time applicable to this Note.

2. **REPAYMENT AND PREPAYMENT**:

2.1. Repayment. Principal shall be payable on the 27th day of each month in installments of **$104,166.57** each, commencing **June 27, 2004**, and continuing up to and including **April 27, 2008**, with a final installment consisting of all remaining unpaid principal due and payable in full on **May 27, 2008**.

2.2 Application of Payments. Each payment made on this Note shall be credited first, to any interest then due and second, to the outstanding principal balance hereof.

2.3 Prepayment. Borrower may prepay principal on this Note at any time, in any amount and without penalty. All prepayments of principal shall be applied on the most remote principal installment or installments then unpaid.

3. **EVENTS OF DEFAULT**:

This Note is made pursuant to and is subject to the terms and conditions of that certain Credit Agreement between Borrower and Bank dated as of **May 27, 2004**, as amended from time to time (the "Credit Agreement"). Any default in the payment or performance of any obligation under this Note, or any defined event of default under the Credit Agreement, shall constitute an "Event of Default" under this Note.

4. **MISCELLANEOUS**:

4.1 Remedies. Upon the occurrence of any Event of Default, the holder of this Note, at the holder's option, may declare all sums of principal and interest outstanding hereunder to be immediately due and payable without presentment, demand, notice of nonperformance, notice of protest, protest or notice of dishonor, all of which are expressly waived by each Borrower, and the obligation, if any, of the holder to extend any further credit hereunder shall immediately cease and terminate. Each Borrower shall pay to the holder immediately upon demand the full amount of all payments, advances, charges, costs and expenses, including reasonable attorneys' fees (to include outside counsel fees and all allocated costs of the holder's in-house counsel), expended or incurred by the holder in connection with the enforcement of the holder's rights and/or the collection of any amounts which become due to the holder under this Note, and the prosecution or defense of any action in any way related to this Note, including without limitation, any action for declaratory relief, whether incurred at the trial or appellate level, in an arbitration proceeding or otherwise, and including any of the foregoing incurred in connection with any bankruptcy proceeding (including without limitation, any adversary proceeding, contested matter or motion brought by Bank or any other person) relating to any Borrower or any other person or entity.

4.2 Obligations Joint and Several. Should more than one person or entity sign this Note as a Borrower, the obligations of each such Borrower shall be joint and several.

4.3 Governing Law. This Note shall be governed by and construed in accordance with the laws of the State of California.

IN WITNESS WHEREOF, the undersigned has executed this Note as of the date first written above.

Iteris, Inc.

By: /s/ Jack Johnson

Title: CEO

By: /s/ Abbas Mohaddes

Title: Secretary

ADDENDUM TO PROMISSORY NOTE
(PRIME RATE PRICING ADJUSTMENTS)

THIS ADDENDUM is attached to and made a part of that certain term note executed by Iteris, Inc. ("Borrower") and payable to WELLS FARGO BANK, NATIONAL ASSOCIATION ("Bank"), or order, dated as of May 27, 2004, in the principal amount of Five Million Dollars ($5,000,000.00) (the "Note").

The following provisions are hereby incorporated into the Note to reflect the interest rate adjustments agreed to by Bank and Borrower.

INTEREST RATE ADJUSTMENTS:

(a) Initial Prime Rate Margin. The initial Prime Rate margin applicable to this Note shall be as set forth in the " interest" paragraph herein.

(b) Prime Rate Adjustments. In addition to any interest rate adjustments resulting from changes in the Prime Rate, Bank shall adjust the Prime Rate margin applicable to Prime Rate options selected by Borrower under this Note on a quarterly basis, commencing with the Borrower's fiscal quarter ending June 30, 2004, if required to reflect a change in Borrower's ratio of Senior Funded Debt to EBITDA (as defined in the Credit Agreement referenced herein), in accordance with the following grid:

Senior Funded Debt to EBITDA	**Applicable Prime Rate Margin**
3.50 to 1.0 or greater	.50%
less than 3.50 to 1.0	.25%

Each such adjustment shall be effective on the first Business Day of Borrower's fiscal quarter following the quarter during which Bank receives and reviews Borrower's most current fiscal quarter-end financial statements in accordance with any requirements established by Bank for the preparation and delivery thereof.

IN WITNESS WHEREOF, this Addendum has been executed as of the same date as the Note.

ITERIS, INC.

By: /s/ Jack Johnson

Title: CEO

By: /s/ Abbas Mohaddes

Title: Secretary

Exhibit 10.29

WELLS FARGO

CONTINUING SECURITY AGREEMENT
RIGHTS TO PAYMENT AND INVENTORY

1. GRANT OF SECURITY INTEREST. For valuable consideration, the undersigned, **Iteris, Inc.**, or any of them ("Debtor"), hereby grants and transfers to WELLS FARGO BANK, NATIONAL ASSOCIATION ("Bank") a security interest in all accounts, deposit accounts, chattel paper (whether electronic or tangible), instruments, promissory notes, documents, general intangibles, payment intangibles, software, letter of credit rights, health-care insurance receivables and other rights to payment (collectively called "Rights to Payments"), now existing or at any time hereafter, and prior to the termination hereof, arising (whether they arise from the sale, lease or other disposition of inventory or from performance of contracts for service, manufacture, construction, repair or otherwise or from any other source whatsoever), including all securities, guaranties, warranties, indemnity agreements, insurance policies, supporting obligations and other agreements pertaining to the same or the property described therein, and in all goods returned by or repossessed from Debtor's customers, together with a security interest in all inventory, goods held for sale or lease or to be furnished under contracts for service, goods so leased or furnished, raw materials, component parts and embedded software, work in process or materials used or consumed in Debtor's business and all warehouse receipts, bills of lading and other documents evidencing goods owned or acquired by Debtor, and all goods covered thereby, now or at any time hereafter, and prior to the termination hereof, owned or acquired by Debtor, wherever located, and all products thereof (collectively called "Inventory"), whether in the possession of Debtor, warehousemen, bailees or any other person, or in process of delivery and whether located at Debtor's places of business or elsewhere (with all Rights to Payment and Inventory referred to herein collectively as the "Collateral") together with whatever is receivable or received when any of the Collateral or proceeds thereof are sold, leased, collected, exchanged or otherwise disposed of, whether such disposition is voluntary or involuntary, including without limitation, all rights to payment, including returned premiums, with respect to any insurance relating to any of the foregoing, and all rights to payment with respect to any claim or cause of action affecting or relating to any of the foregoing (hereinafter called "Proceeds").

2. OBLIGATIONS SECURED. The obligations secured hereby are the payment and performance of: (a) all present and future Indebtedness of Debtor to Bank; (b) all obligations of Debtor and rights of Bank under this Agreement; and (c) all present and future obligations of Debtor to Bank of other kinds. The word "Indebtedness" is used herein in its most comprehensive sense and includes any and all advances, debts, obligations and liabilities of Debtor, or any of them, heretofore, now or hereafter made, incurred or created, whether voluntary or involuntary and however arising, whether due or not due, absolute or contingent, liquidated or unliquidated, determined or undetermined, and whether Debtor may be liable individually or jointly, or whether recovery upon such Indebtedness may be or hereafter becomes unenforceable.

3. TERMINATION. This Agreement will terminate upon the performance of all obligations of Debtor to Bank, including without limitation, the payment of all Indebtedness of Debtor to Bank, and the termination of all commitments of Bank to extend credit to Debtor. Upon termination, Bank will, at Borrower's cost and within a reasonable time period, execute (if necessary) and deliver such instruments and documents, including termination statements on form UCC-3, evidencing and acknowledging the termination of Bank's security interest in the Collateral and Bank shall deliver to Borrower any Collateral in Bank's possession.

4. OBLIGATIONS OF BANK. Bank has no obligation to make any loans hereunder. Any money received by Bank in respect of the Collateral may be deposited, at Bank's option, into a non-interest bearing account over which Debtor shall have no control, and the same shall, for all purposes, be deemed Collateral hereunder.

5. REPRESENTATIONS AND WARRANTIES. Debtor represents and warrants to Bank that: (a) Debtor's legal name is exactly as set forth on the first page of this Agreement, and all of Debtor's organizational documents or agreements delivered to Bank are complete and accurate in every respect; (b) Debtor is the owner and has possession or control of the Collateral and Proceeds; (c) Debtor has the

exclusive right to grant a security interest in the Collateral and Proceeds; (d) all Collateral and Proceeds are genuine, free from liens, adverse claims, setoffs, default, prepayment, defenses and conditions precedent of any kind or character, except the lien created hereby or as otherwise agreed to by Bank, or heretofore disclosed by Debtor to Bank, in writing; (e) all statements contained herein and, where applicable, in the Collateral are true and complete in all material respects; (f) no financing statement covering any of the Collateral or Proceeds, and naming any secured party other than Bank, is on file in any public office; (g) all persons appearing to be obligated on Rights to Payment and Proceeds have authority and capacity to contract and are bound as they appear to be; (h) all property subject to chattel paper has been properly registered and filed in compliance with law and to perfect the interest of Debtor in such property; and (i) all Rights to Payment and Proceeds comply with all applicable laws concerning form, content and manner of preparation and execution, including where applicable Federal Reserve Regulation Z and any State consumer credit laws.

6. COVENANTS OF DEBTOR.

6.1 Debtor Agrees in general: (a) to pay Indebtedness secured hereby when due; (b) to indemnify Bank against all losses, claims, demands, liabilities and expenses of every kind caused by property subject hereto; (c) to pay all costs and expenses, including reasonable attorneys' fees, incurred by Bank in the perfection and preservation of the Collateral or Bank's interest therein and/or the realization, enforcement and exercise of Bank's rights, powers and remedies hereunder; (d) to permit Bank to exercise its powers; (e) to execute and deliver such documents as Bank deems necessary to create, perfect and continue the security interests contemplated hereby; (f) not to change its name, and as applicable, its chief executive office, its principal residence or the jurisdiction in which it is organized and/or registered without giving Bank prior written notice thereof; (g) not to change the places where Debtor keeps any Collateral or Debtor's records concerning the Collateral and Proceeds without giving Bank prior written notice of the address to which Debtor is moving same; and (h) to cooperate with Bank in perfecting all security interests granted herein and in obtaining such agreements from third parties as Bank deems necessary, proper or convenient in connection with the preservation, perfection or enforcement of any of its rights hereunder.

6.2 Debtor agrees with regard to the Collateral and Proceeds, unless Bank agrees otherwise in writing: (a) that Bank is authorized to file financing statements in the name of Debtor to perfect Bank's security interest in Collateral and Proceeds; (b) to insure Inventory and, where applicable, Rights to Payment with Bank named as loss payee, in form, substance and amounts, under agreements, against risks and liabilities, and with insurance companies satisfactory to Bank; (c) not to use any inventory for any unlawful purpose or in any way that would void any insurance required to be carried in connection therewith; (d) not to remove Inventory from Debtor's premises, except for deliveries to buyers in the ordinary course of Debtor's business and except Inventory which consists of mobile goods as defined in the California Uniform Commercial Code, in which case Debtor agrees not to remove or permit the removal of the Inventory from its state of domicile for a period in excess of 30 calendar days; (e) not to permit any security interest in or lien on the Collateral or Proceeds, including without limitation, liens arising from the storage of Inventory, except in favor of Bank; (f) not to sell, hypothecate or otherwise dispose of, nor permit the transfer by operation of law of, any of the Collateral or Proceeds or any interest therein, except sales of Inventory to buyers in the ordinary course of Debtor's business; (g) to furnish reports to Bank of all acquisitions, returns, sales and other dispositions of the Inventory in such form and detail and at such times as Bank may require; (h) to permit Bank to inspect the Collateral at any time; (i) to keep, in accordance with generally accepted accounting principles, complete and accurate records regarding all Collateral and Proceeds, and to permit Bank to inspect the same and make copies thereof at any reasonable time; (j) if requested by Bank, to receive and use reasonable diligence to collect Rights to Payment and Proceeds, in trust and as the property of Bank, and to immediately endorse as appropriate and deliver such Rights to Payment and Proceeds to Bank daily in the exact form in which they are received together with a collection report in form satisfactory to Bank; (k) not to commingle Rights to Payment, Proceeds or collections thereunder with other property; (l) to give only normal allowances and credits and to advise Bank thereof immediately in writing If they affect any Rights to Payment or Proceeds in any material respect; (m) on demand, to deliver to Bank returned property resulting from, or payment equal to, such allowances or credits on any Rights to Payment or Proceeds or to execute such

documents and do such other things as Bank may reasonably request for the purpose of perfecting, preserving and enforcing its security interest in such returned property; (n) from time to time, when requested by Bank, to prepare and deliver a schedule of all Collateral and Proceeds subject to this Agreement and to deliver to Bank such instruments as bank may reasonably, from the standpoint of a secured creditor, require to evidence the grant of the security interest created by this Agreement in all accounts, contracts, leases and other chattel paper, instruments, documents and other evidences thereof; (o) in the event Bank elects to receive payments of Rights to Payment or Proceeds hereunder, to pay all expenses incurred by Bank in Connection therewith, including expenses of accounting, correspondence, collection efforts, reporting to account or contract debtors, filing, recording, record keeping and expenses incidental thereto; and (p) to provide any service and do any other acts which may be necessary to maintain, preserve and protect all Collateral and, as appropriate and applicable, to keep all Collateral in good and saleable condition in accordance with the standards and practices adhered to generally by users and manufacturers of like property, and to keep all Collateral and Proceeds free and clear of all defenses, rights of offset and counterclaims.

7. POWERS OF BANK. Debtor appoints Bank its true attorney-in-fact to perform any of the following powers, which are coupled with an interest, are irrevocable until termination of this Agreement and may be exercised from time to time by Bank's officers and employees, or any of them, after and during the continuance of an Event of Default, or with respect to subsections (b), (g), (i), (j), (k) and (n) only, whether or not Debtor is in default: (a) to perform any obligation of Debtor hereunder in Debtor's name or otherwise; (b) to give notice to account debtors or others of Bank's rights in the Collateral and Proceeds, (c) to enforce or forebear from enforcing the Debtor's rights with respect to account debtors or others of Bank's rights in the Collateral and Proceeds and to make extension or modification agreements with respect thereto; (d) to release persons liable on Proceeds and to give receipts and acquittances and compromise disputes in connection therewith; (e) to release or substitute security; (f) to resort to security in any order; (g) to prepare, execute, file, record or deliver notes, assignments, schedules, designation statements, financing statements, continuation statements, termination statements, statements of assignment, applications for registration or like papers to perfect, preserve or release Bank's interest in the Collateral and Proceeds; (h) to receive, open and read mail addressed to Debtor; (i) to take cash, instruments for the payment of money and other property to which Bank is entitled; (j) to verify facts concerning the Collateral and Proceeds by inquiry of obligors thereon, or otherwise, in its own name or a fictitious name; (k) to endorse, collect, deliver and receive payment under instruments for the payment of money constituting or relating to Proceeds; (l) to prepare, adjust, execute, deliver and receive payment under insurance claims, and to collect and receive payment of and endorse any instrument in payment of loss or returned premiums or any other insurance refund or return, and to apply such amounts received by Bank, at Bank's sole option, toward repayment of the Indebtedness or replacement of the Collateral; (m) to exercise all rights, powers and remedies which Debtor would have, but for this Agreement, with respect to all Collateral and Proceeds subject hereto; (n) to enter onto Debtor's premises in inspecting the Collateral; (o) to make withdrawals from and to close deposit accounts or other accounts with any financial institution, wherever located, into which Proceeds may have been deposited, and to apply funds so withdrawn to payment of the Indebtedness; (p) to preserve or release the interest evidenced by chattel paper to which Bank is entitled hereunder and to endorse and deliver any evidence of title incidental thereto; and (q) to do all acts and things and execute all documents in the name of Debtor or otherwise, deemed by Bank as necessary, proper and convenient in connection with the preservation, perfection or enforcement of its rights hereunder.

8. PAYMENT OF PREMIUMS, TAXES, CHARGES, LIENS AND ASSESSMENTS. Debtor agrees to pay, prior to delinquency, all insurance premiums, taxes, charges, liens and assessments against the Collateral and Proceeds, and upon the failure of Debtor to do so, Bank at its option may pay any of them and shall be the sole judge of the legality or validity thereof and the amount necessary to discharge the same. Any such payments made by Bank shall be obligations of Debtor to Bank, due and payable immediately upon demand, together with interest at a rate determined in accordance with the provisions of this Agreement, and shall be secured by the Collateral and Proceeds, subject to all terms and conditions of this Agreement.

9. EVENTS OF DEFAULT. The occurrence of any of the following shall constitute an "Event of Default" under this Agreement: (a) any default in the payment or performance of any obligation, or any defined event of default, under (i) any contract or instrument evidencing any Indebtedness, or (ii) any other agreement between Debtor and Bank, including without limitation any loan agreement, relating to or executed in connection with any Indebtedness; (b) any representation or warranty made by Debtor herein shall prove to be incorrect, false or misleading in any material respect when made; (c) Debtor shall fail to observe or perform any obligation or agreement contained herein; (d) any impairment of the rights of Bank in any Collateral or Proceeds or any attachment or like levy on any property of Debtor; and (e) Bank, in good faith, believes any material portion or all of the Collateral and/or Proceeds to be in danger of misuse, dissipation, commingling, loss, theft, damage or destruction, or otherwise in jeopardy or unsatisfactory in character or value.

10. REMEDIES. Upon the occurrence of any Event of Default, Bank shall have the right to declare immediately due and payable all or any Indebtedness secured hereby and to terminate any commitments to make loans or otherwise extend credit to Debtor. Bank shall have all other rights, powers, privileges and remedies granted to a secured party upon default under the California Uniform Commercial Code or otherwise provided by law, including without limitation, the right (a) to contact all persons obligated to Debtor on any Collateral or Proceeds and to instruct such persons to deliver all Collateral and/or Proceeds directly to Bank, and (b) to sell, lease, license or otherwise dispose of any or all Collateral. All rights, powers, privileges and remedies of Bank shall be cumulative. No delay, failure or discontinuance of Bank in exercising any right, power, privilege or remedy hereunder shall affect or operate as a waiver of such right, power, privilege or remedy; nor shall any single or partial exercise of any such right, power, privilege or remedy preclude, waive or otherwise affect any other or further exercise thereof or the exercise of any other right, power, privilege or remedy. Any waiver, permit, consent or approval of any kind by Bank of any default hereunder, or any such waiver of any provisions or conditions hereof, must be in writing and shall be effective only to the extent set forth in writing. It is agreed that public or private sales or other dispositions, for cash or on credit, to a wholesaler or retailer or investor, or user of property of the types subject to this Agreement, or public auctions, are all commercially reasonable since differences in the prices generally realized in the different kinds of dispositions are ordinarily offset by the differences in the costs and credit risks of such dispositions.

While an Event of Default exists: (a) Debtor will deliver to Bank from time to time, as requested by Bank, current lists of all Collateral and Proceeds; (b) Debtor will not dispose of any Collateral or Proceeds except on terms approved by Bank; (c) at Bank's request, Debtor will assemble and deliver all Collateral and Proceeds, and books and records pertaining thereto, to Bank at a reasonably convenient place designated by Bank; and (d) bank may, without notice to Debtor, enter onto Debtor's premises and take possession of the Collateral. With respect to any sale by Bank of any Collateral subject to this Agreement, Debtor hereby expressly grants to Bank the right to sell such Collateral using any or all of Debtor's trademarks, trade names, trade name rights and/or proprietary labels or marks. Debtor further agrees that Bank shall have no obligation to process or prepare any Collateral for sale or other disposition.

11. DISPOSITION OF COLLATERAL AND PROCEEDS; TRANSFER OF INDEBTEDNESS. In disposing of Collateral hereunder, Bank may disclaim all warranties of title, possession, quiet enjoyment and the like. Any proceeds of any disposition of any Collateral or Proceeds, or any part thereof, may be applied by Bank to the payment of expenses incurred by Bank in connection with the foregoing, including reasonable attorneys' fees, and the balance of such proceeds may be applied by Bank toward the payment of the Indebtedness in such order of application as Bank may from time to time elect. Upon the transfer of all or any part of the Indebtedness, Bank may transfer all or any part of the Collateral or Proceeds and shall be fully discharged thereafter from all liability and responsibility with respect to any of the foregoing so transferred, and the transferee shall be vested with all rights and powers of Bank hereunder with respect to any of the foregoing so transferred; but with respect to any Collateral or Proceeds not so transferred Bank shall retain all rights, powers, privileges and remedies herein given.

12. STATUTE OF LIMITATIONS. Until all Indebtedness shall have been paid in full and all commitments by Bank to extend credit to Debtor have been terminated, the power of sale or other disposition and all other rights, powers, privileges and remedies granted to Bank hereunder shall continue to exist and may be exercised by Bank at any time and from time to time irrespective of the fact that the Indebtedness or any part thereof may have become barred by any statute of limitations, or that the personal liability of Debtor may have ceased, unless such liability shall have ceased due to the payment in full of all Indebtedness secured hereunder.

13. MISCELLANEOUS. When there is more than one Debtor named herein: (a) the word "Debtor" shall mean all or any one or more of them as the context requires; (b) the obligations of each Debtor hereunder are joint and several; and (c) until all Indebtedness shall have been paid in full, no Debtor shall have any right of subrogation or contribution, and each Debtor hereby waives any benefit of or right to participate in any of the Collateral or Proceeds or any other security now or hereafter held by Bank. Debtor hereby waives any right to require Bank to (i) proceed against Debtor or any other person, (ii) proceed against or exhaust any security from Debtor or any other person, (iii) perform any obligation of Debtor with respect to any Collateral or Proceeds, and (d) make any presentment or demand, or give any notice of nonpayment or nonperformance, protest, notice of protest, or notice of dishonor hereunder or in connection with any Collateral or Proceeds. Debtor further waives any right to direct the application of payments or security for any Indebtedness of Debtor or Indebtedness of customers of Debtor.

14. NOTICES. All notices, requests and demands required under this Agreement must be in writing, addressed to Bank at the address specified in any other loan documents entered into between Debtor and Bank and to Debtor at the address of its chief executive office (or principal residence, if applicable) specified below or to such other address as any party may designate by written notice to each other party, and shall be deemed to have been given or made as follows: (a) if personally delivered, upon delivery; (b) if sent by mail, upon the earlier of the date of receipt or 3 days after deposit in the U.S. mail, first class and postage prepaid; and (c) if sent by telecopy, upon receipt.

15. COSTS, EXPENSES AND ATTORNEYS' FEES. Debtor shall pay to Bank immediately upon demand the full amount of all payments, advances, charges, costs and expenses, including reasonable attorneys' fees (to include outside counsel fees and all allocated costs of Bank's in-house counsel), expended or incurred by Bank in exercising any right, power, privilege or remedy conferred by this Agreement or in the enforcement thereof, whether incurred at the trial or appellate level, in an arbitration proceeding or otherwise, and including any of the foregoing incurred in connection with any bankruptcy proceeding (including without limitation, any adversary proceeding, contested matter or motion brought by Bank or any other person) relating to Debtor or in any way affecting any of the Collateral or Bank's ability to exercise any of its rights or remedies with respect thereto. All of the foregoing shall be paid by Debtor with interest from the date of demand until paid in full at a rate per annum equal to the greater of ten percent (10%) or Bank's Prime Rate in effect from time to time.

16. SUCCESSORS; ASSIGNS; AMENDMENT. This Agreement shall be binding upon and inure to the benefit of the heirs, executors, administrators, legal representatives, successors and assigns of the parties, and may be amended or modified only in writing signed by Bank and Debtor.

17. SEVERABILITY OF PROVISIONS. If any provision of this Agreement shall be held to be prohibited by or invalid under applicable law, such provision shall be ineffective only to the extent of Such prohibition or invalidity, without invalidating the remainder of such provision or any remaining provisions of this Agreement.

18. GOVERNING LAW. This Agreement shall be governed by and construed in accordance with the laws of the State of California.

Debtor warrants that Debtor is an organization registered under the laws of the State of Delaware.

Debtor warrants that its chief executive office (or principal residence, if applicable) is located at the following address: **1515 S. Manchester, Anaheim, CA 92802**

Debtor warrants that the Collateral (except goods in transit) is located or domiciled at the following additional addresses: **1585 S. Manchester, Anaheim, CA 92802**

IN WITNESS WHEREOF, this Agreement has been duly executed as of **May 27, 2004**.

Iteris, Inc.

By: /s/ Jack Johnson

Title: CEO

By: /s/ Abbas Mohaddes

Title: Secretary

Exhibit 10.30

SECURITY AGREEMENT
EQUIPMENT

WELLS FARGO

1. GRANT OF SECURITY INTEREST. For valuable consideration, the undersigned **Iteris, Inc.**, or any of them ("Debtor"), hereby grants and transfers to WELLS FARGO BANKS NATIONAL ASSOCIATION ("Bank") a security interest in all goods, tools, machinery, furnishings, furniture and other equipment, now or at any time hereafter, and prior to the termination hereof, owned or acquired by Debtor, wherever located, whether in the possession of Debtor or any other person and whether located on Debtor's property or elsewhere, and all improvements, replacements, accessions and additions thereto and embedded software Included therein (collectively called "Collateral"), together with whatever is receivable or received when any of the Collateral or proceeds thereof are sold, leased, collected, exchanged or otherwise disposed of, whether such disposition is voluntary or involuntary, including without limitation, (a) all accounts, contract rights, chattel paper (whether electronic or tangible), instruments, promissory notes, documents, general intangibles, payment intangibles and other rights to payment of every kind now or at any time hereafter arising from any such sale, lease, collection, exchange or other disposition of any of the foregoing, (b) all rights to payment, including returned premiums, with respect to any insurance relating to any of the foregoing, and (c) all rights to payment with respect to any claim or cause of action effecting or relating to any of the foregoing (hereinafter called "Proceeds").

2. OBLIGATIONS SECURED. The obligations secured hereby are the payment and performance of: (a) all present and future Indebtedness of Debtor to Bank; (b) all obligations of Debtor and rights of Bank under this Agreement; and (c) all present and future obligations of Debtor to Bank of other kinds. The word "Indebtedness" is used herein in its most comprehensive sense and includes any and all advances, debts, obligations and liabilities of Debtor, or any of them, heretofore, now or hereafter made, incurred or created, whether voluntary or involuntary and however arising, whether due or not due, absolute or contingent, liquidated or unliquidated, determined or undetermined, and whether Debtor may be liable individually or jointly, or whether recovery upon such Indebtedness may be or hereafter becomes unenforceable.

3. TERMINATION. This Agreement will terminate upon the performance of all obligations of Debtor to Bank, including without limitation, the payment of all Indebtedness of Debtor to Bank, and the termination of all commitments of Bank to extend credit to Debtor. Upon termination, Bank will, at Borrower's cost and within a reasonable time period, execute (if necessary) and deliver such instruments and documents, including termination statements on form UCC-3, evidencing and acknowledging the termination of Bank's security interest in the Collateral and Bank shall deliver to Borrower any Collateral in Bank's possession.

4. OBLIGATIONS OF BANK. Bank has no obligation to make any loans hereunder. Any money received by Bank in respect of the Collateral may be deposited, at Bank's option, into a non-interest bearing account over which Debtor shall have no control, and the same shall, for all purposes, be deemed Collateral hereunder.

5. REPRESENTATIONS AND WARRANTIES. Debtor represents and warrants to Bank that: (a) Debtor's legal name is exactly as set forth on the first page of this Agreement, and all of Debtor's organizational documents or agreements delivered to Bank are complete and accurate in every respect; (b) Debtor is the owner and has possession or control of the Collateral and Proceeds; (c) Debtor has the exclusive right to grant a security interest in the Collateral and Proceeds; (d) all Collateral and Proceeds are genuine, free from liens, adverse claims, setoffs, default, prepayment, defenses and conditions precedent of any kind or character, except the lien created hereby or as otherwise agreed to by Bank, or heretofore disclosed by Debtor to Bank, in writing; (e) all statements contained herein are true and complete in all material respects; (f) no financing statement covering any of the Collateral or Proceeds, and naming any secured party other than Bank, is on file in any public office; and (g) Debtor is not in the business of selling goods of the kind included within the Collateral subject to this Agreement, and Debtor acknowledges that no sale or other disposition of any Collateral, including without limitation, any Collateral which Debtor may deem to be surplus, has been or shall be consented to or acquiesced in by Bank, except as specifically set forth in writing by Bank.

6. COVENANTS OF DEBTOR.

6.1 Debtor Agrees in general: (a) to pay indebtedness secured hereby when due; (b) to indemnify Bank against all losses, claims, demands, liabilities and expenses of every kind caused by property subject hereto; (c) to pay all costs and expenses, including reasonable attorneys' fees, incurred by Bank in the perfection and preservation of the Collateral or Bank's interest therein and/or the realization, enforcement and exercise of Bank's rights, powers and remedies hereunder; (d) to permit Bank to exercise its powers; (e) to execute and deliver such documents as Bank deems necessary to create, perfect and continue the security interests contemplated hereby; (f) not to change its name, and as applicable, its chief executive office, its principal residence or the jurisdiction in which it is organized and/or registered without giving Bank prior written notice thereof; (g) not to change the places where Debtor keeps any Collateral or Debtor's records concerning the Collateral and Proceeds without giving Bank prior written notice of the address to which Debtor is moving same; and (h) to cooperate with Bank in perfecting all security interests granted herein and in obtaining such agreements from third parties as Bank deems necessary, proper or convenient in connection with the preservation, perfection or enforcement of any of its rights hereunder.

6.2 Debtor agrees with regard to the Collateral and Proceeds, unless Bank agrees otherwise in writing: (a) that Bank is authorized to file financing statements in the name of Debtor to perfect Bank's security interest in Collateral and Proceeds; (b) to insure the Collateral with Bank named as loss payee, in form, substance and amounts, under agreements, against risks and liabilities, and with insurance companies satisfactory to Bank; (c) to operate the Collateral in accordance with all applicable statutes, rules and regulations relating to the use and control thereof, and not to use the Collateral for any unlawful purpose or in any way that would void any insurance required to be carried in connection therewith; (d) not to permit any security interest in or lien on the Collateral or Proceeds, including without limitation, liens arising from repairs to or storage of the Collateral, except in favor of Bank; (e) to pay when due all license fees, registration fees and other charges in connection with any Collateral; (f) not to remove the Collateral from Debtor's premises unless the Collateral consists of mobile goods as defined in the California Uniform Commercial Code, in which case Debtor agrees not to remove or permit the removal of the Collateral from its state of domicile for a period in excess of 30 calendar days; (g) not to sell, hypothecate or otherwise dispose of, nor permit the transfer by operation of law of, any of the Collateral or Proceeds or any interest therein; (h) not to rent, lease or charter the Collateral; (i) to permit Bank to inspect the Collateral at any time; (j) to keep, in accordance with generally accepted accounting principles, complete and accurate records regarding all Collateral and Proceeds, and to permit Bank to inspect the same and make copies thereof at any reasonable time; (k) if requested by Bank, to receive and use reasonable diligence to collect Proceeds, in trust and as the property of Bank, and to Immediately endorse as appropriate and deliver such Proceeds to Bank daily in the exact form in which they are received together with a collection report in form satisfactory to Bank; (l) not to commingle Proceeds or collections thereunder with other property; (m) to give only normal allowances and credits and to advise Bank thereof immediately in writing if they affect any Collateral or Proceeds in any material respect; (n) in the event Bank elects to receive payments of Proceeds hereunder, to pay all expenses incurred by Bank in connection therewith, including expenses of accounting, correspondence, collection efforts, reporting to account or contract debtors, filing, recording, record keeping and expenses incidental thereto; and (o) to provide any service and do any other acts which may be necessary to maintain, preserve and protect all Collateral and, as appropriate and applicable, to keep the Collateral in good and saleable condition and repair, to deal with the Collateral in accordance with the standards and practices adhered to generally by owners of like property, and to keep all Collateral and Proceeds free and clear of all defenses, rights of offset and counterclaims.

7. Debtor appoints Bank its true attorney-in-fact to perform any of the following powers, which are coupled with an interest, are irrevocable until termination of this Agreement and may be exercised from time to time by Bank's officers and employees, or any of them, after and during the continuance of an Event of Default, or with respect to subsections (b), (g), (i), (j), (k) and (n) only, whether or not Debtor is in

default: (a) to perform any obligation of Debtor hereunder in Debtor's name or otherwise; (b) to give notice to account debtors or others of Bank's rights in the Collateral and Proceeds, (c) to enforce or forebear from enforcing the Debtor's rights with respect to account debtors or others of Bank's rights in the Collateral and Proceeds and to make extension or modification agreements with respect thereto; (d) to release persons liable on Proceeds and to give receipts and acquittances and compromise disputes in connection therewith; (e) to release or substitute security; (f) to resort to security in any order; (g) to prepare, execute, file, record or deliver notes, assignments, schedules, designation statements, financing statements, continuation statements, termination statements, statements of assignment, applications for registration or like papers to perfect, preserve or release Bank's interest in the Collateral and Proceeds; (h) to receive, open and read mail addressed to Debtor; (i) to take cash, instruments for the payment of money and other property to which Bank is entitled; (j) to verify facts concerning the Collateral and Proceeds by inquiry of obligors thereon, or otherwise, in its own name or a fictitious name; (k) to endorse, collect, deliver and receive payment under instruments for the payment of money constituting or relating to Proceeds; (l) to prepare, adjust, execute, deliver and receive payment under insurance claims, and to collect and receive payment of and endorse any instrument in payment of loss or returned premiums or any other insurance refund or return, and to apply such amounts received by Bank, at Bank's sole option, toward repayment of the Indebtedness or replacement of the Collateral; (m) to exercise all rights, powers and remedies which Debtor would have, but for this Agreement, with respect to all Collateral and Proceeds subject hereto; (n) to enter onto Debtor's premises in inspecting the Collateral; (o) to preserve or release the interest evidenced by chattel paper to which Bank is entitled hereunder and to endorse and deliver any evidence of title incidental thereto; and (p) to do all acts and things and execute all documents in the name of Debtor or otherwise, deemed by Bank as necessary, proper and convenient in connection with the preservation, perfection or enforcement of its rights hereunder.

8. PAYMENT OF PREMIUMS, TAXES, CHARGES, LIENS AND ASSESSMENTS. Debtor agrees to pay, prior to delinquency, all insurance premiums, taxes, charges, liens and assessments against the Collateral and Proceeds, and upon the failure of Debtor to do so, Bank at its option may pay any of them and shall be the sole judge of the legality or validity thereof and the amount necessary to discharge the same. Any such payments made by Bank shall be obligations of Debtor to Bank, due and payable immediately upon demand, together with interest at a rate determined in accordance with the provisions of this Agreement, and shall be secured by the Collateral and Proceeds, subject to all terms and conditions of this Agreement.

9. EVENTS OF DEFAULT. The occurrence of any of the following shall constitute an "Event of Default" under this Agreement: (a) any default in the payment or performance of any obligation, or any defined event of default, under (i) any contract or instrument evidencing any Indebtedness, or (ii) any other agreement between Debtor and Bank, including without limitation any loan agreement, relating to or executed in connection with any indebtedness; (b) any representation or warranty made by Debtor herein shall prove to be incorrect, false or misleading in any material respect when made; (c) Debtor shall fail to observe or perform any obligation or agreement contained herein; (d) any impairment of the rights of Bank in any Collateral or Proceeds or any attachment or like levy on any property of Debtor; and (e) Bank, in good faith, believes any material portion or all of the Collateral and/or Proceeds to be in danger of misuse, dissipation, commingling, loss, theft, damage or destruction, or otherwise in jeopardy or unsatisfactory in character or value.

10. REMEDIES. Upon the occurrence of any Event of Default, Bank shall have the right to declare immediately due and payable all or any Indebtedness secured hereby and to terminate any commitments to make loans or otherwise extend credit to Debtor. Bank shall have all other rights, powers, privileges and remedies granted to a secured party upon default under the California Uniform Commercial Code or otherwise provided by law, including without limitation, the right (a) to contact all persons obligated to Debtor on any Collateral or Proceeds and to instruct such persons to deliver all Collateral and/or Proceeds directly to Bank, and (b) to sell, lease, license or otherwise dispose of any or all Collateral. All rights, powers, privileges and remedies of Bank shall be cumulative. No delay, failure or discontinuance of Bank in exercising any right, power, privilege or remedy hereunder shall affect or operate as a waiver of such right, power, privilege or remedy; nor shall any single or partial exercise of any such right, power, privilege or remedy preclude, waive or otherwise affect any other or further exercise thereof or the

exercise of any other right, power, privilege or remedy. Any waiver, permit, consent or approval of any kind by Bank of any default hereunder, or any such waiver of any provisions or conditions hereof, must be in writing and shall be effective only to the extent set forth in writing. It is agreed that public or private sales or other dispositions, for cash or on credit, to a wholesaler or retailer or investor, or user of property of the types subject to this Agreement, or public auctions, are all commercially reasonable since differences in the prices generally realized in the different kinds of dispositions are ordinarily offset by the differences in the costs and credit risks of such dispositions.

While an Event of Default exists: (a) Debtor will deliver to Bank from time to time, as requested by Bank, current lists of all Collateral and Proceeds; (b) Debtor will not dispose of any Collateral or Proceeds except on terms approved by Bank; (c) at Bank's request, Debtor will assemble and deliver all Collateral and Proceeds, and books and records pertaining thereto, to Bank at a reasonably convenient place designated by Bank; and (d) Bank may, without notice to Debtor, enter onto Debtor's premises and take possession of the Collateral. Debtor further agrees that Bank shall have no obligation to process or prepare any Collateral for sale or other disposition.

11. DISPOSITION OF COLLATERAL AND PROCEEDS; TRANSFER OF INDEBTEDNESS. In disposing of Collateral hereunder, Bank may disclaim all warranties of title, possession, quiet enjoyment and the like. Any proceeds of any disposition of any Collateral or Proceeds, or any part thereof, may be applied by Bank to the payment of expenses incurred by Bank in connection with the foregoing, including reasonable attorneys' fees, and the balance of such proceeds may be applied by Bank toward the payment of the indebtedness in such order of application as Bank may from time to time elect. Upon the transfer of all or any part of the Indebtedness, Bank may transfer all or any part of the Collateral or Proceeds and shall be fully discharged thereafter from all liability and responsibility with respect to any of the foregoing so transferred, and the transferee shall be vested with all rights and powers of Bank hereunder with respect to any of the foregoing so transferred; but with respect to any Collateral or Proceeds not so transferred Bank shall retain all rights, powers, privileges and remedies herein given.

12. STATUTE OF LIMITATIONS. Until all Indebtedness shall have been paid in full and all commitments by Bank to extend credit to Debtor have been terminated, the power of sale or other disposition and all other rights, powers, privileges and remedies granted to Bank hereunder shall continue to exist and may be exercised by Bank at any time and from time to time irrespective of the fact that the Indebtedness or any part thereof may have become barred by any statute of limitations, or that the personal liability of Debtor may have ceased, unless such liability shall have ceased due to the payment in full of all Indebtedness secured hereunder.

13. MISCELLANEOUS. When there is more than one Debtor named herein: (a) the word "Debtor" shall mean all or any one or more of them as the context requires; (b) the obligations of each Debtor hereunder are joint and several; and (c) until all Indebtedness shall have been paid in full, no Debtor shall have any right of subrogation or contribution, and each Debtor hereby waives any benefit of or right to participate in any of the Collateral or Proceeds or any other security now or hereafter held by Bank. Debtor hereby waives any right to require Bank to (i) proceed against Debtor or any other person, (ii) proceed against or exhaust any security from Debtor or any other person, (iii) perform any obligation of Debtor with respect to any Collateral or Proceeds, and (d) make any presentment or demand, or give any notice of nonpayment or nonperformance, protest, notice of protest or notice of dishonor hereunder or in connection with any Collateral or Proceeds. Debtor further waives any right to direct the application of payments or security for any Indebtedness of Debtor or indebtedness of customers of Debtor.

14. NOTICES. All notices, requests and demands required under this Agreement must be in writing, addressed to Bank at the address specified in any other loan documents entered into between Debtor and Bank and to Debtor at the address of its chief executive office (or principal residence, if applicable) specified below or to such other address as any party may designate by written notice to each other party, and shall be deemed to have been given or made as follows: (a) if personally delivered, upon delivery; (b) if sent by mail, upon the earlier of the date of receipt or 3 days after deposit in the U.S. mail, first class and postage prepaid; and (c) if sent by telecopy, upon receipt.

15. COSTS, EXPENSES AND ATTORNEYS' FEES. Debtor shall pay to Bank immediately upon demand the full amount of all payments, advances, charges, costs and expenses, including reasonable attorneys' fees (to include outside counsel fees and all allocated costs of Bank's in-house counsel), expended or incurred by Bank in exercising any right, power, privilege or remedy conferred by this Agreement or in the enforcement thereof, whether incurred at the trial or appellate level, in an arbitration proceeding or otherwise, and including any of the foregoing incurred in connection with any bankruptcy proceeding (including without limitation, any adversary proceeding, contested matter or motion brought by Bank or any other person) relating to Debtor or in any way affecting any of the Collateral or Bank's ability to exercise any of its rights or remedies with respect thereto. All of the foregoing shall be paid by Debtor with interest from the date of demand until paid in full at a rate per annum equal to the greater of ten percent (10%) or Bank's Prime Rate in effect from time to time.

16. SUCCESSORS; ASSIGNS; AMENDMENT. This Agreement shall be binding upon and inure to the benefit of the heirs, executors, administrators, legal representatives, successors and assigns of the parties, and may be amended or modified only in writing signed by Bank and Debtor.

17. SEVERABILITY OF PROVISIONS. If any provision of this Agreement shall be held to be prohibited by or invalid under applicable law, such provision shall be ineffective only to the extent of such prohibition or invalidity, without invalidating the remainder of such provision or any remaining provisions of this Agreement.

18. GOVERNING LAW. This Agreement shall be governed by and construed in accordance with the laws of the State of California.

Debtor warrants that Debtor is an organization registered under the laws of the State of Delaware.

Debtor warrants that its chief executive office (or principal residence, if applicable) is located at the following address: **1515 S. Manchester, Anaheim, CA 92802**

Debtor warrants that the Collateral (except goods in transit) is located or domiciled at the following additional addresses: **1585 S. Manchester, Anaheim, CA 92802**

IN WITNESS WHEREOF, this Agreement has been duly executed as of **May 27, 2004**.

Iteris, Inc.

By: /s/ Jack Johnson

Title: CEO

By: /s/ Abbas Mohaddes

Title: Secretary

Exhibit 10.31

ITERIS, INC.
Deferred Compensation Savings Plan

ITERIS, INC.

Deferred Compensation Savings Plan

This Deferred Compensation Savings Plan (hereinafter referred to as the "Plan") has been adopted by the board of directors of Iteris, Inc. (hereinafter referred to as the "Employer"), effective as of March 29, 2002.

1. Purpose

The purpose of the Plan is to provide supplemental retirement income and death benefits for certain Executives (hereinafter defined).

2. Definitions

The following definitions, set forth in alphabetical order, are used throughout the Plan. Whenever words or phrases have initial capital letters in the Plan, a special definition for those words or phrases is set forth below.

(a) "Beneficiary" means the person, persons or entity designated in writing by the Participant on forms provided by the committee to receive distribution of certain death benefits under the Plan in the event of the Participant's death. A Participant may change the designated Beneficiary from time to time by filing a new written designation with the Committee, and such designation shall be effective upon receipt by the Committee. The designation of a Beneficiary other than the Participant's spouse, must be consented to in writing by the spouse. If a Participant has not designated a Beneficiary, or if a designated Beneficiary is not living or in existence at the time of a Participant's death, any death benefits payable under the Plan shall be paid to the Participant's spouse, if then living, and if the Participant's spouse is not then living, to the Participant's estate.

(b) "Benefit Agreement" means a benefit agreement described in Section 8(a) relating to a Participant Deferral election.

(c) "Board of Directors" means the board of directors of the Employer.

(d) "Code" means the Internal Revenue Code of 1986.

(e) "Committee" means the Committee appointed by the Board of Directors to administer the Plan.

(f) "Covered Compensation" means annual salary and cash bonuses, but excluding any other form of remuneration.

(g) "Deferral" means the portion of a Participant's Covered Compensation that has been deferred in accordance with Section 3.

(h) "Disabled" means permanently unable to perform substantially all the material duties of his regular job because of disease or bodily injury originating after March 29, 2002.

(i) "Distributable Event" means the date upon which the Participant terminates employment with the Employer, dies or becomes Disabled.

(j) "ERISA" means the Employee Retirement Income Security Act of 1974, as amended.

(k) "Executive" means a management or highly-compensated employee of the Employer who has been specifically designated, by the Board of Directors or the Committee, as eligible to participate in the Plan.

(l) "Participant" means an Executive who has made a written election to participate in the Plan in accordance with Section 3(a).

(m) "Plan Year" means the calendar year.

(n) "Trust" means the Iteris Deferred Compensation Savings Trust.

3. Deferrals

(a) Commencement of Deferrals:

An Executive shall become a Participant hereunder upon execution by the Participant and the Committee of a Benefit Agreement. The Benefit Agreement will set forth the amount of Deferrals elected by the Executive. Participants can change the amount of their Deferrals at any time with a new Benefit Agreement. Each Benefit Agreement will become effective with the next payroll period after execution.

(b) Duration of Deferrals:

A Participant may continue to make Deferrals until his designation as an Executive is revoked by the Board of Directors (in which event he shall be treated as a terminated Participant) or he terminates employment with the Employer.

(c) Limitation on Deferrals:

Participants may only elect Deferrals if they have elected the maximum amount of deferrals under the Employer's Code Section 401(k) plan. Participants may not elect Deferrals in excess of fifty percent (50%) of regular salary, and one hundred percent (100%) of any bonuses, in any Plan Year.

(d) Time and Manner of Payment:

Each Participant Deferral hereunder shall be withheld by the Employer from the Participant's Covered Compensation and contributed into the Trust within forty-five (45) days of each such Deferral. Deferrals from regular salary compensation shall be taken pro rata from such Covered Compensation for the payroll period selected by Employer during the Plan Year. Deferrals from any bonus sums shall be taken from the bonus payment when it is paid to the Participant. Deferrals will cease upon the occurrence of a Distributable Event.

(e) No Employer Contributions:

No Employer contributions shall be made under this Plan.

4. Participant Benefits

(a) A Participant shall be entitled to receive, in accordance with the method of payout elected under Section 4(c), the entire balance of his subtrust within the Trust at the time of a Distributable Event other than his death.

(b) A Participant's Beneficiary shall be entitled to receive, in accordance with the method of payout elected under Section 4(c), the entire balance of the Participant's subtrust within the Trust as of the date of the Participant's death.

(c) Distribution of the benefit shall be as follows:

(i) two substantially equal lump sum payments, with the first such payment made on the date which is sixty (60) days after the Distributable Event and with the second such payment made on the date which is four hundred twenty seven (427) days after the Distributable Event; or

(ii) a series of sixty (60) equal monthly payments; or

(iii) a series of one hundred twenty (120) equal monthly payments.

A Participant's election regarding the manner of payment under the Plan shall be made as part of his Benefit Agreement. This election shall remain in effect unless and until the Participant delivers an amended election; an amended election shall apply to distributions of benefits for Distributable Events occurring at least six (6) months after the date on which the amended election is delivered to the Employer.

5. Hardship Withdrawal

At any time prior to a Distributable Event, a Participant may request the Committee to make a distribution to him from his subtrust within the Trust within thirty days. Such distribution shall be made only if the Committee determines that the Participant is suffering from a financial hardship that cannot be satisfied by his normal sources of income. In making this determination, the Committee shall utilize the regulations adopted by the Treasury pursuant to Section 401(k) of the Code. Only the amount necessary to ameliorate the hardship may be withdrawn.

6. Limited Withdrawal Right

At any time prior to a Distributable Event, a Participant may request the Committee to make a distribution to him from his subtrust within the Trust (within 10 business days) of the entire balance of his subtrust within the Trust, less any gains incurred in such subtrust (other than Deferrals) during the period commencing with the first day of the month coincident with or immediately preceding the date 12 months before the date of such distribution, and ending an the date of such distribution ("12 months of earnings"). The Participant will forfeit such 12 months of earnings, which the Trustee shall distribute as soon as practical to be Employer. Each Participant may exercise this limited withdrawal right only once.

7. Vesting of Benefits

Except as provided in Section 6, a Participant shall be 100% vested in his subtrust within the Trust at all times.

8. Additional Provisions

(a) Benefit Agreement:

The Committee will provide to each Executive a form of Benefit Agreement which will permit the Executive to make Deferrals, which will set forth the Executive's acceptance of the benefits provided hereunder, his agreement to be bound by the terms of the Plan and the Trust and such other matters as are set forth in this Plan or deemed advisable by the Committee.

(b) Withholding:

Benefit payments hereunder shall be subject to applicable federal, state or local withholding laws.

(c) Funding of Benefits:

The benefits shall be funded through the Trust. Notwithstanding the foregoing, to the extent that any amounts are withdrawn from the Trust for purposes other than the provision of benefits hereunder, such amounts shall become the direct obligation of the Employer to pay to the Participant (or Beneficiary) in the form of benefits hereunder. As to such amounts, the Participant (or Beneficiary) shall have the status of a general unsecured creditor of the Employer.

9. Administration of the Plan

(a) The Committee:

The Committee shall administer the Plan and shall keep a written record of its action and proceedings regarding the Plan and all dates, records and documents relating to its administration of the Plan.

The Committee is authorized to interpret the Plan, to make, amend and rescind such rules as it deems necessary for the proper administration of the Plan, to make all other determinations necessary or advisable for the administration of the Plan and to correct any defect or supply any omission or reconcile any inconsistency in the Plan in the manner and to the extent that the Committee deems desirable to carry the Plan into effect. The powers and duties of the Committee shall include, without limitation, the following:

(i) Resolving all questions relating to the eligibility of Executives to become Participants;

(ii) Determining the amount of benefits payable to Participants or their Beneficiaries and authorizing and directing the Employer and Trustee with respect to the payment of benefits under the Plan.

(iii) Construing and interpreting the Plan whenever necessary to carry out its intention and purpose and making and publishing such rules for the regulation of the Plan as are not inconsistent with the terms of the Plan.

(iv) Compiling and maintaining all records it determines to be necessary, appropriate or convenient in connection with the administration of the Plan; and

(v) Engaging any administrative, legal, medical, accounting, clerical, or other services it may deem appropriate to effectuate the Plan.

Any action taken or determination made by the Committee shall, except as otherwise provided in Section 10 below, be conclusive on all parties. No members of the Committee shall vote on any matter affecting such member.

(b) Expenses of the Committee:

The expenses of the Committee properly and actually incurred in the performance of its duties under the Plan shall be paid equally by Employer.

(c) Bonding and Compensation:

The members of the Committee shall serve without bond, and without compensation for their services as Committee members except as the Employer may provide in its discretion.

(d) Information to be Submitted to the Committee:

To enable the Committee to perform its functions, the Employer shall supply full and timely information to the Committee on all matters relating to Executives and Participants as the committee may require, and shall maintain such other records as the Committee may determine are necessary in order to determine the benefits due or which may become due to Participants or their Beneficiaries under the Plan. The Committee may rely on such records as conclusive with respect to the matters set forth therein.

(e) Notices, Statements and Reports:

The Employer shall be the "administrator" of the Plan as defined in Section 3(16)(A) of ERISA for purposes of the reporting and disclosure requirements imposed by ERISA and the Code.

(f) Service of Process:

The Committee may from time to time designate an agent of the Plan for the service of legal process. The committee shall cause such agent to be identified in materials it distributes or causes to be distributed when such identification is required under applicable law. In the absence of such a designation, the Employer shall be the agent of the Plan for the service of legal process.

(g) Insurance:

The Employer, in its discretion, may obtain, pay for and keep current a policy or policies of insurance insuring the Committee members, the members of the Board of Directors and other employees to whom any responsibility with respect to the administration of the Plan has been delegated, against any and all costs, expenses and liabilities (including attorneys' fees) incurred by such persons as a result of any act, or omission to act, in connection with the performance of their duties, responsibilities, and obligations under the Plan and any applicable law.

(h) Indemnity:

If the Employer does not obtain, pay for and keep current the type of insurance policy or policies referred to in subsection (g), or if such insurance is provided but any of the parties referred to in subsection (g) incur any costs or expenses which are not covered under such policies, then the Employer shall indemnify and hold harmless, to the extent permitted by law, such parties against any and all costs, expenses and liabilities (including attorneys' fees) incurred by such parties in performing their duties and responsibilities under this Plan, provided that such party or parties were not guilty of willful misconduct. In the event that such party is named as a defendant in a lawsuit or proceeding involving the Plan, the party shall be entitled to receive on a current basis the indemnity payments provided for in this subsection, provided however that if the final judgment entered in the lawsuit or proceeding holds that the party is guilty of willful misconduct with respect to the Plan, the party shall be required to refund the indemnity payments that it has received.

10. Claims Procedure

(a) Filing Claim for Benefits:

If a Participant or Beneficiary (hereinafter referred to as the "Applicant") does not receive the timely payment of the benefits which the Applicant believes are due under the plan, the Applicant may make a claim for benefits in the manner hereinafter provided.

All claims for benefits under the Plan shell be made in writing and shall be signed by the Applicant. Claims shall be submitted to a representative designated by the Committee and hereinafter referred to as the "Claims Coordinator," The Claims Coordinator may, but need not, be a member of the Committee. If the Applicant does not furnish sufficient information with the claim for the Claims Coordinator to determine the

validity of the claim, the Claims Coordinator shall indicate to the Applicant any additional information which is necessary for the Claims Coordinator to determine the validity of the claim.

Each claim hereunder shall be acted on and approved or disapproved by the Claims Coordinator within 90 days following the receipt by the Claims Coordinator of the information necessary to process the claim.

In the event the Claims Coordinator denies a claim for benefits in whole or in part, the Claims Coordinator shall notify the Applicant in writing of the denial of the claim and notify the Applicant of his right to a review of the Claims Coordinator's decision by the Committee. Such notice by the Claims Coordinator shall also set forth, in a manner calculated to be understood by the Applicant, the specific denial, the specific provisions of the Plan or Agreement on which the denial is based, a description of any additional material or information necessary to perfect the claim with an explanation of why such material or information is necessary, and an explanation of the Plan's appeals procedure as set forth in this section.

If no action is taken by the Claims Coordinator on an Applicant's claim within 90 days after receipt by the Claims Coordinator, such claim shall be deemed to be denied for purposes of the following appeals procedure.

(b) Appeals Procedure:

Any Applicant whose claim for benefits is denied in whole or in part may appeal from such denial to the Committee for a review of the decision by the Committee. Such appeal must be made within three months after the Applicant has received actual or constructive notice of the denial as provided above. An appeal must be submitted in writing within such period and must:

(i) Request a review by the Committee of the claim for benefits under the Plan;

(ii) Set forth all of the grounds upon which the Applicant's request for review is based and any facts in support thereof; and

(iii) Set forth any issues or comments which the Applicant deems pertinent to the appeal.

The committee shall regularly review appeals by Applicants. The Committee shall act upon each appeal within 60 days after receipt thereof unless special circumstances require an extension of the time for processing, in which case a decision shall be rendered by the Committee as soon as possible but not later than 90 days after the last documentation is received by the Committee.

The committee shall make full and fair review of each appeal and any written materials submitted by the Applicant in connection therewith. The Committee may require the Applicant to submit such additional facts, documents or other evidence as the Committee in its discretion deems necessary or advisable in making its review. The Applicant shall be given the opportunity to review pertinent documents or materials upon submission of a written request to the committee, provided the Committee finds the requested documents or materials are pertinent to the appeal.

On the basis of its review, the Committee shall make an independent determination of the Applicant's eligibility for benefits under the Plan. The decision of the committee on any claim for benefits shall be final and conclusive upon all parties thereto.

In the event the Committee denies an appeal in whole or in part, the Committee shall give written notice of the decision to the Applicant, which notice shall set forth, in a manner calculated to be understood by the Applicant, the specific reasons for such denial and which shall make specific reference to the pertinent provisions of the Plan on which the Committee's decision is based.

(c) Exhaustion of Remedy:

No action may be brought for benefits or to enforce any rights hereunder until after the Applicant has exhausted his administrative remedies under this section.

11. Amendment or Termination

The Plan may be amended or terminated by the Board of Directors at any time. Such amendment or termination may modify or eliminate any benefit hereunder other than a benefit that is vested.

12. Miscellaneous

(a) Participant Rights:

Nothing in the Plan shall confer upon a Participant the right to continue in the employ of the Employer or shall limit or restrict the right of the Employer to terminate the employment of a Participant at any time with or without cause.

(b) Alienation:

Except as otherwise provided in the Plan, no right or benefit under the Plan shall be subject to anticipation, alienation, sale, assignment, pledge, encumbrance or charge, and any attempt to anticipate, alienate, sell, assign, pledge, encumber or charge such right or benefit shall be void. No such right or benefit shall in any manner be liable for or subject to the debts, liability or torts of a Participant or Beneficiary.

(c) Partial Invalidity:

If any provision in the Plan is held by a court of competent jurisdiction to be invalid, void or unenforceable, the remaining provisions shall nevertheless continue to be in full force and effect without being impaired or invalidated in any way.

(d) Choice of Law:

The Plan shall be construed in accordance with ERISA and the laws of the State of California.

(e) Payment to Minors or Persons Under Legal Disability :

If any benefit becomes payable to a minor or to a person under a legal disability, payment of such benefit shall be made only to the conservator or the guardian of the estate of such intended recipient appointed by a court of competent jurisdiction or any other individual or institution maintaining or having custody of such intended recipient. A release by such conservator, guardian, individual or institution shall constitute a legal discharge of the Plan's obligation to the intended recipient.

(f) Spouse's Interest:

The interest in the benefits hereunder of a spouse of a Participant who has predeceased the Participant shall automatically pass to the Participant and shall not be transferable by such spouse in any manner including not limited to such spouse's will, nor shall such interest pass under the laws of intestate succession.

(g) Successors:

In the event of any consolidation, merger, acquisition or reorganization of the Employer, the obligations of the Employer under this Plan shall continue and be binding upon the Employer and successors.

(h) Gender, Tense and Headings:

Whenever any words are used herein in the masculine gender, they shall be construed as though they were also used in the feminine gender in all cases where they would so apply. Whenever any words used herein are in the singular form, they shall be construed as though they were also used in the plural form in all cases where they would so apply. Headings of sections and subsections as used herein are inserted solely for convenience and reference and constitute no part of the Plan.

Executed at Anaheim, California this 29th day of March 2002.

ITERIS, INC.

By /s/ Jack Johnson

Jack Johnson,
President

GRANTOR TRUST

FOR

ITERIS, INC.

ITERIS, INC. DEFERRED COMPENSATION SAVINGS TRUST

This Trust Agreement made this 31st day of March, 2002 by and between Iteris, Inc., a Delaware corporation (the "Company") and First American Trust, FSB (the "Trustee");

WHEREAS, the Company has entered into the plan or plans designated in Exhibit A hereto (referred to together herein as the "Plan" pursuant to which the Company has agreed to provide participants in the Plan (the "Participants") with certain supplemental retirement benefits;

WHEREAS, the Company has incurred or expects to incur liability under the terms of such Plan with respect to the individuals participating in such Plan;

WHEREAS, the Company wishes to establish a trust (the "Trust") and to contribute to the Trust assets that shall be held therein, subject to the claims of the Company's creditors in the event of the Company's Insolvency (as defined in Article 14 of the Trust Agreement) until paid to Plan Participants and their beneficiaries in such manner and at such times as specified in the Plan;

WHEREAS, it is the intention of the parties that this Trust shall constitute an unfunded arrangement and shall not affect the status of the Plan as an unfunded plan maintained for the purpose of providing deferred compensation for a select group of management or highly compensated employees for purposes of Title I of the Employee Retirement Income Security Act of 1974;

WHEREAS, it is the intention of the Company to make contributions to the Trust to provide itself with a source of funds to assist it in the meeting of its liabilities under the Plan;

NOW, THEREFORE, the parties do hereby establish the Trust and agree that the Trust shall be comprised, held and disposed of as follows:

ARTICLE 1

ESTABLISHMENT OF TRUST

1.1 *Contributions.*

(a) *Required Contributions.* The Company hereby deposits with the Trustee in trust the assets listed in Exhibit B to this Trust Agreement, which shall become the principal of the Trust to be held, administered and disposed of by the Trustee as provided in this Trust Agreement. On or before June fifteenth (15^{th}) of each year, the Company shall make additional deposits equal to the deferrals (or actuarially determined accruals) made under the Plan for the prior Plan Year, which amount shall be deposited with the Trustee in trust to augment the principal to be held, administered and deposited by the Trustee as provided in this Agreement.

(b) *Failure to Make Required Contributions*. In the event the Company fails to make the contributions required by Section 1.1 (a) or required to enable the Trustee to pay Plan benefits or tax payments associated therewith which are not paid directly by the Company when they become due under the terms of the Plan, such failure shall constitute a Default and shall continue

until the cure of such failure. The Company and any Plan fiduciary with actual knowledge that there has been a Default shall have the obligation to notify the Trustee of such Default. Any Plan Participant may also notify the Trustee of a Default and the Trustee shall request that the Company furnish evidence to determine, or enable the Trustee to determine, whether a Default has indeed occurred. Unless the Trustee has actual knowledge or has received notice of a Default, the Trustee shall have no duty to inquire whether a Default has occurred. In making such determination of Default, the Trustee may rely on information received from the Company, taxing authorities, qualified experts or legal counsel that provides the Trustee with a reasonable basis for making a determination that a Default has occurred. Any dispute regarding whether a Default has occurred shall be resolved as provided in Article 8. The Company may at any time cure such Default by making the required contributions or payments plus interest thereon from the date of such Default through the date of cure at the average rate credited on other Trust assets during such period. A Default shall be considered a Triggering Event for purposes of the provisions of the Trust Agreement. However, if after a Default, the Company at any time cures such Default, it shall cease to be deemed that a Triggering Event has occurred for purposes of this Trust Agreement.

1.2 *Irrevocability.* The Trust hereby established shall be irrevocable and all contributions made to the Trust shall be irrevocable regardless of whether such contributions are voluntary or required by the Trust Agreement.

1.3 *Grantor Trust.* The Trust is intended to be a grantor trust, of which the Company is the grantor, within the meaning of Subpart E, Part I, Subchapter J, Chapter 1, Subtitle A of the Internal Revenue Code of 1986, as amended, and shall be construed accordingly. The Company shall be responsible for reporting and paying any and all federal, state and local income taxes that may become due as a result of any earning or realized gain on any Trust assets. The principal of the Trust, and any earnings thereon, shall be held separate and apart from other funds of the Company and shall be used exclusively for the uses and purposes of Plan Participants and general creditors as herein set forth. Plan Participants and their beneficiaries shall have no preferred claim on, or any beneficial ownership interest in, any assets of the Trust. Any rights created under the Plan and this Trust Agreement shall be mere unsecured contractual rights of Plan Participants and their beneficiaries against the Company. Any assets held by the Trust will be subject to the claims of the Company's general creditors under federal and state law in the event of Insolvency, as defined in Section 3.1 herein.

1.4 *Establishment of Subtrusts.* At the written direction of the Company, the Trustee shall establish separate subtrusts for separate Plans or groups of Participants covered by the Trust. At the discretion of the Company, such subtrusts may reflect a segregation of particular assets or may reflect an undivided interest in the assets of the Trust, not requiring any segregation of assets. If a Triggering Event occurs, the Trustee shall establish a separate subtrust for all then-existing Participants in the Plan (or, at the written direction of either the Company or the Participant Committee, for each Participant in the Plan who is covered by the Trust). The subtrust established for all then-existing Participants upon a Triggering Event shall require segregation of particular assets. However, individual subtrusts established for each Participant may reflect an undivided interest in the assets of the subtrust for all then-existing Participants and shall not require segregation of particular assets among particular individual subtrusts. Whenever separate subtrusts are established, the then-existing assets of the Trust or affected portion thereof shall be allocated, as directed by the Company or after a Triggering Event by the Participant Committee, in proportion

to the vested accrued benefits, and, then, if any assets remain, the unvested (if any) accrued benefits of the Participants affected thereby, in both instances as of the end of the month immediately preceding such allocation. With respect to any new contributions to the Trust by the Company after separate subtrusts have been established, the Company shall designate the subtrust for which such contributions are made. Except as provided in Section 4.1 herein, after separate subtrusts are established, assets allocated to one subtrust may not be utilized to provide benefits under any other subtrust until all benefits payable under such subtrust have been paid in full. Payments to general creditors in the event of the Company becoming Insolvent shall be charged against the subtrusts in proportion to their account balances, except that payment of benefits to a Participant as a general creditor shall be charged against the subtrust for that Participant.

1.5 *Signing Authority.* The Company shall certify in writing to the Trustee the names and specimen signatures of all those who are authorized to act as or on behalf of the Company (and after a Triggering Event the Participant Committee), and those names and specimen signatures shall be updated as necessary by a duly authorized officer of the Company. The Company shall promptly notify the Trustee if any person so designated is no longer authorized to act on behalf of the Company. Until the Trustee receives written notice that a person is no longer authorized to act on behalf of the Company, the Trustee may continue to rely on the prior designation of such person.

ARTICLE 2

PAYMENTS TO PLAN PARTICIPANTS AND THEIR BENEFICIARIES

2.1 *Benefit Payments Directed by the Company.* Prior to a Triggering Event, the Company Shall direct the Trustee with respect to the amount and timing of any payment to be made to Plan Participants or their beneficiaries. The Company may appoint an Agent to direct the Company with respect to the amount and timing of such payments. After a Triggering Event, the Participant Committee shall be responsible for directing the Trustee with respect to the amount and timing of any payments to Plan Participants and their beneficiaries. The Participant Committee may approve the continued appointment of the Agent previously appointed by the Company or may appoint a new Agent to act on its behalf in directing the Trustee with respect to the amount and timing of payments from the Trust. The Trustee shall have no duty or responsibility to supervise the Company, Agent or Participant Committee regarding payments to be made to Plan Participants or their beneficiaries under the Trust.

2.2 *Direct Payment by the Company.* The Company may make payments of benefits directly to Plan Participants or their beneficiaries as they become due under the terms of the Plan and may obtain reimbursement for such benefit payments from the Trust (or offset required contributions to the Trust) within twelve (12) months following the date such payments are made. In addition, if the principal of the Trust, and any earnings thereon, are not sufficient to make payments of benefits in accordance with the terms of the Plan, the Company shall make the balance of each such payment as it falls due. The Trustee shall notify the Company when principal and earnings are not sufficient to make payments the Trustee has been directed to make by the Company, the Agent or the Participant Committee.

2.3 *Tax Reporting and Withholding Requirements.* The Company shall direct the Trustee to make provisions for reporting and withholding of any federal, state or local taxes that may be required to be withheld with respect to the payment of benefits by the Trustee pursuant to the terms of the Plan and to pay amounts withheld to the Company for remittance to the appropriate taxing authorities. The Company shall have the responsibility for reporting and withholding of all federal, state or local taxes required to be withheld with respect to such payments and for paying such amounts withheld to the appropriate taxing authorities. The Trustee shall have no duty or responsibility with respect to the reporting and withholding or payment of such taxes and shall have no responsibility to determine that the Company has provided for the reporting, withholding and payment of such taxes. The Company shall indemnify and hold harmless the Trustee from any and all losses, liabilities, claims, penalties or damages which may occur as a result of the Trustee following in good faith the written direction of the Company to remit payments to or reimburse the Company for payments made hereunder to or on behalf of Participants or arising from the Company's tax reporting, withholding and payment obligations hereunder. This indemnification shall survive termination of this Agreement and shall be binding upon the parties, their successors and assigns.

ARTICLE 3

THE TRUSTEE RESPONSIBILITY REGARDING PAYMENTS TO TRUST BENEFICIARY WHEN THE COMPANY IS INSOLVENT

3.1 *Insolvency Defined.* The Trustee shall cease payment of benefits to Plan Participants and their beneficiaries if the Company is Insolvent. The Company shall be considered "Insolvent" for purposes of this Trust Agreement if (a) the Company is unable to pay its debts as they become due, or (b) the Company is subject to a pending proceeding as a debtor under the United States Bankruptcy Code.

3.2 *Assets Subject to Claims of Creditors on Insolvency.* At all times during the continuance of this Trust, the principal and income of the Trust shall be subject to claims of general creditors of the Company under federal and state law as set forth below.

(a) The Board of Directors and the Chief Executive Officer of the Company shall have the duty to inform the Trustee in writing of the Company's Insolvency. If a person claiming to be a creditor of the Company alleges in writing to the Trustee that the Company has become Insolvent, the Trustee shall determine whether the Company is Insolvent and, pending such determination, the Trustee shall discontinue payment of benefits to Plan Participants or their beneficiaries.

(b) Unless the Trustee has actual knowledge of the Company's Insolvency, or has received notice from the Company or a person claiming to be a creditor alleging that the Company is Insolvent, the Trustee shall have no duty to inquire whether the Company is Insolvent. The Trustee may in all events rely on such evidence concerning the Company's solvency as may be furnished to the Trustee and that provides the Trustee with a reasonable basis for making a determination concerning the Company's solvency.

(c) If at any time the Trustee has been notified or has determined that the Company is Insolvent, the Trustee shall discontinue payments to Plan Participants or their beneficiaries and shall hold the assets of the Trust for the benefit of the Company's general creditors. Nothing in this Trust Agreement shall in any way diminish any rights of Plan Participants or their beneficiaries to pursue their rights as general creditors of the Company with respect to benefits due under the Plan or otherwise.

(d) The Trustee shall resume the payment of benefits to Plan Participants or their beneficiaries in accordance with Article 2 of this Trust Agreement only after the Trustee has determined that the Company is not Insolvent (or is no longer Insolvent).

3.3 *Make Up of Suspended Benefits After Insolvency.* Provided that there are sufficient assets, if the Trustee discontinues the payment of benefits from the Trust pursuant to Section 3.2 hereof and subsequently resumes such payments, the first payment following such discontinuance shall include the aggregate amount of all payments due to Plan Participants or their beneficiaries under the terms of the Plan for the period of such discontinuance, less the aggregate amount of any payments made to Plan Participants or their beneficiaries by the Company in lieu of the payments provided for hereunder during any such period of discontinuance.

ARTICLE 4

PAYMENTS TO THE COMPANY

4.1 *No Return of Assets to the Company Prior to Payment of Benefits.* Except as provided in Article 3 hereof, the Company shall have no right or power to direct the Trustee to return to the Company or to divert to others any of the Trust assets before all payments of benefits have been made to Plan Participants and their beneficiaries pursuant to the terms of the Plan.

ARTICLE 5

POWERS OF THE TRUSTEE

5.1 *Investment Authority.* Prior to a Triggering Event, the Company shall have the power over and responsibility for the management and investment of Trust assets, unless otherwise agreed in writing between the Company and the Trustee. The Company may appoint an Agent to act as investment manager and to direct the investment of Trust assets on behalf of the Company, provided the Trustee is notified in writing prior to such appointment taking effect. After a Triggering Event, the Participant Committee shall have the power over and responsibility for management and investment of the Trust assets and appointment of any Agent. The Participant Committee may approve the continued appointment of the Agent previously appointed by the Company or may appoint a new Agent to act as investment manager and to direct the investment of Trust assets. The Trustee shall have no duty to supervise the Agent or to make recommendations regarding Trust assets and shall retain assets until directed in writing by the Company, Agent or Participant Committee to dispose of them. In the event the Company or the Participant Committee delegates investment responsibility to the Trustee, fails to contact or direct the Trustee regarding investment for a period of six (6) months or the Trustee is otherwise required to take responsibility for the investment of Trust assets at any time, for any reason, the Trustee is hereby specifically authorized

to retain and maintain any insurance contracts and employer securities purchased at the direction of the company, Agent or Participant Committee regardless of the desirability of diversification of Trust assets. In no event shall the Trustee assume investment responsibility for Trust assets which consist of [employer securities or] insurance products. The Company and, after a Triggering Event, the Participant Committee shall continue, at all times, to maintain investment management authority and control of such assets.

5.2 *Administrative Powers.* Subject in all respects to applicable provisions of this Trust Agreement and the Plan, at the direction of the Company. Agent or Participant Committee, as applicable, the Trustee shall have the rights, powers and privileges of an absolute owner when dealing with property of the Trust, including, without limiting the generality of the foregoing, the powers listed below:

(a) To invest and reinvest the Trust assets in any one or more kind, type, class, item or parcel of property, real or personal, tangible or intangible; or in any one or more kind, type, class, or item of obligation, secured or unsecured; or in any combination of them and to retain the property for the period of time that the Company, Agent or Participant Committee deems appropriate, despite fluctuations in the market price or the property.

(b) To sell, convey, transfer, exchange, partition, lease, and otherwise dispose of any of the assets of the Trust at any time held by the Trustee under this Trust Agreement, with or without notice.

(c) To exercise any option, conversion privilege or subscription right given the Trustee as the owner of any security held in the Trust; to vote any corporate stock either in person or by proxy, with or without power of substitution; to consent to or opposee any reorganization, consolidation, merger, readjustment of financial structure, sale, lease or other disposition of the assets of any corporation or other organization, the securities of which may be an asset of the Trust; to take any action in connection therewith and receive and retain any securities resulting therefrom.

(d) To cause any property of the Trust to be issued, held or registered in the name of the Trustee as the Trustee, or in the name of one or more of its nominees, or one or more nominees of any system for the central handling of securities, or in such form that title will pass by delivery, provided that the records of the Trustee shall in all events indicate the true ownership of such property.

(e) To renew or extend the time of payment of any obligation due or to become due.

(f) To commence or defend lawsuits or legal or administrative proceedings; to compromise, arbitrate or settle claims, debts or damages in favor of or against the Trust; to deliver or accept, in either total or partial satisfaction of any indebtedness or other obligation, any property; to continue to hold for such period of time as the Trustee may deem appropriate any property so received; and to pay all costs and reasonable attorneys' fees in connection therewith out of the assets of the Trust.

(g) To manage any real property in the Trust in the same manner as if the Trustee were the absolute owner thereof.

(h) To borrow money from any person in such amounts upon such terms and conditions and for such purposes as the Trustee, in its discretion, may deem appropriate; in connection therewith to pledge or mortgage any Trust asset as security; to lend money on a secured or unsecured basis to any person other than a party in interest.

(i) To hold such part of the assets of the Trust uninvested for such limited periods of time as may be necessary for purposes of orderly account administration or pending required directions, without liability for payment of interest.

(j) To determine how all receipts and disbursements shall be credited, charged or apportioned as between income and principal according to the Principal and Income Act and other applicable authorities.

(k) To dispose of any property in the Trust and to enforce any note or obligations of the Company to the Trust (and foreclose on any collateral securing such notes, subject to the terms of any pledge agreement to the Trustee) in the event the Company fails to make required contributions to the Trust after sixty (60) days' written notice to the Company of its failure to make such required contributions.

(1) To invest in any mutual fund, whether sponsored or advised by the Trustee or any of its affiliates, and the Trustee and its affiliates may be compensated for providing investment advice and other services to such fund, in addition to any Trustee fees received under this Trust Agreement.

(m) Generally to do all which the trustee may deem necessary or desirable for the orderly administration or protection of the Trust.

5.3 *Investment in the Company Securities.* The Trustee may invest in securities (including stock or rights to acquire stock) or obligations issued by the Company. All rights associated with such securities or obligations acquired by the Trust shall be exercised by the Trustee or the person designated by the Trustee, and shall in no event be exercisable by or rest with Plan Participants.

5.4 *Limitation With Respect to Insurance Policies.* The Trustee shall have, without exclusion, all powers conferred on Trustees by applicable law, unless expressly provided otherwise herein; provided, however, that if an insurance policy is held as an asset of the Trust, the Trustee Shall have no power to name a beneficiary of the policy other than the Trust to assign the policy (as distinct from conversion of the policy to a different form) other than to a successor Trustee, or to loan to any person the proceeds of any borrowing against such policy.

5.5 *Limitation With Respect to the Company as a Business.* Notwithstanding any powers granted to the Trustee pursuant to this Trust Agreement or to applicable law, the Trustee shall not have any power that could give this Trust the objective of carrying on a business and dividing the gains therefrom, within the meaning of Section 301.7701-2 of the Procedure and Administrative Regulations promulgated pursuant to the Internal Revenue Code.

ARTICLE 6

DISPOSITION OF INCOME

During the term of this Trust, all income received by the Trust, net of expenses and taxes, shall be accumulated and reinvested until such time as it is distributed as directed by this Trust Agreement.

ARTICLE 7

ACCOUNTING BY THE TRUSTEE

7.1 *Accounting and Records.* The Trustee shall keep accurate and detailed records of all investments, receipts, disbursements, and all other transactions required to be made, including such specific records as shall be agreed upon in writing between the Company and the Trustee. Such records shall be open to inspection by the Company at all reasonable times. Within sixty (60) days following the close of each calendar year and within sixty (60) days after the removal or resignation of the Trustee, the Trustee shall deliver to the Company a written account of its administration of the Trust during such year or during the period from the close of the last preceding year to the date of such removal or resignation, setting forth all investments, receipts, disbursements and other transactions affected by it, including a description of all securities and investments purchased and sold with the cost or net proceeds of such purchases or sales (accrued interest paid or receivable being shown separately), and showing all cash, securities and other property held in the Trust at the end of such year or as of the date of such removal or resignation, as the case may be. After a Triggering Event, the Participant Committee shall have the same rights of inspection as the Company and the Trustee shall deliver a copy of its written account to the Participant Committee as well as to the Company. The requirements for any other accountings, including without limitation accountings to any Participant or beneficiary, is hereby waived to the fullest extent permitted by applicable law.

7.2 *Valuation.* The assets of the Trust shall be valued at their fair market value on the date of valuation, as determined by the Trustee based upon such sources of information as it may deem reliable; provided, however, that the Company, and, after a Triggering Event, the Participant Committee, shall instruct the Trustee as to asset valuations which are not readily determinable on an established market. The Trustee may rely conclusively on such valuations provided by the Company, the Participant Committee or a duly appointed Agent and shall be indemnified and held harmless by the Company with respect to such reliance. If the Company or Participant Committee fails to provide such values, the Trustee may take whatever action it deems reasonable, including employment of attorneys, appraisers or other professionals, the expense of which will be an expense of administration of the Trust. The value of any insurance contract for purposes of substitution shall be the present value of future projected cash flow or benefits payable under the contract, but not less than the cash surrender value. The projection shall include death benefits based on reasonable mortality assumptions, including facts specifically related to the health of the insured and the terms of the contract to be reacquired.

7.3 *Tax Reporting* The Company and not the Trustee shall be responsible for all income tax reporting and calculation and payment of any wage withholding or other tax requirements in connection with the Trust and any contributions thereto, and any income earned thereby, and payments or distributions therefrom, and the Company agrees to indemnify and defend the Trustee against any liability for any such taxes, interest or penalties resulting from or relating to the Trust. Unless otherwise agreed in witting by the parties, the Trustee shall prepare annually a grantor tax information letter for the Trust and shall promptly transmit that document to the Company for its use in preparing its annual corporate income tax return. If any part of the Trust may become liable for payment of any estate, inheritance, or other taxes, charges or assessments, the Trustee shall refer such matter to the Company and may take such action as the Company shall direct.

ARTICLE 8

RESPONSIBILITY OF THE TRUSTEE

8.1 *Fiduciary Responsibility.* The Trustee shall act as a fiduciary on behalf of Participants and all other parties having an interest in the assets of the Trust with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent person acting in like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims.

8.2 *Limitation on Liability of the Trustee.*

(a) The Trustee shall have no powers, duties or responsibilities with regard to the administration of the Plans or to determine the rights or benefits of any person having or claiming an interest under the Plans or in the Trust or under this Trust Agreement or to examine or control any disposition of the Trust or part thereof which is directed by the Company, Participant Committee or Agent, as applicable. Any dispute with respect to a claim for benefit payable under the Plan or Trust, among the Company, the Participant Committee or a Plan Participant or beneficiary shall be governed by and resolved through the claims procedures and dispute resolution provisions contained in the Plan document.

(b) The Trustee shall have no liability for the adequacy of contributions for the purposes of the Plans or for enforcement of the payment thereof.

(c) The Trustee shall have no liability for the acts or omissions of the Company, Agent, Participant Committee or any of their agents.

(d) The Trustee shall have no liability for following proper directions of the Company, Agent, Participant Committee or any of their agents or of any Participant when such directions are made in accordance with this Trust Agreement.

(e) During such period or periods of time, if any, as the Company, Participant Committee or Agent is directing the investment and management of Trust assets, the Trustee shall have no obligation to determine the existence of any conversion, redemption, exchange, subscription or other right relating to any securities purchased on the directions of such directing party if notice of any such right was given prior to the purchase of such securities. If such notice is given after the purchase of such securities, the Trustee shall notify such directing party. The Trustee shall have no obligation to exercise any such right unless it is instructed to exercise such right, in writing, by the directing party within a reasonable time prior to the expiration of such right.

(f) During such period or periods of time, if any, as the Company, Participant Committee or Agent is directing the investment and management of Trust assets, if such directing party directs the Trustee to purchase securities issued by any foreign government or agency thereof, or by any corporation domiciled outside of the United States, it shall be the responsibility of the directing party to advise the Trustee in writing with respect to any laws or regulations of any foreign countries or any United States territories or possessions which shall apply, in any manner whatsoever, to such securities, including, but not limited to, receipt of dividends or interest by the Trustee for such securities.

8.3 *Indemnification.*

(a) The Company hereby agrees to indemnify and hold harmless the Trustee, its officers, directors, employees or agents, from and against any and all liabilities, claims for breach of fiduciary duty or otherwise, demands, damages, costs and expenses, including reasonable attorneys' fees, arising in any way from the Trustee's performance of its duties under and according to the terms of this Trust Agreement, including but not limited to, (i) any act taken or omitted by the Trustee in good faith in accordance with or due to the absence of directions from the Company, Agent, Participant Committee, Plan Participant or any of their agents, (ii) any act taken or omitted by the Company, Agent, Participant Committee, Plan Participant or their agents in breach of such party's responsibilities under the Plan or this Agreement, and (iii) any action taken by the Trustee pursuant to a notification of an order to purchase or sell securities issued by the Company, Agent, Participant Committee, Plan Participant or their agents directly to a broker or dealer.

(b) If the Trustee is named as a defendant in any lawsuit or other proceeding involving the Plan or the Trust for any reason including, without limitation, an alleged breach by the Trustee of its responsibilities under this Agreement, the Company hereby agrees to indemnify the Trustee against all liabilities, costs, and expenses, including reasonable attorneys' fees, incurred by the Trustee unless the final judgment entered in the lawsuit or proceeding holds the Trustee guilty of gross negligence, willful misconduct, or a breach of fiduciary responsibility.

(c) The Company shall have the right, but not the obligation, to conduct the defense of the Trustee in any legal proceeding covered by this section. However, any legal counsel selected to defend the Trustee must be acceptable to the Trustee, and the Trustee may elect to choose counsel, including in-house counsel, other than that selected by the Company. The Company may satisfy all or any part of its obligations under this section through insurance arrangements acceptable to the Trustee.

8.4 *Arbitration.* Any claim, dispute or other matter in question arising out of or related to this Trust Agreement shall be resolved by binding arbitration in accordance with the applicable employment dispute resolution rules of the American Arbitration Association, or such other arbitration organization as is mutually agreeable to the interested parties. The arbitration shall be legally binding upon all parties to the fullest extent allowed by law, and the decision of the arbitrators shall be final and enforceable in any court of competent jurisdiction. The fees and expenses (including reasonable attorneys' fees and expert fees) incurred in the arbitration shall be paid as directed by the arbitrator. However, all of the Trustee's fees and expenses incurred in any arbitration or enforcement proceeding to resolve a dispute between, the Company and a Participant, the Participant Committee, an Agent or a beneficiary shall be allowed as an administrative expense of the Trust.

8.5 *Legal Counsel.* The Trustee may consult with legal counsel (who may also be counsel for the Company generally) with respect to any of its duties or obligations hereunder.

8.6 *Experts.* The Trustee may hire agents, accountants, actuaries, investment advisors, financial consultants or other professionals to assist it in performing any of its duties or obligations hereunder.

ARTICLE 9

COMPENSATION AND EXPENSES OF THE TRUSTEE

The Trustee shall be paid a reasonable Trustee fee fixed by agreement with the Company from time to time and shall be reimbursed for all reasonable authorized administrative expenses, including, but not limited to, legal fees, experts' fees or fees and expenses associated with arbitration proceedings. No increase in the Trustee fees shall be effective before sixty (60) days after the Trustee gives notice to the Company of the increase. The Trustee shall notify the Company periodically of administrative expenses it has incurred. The Company shall pay the Trustee fees and other reasonable authorized administrative expenses. However, to the extent that any such fees or expenses are not paid by the Company within sixty (60) days after the Company's receipt of the Trustee's invoice therefor, the Trustee may charge the Trust for such fees or expenses.

ARTICLE 10

RESIGNATION AND REMOVAL OF THE TRUSTEE

10.1 *Resignation.* The Trustee may resign at any time by written notice to the Company, which shall be effective sixty (60) days after receipt of such notice unless the Company and the Trustee agree otherwise. If the Trustee resigns, the Company shall select a successor Trustee in accordance with the provisions of Section 11.1 hereof prior to the effective date of the Trustee's resignation or removal. On or after a Triggering Event, the selection of the successor Trustee shall be subject to the approval of the Participant Committee prior to the effective date of the Trustee's resignation.

10.2 *Removal.* The Trustee may be removed by the Company at any time prior to a Triggering Event on sixty (60) days' notice or upon shorter notice accepted by the Trustee. On or after a Triggering Event, the Trustee may be removed by the Participant Committee on sixty (60) days' notice or upon shorter notice accepted by the Trustee. If the Trustee is removed, a successor shall be appointed, in accordance with Section 11.2 hereof, by the effective date of removal. If no such appointment has been made, the Trustee may apply to a court of competent jurisdiction for instructions. All expenses of the Trustee in connection with the proceeding shall be allowed as administrative expenses of the Trust payable by the Company as provided in Article 9.

10.3 *Transfer of Assets.* Upon resignation or removal of the Trustee and appointment of a successor Trustee, all assets shall subsequently be transferred to the successor Trustee. The transfer shall be completed within ninety (90) days after receipt of notice of resignation or removal, unless the Company extends the time limit.

ARTICLE 11

APPOINTMENT OF SUCCESSOR

11.1 *On Resignation of the Trustee.* If the Trustee resigns pursuant to the provisions of Section 10.1 hereof, the Company may appoint as successor Trustee any third party, such as a bank trust department or other entity, with at least one billion dollars ($1,000.000,000) in trust assets and that may be granted corporate trustee powers under applicable law, subject to the approval of the Participant Committee as provided in Section 10.1 on or after a Triggering Event. The appointment of a successor Trustee shall be effective when accepted in writing by the new Trustee. The new Trustee shall have all the rights and powers of the former Trustee, including ownership rights in Trust assets. The former Trustee shall execute any instrument necessary or reasonably requested by the successor Trustee to evidence the transfer. If no such appointment has been made, the Trustee may apply to a court of competent jurisdiction for instructions. All expenses of the Trustee in connection with the proceeding shall be allowed as administrative expenses of the Trust payable by the Company as provided in Article 9.

11.2 *On Removal of the Trustee.* If the Trustee is removed in accordance with Section 10.2 hereof, the Company or the Participant Committee having the authority to make such removal may appoint any third party, such as a bank trust department or other entity, with at least one billion dollars ($1 000,000,000) in trust assets and that may be granted corporate trustee powers under applicable law, as a successor to replace the Trustee upon resignation or removal. The appointment shall be effective when accepted in writing by the new Trustee, who shall have all of the rights and powers of the former Trustee, including ownership rights in the Trust assets. The former Trustee shall execute any instrument necessary or reasonably requested by the Company, the Participant Committee or the successor Trustee to evidence the transfer.

11.3 *Responsibility of Successor Trustee.* The successor Trustee need not examine the records and acts of any prior Trustee and may retain or dispose of existing Trust assets, subject to the terms of this Trust Agreement. The successor Trustee shall not be responsible for and the Company shall indemnify and defend the successor Trustee from any claim, or liability resulting from any action or inaction of any prior Trustee or from any other past event, or any condition existing at the time it becomes successor Trustee.

ARTICLE 12

AMENDMENT OR TERMINATION

12.1 *Amendment.* Prior to a Triggering Event, this Trust Agreement may be amended by a written instrument executed by the Trustee and the Company. After a Triggering Event, this Trust Agreement may only be amended by a written instrument executed by the Trustee, the Company and an authorized representative of the Participant Committee. Notwithstanding the foregoing, no such amendment shall result in more than an incidental or de minimis reduction in the rights of Participants, conflict with the terms of the Plan or make the Trust revocable.

12.2 *Termination.* The Trust shall not terminate until the date on which all Plan Participants and their beneficiaries are no longer entitled to benefits pursuant to the terms of the Plan. Upon termination of the Trust, any assets remaining in the Trust shall be returned to the Company. Notwithstanding the foregoing, upon written approval of all Participants or beneficiaries entitled to payment of benefits pursuant to the terms of the Plan, the Company may terminate this Trust prior to the time all benefit payments under the Plan have been made and all assets in the Trust at such time shall be returned to the Company. In the event of such Trust termination approved by all Participants or beneficiaries and the Company, it is understood that the Company and not the Trustee has knowledge of the identities and entitlements of all Participants or beneficiaries in the Plan. Therefore, in any such Trust termination direction to the Trustee from the Company, the Trustee may rely conclusively on the Company's representation in its directive that all Participants or beneficiaries, as applicable, have consented to such revocation and termination.

ARTICLE 13

MISCELLANEOUS

13.1 *Binding Effect; Successor Company.* This Trust Agreement shall be binding upon and inure to the benefit of any successor to the Company or its business as the result of merger, consolidation, reorganization, transfer of assets or otherwise, and any subsequent successor thereto. In the event of any such merger, consolidation, reorganization, transfer of assets or other similar transaction, the successor to the Company or its business or any subsequent successor thereto shall promptly notify the Trustee in writing of its successorship and shall promptly supply information required by the Trustee.

13.2 *Severability.* Any provision of this Trust Agreement prohibited by law shall be ineffective to the extent of any such prohibition, without invalidating the remaining provisions hereof.

13.3 *Nonassignability.* Benefits payable to Plan Participants and their beneficiaries under this Trust Agreement may not be anticipated, assigned (either at law or in equity), alienated, pledged, encumbered or subjected to attachment, garnishment, levy, execution or other legal or equitable process.

13.4 Applicable Law. This Trust Agreement shall be governed by and construed in accordance with the laws of California except where preempted by federal law.

ARTICLE 14

DEFINITIONS

14.1 *Agent* shall mean the advisor, administrator, consultant or investment manager appointed by the Company or the Participant Committee in writing to direct the Trustee regarding the payment of benefits and/or the investment of assets in the Trust.

14.2 *Assumptions and Methodology* shall mean the actuarial assumptions and method of calculation used in determining the present or future value of benefits, earnings, payments, fees, expenses or any other amounts required to be calculated under the terms of the Trust Agreement.

Such Assumptions and Methodology shall be outlined in detail in Exhibit C to the Trust Agreement and may be changed from time to time by the Company prior to a Triggering Event and with approval of the Participant Committee after a Triggering Event.

14.3 *Change in Control* shall mean either: (a) the dissolution or liquidation of the Company; (b) a reorganization, merger or consolidation of the Company with one or more corporations as a result of which the Company is not the surviving corporation; (c) approval by the stockholders of the Company of any sale, lease, exchange or other transfer (in one or a series of transactions) of all or substantially all of the assets of the Company; (d) approval by the stockholders of the Company of any merger or consolidation of the Company in which the holders of the voting stock of the Company immediately before the merger or consolidation will not own fifty percent (50%) or more of the voting shares of the continuing or surviving corporation immediately after such merger or consolidation; or (e) a change in twenty-five percent (25%) (rounded to the next whole person) in the membership of the Board of Directors of the Company within a twelve-month period, unless the election or nomination for election by stockholders of each new director within such period was approved by the vote of eighty-five percent (85%) (rounded to the next whole person) of the directors then still in office who were in office at the beginning of the twelve-month period. The Board of Directors and the Chief Executive Officer of the Company shall have the duty to inform the Trustee in writing when there has been a Change in Control. If a Plan Participant alleges in writing to the Trustee that a Change in Control has occurred, the Trustee shall inquire of the Company to determine if there has been a Change in Control. Unless the Trustee has actual knowledge of a Change in Control, or has received notice from the Company or a Plan Participant alleging this such, the Trustee shall have no duty to inquire whether a Change in Control has occurred. The Trustee may, in all events, rely on such evidence concerning the occurrence of a Change in Control as may be furnished by the Company to the Trustee and that provides the Trustee with a reasonable basis for making a determination.

14.4 *Company* shall have the same meaning given to such term in the introductory paragraph of this Agreement.

14.5 *Default* shall mean failure by the Company to make contributions to the Trust or to make benefit or tax payments required by the Plan as provided by Section 1.1.

14.6 *Insolvent/Insolvency* shall have the meaning given to such term in Section 3.1 of the Trust Agreement.

14.7 *Participant* shall mean a participant in the Plan and shall have the meaning given to such term in the Plan.

14.8 *Participant Committee* shall mean the committee of Participants established after a Triggering Event to direct the Trustee. Upon a Triggering Event, it shall be the responsibility of the Company to notify the three Participants having the largest vested and unvested accrued benefits protected by the Trust assets of their obligation to establish a Participant Committee. The three largest Participants shall act as the Participant Committee until such time as three other Participant representatives shall be nominated and elected by the individual Participants having an interest in the Trust assets as of the date of such election, which election shall take place at least annually under supervision of the incumbent Participant Committee. Any action taken by the Participant Committee

shall require a unanimous vote of all three members of the committee. In the event one of the three largest Participants is incompetent or otherwise unavailable to serve, it shall be the responsibility of the Company to notify the Participant having the next largest interest in the Trust assets of his or her obligation to take the place of such unavailable Participant and serve on the Participant Committee. After a Triggering Event, it shall be the responsibility of the Company to provide the Trustee with the names, specimen signatures and contact information, including business addresses and telephone numbers, of the members of the Participant Committee.

14.9 *Plan* shall mean the plan or plans sponsored by the Company and funded by the assets of the Trust. Such Plans shall be listed in Exhibit A to the Trust Agreement. Additional plans may be added from time to time by the Company prior to a Triggering Event and with approval of the Participant Committee after a Triggering Event.

14.10 *Triggering Event* shall mean a Default and/or a Change in Control.

14.11 *Trust* shall mean the trust fund established by this Trust Agreement.

14.12 *Trustee* shall have the same meaning given to such term in the introductory paragraph of this Trust Agreement.

IN WITNESS WHEREOF, the parties hereto have executed and entered into this Trust Agreement as of the date first above written.

TRUSTEE: FIRST AMERICAN TRUST, FSB

By /s/ Denise C. Mehus
Its Vice President

COMPANY: Iteris, Inc.
A Delaware Corporation

By /s/ Jack Johnson
Its 3/29/02

Exhibit A

Plans Funded by Trust

ITERIS, INC. Deferred Compensation Savings Plan, effective March 29, 2002, and as it may be amended from time to time

This Exhibit shall supercede any prior Exhibit A and shall be effective *March 31, 2002.*

TRUSTEE: By /s/ Denise C. Mehus
Denise C. Mehus, Vice President

Date 3-29-02

COMPANY: By /s/ Jack Johnson
Its 3/29/02 CEO
Date 3/29/02

Exhibit B

Initial Contributions to Trust

133,333 shares of Iteris, Inc. stock and approximately $30,000 in cash (all fbo Jack Johnson)

This Exhibit shall supercede any prior Exhibit B and shall be effective March 31, 2002.

TRUSTEE: By /s/ Denise C. Mehus
Vice President
Date 3-29-02

COMPANY: By /s/ Jack Johnson
Its CEO
Date 3/29/02

Exhibit 10.32

ITERIS, INC.*
1997 STOCK INCENTIVE PLAN
(Amended and Restated as of May 3, 2002, and as further amended December 15, 2004)

ARTICLE ONE

GENERAL PROVISIONS

I. PURPOSE OF THE PLAN

This 1997 Stock Incentive Plan is intended to promote the interests of Iteris, Inc., a Delaware corporation formerly known as Odetics, Inc. and Iteris Holdings, Inc., by providing eligible persons with the opportunity to acquire a proprietary interest, or otherwise increase their proprietary interest, in the Corporation as an incentive for them to remain in the service of the Corporation.

Capitalized terms shall have the meanings assigned to such terms in the attached Appendix.

II. STRUCTURE OF THE PLAN

A. The Plan shall be divided into three separate equity programs:

- The Discretionary Option Grant Program under which eligible person may, at the discretion of the Plan Administrator, be granted options to purchase shares of Common Stock,

- the Stock Issuance Program under which eligible persons may, at the discretion of the Plan Administrator, be issued shares of Common Stock directly, either through the immediate purchase of such shares or as a bonus for services rendered the Corporation (or any Parent or Subsidiary), and

- the Automatic Option Grant Program under which eligible non-employee Board members shall automatically receive option grants at periodic intervals to purchase shares of Common Stock.

B. The provisions of Articles One and Five shall apply to all equity programs under the Plan and shall govern the interests of all persons under the Plan.

III. ADMINISTRATION OF THE PLAN

A. The Primary Committee shall have sole and exclusive authority to administer the Discretionary Option Grant and Stock Issuance Programs with respect to Section 16 Insiders. Administration of the Discretionary Option Grant and Stock Issuance Programs with respect to all other persons eligible to participate in those programs may, at the Board's discretion, be vested in the Primary Committee or a Secondary Committee, or the Board may retain the power to administer those programs with respect to all such persons.

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* Formerly known as the "Odetics, Inc. 1997 Stock Incentive Plan"

B. Members of the Primary Committee or any Secondary Committee shall serve for such period of time as the Board may determine and may be removed by the Board at any time. The Board may also at any time terminate the functions of any Secondary Committee and reassume all powers and authority previously delegated to such committee.

C. Each Plan Administrator shall, within the scope of its administrative functions under the Plan, have full power and authority (subject to the provisions of the Plan) to establish such rules and regulations as it may deem appropriate for proper administration of the Discretionary Option Grant and Stock Issuance Programs and to make such determinations under, and issue such interpretations of, the provisions of such programs and any outstanding options or stock issuances thereunder as it may deem necessary or advisable. Decisions of the Plan Administrator within the scope of its administrative functions under the Plan shall be final and binding on all parties who have an interest in the Discretionary Option Grant and Stock Issuance Programs under its jurisdiction or any option or stock issuance thereunder.

D. Service on the Primary Committee or the Secondary Committee shall constitute service as a Board member, and members of each such committee shall accordingly be entitled to full indemnification and reimbursement as Board members for their service on such committee. No member of the Primary Committee or the Secondary Committee shall be liable for any act or omission made in good faith with respect to the Plan or any option grants or stock issuances under the Plan.

E. Administration of the Automatic Option Grant Program shall be self-executing in accordance with the terms of that program, and no Plan Administrator shall exercise any discretionary functions with respect to any option grants or stock issuances made under such program.

IV. ELIGIBILITY

A. The persons eligible to participate in the Discretionary Option Grant and Stock Issuance Programs are as follows:

(i) employees,

(ii) non-employee members of the Board or the board of directors of any Parent or Subsidiary, and

(iii) consultants and other independent advisors who provide services to the Corporation (or any Parent or Subsidiary).

B. Each Plan Administrator shall, within the scope of its administrative jurisdiction under the Plan, have full authority to determine, (i) with respect to the option grants under the Discretionary Option Grant Program, which eligible persons are to receive option grants, the time or times when such option grants are to be made, the number of shares to be covered by each such grant, the status of the granted option as either an Incentive Option or a Nonstatutory Option, the time or times when each option is to become exercisable, the vesting schedule (if any) applicable to the option shares and the maximum term for which the option is to remain outstanding and (ii) with respect to stock issuances under the Stock Issuance Program, which eligible persons are to receive stock issuances, the time or times when such issuances are to be made, the number of shares to be issued to each Participant, the vesting schedule (if any) applicable to the issued shares and the consideration to be paid for such shares.

C. The Plan Administrator shall have the absolute discretion either to grant options in accordance with the Discretionary Option Grant Program or to effect stock issuances in accordance with the Stock Issuance Program.

D. The individuals who shall be eligible to participate in the Automatic Option Grant Program shall be limited to (i) those individuals serving as non- employee Board members on the Plan Effective Date, (ii) those individuals who first become non-employee Board members on or after the Plan Effective Date, whether through appointment by the Board or election by the Corporation's stockholders, and (ii) those individuals who continue to serve as non-employee Board members at one or more Annual Stockholders Meetings held after the Plan Effective Date.

V. STOCK SUBJECT TO THE PLAN

A. The stock issuable under the Plan shall be shares of authorized but unissued or reacquired Common Stock, including shares repurchased by the Corporation on the open market. The maximum number of shares of Common Stock reserved for issuance over the term of the Plan shall not exceed 1,805,000 shares. This reserve includes (i) the 530,000 shares originally reserved for issuance under the Plan, (ii) the 400,000 share increased approved by the Corporation's stockholders at the 1999 Annual Meeting, (iii) the 400,000 share increase approved by the Corporation's stockholders at the 2000 Annual Meeting, and (iv) the 475,000 share increase approved by the Corporation's stockholders at the 2001 Annual Meeting.

B. No one person participating in the Plan may receive options, separately exercisable stock appreciation rights and direct stock issuances for more than 80,000 shares of Common Stock in the aggregate per calendar year, beginning with the 1997 calendar year.

C. Shares of Common Stock subject to outstanding options shall be available for subsequent issuance under the Plan to the extent (i) those options expire or terminate for any reason prior to exercise in full or (ii) those options are cancelled in accordance with the option cancellation/regrant provisions of Section IV of Article Two. Unvested shares issued under the Plan and subsequently cancelled or repurchased by the Corporation, at the original exercise or direct issue price paid per share, pursuant to the Corporation's repurchase rights under the Plan shall be added back to the number of shares of Common Stock reserved for issuance under the Plan and shall accordingly be available for reissuance through one or more subsequent option grants or direct stock issuances under the Plan. However, shares subject to any options surrendered in connection with the stock appreciation right provisions of the Plan shall not be available for reissuance. Should the exercise price of an option under the Plan be paid with shares of Common Stock or should shares of Common Stock otherwise issuable under the Plan be withheld by the Corporation in satisfaction of the withholding taxes incurred in connection with the exercise of an option or the vesting of a stock issuance under the Plan, then the number of shares of Common Stock available for issuance under the Plan shall be reduced by the gross number of shares for which the option is exercised or which vest under the stock issuance, and not by the net number of shares of Common Stock issued to the holder of such option or stock issuance.

D. If any change is made to the Common Stock by reason of any stock split, reverse stock split, stock dividend, distribution, recapitalization, combination or reclassification of shares, exchange of shares or other change affecting the outstanding Common Stock as a class without the Corporation's receipt of consideration, appropriate adjustments shall be made to (i) the maximum number and/or class of securities issuable under the Plan, (ii) the number and/or class of securities for which any one person may be granted stock options, separately exercisable stock appreciation rights and direct stock issuances under the Plan per calendar year, (iii) the number and/or class of securities for which grants are

subsequently to be made under the Automatic Option Grant Program to new and continuing non-employee Board members, and (iv) the number and/or class of securities and the exercise price per share in effect under each outstanding option under the Plan. Such adjustments to the outstanding options are to be effected in a manner which shall preclude the enlargement or dilution of rights and benefits under such options. The adjustments determined by the Plan Administrator shall be final, binding and conclusive.

E. Should the Corporation effect a divestiture of one or more Subsidiaries through a distribution or spin-off to the Corporation's stockholders of the securities of the Subsidiary held by the Corporation ("Divestiture"), then the Plan Administrator may, in its sole discretion, make appropriate adjustments to the number and/or class of securities subject to each outstanding option and the exercise price payable per share in order to reflect the effect of the Divestiture on the Corporation's capital structure and the relative Fair Market Values of the Common Stock and the distributed securities of the Subsidiary following the Divestiture. Such adjustment may include the division of the option into two separate options, one for the shares of Common Stock at the time subject to the option and a second option for the securities of the Subsidiary distributable with respect to those shares. The Plan Administrator may also, in its sole discretion, accelerate the vesting and exercisability of the option (or any separated option) with respect to one or more shares of the Common Stock or distributed securities at the time subject to such option (or the separated option), if and to the extent the Optionee is to remain in the Corporation's Service following such Divestiture or is otherwise to provide services to the divested Subsidiary.

ARTICLE TWO

DISCRETIONARY OPTION GRANT PROGRAM

I. OPTION TERMS

Each option shall be evidenced by one or more documents in the form approved by the Plan Administrator; provided, however, that each such document shall comply with the terms specified below. Each document evidencing an Incentive Option shall, in addition, be subject to the provisions of the Plan applicable to such options.

A. **Exercise Price**.

1. The exercise price per share shall be fixed by the Plan Administrator but shall not be less than one hundred percent (100%) of the Fair Market Value per share of Common Stock on the option grant date.

2. The exercise price shall become immediately due upon exercise of the option and shall, subject to the provisions of Section I of Article Five and the documents evidencing the option, be payable in one or more of the forms specified below:

(i) cash or check made payable to the Corporation,

(ii) shares of Common Stock held for the requisite period necessary to avoid a charge to the Corporation's earnings for financial reporting purposes and valued at Fair Market Value on the Exercise Date, or

(iii) to the extent the option is exercised for vested shares, through a special sale and remittance procedure pursuant to which the Optionee shall concurrently provide irrevocable instructions to (a) a Corporation designated brokerage firm to effect the immediate sale of the purchased shares and remit to the Corporation, out of the sale proceeds available on the settlement date, sufficient funds to cover the aggregate exercise price payable for the purchased shares plus all applicable Federal, state and local income and employment taxes required to be withheld by the Corporation by reason of such exercise and (b) the Corporation to deliver the certificates for the purchased shares directly to such brokerage firm in order to complete the sale.

Except to the extent such sale and remittance procedure is utilized, payment of the exercise price for the purchased shares must be made on the Exercise Date.

B. **Exercise and Term of Options**. Each option shall be exercisable at such time or times, during such period and for such number of shares as shall be determined by the Plan Administrator and set forth in the documents evidencing the option. However, no option shall have a term in excess of ten (10) years measured from the option grant date.

C. **Effect of Termination of Service**.

1. The following provisions shall govern the exercise of any options held by the Optionee at the time of cessation of Service or death:

(i) Any option outstanding at the time of the Optionee's cessation of Service for any reason shall remain exercisable for such period of time thereafter as shall be determined by the Plan Administrator and set forth in the documents evidencing the option, but no such option shall be exercisable after the expiration of the option term.

(ii) Any option exercisable in whole or in part by the Optionee at the time of death may be subsequently exercised by the personal representative of the Optionee's estate or by the person or persons to whom the option is transferred pursuant to the Optionee's will or in accordance with the laws of descent and distribution.

(iii) During the applicable exercise period following termination of Service, the option may not be exercised in the aggregate for more than the number of vested shares for which the option is exercisable on the date of the Optionee's cessation of Service. Upon the expiration of the applicable exercise period or (if earlier) upon the expiration of the option term, the option shall terminate and cease to be outstanding for any vested shares for which the option has not been exercised. However, the option shall, immediately upon the Optionee's cessation of Service, terminate and cease to be outstanding to the extent the option is not otherwise at that time exercisable for vested shares.

(iv) Should the Optionee's Service be terminated for Misconduct, then all outstanding options held by the Optionee shall terminate immediately and cease to be outstanding.

2. The Plan Administrator shall have complete discretion, exercisable either at the time an option is granted or at any time while the option remains outstanding, to:

(i) extend the period of time for which the option is to remain exercisable following the Optionee's cessation of Service from the limited exercise period otherwise in effect for that option to such greater period of time as the Plan Administrator shall deem appropriate, but in no event beyond the expiration of the option term, and/or

(ii) permit the option to be exercised, during the applicable Service exercise period following termination of service, not only with respect to the number of vested shares of Common Stock for which such option is exercisable at the time of the Optionee's cessation of Service but also with respect to one or more additional installments in which the Optionee would have vested had the Optionee continued in Service.

D. **Stockholder Rights**. The holder of an option shall have no stockholder rights with respect to the shares subject to the option until such person shall have exercised the option, paid the exercise price and become a holder of record of the purchased shares.

E. **Repurchase Rights**. The Plan Administrator shall have the discretion to grant options which are exercisable for unvested shares of Common Stock. Should the Optionee cease Service while holding such unvested shares, the Corporation shall have the right to repurchase, at the exercise price paid per share, any or all of those unvested shares. The terms upon which such repurchase right shall be exercisable (including the period and procedure for exercise and the appropriate vesting schedule for the purchased shares) shall be established by the Plan Administrator and set forth in the document evidencing such repurchase right.

F. **Limited Transferability of Options**. During the lifetime of the Optionee, Incentive Options shall be exercisable only by the Optionee and shall not be assignable or transferable other than by will or by the laws of descent and distribution following the Optionee's death. However, a Nonstatutory Option may be assigned in whole or in part during the Optionee's lifetime to one or more "family members" (as defined in Rule 701 of the 1933 Act) of the Optionee if such assignment is a gift or pursuant to a domestic relations order. The terms applicable to the assigned portion shall be the same as those in effect for the option immediately prior to such assignment and shall be set forth in such documents issued to the assignee as the Plan Administrator may deem appropriate.

II. INCENTIVE OPTIONS

The terms specified below shall be applicable to all Incentive Options. Except as modified by the provisions of this Section II, all the provisions of Articles One, Two and Five shall be applicable to Incentive Options. Options which are specifically designated as Nonstatutory Options when issued under the Plan shall not be subject to the terms of this Section II.

A. **Eligibility**. Incentive Options may only be granted to Employees.

B. **Dollar Limitation**. The aggregate Fair Market Value of the shares of Common Stock (determined as of the respective date or dates of grant) for which one or more options granted to any Employee under the Plan (or any other option plan of the Corporation or any Parent or Subsidiary) may for the first time become exercisable as Incentive Options during any one calendar year shall not exceed the sum of One Hundred Thousand Dollars ($100,000). To the extent the Employee holds two (2) or more such options which become exercisable for the first time in the same calendar year, the foregoing limitation on the exercisability of such options as Incentive Options shall be applied on the basis of the order in which such options are granted.

C. **10% Stockholder**. If any Employee to whom an Incentive Option is granted is a 10% Stockholder, then the exercise price per share shall not be less than one hundred ten percent (110%) of the Fair Market Value per share of Common Stock on the option grant date, and the option term shall not exceed five (5) years measured from the option grant date.

III. CORPORATE TRANSACTION/CHANGE IN CONTROL

A. In the event of any Corporate Transaction, each outstanding option shall automatically accelerate so that each such option shall, immediately prior to the effective date of the Corporate Transaction, become fully exercisable with respect to the total number of shares of Common Stock at the time subject to such option and may be exercised for any or all of those shares as fully vested shares of Common Stock. However, an outstanding option shall not become exercisable on such an accelerated basis if and to the extent: (i) such option is, in connection with the Corporate Transaction, to be assumed by the successor corporation (or parent thereof) or (ii) such option is to be replaced with a cash incentive program of the successor corporation which preserves the spread existing at the time of the Corporate Transaction on any shares for which the option is not otherwise at that time exercisable and provides for subsequent payout in accordance with the same exercise/vesting schedule applicable to those option shares or (iii) the acceleration of such option is subject to other limitations imposed by the Plan Administrator at the time of the option grant.

B. All outstanding repurchase rights shall automatically terminate, and the shares of Common Stock subject to those terminated rights shall immediately vest in full, in the event of any Corporate Transaction, except to the extent: (i) those repurchase rights are to be assigned to the successor

corporation (or parent thereof) in connection with such Corporate Transaction or (ii) such accelerated vesting is precluded by other limitations imposed by the Plan Administrator at the time the repurchase right is issued.

C. Immediately following the consummation of the Corporate Transaction, all outstanding options shall terminate and cease to be outstanding, except to the extent assumed by the successor corporation (or parent thereof).

D. Each option which is assumed in connection with a Corporate Transaction shall be appropriately adjusted, immediately after such Corporate Transaction, to apply to the number and class of securities which would have been issuable to the Optionee in consummation of such Corporate Transaction had the option been exercised immediately prior to such Corporate Transaction. Appropriate adjustments to reflect such Corporate Transaction shall also be made to (i) the exercise price payable per share under each outstanding option, provided the aggregate exercise price payable for such securities shall remain the same, (ii) the maximum number and/or class of securities available for issuance over the remaining term of the Plan and (iii) the maximum number and/or class of securities for which any one person may be granted stock options, separately exercisable stock appreciation rights and direct stock issuances under the Plan per calendar year.

E. The Plan Administrator shall have the discretionary authority to provide for the automatic acceleration of one or more outstanding options under the Discretionary Option Grant Program upon the occurrence of a Corporate Transaction, whether or not those options are to be assumed in the Corporate Transaction, so that each such option shall, immediately prior to the effect date of such Corporate Transaction, become fully exercisable with respect to the total number of shares of Common Stock at the time subject to that option and may be exercised for any or all of those shares as fully vested shares of Common Stock. In addition, the Plan Administrator shall have the discretionary authority to structure one or more of the Corporation's repurchase rights under the Discretionary Option Grant Program so that those rights shall not be assignable in connection with such Corporate Transaction and shall accordingly terminate upon the consummation of such Corporate Transaction, and the shares subject to those terminated rights shall thereupon vest in full.

F. The Plan Administrator shall have full power and authority, exercisable either at the time the option is granted or at any time while the option remains outstanding, to provide for the automatic acceleration of one or more outstanding options under the Discretionary Option Grant Program in the event the Optionee's Service is subsequently terminated by reason of an Involuntary Termination within a designated period (not to exceed eighteen (18) months) following the effective date of any Corporate Transaction in which those options are assumed and do not otherwise accelerate. Any options so accelerated shall remain exercisable for fully vested shares until the earlier of (i) the expiration of the option term or (ii) the expiration of the one (1) year period measured from the effective date of the Involuntary Termination. In addition, the Plan Administrator may provide that one or more of the Corporation's outstanding repurchase rights with respect to shares held by the Optionee at the time of such Involuntary Termination shall immediately terminate, and the shares subject to those terminated repurchase rights shall accordingly vest in full.

G. The Plan Administrator shall have the discretionary authority to provide for the automatic acceleration of one or more outstanding options under the Discretionary Option Grant Program upon the occurrence of a Change in Control so that each such option shall, immediately prior to the effect date of such Change in Control, become fully exercisable with respect to the total number of shares of Common Stock at the time subject to that option and may be exercised for any or all of those shares as fully vested shares of Common Stock. Each such accelerated option shall remain exercisable until the

expiration or sooner termination of the option term. In addition, the Plan Administrator shall have the discretionary authority to structure one or more of the Corporation's repurchase rights under the Discretionary Option Grant Program so that those rights shall terminate automatically upon the consummation of such Change in Control, and the shares subject to those terminated rights shall thereupon vest in full. Alternatively, the Plan Administrator may condition the automatic acceleration of one or more outstanding options under the Discretionary Option Grant Program and the termination of one or more of the Corporation's outstanding repurchase rights under such program upon the subsequent termination of the Optionee's Service by reason of an Involuntary Termination within a designated period (not to exceed eighteen (18) months) following the effective date of such Change in Control. Each option so accelerated shall remain exercisable for fully vested shares until the earlier of (i) the expiration of the option term or (ii) the expiration of the one (1) year period measured from the effective date of such Involuntary Termination.

H. The portion of any Incentive Option accelerated in connection with a Corporate Transaction or Change in Control shall remain exercisable as an Incentive Option only to the extent the applicable One Hundred Thousand Dollar ($100,000) limitation is not exceeded. To the extent such dollar limitation is exceeded, the accelerated portion of such option shall be exercisable as a Nonstatutory Option under the Federal tax laws.

I. The outstanding options shall in no way affect the right of the Corporation to adjust, reclassify, reorganize or otherwise change its capital or business structure or to merge, consolidate, dissolve, liquidate or sell or transfer all or any part of its business or assets.

IV. CANCELLATION AND REGRANT OF OPTIONS

The Plan Administrator shall have the authority to effect, at any time and from time to time, with the consent of the affected option holders, the cancellation of any or all outstanding options under the Discretionary Option Grant Program and to grant in substitution new options covering the same or different number of shares of Common Stock but with an exercise price per share equal to the Fair Market Value per share of Common Stock on the new grant date.

V. STOCK APPRECIATION RIGHTS

A. The Plan Administrator shall have the authority to grant to selected Optionees tandem stock appreciation rights and/or limited stock appreciation rights.

B. The following terms shall govern the grant and exercise of tandem stock appreciation rights:

(i) One or more Optionees may be granted the right, exercisable upon such terms as the Plan Administrator may establish, to elect between the exercise of the underlying option for shares Common Stock and the surrender of that option in exchange for a distribution from the Corporation in an amount equal to the excess of (a) the Fair Market Value (on the option surrender date) of the number of shares in which the Optionee is at the time vested under the surrendered option (or surrendered portion) over (b) the aggregate exercise price payable for those shares.

(ii) No such option surrender shall be effective unless it is approved by the Plan Administrator, either at the time of the actual option surrender or at any earlier time. If the surrender is so approved, then the distribution to which the Optionee shall be entitled may

be made in shares of Common Stock valued at Fair Market Value on the option surrender date, in cash, or partly in shares and partly in cash, as the Plan Administrator shall in its sole discretion deem appropriate.

(iii) If the surrender of an option is not approved by the Plan Administrator, then the Optionee shall retain whatever rights the Optionee had under the surrendered option (or surrendered portion) on the option surrender date and may exercise such rights at any time prior to the later of (a) five (5) business days after the receipt of the rejection notice or (b) the last day on which the option is otherwise exercisable in accordance with the terms of the documents evidencing such option, but in no event may such rights be exercised more than ten (10) years after the option grant date.

2. The following terms shall govern the grant and exercise of limited stock appreciation rights:

(i) One or more Section 16 Insiders may be granted limited stock appreciation rights with respect to their outstanding options.

(ii) Upon the occurrence of a Hostile Takeover, each individual holding one or more options with such a limited stock appreciation right shall have the unconditional right (exercisable for a thirty (30) day period following such Hostile Takeover) to surrender each such option to the Corporation, to the extent the option is at the time exercisable for vested shares of Common Stock. In return for the surrendered option, the Optionee shall receive a cash distribution from the Corporation in an amount equal to the excess of (A) the Takeover Price of the shares of Common Stock which are at the time vested under each surrendered option (or surrendered portion) over (B) the aggregate exercise price payable for those shares. Such cash distribution shall be paid within five (5) days following the option surrender date.

(iii) The Plan Administrator shall pre-approve, at the time the limited right is granted, the subsequent exercise of that right in accordance with the terms of the grant and the provisions of this Section V. No additional approval of the Plan Administrator or the Board shall be required at the time of the actual option surrender and cash distribution.

(iv) The balance of the option (if any) shall remain outstanding and exercisable in accordance with the documents evidencing such option.

ARTICLE THREE

STOCK ISSUANCE PROGRAM

I. STOCK ISSUANCE TERMS

Shares of Common Stock may be issued under the Stock Issuance Program through direct and immediate issuances without any intervening option grants. Each such stock issuance shall be evidenced by a Stock Issuance Agreement which complies with the terms specified below.

A. **Purchase Price**.

1. The purchase price per share shall be fixed by the Plan Administrator, but shall not be less than one hundred percent (100%) of the Fair Market Value per share of Common Stock on the issuance date.

2. Subject to the provisions of Section I of Article Five, shares of Common Stock may be issued under the Stock Issuance Program for any combination of the following items of consideration which the Plan Administrator may deem appropriate in each individual instance:

(i) cash or check made payable to the Corporation, or

(ii) past services rendered to the Corporation (or any Parent or Subsidiary).

B. **Vesting Provisions**.

1. Shares of Common Stock issued under the Stock Issuance Program may, in the discretion of the Plan Administrator, be fully and immediately vested upon issuance or may vest in one or more installments over the Participant's period of Service or upon attainment of specified performance objectives. The elements of the vesting schedule applicable to any unvested shares of Common Stock issued under the Stock Issuance Program shall be determined by the Plan Administrator and incorporated into the Stock Issuance Agreement.

2. Any new, substituted or additional securities or other property (including money paid other than as a regular cash dividend) which the Participant may have the right to receive with respect to the Participant's unvested shares of Common Stock by reason of any stock dividend, stock split, recapitalization, combination of shares, exchange of shares or other change affecting the outstanding Common Stock as a class without the Corporation's receipt of consideration shall be issued subject to (i) the same vesting requirements applicable to the Participant's unvested shares of Common Stock and (ii) such escrow arrangements as the Plan Administrator shall deem appropriate.

3. The Participant shall have full stockholder rights with respect to any shares of Common Stock issued to the Participant under the Stock Issuance Program, whether or not the Participant's interest in those shares is vested. Accordingly, the Participant shall have the right to vote such shares and to receive any regular cash dividends paid on such shares.

4. Should the Participant cease to remain in Service while holding one or more unvested shares of Common Stock issued under the Stock Issuance Program or should the performance objectives not be attained with respect to one or more such unvested shares of Common

Stock, then those shares shall be immediately surrendered to the Corporation for cancellation, and the Participant shall have no further stockholder rights with respect to those shares. To the extent the surrendered shares were previously issued to the Participant for consideration paid in cash or cash equivalent (including the Participant's purchase money indebtedness), the Corporation shall repay to the Participant the cash consideration paid for the surrendered shares and shall cancel the unpaid principal balance of any outstanding purchase money note of the Participant attributable to the surrendered shares.

5. The Plan Administrator may in its discretion waive the surrender and cancellation of one or more unvested shares of Common Stock which would otherwise occur upon the cessation of the Participant's Service or the non attainment of the performance objectives applicable to those shares. Such waiver shall result in the immediate vesting of the Participant's interest in the shares as to which the waiver applies. Such waiver may be effected at any time, whether before or after the Participant's cessation of Service or the attainment or non-attainment of the applicable performance objectives.

C. **Nontransferability of Rights to Purchase**. During the lifetime of the Participant, the right to purchase shares of Common Stock pursuant to the Stock Issuance Program shall be exercisable only by the Participant and shall not be assignable or transferable other than by will or by the laws of descent and distribution following the Participant's death.

II. CORPORATE TRANSACTION/CHANGE IN CONTROL

A. All of the Corporation's outstanding repurchase rights under the Stock Issuance Program shall terminate automatically, and all the shares of Common Stock subject to those terminated rights shall immediately vest in full, in the event of any Corporate Transaction, except to the extent (i) those repurchase rights are to be assigned to the successor corporation (or parent thereof) in connection with such Corporate Transaction or (ii) such accelerated vesting is precluded by other limitations imposed in the Stock Issuance Agreement.

B. The Plan Administrator shall have the discretionary authority, exercisable either at the time the unvested shares are issued under the Stock Issuance Program or any time while the Corporation's repurchase rights with respect to those shares remain outstanding, to structure one or more of those repurchase rights so that such rights shall not be assignable in connection with a Corporate Transaction and shall accordingly terminate upon the consummation of such Corporate Transaction, and the shares subject to those terminated repurchase rights shall thereupon vest in full.

C. The Plan Administrator shall have the discretionary authority, exercisable either at the time the unvested shares are issued or any time while the Corporation's repurchase rights remain outstanding under the Stock Issuance Program, to provide that those rights shall automatically terminate in whole or in part, and the shares of Common Stock subject to those terminated rights shall immediately vest, in the event the Participant's Service should subsequently terminate by reason of an Involuntary Termination within a designated period (not to exceed eighteen (18) months) following the effective date of any Corporate Transaction in which those repurchase rights are assigned to the successor corporation (or parent thereof).

D. The Plan Administrator shall have the discretionary authority, exercisable either at the time the unvested shares are issued or any time while the Corporation's repurchase rights with respect to those shares remain outstanding under the Stock Issuance Program, to structure one or more of those repurchase rights so that such rights shall automatically terminate in whole or in part, and the shares of Common Stock subject to those terminated rights shall immediately vest, upon (i) a Change in Control

or (ii) the subsequent termination of the Participant's Service by reason of an Involuntary Termination within a designated period (not to exceed eighteen (18) months) following the effective date of such Change in Control or Involuntary Termination.

III. SHARE ESCROW/LEGENDS

Unvested shares may, in the Plan Administrator's discretion, be held in escrow by the Corporation until the Participant's interest in such shares vests or may be issued directly to the Participant with restrictive legends on the certificates evidencing those unvested shares.

ARTICLE FOUR

AUTOMATIC OPTION GRANT PROGRAM

I. OPTION TERMS

A. **Grant Dates**. Option grants shall be made on the dates specified below:

1. Each individual serving as a non-employee Board member on the Plan Effective Date shall automatically be granted at that time a Nonstatutory Option to purchase 5,000 shares of Common Stock, provided that individual has not previously been in the employ of the Corporation or any Parent or Subsidiary.

2. Each individual who is first elected or appointed as a non-employee Board member on or after the Plan Effective Date shall automatically be granted, on the date of such initial election or appointment, a Nonstatutory Option to purchase 20,000 shares of Common Stock, provided that individual has not previously been in the employ of the Corporation or any Parent or Subsidiary.

3. In the date of each Annual Stockholders Meeting, beginning with the 1998 Annual Stockholders Meeting, each individual who is to continue to serve as a non-employee Board member, whether or not that individual is standing for reelection to the Board at that particular Annual Meeting, shall automatically be granted a Nonstatutory Option to purchase 5,000 shares of Common Stock, provided such individual has served as a non-employee Board member for at least six (6) months. There shall be no limit on the number of such 5,000 share option grants any one non-employee Board member may receive over his or her period of Board service, and non-employee Board members who have previously been in the employ of the Corporation (or any Parent or Subsidiary) shall be eligible to receive one or more such annual option grants over their period of continued Board service.

B. **Exercise Price**.

1. The exercise price per share shall be equal to one hundred percent (100%) of the Fair Market Value per share of Common Stock on the option grant date.

2. The exercise price shall be payable in one or more of the alternative forms authorized under the Discretionary Option Grant Program. Except to the extent the sale and remittance procedure specified thereunder is utilized, payment of the exercise price for the purchased shares must be made on the Exercise Date.

C. **Option Term**. Each option shall have a term of ten (10) years measured from the option grant date.

D. **Exercise and Vesting of Options**. Each initial 20,000 share option grant shall be immediately exercisable for any or all of the option shares as fully vested shares of Common Stock and shall remain so exercisable until the expiration or sooner termination of the option term. Each annual 5,000 share grant shall also be immediately exercisable for any or all of the option shares. However, the shares of Common Stock purchased under each annual 5,000 share grant shall be subject to repurchase by the Corporation, at the exercise price paid per share, upon the Optionee's cessation of Board service prior to vesting in those shares. Each annual 5,000 share grant shall vest, and the Corporation's repurchase right shall lapse, in a series of four (4) successive equal annual installments upon the Optionee's

completion of each year of Board service over the four (4) year period measured from the automatic grant date.

E. **Termination of Board Service**. The following provisions shall govern the exercise of any options held by the Optionee at the time the Optionee ceases to serve as a Board member:

(i) The Optionee (or, in the event of Optionee's death, the personal representative of the Optionee's estate or the person or persons to whom the option is transferred pursuant to the Optionee's will or in accordance with the laws of descent and distribution) shall have a twelve (12) month period following the date of such cessation of Board service in which to exercise each such option.

(ii) During the twelve (12) month exercise period, the option may not be exercised in the aggregate for more than the number of vested shares of Common Stock for which the option is exercisable at the time of the Optionee's cessation of Board service.

(iii) Should the Optionee cease to serve as a Board member by reason of death or Permanent Disability, then all shares at the time subject to the option shall immediately vest so that such option may, during the twelve (12) month exercise period following such cessation of Board service, be exercised for all or any portion of those shares as fully vested shares of Common Stock.

(iv) In no event shall the option remain exercisable after the expiration of the option term. Upon the expiration of the twelve (12) month exercise period or (if earlier) upon the expiration of the option term, the option shall terminate and cease to be outstanding for any vested shares for which the option has not been exercised. However, the option shall, immediately upon the Optionee's cessation of Board service for any reason other than death or Permanent Disability, terminate and cease to be outstanding to the extent the option is not otherwise at that time exercisable for vested shares.

II. CORPORATE TRANSACTION/CHANGE IN CONTROL/HOSTILE TAKEOVER

A. The shares of Common Stock subject to each option outstanding under this Article Four at the time of a Corporate Transaction but not otherwise vested shall automatically vest in full so that each such option shall, immediately prior to the effective date of the Corporate Transaction, become fully exercisable for all of the shares of Common Stock at the time subject to such option and may be exercised for all or any portion of those shares as fully vested shares of Common Stock. Immediately following the consummation of the Corporate Transaction, each automatic option grant shall terminate and cease to be outstanding, except to the extent assumed by the successor corporation (or parent thereof).

B. The shares of Common Stock subject to each option outstanding under this Article Four at the time of a Change in Control but not otherwise vested shall automatically vest in full so that each such option shall, immediately prior to the effective date of the Change in Control, become fully exercisable for all of the shares of Common Stock at the time subject to such option and may be exercised for all or any portion of those shares as fully vested shares of Common Stock. Each such option shall remain exercisable for such fully vested option shares until the expiration or sooner termination of the option term or the surrender of the option in connection with a Hostile Takeover.

C. All outstanding repurchase rights under the Automatic Option Grant Program shall automatically terminate, and the unvested shares of Common Stock subject to those terminated rights shall immediately vest in full, in the event of any Corporate Transaction or Change in Control.

D. Upon the occurrence of a Hostile Takeover, the Optionee shall have a thirty (30) day period in which to surrender to the Corporation each of his or her outstanding automatic option grants. The Optionee shall in return be entitled to a cash distribution from the Corporation in an amount equal to the excess of (i) the Takeover Price of the shares of Common Stock at the time subject to each surrendered option (whether or not the Optionee is otherwise at the time vested in those shares) over (ii) the aggregate exercise price payable for such shares. Such cash distribution shall be paid within five (5) days following the surrender of the option to the Corporation. Stockholder approval of the Plan on the Plan Effective Date shall constitute pre-approval of the grant of each such option surrender right under this Automatic Option Grant Program and the subsequent exercise of that right in accordance with the terms and provisions of this Section II.

E. No additional approval or consent of the Plan Administrator or the Board shall be required at the time of the actual option surrender and cash distribution.

F. Each option which is assumed in connection with a Corporate Transaction shall be appropriately adjusted, immediately after such Corporate Transaction, to apply to the number and class of securities which would have been issuable to the Optionee in consummation of such Corporate Transaction had the option been exercised immediately prior to such Corporate Transaction. Appropriate adjustments shall also be made to the exercise price payable per share under each outstanding option, provided the aggregate exercise price payable for such securities shall remain the same.

G. The grant of options under the Automatic Option Grant Program shall in no way affect the right of the Corporation to adjust, reclassify, reorganize or otherwise change its capital or business structure or to merge, consolidate, dissolve, liquidate or sell or transfer all or any part of its business or assets.

III. REMAINING TERMS

The remaining terms of each option granted under the Automatic Option Grant Program shall be the same as the terms in effect for option grants made under the Discretionary Option Grant Program.

ARTICLE FIVE

MISCELLANEOUS

I. FINANCING

The Plan Administrator may permit any Optionee or Participant to pay the option exercise price under the Discretionary Option Grant Program or the purchase price of shares issued under the Stock Issuance Program by delivering a full recourse, interest bearing promissory note payable in one or more installments. The terms of any such promissory note (including the interest rate and the terms of repayment) shall be established by the Plan Administrator in its sole discretion. In no event may the maximum credit available to the Optionee or Participant exceed the sum of (i) the aggregate option exercise price or purchase price payable for the purchased shares (less the par value of those shares) plus (ii) any Federal, state and local income and employment tax liability incurred by the Optionee or the Participant in connection with the option exercise or share purchase.

II. TAX WITHHOLDING

A. The Corporation's obligation to deliver shares of Common Stock upon the exercise of options or the issuance or vesting of such shares under the Plan shall be subject to the satisfaction of all applicable Federal, state and local income and employment tax withholding requirements.

B. The Plan Administrator may, in its discretion, provide any or all holders of Nonstatutory Options or unvested shares of Common Stock under the Plan (other than the options granted or the shares issued under the Automatic Option Grant Program) with the right to use shares of Common Stock in satisfaction of all or part of the Taxes incurred by such holders in connection with the exercise of their options or the vesting of their shares. Such right may be provided to any such holder in either or both of the following formats:

1. **Stock Withholding**: The election to have the Corporation withhold, from the shares of Common Stock otherwise issuable upon the exercise of such Nonstatutory Option or the vesting of such shares, a portion of those shares with an aggregate Fair Market Value equal to the percentage of the Taxes (not to exceed one hundred percent (100%)) designated by the holder.

2. **Stock Delivery**: The election to deliver to the Corporation, at the time the Nonstatutory Option is exercised or the shares vest, one or more shares of Common Stock previously acquired by such holder (other than in connection with the option exercise or share vesting triggering the Taxes) with an aggregate Fair Market Value equal to the percentage of the Taxes (not to exceed one hundred percent (100%)) designated by the holder.

III. EFFECTIVE DATE AND TERM OF THE PLAN

A. The Plan was adopted by the Board on July 25, 1997 and shall become effective upon approval by the Corporation's stockholders at the 1997 Annual Meeting held on the Plan Effective Date.

B. The Plan shall terminate upon the earliest to occur of (i) July 25, 2007, (ii) the date on which all shares available for issuance under the Plan shall have been issued as fully vested shares or (iii) the termination of all outstanding options in connection with a Corporate Transaction. Upon such

plan termination, all outstanding option grants and unvested stock issuances shall thereafter continue to have force and effect in accordance with the provisions of the documents evidencing those grants or issuances.

IV. AMENDMENT OF THE PLAN

A. The Board shall have complete and exclusive power and authority to amend or modify the Plan in any or all respects. However, no such amendment or modification shall adversely affect the rights and obligations with respect to stock options or unvested stock issuances at the time outstanding under the Plan unless the Optionee or the Participant consents to such amendment or modification. In addition, certain amendments may require stockholder approval pursuant to applicable laws or regulations.

B. The Board amended the Plan in 1999 to increase the number of shares of Common Stock reserved for issuance under the Plan from 530,000 to 930,000. The Plan was amended in 2000 to (1) increase the number of shares of Common Stock reserved for issuance under the Plan by an additional 400,000 shares, (2) increase the number of shares of Common Stock subject to the initial automatic option grant pursuant to the Automatic Option Grant Program from 5,000 shares to 20,000 shares and (3) increase the number of shares of Common Stock subject to the annual automatic option grant pursuant to the Automatic Option Grant Program from 4,000 shares to 5,000 shares. In 2001, the Plan was amended to increase the number of shares of Common Stock reserved for issuance under the Plan by 475,000 shares. In 2002, the Plan was amended to comply with the requirements of the California Department of Corporations. In 2004, the Plan was amended to reflect the new corporate name of the Corporation and the new name for its Common Stock.

C. Options to purchase shares of Common Stock may be granted under the Discretionary Option Grant Program and shares of Common Stock may be issued under the Stock Issuance Program that are in each instance in excess of the number of shares then available for issuance under the Plan, provided any excess shares actually issued under those programs shall be held in escrow until there is obtained stockholder approval of an amendment sufficiently increasing the number of shares of Common Stock available for issuance under the Plan. If such stockholder approval is not obtained within twelve (12) months after the date the first such excess issuances are made, then (i) any unexercised options granted on the basis of such excess shares shall terminate and cease to be outstanding and (ii) the Corporation shall promptly refund to the Optionees and the Participants the exercise or purchase price paid for any excess shares issued under the Plan and held in escrow, together with interest (at the applicable Short Term Federal Rate) for the period the shares were held in escrow, and such shares shall thereupon be automatically cancelled and cease to be outstanding.

V. USE OF PROCEEDS

Any cash proceeds received by the Corporation from the sale of shares of Common Stock under the Plan shall be used for general corporate purposes.

VI. REGULATORY APPROVALS

A. The implementation of the Plan, the granting of any stock option under the Plan and the issuance of any shares of Common Stock (i) upon the exercise of any granted option or (ii) under the Stock Issuance Program shall be subject to the Corporation's procurement of all approvals and permits required by regulatory authorities having jurisdiction over the Plan, the stock options granted under it and the shares of Common Stock issued pursuant to it.

B. No shares of Common Stock or other assets shall be issued or delivered under the Plan unless and until there shall have been compliance with all applicable requirements of Federal and state securities laws, including the filing and effectiveness of the Form S-8 registration statement for the shares of Common Stock issuable under the Plan, and all applicable listing requirements of any stock exchange (or the Nasdaq National Market, if applicable) on which Common Stock is then listed for trading.

VII. NO EMPLOYMENT/SERVICE RIGHTS

Nothing in the Plan shall confer upon the Optionee or the Participant any right to continue in Service for any period of specific duration or interfere with or otherwise restrict in any way the rights of the Corporation (or any Parent or Subsidiary employing or retaining such person) or of the Optionee or the Participant, which rights are hereby expressly reserved by each, to terminate such person's Service at any time for any reason, with or without cause.

VIII. CALIFORNIA BLUE SKY PROVISIONS

If the Common Stock is not exempt from California securities laws, the following provisions shall apply to any sale of Common Stock or any option grant to an individual who is eligible to receive such grants pursuant to the Plan who resides in the State of California.

A. **Option Grant Program.**

1. If the person to whom the option is granted is a 10% Stockholder, then the exercise price per share shall not be less than 110% of the Fair Market Value per share of Common Stock on the date the option is granted.

2. The Plan Administrator may not impose a vesting schedule upon any option grant or the shares of Common Stock subject to that option which is more restrictive than 20% per year vesting, with the initial vesting to occur not later than one year after the option grant date. However, such limitation shall not be applicable to any option grants made to individuals who are officers of the Corporation, non-employee Board members or consultants.

3. Unless the Optionee's Service is terminated for Misconduct (in which case the option shall terminate immediately), the option (to the extent it was vested and exercisable at that the time Optionee's Service ceased) must remain exercisable, following Optionee's termination of Service, for at least (a) six months if Optionee's Service terminates due to death or Permanent Disability or (b) thirty days in all other cases.

B. **Stock Issuance Program**. The Plan Administrator may not impose a vesting schedule upon any stock issuance effected under the Stock Issuance Program which is more restrictive than 20% per year vesting, with initial vesting to occur not later than one year after the issuance date. Such limitation shall not apply to any Common Stock issuances made to the officers of the Corporation, non-employee Board members or consultants.

C. **Repurchase Rights**. To the extent specified in a stock purchase agreement or stock issuance agreement, the Corporation and/or its stockholders shall have the right to repurchase any or all of the unvested shares of Common Stock held by an Optionee or Participant when such person's Service ceases. However, except with respect to grants to officers, non-employee Board members, and consultants of the Corporation, the repurchase right must satisfy the following conditions:

1. The Corporation's right to repurchase the unvested shares of Common Stock must lapse at the rate of at least 20% per year over five years from the date the option was granted or the shares were issued under the Plan.

2. The Corporation's repurchase right must be exercised within ninety days of the date that Service ceased (or the date the shares were purchased, if later).

3. The purchase price must be paid in the form of cash or cancellation of the purchase money indebtedness for the shares of Common Stock.

D. **Information Requirements**. Annually, the Corporation shall deliver or cause to be delivered to each Optionee or Participant, no later than such information is delivered to the Corporation's security holders, one of the following:

1. The Corporation's annual report to security holders containing the information required by Rule 14a-3(b) under the 1934 Act for its latest fiscal year;

2. The Corporation's annual report on Form 10-K for its latest fiscal year;

3. The Corporation's latest prospectus filed pursuant to 424(b) under the 1933 Act that contains audited financial statements for the latest fiscal year, provided that the financial statements are not incorporated by reference from another filing, and provided further that such prospectus contains substantially the information required by Rule 14a-3(b); or

4. The Corporation's effective 1934 Act registration statement containing audited financial statements for the latest fiscal year.

APPENDIX

The following definitions shall be in effect under the Plan:

A. **Automatic Option Grant Program** shall mean the automatic option grant program in effect under the Plan.

B. **Board** shall mean the Corporation's Board of Directors.

C. **Change in Control** shall mean a change in ownership or control of the Corporation effected through either of the following transactions:

(i) the acquisition, directly or indirectly by any person or related group of persons (other than the Corporation or a person that directly or indirectly controls, is controlled by, or is under common control with, the Corporation), of beneficial ownership (within the meaning of Rule 13d-3 of the 1934 Act) of securities possessing more than fifty percent (50%) of the total combined voting power of the Corporation's outstanding securities pursuant to a tender or exchange offer made directly to the Corporation's stockholders, or

(ii) a change in the composition of the Board over a period of thirty- six (36) consecutive months or less such that a majority of the Board members ceases, by reason of one or more contested elections for Board membership, to be comprised of individuals who either (A) have been Board members continuously since the beginning of such period or (B) have been elected or nominated for election as Board members during such period by at least a majority of the Board members described in clause (A) who were still in office at the time the Board approved such election or nomination.

D. **Common Stock** shall mean the Corporation's Common Stock, which shall be registered under Section 12(g) of the 1934 Act and shall be entitled to one-tenth of one vote per share on all matters subject to stockholder approval.

E. **Code** shall mean the Internal Revenue Code of 1986, as amended.

F. **Corporate Transaction** shall mean either of the following stockholder approved transactions to which the Corporation is a party:

(i) a merger or consolidation in which securities possessing more than fifty percent (50%) of the total combined voting power of the Corporation's outstanding securities are transferred to a person or persons different from the persons holding those securities immediately prior to such transaction, or

(ii) the sale, transfer or other disposition of all or substantially all of the Corporation's assets in complete liquidation or dissolution of the Corporation.

G. **Corporation** shall mean Iteris, Inc., a Delaware corporation (formerly known as Odetics, Inc. and Iteris Holdings, Inc.) and its successors.

H. **Discretionary Option Grant Program** shall mean the discretionary option grant program in effect under the Plan.

I. **Eligible Director** shall mean a non-employee Board member eligible to participate in the Automatic Option Grant Program in accordance with the eligibility provisions of Article One.

J. **Employee** shall mean an individual who is in the employ of the Corporation (or any Parent or Subsidiary), subject to the control and direction of the employer entity as to both the work to be performed and the manner and method of performance.

K. **Exercise Date** shall mean the date on which the Corporation shall have received written notice of the option exercise.

L. **Fair Market Value** per share of Common Stock on any relevant date shall be determined in accordance with the following provisions:

(i) If the Common Stock is at the time traded on the Nasdaq National Market, then the Fair Market Value shall be deemed equal to the closing selling price per share of Common Stock on the date in question, as such price is reported on the Nasdaq National Market or any successor system. If there is no closing selling price for the Common Stock on the date in question, then the Fair Market Value shall be the closing selling price on the last preceding date for which such quotation exists.

(ii) If the Common Stock is at the time listed on any Stock Exchange, then the Fair Market Value shall be deemed equal to the closing selling price per share of Common Stock on the date in question on the Stock Exchange determined by the Plan Administrator to be the primary market for the Common Stock, as such price is officially quoted in the composite tape of transactions on such exchange. If there is no closing selling price for the Common Stock on the date in question, then the Fair Market Value shall be the closing selling price on the last preceding date for which such quotation exists.

M. **Hostile Takeover** shall mean the acquisition, directly or indirectly, by any person or related group of persons (other than the Corporation or a person that directly or indirectly controls, is controlled by, or is under common control with, the Corporation) of beneficial ownership (within the meaning of Rule 13d-3 of the 1934 Act) of securities possessing more than fifty percent (50%) of the total combined voting power of the Corporation's outstanding securities pursuant to a tender or exchange offer made directly to the Corporation's stockholders which the Board does not recommend such stockholders to accept.

N. **Incentive Option** shall mean an option which satisfies the requirements of Code Section 422.

O. **Involuntary Termination** shall mean the termination of the Service of any individual which occurs by reason of:

(i) such individual's involuntary dismissal or discharge by the Corporation for reasons other than Misconduct, or

(ii) such individual's voluntary resignation following (A) a change in his or her position with the Corporation which materially reduces his or her duties and responsibilities or the level of management to which he or she reports, (B) a reduction in his or her level of compensation (including base salary, fringe benefits and target bonus under any corporate performance based bonus or incentive programs) by more than fifteen percent (15%) or

(C) a relocation of such individual's place of employment by more than fifty (50) miles, provided and only if such change, reduction or relocation is effected by the Corporation without the individual's consent.

P. **Misconduct** shall mean the commission of any act of fraud, embezzlement or dishonesty by the Optionee or Participant, any unauthorized use or disclosure by such person of confidential information or trade secrets of the Corporation (or any Parent or Subsidiary), or any other intentional misconduct by such person adversely affecting the business or affairs of the Corporation (or any Parent or Subsidiary) in a material manner. The foregoing definition shall not be deemed to be inclusive of all the acts or omissions which the Corporation (or any Parent or Subsidiary) may consider as grounds for the dismissal or discharge of any Optionee, Participant or other person in the Service of the Corporation (or any Parent or Subsidiary).

Q. **1934 Act** shall mean the Securities Exchange Act of 1934, as amended.

R. **1933 Act** shall mean the Securities Act of 1933, as amended.

S. **Nonstatutory Option** shall mean an option not intended to satisfy the requirements of Code Section 422.

T. **Optionee** shall mean any person to whom an option is granted under the Discretionary Option Grant or Automatic Option Grant Program.

U. **Parent** shall mean any corporation (other than the Corporation) in an unbroken chain of corporations ending with the Corporation, provided each corporation in the unbroken chain (other than the Corporation) owns, at the time of the determination, stock possessing fifty percent (50%) or more of the total combined voting power of all classes of stock in one of the other corporations in such chain.

V. **Participant** shall mean any person who is issued shares of Common Stock under the Stock Issuance Program.

W. **Permanent Disability** or **Permanently Disabled** shall mean the inability of the Optionee or the Participant to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment expected to result in death or to be of continuous duration of twelve (12) months or more. However, solely for purposes of the Automatic Option Grant Program, Permanent Disability or Permanently Disabled shall mean the inability of the non-employee Board member to perform his or her usual duties as a Board member by reason of any medically determinable physical or mental impairment expected to result in death or to be of continuous duration of twelve (12) months or more.

X. **Plan** shall mean the Corporation's 1997 Stock Incentive Plan, as set forth in this document.

Y. **Plan Administrator** shall mean the particular entity, whether the Primary Committee, the Board or the Secondary Committee, which is authorized to administer the Discretionary Option Grant and Stock Issuance Programs with respect to one or more classes of eligible persons, to the extent such entity is carrying out its administrative functions under those programs with respect to the persons under its jurisdiction.

Z. **Plan Effective Date** shall mean September 5, 1997, the date of the 1997 Annual Stockholders Meeting at which the Plan is approved by the Corporation's stockholders.

AA. **Primary Committee** shall mean the committee of two (2) or more non- employee Board members appointed by the Board to administer the Discretionary Option Grant and Stock Issuance Programs with respect to Section 16 Insiders.

BB. **Secondary Committee** shall mean a committee of one (1) or more Board members appointed by the Board to administer the Discretionary Option Grant and Stock Issuance Programs with respect to eligible persons other than Section 16 Insiders.

CC. **Section 16 Insider** shall mean an officer or director of the Corporation subject to the short swing profit liabilities of Section 16 of the 1934 Act.

DD. **Service** shall mean the performance of services for the Corporation (or any Parent or Subsidiary) by a person in the capacity of an Employee, a non- employee member of the board of directors or a consultant or independent advisor, except to the extent otherwise specifically provided in the documents evidencing the option grant or stock issuance.

EE. **Stock Exchange** shall mean either the American Stock Exchange or the New York Stock Exchange.

FF. **Stock Issuance Agreement** shall mean the agreement entered into by the Corporation and the Participant at the time of issuance of shares of Common Stock under the Stock Issuance Program.

GG. **Stock Issuance Program** shall mean the stock issuance program in effect under the Plan.

HH. **Subsidiary** shall mean any corporation (other than the Corporation) in an unbroken chain of corporations beginning with the Corporation, provided each corporation (other than the last corporation) in the unbroken chain owns, at the time of the determination, stock possessing fifty percent (50%) or more of the total combined voting power of all classes of stock in one of the other corporations in such chain.

II. **Takeover Price** shall mean the greater of (i) the Fair Market Value per share of Common Stock on the date the option is surrendered to the Corporation in connection with a Hostile Takeover or (ii) the highest reported price per share of Common Stock paid by the tender offeror in effecting such Hostile Takeover. However, if the surrendered option is an Incentive Option, the Takeover Price shall not exceed the clause (i) price per share.

JJ. **Taxes** shall mean the Federal, state and local income and employment tax liabilities incurred by the holder of Nonstatutory Options or unvested shares of Common Stock in connection with the exercise of those options or the vesting of those shares.

KK. **10% Stockholder** shall mean the owner of stock (as determined under Code Section 424(d)) possessing more than ten percent (10%) of the total combined voting power of all classes of stock of the Corporation (or any Parent or Subsidiary).

Exhibit 21

LIST OF SUBSIDIARIES

Subsidiary	State of Incorporation
Meyer Mohaddes Associates, Inc.	California

Exhibit 23.1

Consent of Independent Registered Public Accounting Firm

We hereby consent to the incorporation by reference of our report dated June 1, 2005 (except for the four paragraphs under the caption "Deferred Compensation Plan" in Note 7 as to which the date is July 12, 2005) relating to our audit of the consolidated financial statements and financial statement schedule appearing in this Annual Report on Form 10-K of Iteris, Inc. for the year ended March 31, 2005 in the previously filed Registration Statements of Iteris, Inc. on Form S-1 (File No. 333-117353), on Form S-3 (File No. 333-121942) and on Form S-8 (File Nos. 333-75728, 333-05735, 333-44907 and 333-30396).

/s/ McGladrey & Pullen, LLP

Irvine, California
July 13, 2005

Exhibit 23.2

Consent of Independent Registered Public Accounting Firm

We consent to the incorporation by reference in the Registration Statement (Form S-1 No. 333-117353) of Iteris, Inc. and in the related Prospectus, and in the Registration Statements (Form S-8 Nos. 333-75728, 333-05735, 333-44907 and 333-30396) of our report dated June 8, 2004, except for Note 1 – Restatement of Consolidated Financial Statements for the Year Ended March 31, 2004, and Note 7 – Deferred Compensation Plan, as to which the date is July 13, 2005, with respect to the restated consolidated financial statements and schedule of Iteris, Inc. included in the Annual Report (Form 10-K) for the year ended March 31, 2005.

/s/ Ernst & Young LLP
Irvine, California
July 13, 2005

EXHIBIT 31.1

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

I, Jack Johnson, certify that:

1. I have reviewed this annual report on Form 10-K of Iteris, 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)) 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 Subsidiary, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) 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

(c) 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.

Date: July 13, 2005

/s/ JACK JOHNSON
Jack Johnson
Chief Executive Officer
(*Principal Executive Officer*)

EXHIBIT 31.2

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

I, James S. Miele, certify that:

1. I have reviewed this annual report on Form 10-K of Iteris, 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)) 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 Subsidiary, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) 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

(c) 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.

Date: July 13, 2005

/s/ JAMES S. MIELE
James S. Miele
Chief Financial Officer
(*Principal Financial Officer*)

Exhibit 32.1

CERTIFICATION PURSUANT TO 18 U.S.C. §1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Iteris, Inc. (the "Company") on Form 10-K for the fiscal year ended March 31, 2005, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Jack Johnson, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully 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 Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: July 13, 2005

/s/ JACK JOHNSON
Jack Johnson,
Chief Executive Officer

A signed original of this written statement required by Section 906, or any other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

Exhibit 32.2

CERTIFICATION PURSUANT TO 18 U.S.C. §1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Iteris, Inc. (the "Company") on Form 10-K for the fiscal year ended March 31, 2005 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, James S. Miele, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully 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 Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: July 13, 2005

/s/ JAMES S. MIELE
James S. Miele,
Chief Financial Officer

A signed original of this written statement required by Section 906, or any other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.