

**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, 2012

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
(State or Other Jurisdiction
of Incorporation or Organization)

95-2588496
(I.R.S. Employer
Identification No.)

1700 Carnegie Ave., Santa Ana, California 92705
(Address of Principal Executive Offices) (Zip Code)

Registrant's Telephone Number, Including Area Code: **(949) 270-9400**

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

<u>Title of each class</u>	<u>Name of each exchange on which registered</u>
Common Stock, \$0.10 par value	NYSE Amex

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

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

Based on the closing sale price of the registrant's common stock on 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 approximately \$33,247,000. 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 1, 2012, there were 33,998,351 shares of our common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Part III incorporates by reference certain information from the registrant's definitive proxy statement for the 2012 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, 2012. Except with respect to information specifically incorporated by reference in this report, the registrant's proxy statement is not deemed to be filed as a part hereof.

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FOR THE FISCAL YEAR ENDED MARCH 31, 2012
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Unless otherwise indicated in this report, the "Company," "we," "us" and "our" refer to Iteris, Inc. and our wholly-owned subsidiaries.

Iteris®, Vantage®, Abacus®, VantageView™, VersiCam™, Pico™, RZ-4™, Vantage Vector™, iPerform™ and IterisPeMS™ are among the trademarks of Iteris, Inc. Any other trademarks or trade names mentioned herein are the property of their respective owners.

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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," "would," "could," "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 future sales, revenue and operating results, expansion plans, market share, capital needs, competition, backlog and manufacturing capabilities, acceptance of our products and services, and the impact of recent accounting pronouncements. 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 in "Risk Factors" in Item 1A 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**

We are a leading provider of intelligent information solutions to the traffic management market. We are focused on the development and application of advanced technologies and software-based information systems that reduce traffic congestion, provide measurement, management and predictive traffic analytics and improve the safety of surface transportation systems infrastructure. We believe that our products, services and solutions, in conjunction with sound traffic management, minimize the environmental impact of traffic congestion. By combining our image processing, traffic engineering, information technology, and other products and services, we offer a broad range of Intelligent Transportation Systems ("ITS") solutions to customers worldwide.

We were originally incorporated in Delaware in 1987. Our principal executive offices are located at 1700 Carnegie Avenue, Santa Ana, California 92705, and our telephone number at that location is (949) 270-9400. Our Internet website address is www.iteris.com. Our annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K, together with amendments to these reports, are available on the "Investors" section of our website, free of charge, as soon as reasonably practicable after such material is electronically filed with, or furnished to, the Securities and Exchange Commission ("SEC"). The inclusion of our website address in this report does not include or incorporate by reference into this report any information on our website.

Sale of Vehicle Sensors

On July 29, 2011, we completed the sale of substantially all of the assets used in connection with our Vehicle Sensors segment to Bendix Commercial Vehicle Systems LLC ("Bendix"), a member of Knorr-Bremse Group, pursuant to an Asset Purchase Agreement signed on July 25, 2011 (the "Asset Sale"). Upon closing, Bendix paid us \$14 million in cash, subject to a \$2 million holdback and adjustments based upon the working capital of the Vehicle Sensors segment at closing, and Bendix assumed certain specified obligations and liabilities of the Vehicle Sensors segment. We are entitled to additional consideration in the form of certain performance and royalty-related earn-outs. As a result of the Asset Sale, we no longer operate in the Vehicle Sensors segment and we determined that the Vehicle Sensors segment, which previously constituted one of our operating segments, qualifies as a discontinued operation. Refer to Note 3 of Notes to Consolidated Financial Statements, included in Part IV, Item 15 of this report for additional discussion on this transaction. The applicable financial results of the Vehicle Sensors segment through the closing of the Asset Sale have been reported as a discontinued operation for all periods presented.

Products and Services

As a result of the sale of Vehicle Sensors in July 2011, and a reevaluation and reorganization of our operating segments in the first quarter of the fiscal year ended March 31, 2012, we currently operate in two reportable segments: Roadway Sensors and Transportation Systems. The Roadway Sensors segment includes, among other products, our Vantage, Versicam, Pico, Vantage Vector and Abacus vehicle detection systems for traffic intersection control, incident detection and certain highway traffic data collection applications. The Transportation Systems segment includes transportation engineering and consulting services, and the development of transportation management and traveler information systems for the ITS industry. See Note 13 of Notes to Consolidated Financial Statements, included in Part IV, Item 15 of this report, for further details on our reportable segments.

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Our Roadway Sensors segment product line uses advanced image processing technology to capture and analyze video images through sophisticated algorithms, enabling vehicle detection and transmission of both video images and data using various communication technologies.

- Our Vantage video detection systems detect vehicle presence at intersections, as well as vehicle count, speed and other traffic data used in traffic management systems. Our Vantage systems give traffic managers the ability to mitigate roadway congestion by modifying traffic signal timing or detecting incidents quickly. Our VantageView software supplements our Vantage video detection systems by providing an integrated platform to manage and “see” video detection assets remotely over a network connection.
- Our Vantage Vector product is an all-in-one vehicle detection sensor with a wide range of capabilities: stop bar detection, advanced-zone detection, and sensing that enables advanced safety and adaptive control applications. It includes all the proven benefits of Iteris video detection, including high accuracy, high availability remote viewing of video images, no trenching or pavement cutting for installation, bicycle detection capability and high precision for dilemma zone detection by integrating the video field-of-view with radar sensing. Enhanced information includes the number of vehicles, speed, and distance in user configurable zones that can be used for special applications.
- VersiCam, our integrated camera and processor video detection system, is a cost-efficient video detection system for smaller intersections that require only a few detection points.
- Pico, our compact video detection system, was developed primarily to address international video detection needs, and was designed for easy installation and configuration.
- Our Abacus products take advantage of the large number of existing installed closed-circuit television video feeds designed to monitor roadways, signalized intersections, tunnels and bridges to allow for data collection and incident detection without the set-up and calibration generally required with other systems.

We believe that future growth domestically and internationally, particularly in developing countries, will be dependent in part on the continued adoption of above-ground video detection technologies, instead of traditional in-pavement loop technology, to manage traffic.

We have historically experienced seasonality, particularly with respect to our Roadway Sensors net sales in our third and fourth fiscal quarters due to a reduction in road construction and repairs during the winter months due to inclement weather conditions.

Transportation Systems

Our Transportation Systems segment includes transportation engineering and consulting services focused on the planning, 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, design and implementation of surface transportation infrastructure systems. We perform analysis and study goods movement, study commercial vehicle operations, provide travel demand forecasting and systems engineering, and identify mitigation measures to reduce traffic congestion. This segment also includes the activities of Meridian Environmental Technology, Inc. (“MET”), which we acquired in January 2011, and which specializes in 511 advanced traveler information systems as well as Maintenance Decision Support System (“MDSS”) management tools that allow users to create solutions to meet roadway maintenance decision needs. The operations of Berkeley Transportation Systems, Inc. (“BTS”), which we acquired in November 2011, are also included in this segment. BTS specializes in transportation performance measurement and its Performance Measurement System leverages its real-time data collection, diagnostic, fusion and warehousing platform to aggregate and compute performance measures.

Our Transportation Systems segment is largely dependent upon governmental funding and is affected by state and local budgetary issues. We believe the overall expansion of our Transportation Systems segment in the future will at least in part be dependent on the passage of a new Federal Highway Bill. Congress is currently working on such a bill. The previous Federal Highway Bill expired in October 2009 but the funding levels under the expired bill have continued through a series of short-term extensions, the most recent of which extends funding through the end of June 2012. Continued delays in the enactment of such a new Federal Highway Bill, and until such time as a bill becomes law, will prolong the uncertainty regarding the allotment of transportation funds in federal, state and local budgets. We believe that prolonged uncertainty has adversely impacted, and may continue to adversely impact, our net sales and contract revenues and our overall financial performance in future periods.

With the addition of MET in January 2011, we have experienced seasonality particularly related to certain MDSS services in our first and second fiscal quarters mainly because MDSS services are generally not required in the summer months.

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During the fiscal year ended March 31, 2012 (“Fiscal 2012”), we began the development of IterisPeMS. IterisPeMS is an advanced, real-time data collection, diagnostic, fusion and warehousing software platform used to aggregate and compute performance measures across multiple transportation modes, including travel time, travel time variability, delay and lost throughput. This information can then be analyzed by traffic professionals to measure how a transportation network is performing and identify potential areas of improvement. IterisPeMS is also capable of providing users with easy-to-use visualization and animation features for both historical and predictive traffic conditions. Costs incurred during Fiscal 2012, which include research and development expense as well as sales and marketing expenditures were not allocated to either of the Roadway Sensors or Transportation Systems segments as this project

was deemed to be a corporate level development.

Sales, Marketing and Principal Customers

We sell our Roadway Sensors products through indirect sales channels comprised of a network of independent dealers in the U.S. and certain foreign locations, who sell integrated systems and related products to the traffic management market, as well as directly to the traffic management market using a combination of our own sales personnel and an outside sales organization. Our independent dealers are trained in, and primarily responsible for, sales, installation, set-up and support of our products, and maintain an inventory of demonstration traffic products from various manufacturers and sell directly to government agencies and installation contractors. These dealers often have long-term arrangements with local government agencies in their respective territories for the supply of various products for the construction and renovation of traffic intersections, and are generally well-known suppliers of high-quality ITS products to the traffic management market. We periodically hold technical training classes for our dealers and end users and maintain a full-time staff of customer support technicians throughout the U.S. to provide technical assistance when needed. When appropriate, we have the ability to modify or make changes to our dealer network to accommodate the needs of the market and our customer base. In the states where we sell directly, we use our own staff to sell, oversee installations and set-up issues and support our products.

We market and sell our Transportation Systems services directly to government agencies pursuant to negotiated contracts that involve competitive bidding and specific qualification requirements. Most of our contracts are with federal, state and municipal customers and generally provide for cancellation or renegotiation at the option of the customer upon reasonable notice and fees paid for modification. We generally use selected members of our engineering, science and information technology teams on a regional basis to serve in sales and business development functions. Our contracts generally involve long lead times and require extensive specification development, evaluation and price negotiations.

A large portion of our revenues are derived from sales to federal, state and local government agencies. We currently have a diverse customer base, and no individual customer represented greater than 10% of our total net sales and contract revenues in Fiscal 2012 and in the fiscal years ended March 31, 2011 ("Fiscal 2011") and March 31, 2010 ("Fiscal 2010"). Also refer to Note 13 of Notes to Consolidated Financial Statements, included in Part IV, Item 15 of this report.

Manufacturing and Materials

We use contract manufacturers to build subassemblies that are used in our roadway sensors products. Additionally, we procure certain components from qualified suppliers, both globally and locally, and generally use multi-sourcing strategies when technically and economically feasible to mitigate supply risk. These subassemblies and components are delivered to our Santa Ana, California facility where they go through final assembly and testing prior to shipment to our customers. Our key suppliers include CTS Electronics Manufacturing Solutions, Inc., Total Electronics LLC, Sony Electronics, Inc. and LG Electronics, Inc. Our manufacturing activities are conducted in approximately 9,000 square feet of space at our Santa Ana facility. Production volume at our subcontractors is based upon quarterly forecasts that we generally adjust on a monthly basis to control inventory levels. We typically 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 products, as well as follow-up service and support for which we charge separately. Such service revenue was not a material portion of our total net sales and contract revenues for each of Fiscal 2012, Fiscal 2011 and Fiscal 2010. We believe customer support is a key competitive factor.

Backlog

Our total backlog of unfulfilled firm orders was approximately \$35.0 million as of March 31, 2012, which was comprised of \$3.2 million related to Roadway Sensors and \$31.8 million related to Transportation Systems. Substantially the entire backlog for Roadway Sensors is expected to be recognized as revenue in the fiscal year ending March 31, 2013. We have historically recognized between 50% to 70% of our Transportation Systems backlog as of the end of a fiscal year in the subsequent fiscal year, and currently expect that trend to continue for the near future.

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At March 31, 2011, we had backlog of approximately \$28.2 million, which was comprised of \$2.7 million related to Roadway Sensors and \$25.5 million related to Transportation Systems.

The timing and realization of our backlog is subject to the inherent uncertainties of doing business with federal, state and local governments, particularly in view of budgetary constraints, cut-backs and other delays or reallocations of funding that these entities typically face.

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, in particular for our Roadway Sensors segment.

Product Development

Most of our product development activities are conducted at our principal facilities in Santa Ana, California. Our research and development costs and expenses were approximately \$3.2 million for Fiscal 2012, \$2.4 million for Fiscal 2011 and \$2.6 million for Fiscal 2010. We expect to continue to pursue various product development programs and incur research and development expenditures in future periods.

We believe our engineering and product development capabilities are a competitive strength. We strive to continue to develop new products to meet the needs of the ever-changing ITS market as well as enhance and refine our existing product lines. Within the last four fiscal years, our Roadway Sensors segment has introduced our VersiCam and VersiCam wireless products, Pico, RZ-4 Advanced camera and our RZ-4 Advanced Wide Dynamic Range camera, which significantly improve video detection performance in certain harsh lighting conditions, and within the last fiscal year, Vantage Vector. We have also upgraded our Abacus and VantageView software products within the last fiscal year. Additionally, during Fiscal 2012, we began development of our IterisPeMS Performance Measurement System. We plan to continue this development effort in our fiscal year ending March 31, 2013. We believe that developing new offerings across our segments and enhancing, refining and marketing our existing products is a key component of strong organic growth and profitability.

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.

In the market for our Roadway Sensors vehicle detection products, we compete with manufacturers and distributors of other above ground video camera detection systems 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, which have historically, and currently continue to be, the predominant detection system in this market.

The markets in which our Transportation Systems segment operates is highly fragmented and subject to evolving national and regional quality, operations and safety standards. Our competitors vary in number, scope and breadth of the products and services they offer. Our competitors in advanced Transportation Systems include national corporations. Our competitors in transportation engineering, planning and design include major regional firms, as well as many smaller local engineering firms.

In general, the markets for the products and services we offer 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.

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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 five U.S. patents, three pending foreign patents and two provisional patents. One U.S. patent, which expires in May 2019, is for general technology related to CMOS sensors. Four U.S. patents, which expire between 2013 and 2029, two pending foreign patents and two provisional patents relate specifically to our Roadway Sensors technology. One of these U.S. patents and the two pending foreign patents are for an Electronic Traffic Monitor related to our Abacus product in the Roadway Sensors segment. We cannot be certain that any new patents will be granted pursuant to these or subsequent applications. As a result of the Asset Sale, certain patents were transferred to Bendix. We believe these patents were specific to that segment and the transfer of ownership does not impair our proprietary rights related to our current product and service offerings.

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 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 March 31, 2012, we employed an aggregate of 264 full-time associates, including 57 associates in general management, administration and finance; 19 associates in sales and marketing; 160 associates in engineering and product development; 15 associates in operations, manufacturing and quality; and 13 associates in customer service. None of our associates are represented by a labor union, and we have never experienced a work stoppage. We believe our relations with our associates are good.

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 1A. 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.

The economic slowdown has reduced and delayed government funding for transportation infrastructure projects and initiatives, decreased availability of financial capital for our customers and adversely impacted real estate development, all of which have adversely impacted our net sales and contract revenues. Decreased consumer spending, the failure of certain financial institutions and businesses, concerns about the availability and cost of credit, and reduced corporate profits and capital spending have resulted in a downturn in worldwide economic conditions, as well as budgetary shortfalls at all levels of government. These unfavorable economic conditions are having a negative impact on customer orders and government funding of infrastructure projects

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incorporating our products and services. Such factors have and may continue to result in delays, cancellations and rescheduling of backlog and customer orders. In addition, the decline in the U.S. real estate market, particularly in new home and commercial construction, has adversely impacted new road construction and has had and may continue to have adverse effects on Transportation Systems contract revenues and Roadway Sensors net sales. Any of the foregoing economic conditions may adversely affect our net sales and contract revenues in future periods and make it extremely difficult for our customers, our suppliers and us to accurately forecast and plan future business activities. Additionally, there continues to be uncertainty regarding allotment of government funds due to delays in the passage of a new Federal Highway Bill, which has adversely impacted, and may continue to adversely impact, our net sales and contract revenues and overall financial performance in future periods. The previous Federal Highway Bill expired in October 2009 but the funding levels under the previous bill have been continued through a series of short-term extensions, the most recent of which extends funding through the end of June 2012. If the conditions above continue or worsen, or delays in the passage of a new Federal Highway Bill continue, our business, financial condition and results of operations could be materially and adversely affected.

Because we depend on government contracts and subcontracts, we face additional risks related to contracting with federal, state and local governments, including budgetary issues and fixed price contracts. A significant portion of our net sales and contract revenues are derived from contracts with governmental agencies, either as a general contractor, subcontractor or supplier. We anticipate that revenue from government contracts will continue to remain a significant portion of our net sales and contract revenues. Government business is, in general, subject to special risks and challenges, including:

- delays in funding and uncertainty regarding the allocation of funds to state and local agencies from the U.S. federal government as a result of delays in the passage of a new Federal Highway Bill, as well as delays or reductions in other state and local funding dedicated for transportation projects;
- other government budgetary constraints, cut-backs, delays or reallocation of government funding;
- performance bond requirements;
- long purchase cycles or approval processes;
- competitive bidding and qualification requirements;
- changes in government policies and political agendas;

- milestone requirements and liquidated damage provisions for failure to meet contract milestones; and
- international conflicts or other military operations that could cause the temporary or permanent diversion of government funding from transportation or other infrastructure projects.

Governmental budgets and plans are subject to change without warning. Certain risks of selling to governmental entities include dependence on appropriations and administrative allocation of funds, changes in governmental procurement legislation and regulations and other policies that may reflect political developments or agendas, significant changes in contract scheduling, intense competition for government business and termination of purchase decisions for the convenience of the governmental entity. Substantial delays in purchase decisions by governmental entities, and the current constraints on government budgets at the federal, state and local level, could cause our net sales and contract revenues and income to drop substantially or to fluctuate significantly between fiscal periods.

In addition, a 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 and contract revenues in any given period. 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.

California state budgetary constraints may have a material adverse impact on us. The state of California has experienced, and is continuing to experience, a significant budget shortfall and other related budgetary issues and constraints. The state of California has historically been and is considered to be a key geographic region for our Roadway Sensors and Transportation Systems segments. Ongoing uncertainty as to the timing and accessibility of budgetary funding, changes in state funding allocations to local agencies and municipalities, or other delays in purchasing for, or commencement of, transportation projects have had and may continue to have a negative impact on our net sales and contract revenues and our income.

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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 pressures in the marketplace as technologies mature;
- changes in customer requirements;
- additional qualification requirements related to new products or components;
- frequent new product introductions and enhancements;
- inventory issues related to transition to new or enhanced models; 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.

The markets in which we operate are highly competitive and have many more established competitors, which could adversely affect our net sales and contract revenues 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 compete with existing, well-established companies in our Roadway Sensors segment, both domestically and abroad. Certain technological barriers to entry make it difficult for new competitors to enter the market with competing video or other technologies; however, we are aware of new market entrants from time to time. Increased competition could result in loss of market share, price reductions and reduced gross margins, any of which could seriously harm our business, financial condition and results of operations.

The Transportation Systems market is highly fragmented and is subject to evolving national and regional quality and safety standards. Our competitors vary in size, number, scope and breadth of the products and services they offer, and include large multi-national engineering firms and smaller local regional firms.

In both of our segments, 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. Consolidations of end users,

distributors and manufacturers in our target markets exacerbate 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 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 completed three acquisitions since April 2009 and, in the future, we may acquire additional 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;

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- 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, as well as unanticipated accounting charges.

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.

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. The loss of any of our officers, or any of our other executives 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. In particular, the future success of our Transportation Systems segment will depend on our ability to hire additional qualified engineers and planners. Competition for qualified 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.

Our profitability could be adversely affected if we are not able to maintain adequate utilization of our Transportation Systems workforce. The cost of providing our Transportation Systems engineering and consulting services, including the extent to which we utilize our workforce, affects our profitability. The rate at which we utilize our workforce is affected by a number of factors, including:

- our ability to transition employees from completed projects to new assignments and to hire and assimilate new employees;
- our ability to forecast demand for our services and thereby maintain an appropriate headcount in our various regions;
- our need to devote time and resources to training, business development, professional development and other non-chargeable activities; and
- our ability to match the skill sets of our employees to the needs of the marketplace.

Our use of the percentage of completion method of accounting for our contract revenues could result in a reduction or reversal of previously recorded revenues and profits. A significant portion of contract revenues are measured and recognized using the percentage of completion method of accounting. Our use of this accounting method results in recognition of revenues and profits ratably over the life of a contract, based generally on the proportion of costs incurred to date to total costs expected to be incurred for the entire project. The effects of revisions to revenues and estimated costs are recorded when the amounts are known or can be reasonably estimated. Such revisions could occur in any period and their effects could be material. Although we have historically made reasonably reliable estimates of the progress towards completion of long-term engineering, program management, construction management or construction contracts, the uncertainties inherent in the estimating process make it possible for actual costs to vary materially from estimates, including reductions or reversals of previously recorded revenues and profits.

Our failure to successfully bid on new contracts and renew existing contracts could reduce our revenues and profits. Our business depends on our ability to successfully bid on new contracts and renew existing contracts with private and public sector customers. Contract proposals and negotiations are complex and frequently involve a lengthy bidding and selection process, which are affected by a number of factors, such as market conditions, financing

arrangements and required governmental approvals. For example, a customer may require us to provide a surety bond or letter of credit to protect the client should we fail to perform under the terms of the contract. If negative market conditions continue, or if we fail to secure adequate financing arrangements or the required governmental approval or fail to meet other required conditions, we may not be able to pursue particular projects, which could reduce or eliminate our profitability.

We may experience production gaps that could materially and adversely impact our sales and financial results and the ultimate acceptance of our products. It is possible that we could experience unforeseen quality control issues or part shortages as we adjust production to meet current demand for our products. We have historically used single suppliers for certain significant components in our products. Should any such delay or disruption occur, or should a key supplier discontinue operations because of the

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current economic climate, our future sales will likely be materially and adversely affected. Additionally, we rely heavily on select contract manufacturers to produce many of our products and do not have any long-term contracts to guarantee supply of such products. Although we believe our contract manufacturers have sufficient capacity to meet our production schedules for the foreseeable future and we believe we could find alternative contract manufacturing sources for many of our products, if necessary, we could experience a production gap if for any reason our contract manufacturers were unable to meet our production requirements and our cost of goods sold could increase, adversely affecting our margins.

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 production costs. We cannot guarantee the success of these products, and 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.

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. We cannot assure you that we will be able to adequately manage product transition issues. 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 or if we cannot adequately manage inventory issues typically related to new product transitions and introductions. We cannot assure you that any such investments in research and development will lead to any corresponding increase in revenue.

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.

Our international business operations may be threatened by many factors that are outside of our control. While we historically have had limited international sales, contract revenues and operations experience, we began work on our first overseas contracts in the United Arab Emirates in the fiscal year ended March 31, 2010. We plan to expand our international efforts in the future with respect to all of our segments, but cannot assure you that we will be successful in those efforts. International operations subject us to various inherent risks including, among others:

- currency fluctuations and restrictions;
- political, social and economic instability, as well as international conflicts and acts of terrorism;
- longer accounts receivable payment cycles;
- import and export license requirements and restrictions of the U.S. and each other country in which we operate;
- 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;
- difficulties in managing and staffing international operations;
- potentially adverse tax consequences; and
- reduced protection for intellectual property rights in some countries.

Substantially all of our international sales 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 currently engage in any transactions as a hedge against risks of loss due to foreign currency fluctuations.

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Any of the factors mentioned above may adversely affect our future international sales and contract revenues and, consequently, affect our business, financial condition and operating results. Additionally, as we pursue the expansion of our international business, certain fixed and other overhead costs could outpace our revenues, thus adversely affecting our results of operations. We may likewise face local competitors in certain international markets who are more established, have greater economies of scale and stronger customer relationships. 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.

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. Section 404 of the Sarbanes-Oxley Act of 2002 currently requires us to evaluate the effectiveness of our internal controls over financial reporting at the end of each fiscal year and to include a management report assessing the effectiveness of our internal controls over financial reporting in all annual reports. As a smaller reporting company, for our fiscal year ended March 31, 2012, we are exempt from the auditor attestation requirement over our internal control over financial reporting; however, to the extent we do not qualify as a non-accelerated filer or smaller reporting company in subsequent fiscal years, we will be subject to the auditor attestation requirement under Section 404(b) of the Sarbanes-Oxley Act. In such an event, we may not be able to complete the work required for such attestation on a timely basis and, even if we timely complete such requirements, our independent registered public accounting firm may still conclude that our internal controls over financial reporting are not effective.

Our management, including our CEO and CFO, does not expect that our internal controls over financial reporting will prevent all errors 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 Iteris 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 errors or mistakes. 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, our 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.

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:

- delays in government contracts and funding from time to time and budgetary constraints at the federal, state and local levels;
- our ability to access stimulus funding, funding from a new Federal Highway Bill or other funding;
- declines in new home and commercial real estate construction and related road and other infrastructure construction;
- 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;
- the size, timing, rescheduling or cancellation of significant customer orders;
- our ability to control costs;
- our ability to raise additional capital;
- the mix of our products and services sold in a quarter, which has varied and is expected to continue to vary from time to time;
- seasonality due to winter weather conditions;
- seasonality with respect to revenues from our MDSS and related weather forecasting services due to the decrease in revenues generated for such services during the spring and summer time periods;

- 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;
- market acceptance of the products incorporating our technologies and products;
- the introduction of new products by competitors;
- the availability and cost of components used in the manufacture of our products;
- our success in expanding and implementing our sales and marketing programs;
- the effects of technological changes in our target markets;
- the amount of our backlog at any given time;
- the nature of our government contracts;
- 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;
- general economic and political conditions;
- international conflicts and acts of terrorism; and
- other factors beyond our control, including but not limited to, natural disasters such as the earthquake, tsunami and related events in Japan.

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.

We experienced declining or flat net sales and contract revenues in recent years. If we fail to manage this decline effectively, we may be unable to execute our business plan and may experience future weaknesses in our operating results. Based on our business objectives, and in order to achieve future growth, we will need to continue to add additional qualified personnel, and invest in additional research and development and sales and marketing activities, which could lead to increases in our expenses and future declines in our operating results. In addition, our past expansion has placed, and future expansion is expected to place, a significant strain on our managerial, administrative, operational, financial and other resources. If we are unable to manage these activities or any revenue declines successfully, our growth, our business, our financial condition and our results of operations could continue to be adversely affected.

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 U.S. As a result, we may not be able to protect our proprietary rights adequately in the U.S. or abroad.

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, including 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.

injuries that result from traffic accidents. As a provider of traffic engineering services, products and solutions, we have been and could in the future be subject to litigation for traffic related accidents from time to time even if our products or services had nothing to do with the particular accident. While we carry insurance against such claims, if the damages in any given action were high or we were subject to multiple lawsuits, the damages and costs could exceed the limits of our insurance coverage. If we were required to pay substantial damages as a result of these lawsuits, it may harm our business and financial condition. Even defending against unsuccessful claims could cause us to incur significant expenses and result in a diversion of management's attention.

We may need to raise additional capital in the future, which may not be available on terms acceptable to us, or at all. We have historically experienced volatility in our earnings and cash flows from operations from year to year. Although we have a \$12.0 million revolving line of credit, should we have an event of default, which includes, among other things, a failure to meet certain financial covenants and a material adverse change in the business, the bank could choose to limit or take away our ability to borrow these or any funds. Should this occur, or if the credit markets further tighten or our business declines, we may need or choose to raise additional capital to repay indebtedness, pursue acquisitions or expand our operations. 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, and such additional financing may result in further dilution to our stockholders.

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

- market acceptance of our products and product enhancements, and the overall level of sales of our products;
- our ability to control costs;
- the supply of key components for our products;
- our ability to increase revenue and net income;
- increased research and development expenses and sales and marketing expenses;
- our need to respond to technological advancements and our competitors' introductions of new products or technologies;
- capital improvements to new and existing facilities and enhancements to our infrastructure and systems;
- potential acquisitions of businesses and product lines;
- our relationships with customers and suppliers;
- government budgets, political agendas and other funding issues, including potential delays in government contract awards;
- our ability to successfully negotiate credit arrangements with our bank and the state of the financial markets, in general; 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 equity or debt financing may not be available on favorable terms, on a timely basis, 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.

We may be unable to maintain profitability on a quarterly or annual basis. We cannot assure you that we will be able to sustain or improve our financial performance, or that we will be able to continue to achieve profitability on a quarterly or annual basis in the future. Our ability to maintain profitability in future periods could be impacted by budgetary constraints, government and political agendas, economic instability and other items that are not in our control. 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 experience operating losses and net losses in the future, 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.

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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 April 2008, our common stock has traded at closing prices as low as \$0.90 per share and as high as \$2.98 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, improve cash flow and sustain profitability;

- 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;
- transitions to new products or product enhancements;
- acquisitions of businesses, products or technologies;
- the impact of any litigation;
- changes in investor perceptions;
- government funding, political agendas and other budgetary constraints;
- 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 from time to time experienced volatility, which has often 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.

Certain provisions of our charter documents may discourage a third party from acquiring us and may adversely affect the price of our common stock. Certain provisions of our certificate of incorporation 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. In August 2009, we adopted a new stockholder rights plan and declared a dividend of preferred stock purchase rights to our stockholders. Generally, the stockholder rights plan provides that if a person or group acquires 15% or more of our common stock, subject to certain exceptions and under certain circumstances, the rights may be exchanged by us for common stock or the holders of the rights, other than the acquiring person or group, could acquire additional shares of our capital stock at a discount off of the then current market price. Such exchanges or exercise of rights 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 1B. UNRESOLVED STAFF COMMENTS

None.

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ITEM 2. PROPERTIES

Our headquarters and principal operations are housed in approximately 52,000 square feet of leased office, manufacturing and warehouse space located in Santa Ana, California. This facility lease expires in 2015 and contains an option to extend the lease for an additional five years at the market rate at that time.

For additional information regarding our obligations under property leases, see Note 9 of Notes to Consolidated Financial Statements, included in Part IV, Item 15 of this report.

ITEM 3. LEGAL PROCEEDINGS

The information set forth under the heading "Litigation and Other Contingencies" under Note 9 of Notes to Consolidated Financial Statements, included in Part IV, Item 15 of this report, is incorporated herein by reference.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II**ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES****Market Information and Holders**

Our common stock is traded on the NYSE Amex under the symbol "ITI." The following table sets forth, for the periods indicated, the highest and lowest sales prices for our common stock as reported by NYSE Amex:

	High	Low
Fiscal 2012		
Quarter Ended June 30, 2011	\$ 1.58	\$ 1.22
Quarter Ended September 30, 2011	1.35	0.90
Quarter Ended December 31, 2011	1.39	1.08
Quarter Ended March 31, 2012	1.58	1.31
Fiscal 2011		
Quarter Ended June 30, 2010	\$ 2.25	\$ 1.26
Quarter Ended September 30, 2010	1.78	1.25
Quarter Ended December 31, 2010	1.93	1.33
Quarter Ended March 31, 2011	1.92	1.35

On June 1, 2012, the last reported sales price of our common stock on the NYSE Amex was \$1.42. As of June 1, 2012, we had 425 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.

Issuer Purchases of Equity Securities

On August 22, 2011, our Board of Directors approved a stock repurchase program. Under the program, we may acquire up to \$3 million of our outstanding common stock from time to time until August 2012. Purchases may be made in the open market (including pursuant to Rule 10b5-1 trading plans), in privately negotiated transactions or in block purchases, depending on market conditions, share price and other factors. The table below details our common stock repurchases during the fourth quarter of Fiscal 2012. All repurchased shares have been retired and resumed their status as authorized and unissued shares of our common stock.

Issuer Purchases of Equity Securities

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plans or Programs
Jan 1 to Jan 31, 2012	—	\$ —	—	
Feb 1 to Feb 29, 2012	239,273	1.48	239,273	
Mar 1 to Mar 31, 2012	—	—	—	
Total	239,273	\$ 1.48	239,273	\$ 2,239,470

ITEM 6. SELECTED FINANCIAL DATA

As a smaller reporting company, we are not required to make any disclosure pursuant to this Item 6.

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 in Item 1A, as well as other cautionary statements and risks described elsewhere in this report, before deciding to purchase, hold or sell our common stock.

Overview

General. We are a leading provider of intelligent information solutions to the traffic management market. We are focused on the development and application of advanced technologies and software-based information systems that reduce traffic congestion, provide measurement, management and predictive traffic analytics and improve the safety of surface transportation systems infrastructure. Additionally, we believe that our products, services and solutions, in conjunction with sound traffic management, minimize the environmental impact of traffic congestion. By combining image processing, traffic engineering, information technology and other products and services, we offer a broad range of ITS solutions to customers worldwide.

Acquisitions. In November 2011, we acquired all of the outstanding capital stock of Berkeley Transportation Systems, Inc. ("BTS"), a privately-held company based in Berkeley, California which specializes in transportation performance measurement. On or shortly after the acquisition date, we paid a total of approximately \$840,000 in cash. Additionally, we are scheduled to pay up to a total of \$1.5 million within 36 months after the acquisition date pursuant to holdback, deferred payment and earn-out provisions.

In January 2011, we acquired all of the capital stock of Meridian Environmental Technology, Inc. ("MET") for an initial cash payment of approximately \$1.6 million. MET specializes in 511 advanced traveler information systems and offers Maintenance Decision Support System ("MDSS") management tools that allow users to create solutions to meet roadway maintenance decision needs. We also agreed to pay up to \$1 million on each of the first two anniversaries of the closing of the acquisition, as well as up to an additional \$2 million under a 24-month earn-out provision. In January 2012, we made a cash payment of approximately \$668,000 of the first deferred payment to the shareholders of MET and held back \$250,000 in accordance with certain provisions of the purchase agreement. We expect the contingencies related to the \$250,000 holdback to be resolved sometime in the first fiscal quarter of the fiscal year ending March 31, 2013, at which time we may or may not release the holdback. Additionally, no amounts were earned by the MET shareholders related to the first year earn-out provision.

In April 2009, we completed the acquisition of certain assets of Hamilton Signal, Inc., which included the Abacus system, for an aggregate purchase price of approximately \$518,000 in cash.

Refer to Note 4 of Notes to Consolidated Financial Statements, included in Part IV, Item 15 of this report, for additional discussion on these acquisitions.

Sale of Vehicle Sensors. On July 29, 2011, we completed the sale of substantially all of our assets used in connection with our Vehicle Sensors segment to Bendix pursuant to an Asset Purchase Agreement signed on July 25, 2011 (the "Asset Sale"). Upon closing, Bendix paid us \$14 million in cash, subject to a \$2 million holdback and adjustments based upon the working capital of the Vehicle Sensors segment at closing, and Bendix assumed certain specified obligations and liabilities of the Vehicle Sensors segment. We are entitled to additional consideration in the form of certain performance and royalty-related earn-outs. As a result of the Asset Sale, we no longer operate in the Vehicle Sensors segment. Refer to Note 3 of Notes to Consolidated Financial Statements, included in Part IV, Item 15 of this report, for additional discussion on this transaction.

Business Segments. Subsequent to the Asset Sale, we now operate in two reportable segments: Roadway Sensors and Transportation Systems.

Roadway Sensors

The Roadway Sensors segment includes, among other products, our Vantage, Versicam, Pico, Vantage Vector and Abacus vehicle detection systems for traffic intersection control, incident detection and certain highway traffic data collection applications.

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Transportation Systems

The Transportation Systems segment includes transportation engineering and consulting services and the development of transportation management and traveler information systems for the ITS industry. This segment includes the operations of MET, which specializes in 511 advanced traveler information systems and offers MDSS management tools that allow users to create solutions to meet roadway maintenance decision needs. Also included in this segment are the operations of BTS, which specializes in transportation performance measurement.

Business. Given the current ongoing uncertainties regarding global economic conditions, we continue to remain cautious about our overall business. We believe the overall ongoing unfavorable economic environment has negatively affected, and may continue to negatively affect, our financial results for the foreseeable future, and may impair our ability to accurately forecast our future financial performance and other business trends. In addition, since the end users of a majority of our products and services are governmental entities, we have been, and may continue to be, negatively affected by the budgetary issues and delays in purchasing decisions that many municipalities and other state and local agencies continue to face. Spending for new roadways, new systems to address traffic congestion and other transportation infrastructure improvements has been delayed or eliminated in some instances. However, we believe the need to rebuild and modernize aging transportation infrastructure will continue, and in addition to funds available through recent federal stimulus packages and federal highway bills, there exist various other funding mechanisms that support transportation infrastructure and related projects. These include bonds, dedicated sales and gas tax measures and other alternative funding sources.

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 accounting principles generally accepted in the United States. 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 collectability of accounts receivable, the valuation of inventories, the recoverability of long-lived assets and goodwill, the realizability of deferred tax assets, accounting for stock-based compensation, the valuation of equity instruments, warranty reserves and other contingencies. 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. Product revenues and related costs of sales are recognized when all of the following criteria are met: (i) persuasive evidence of an arrangement exists, (ii) delivery has occurred, (iii) the price to the customer is fixed or determinable and (iv) collection of the receivable is reasonably assured. These criteria are typically met at the time of product shipment, but in certain circumstances, may not be met until receipt or acceptance by the customer. Accordingly, at the date revenue is recognized, the significant obligations or uncertainties concerning the sale have been resolved.

We recognize revenue from the sale of deliverables that are part of a multiple-element arrangement in accordance with applicable accounting guidance that establishes a relative selling price hierarchy permitting the use of an estimated selling price to determine the allocation of arrangement consideration to a deliverable in a multiple-element arrangement where neither vendor specific objective evidence ("VSOE") nor third-party evidence ("TPE") of fair value is available for that deliverable. In the absence of VSOE or TPE of the standalone selling price for one or more delivered or undelivered elements that have stand alone value in a multiple-element arrangement, we are required to estimate the selling prices of those elements. Overall arrangement consideration is allocated to each element (both delivered and undelivered items) based on their relative selling prices, regardless of whether those selling prices are evidenced by VSOE or TPE or are based on our estimated selling prices.

We account for multiple-element arrangements that consist only of software and software-related services in accordance with industry-specific accounting guidance for software and software-related transactions. For such transactions, revenue on arrangements that include multiple elements is allocated to each element based on the relative fair value of each element, and fair value is determined by VSOE. If we cannot objectively determine the fair value of any undelivered element included in such multiple-element arrangements and the only undelivered element is post-contract customer support or maintenance, and VSOE of the fair value of such support or maintenance does not exist, revenue from the entire arrangement is recognized ratably over the support period. When the

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fair value of a delivered element has not been established but VSOE of fair value exists for the undelivered elements, we use the residual method to recognize revenue if the fair value of all undelivered elements is determinable. Under the residual method, the fair value of the undelivered elements is deferred and the remaining portion of the arrangement fee is allocated to the delivered elements and is recognized as revenue.

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

Contract Revenues

Contract revenues are derived primarily from long-term contracts with governmental agencies. When appropriate, contract revenues are recognized using the percentage of completion method of accounting. Under this method, revenue is recognized as contract performance progresses, and is based on the relationship of costs incurred to total estimated costs. We generally utilize a cost-to-cost approach in applying the percentage of completion method, whereby revenue is earned in proportion to total costs incurred, divided by total costs expected to be incurred. Costs are generally determined from actual hours of labor effort expended. Direct non-labor costs are charged as incurred plus any mark-up permitted under the contract. Certain of our contract revenues are recognized as services are performed and amounts are earned, which is measured by time incurred or other contractual milestones or output measures. Contract revenues accounted for in this manner generally relate to certain cost-plus fixed fee or time-and-materials contracts for which no specific maximum contract values are stipulated.

Any anticipated losses on contracts are charged to operations 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 contract revenues when their realization is reasonably assured. Under the percentage of completion method, recognition of profit is dependent upon the accuracy of a variety of estimates, including engineering progress, materials quantities, and achievement of milestones, incentives, penalty provisions, labor productivity, cost estimates and others. Such estimates are based on various professional judgments we make with respect to those factors and are subject to change as the project proceeds and new information becomes available. We have a history of making reasonably dependable estimates of the extent of progress towards completion and contract completion costs on our long-term contracts. However, due to uncertainties inherent in the estimation process, it is possible that actual completion costs may vary from our estimates. To the

extent there are material differences between our estimates and our actual results, our future results of operations will be affected.

Substantially all of our contracts are of the following types:

Cost-Plus Fixed Fee. Under cost-plus fixed fee contracts, we charge our customers for our costs, including both direct and indirect costs, plus a fixed negotiated fee.

Fixed-Price. Under fixed-price contracts, our customers pay us an agreed fixed amount negotiated in advance for a specified scope of work. Prior to completion, our recognized profit margins on any fixed price contract depend on the accuracy of our estimates and will increase to the extent that our current estimates of aggregate actual costs are below amounts previously estimated. Conversely, if our current estimated costs exceed prior estimates, our profit margins will decrease and we may realize a loss on a project.

Time-and-Materials. Under our time-and-materials contracts, we negotiate hourly billing rates and charge our customers based on the actual time that we spend on a project. In addition, customers reimburse us for our actual out-of-pocket costs of materials and other direct incidental expenditures incurred in connection with our performance under the contract. The majority of our time-and-material contracts are subject to maximum contract values and, accordingly, revenues under these contracts are generally recognized under the percentage of completion method.

Accounts Receivable. We estimate the collectability of customer receivables on an ongoing basis by reviewing invoices outstanding greater than a certain period of time. We record an allowance for doubtful accounts for specific receivables deemed to be at risk for collection as well as a general allowance based on our historical collections experience. Considerable judgment is required in assessing and estimating 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.

Inventories. Inventories consist of finished goods, work-in-process and raw materials and are stated at the lower of cost or market. We write down the carrying value of our inventories to net realizable value for estimated excess and obsolete inventories in an amount equal to the difference between the cost of the inventories and their estimated realizable value. These estimates are based on management's judgments and assumptions as to future demand requirements and our evaluation of market conditions. Demand for our

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products may fluctuate significantly over time, and actual demand and market conditions may be more or less favorable than those projected by management. In the event that actual demand is lower than originally projected, additional inventory write-downs may be required. Estimated inventory write-downs, once established, are not reversed until the related inventory has been sold or scrapped, so if actual market conditions are more favorable in the fiscal periods subsequent to those in which we record significant write-downs, we may have higher gross margins when products are sold.

Goodwill and Other Long-Lived Assets. Goodwill is recorded as the difference, if any, between the aggregate consideration paid for an acquisition and the fair value of the acquired net tangible and intangible assets. Other long-lived assets primarily represent purchased intangible assets including developed technology, customer relationships, trade names and patents. We currently amortize our intangible assets with definitive lives over periods ranging from one to seven years using a method that reflects the pattern in which the economic benefits of the intangible asset are consumed or otherwise used or, if that pattern cannot be reliably determined, using a straight-line amortization method over the estimated useful life of the asset.

We evaluate goodwill on an annual basis in our fourth fiscal quarter or more frequently if we believe indicators of impairment exist. We have determined that our reporting units for purposes of testing for goodwill impairment are identical to our reportable segments for financial reporting purposes. In Fiscal 2012, we early adopted the new provisions issued by the Financial Accounting Standard Board ("FASB") that are intended to simplify goodwill impairment testing. This guidance permits us to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If we conclude that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, we conduct a two-step goodwill impairment test. The first step of the impairment test involves comparing the fair values of the applicable reporting units with their carrying values. We determine the fair values of our reporting units using the income valuation approach, as well as other generally accepted valuation methodologies. If the carrying amount of a reporting unit exceeds the reporting unit's fair value, we perform the second step of the goodwill impairment test. The second step of the goodwill impairment test involves comparing the implied fair value of the affected reporting unit's goodwill with the carrying value of that goodwill. The amount by which the carrying value of the goodwill exceeds its implied fair value, if any, is recognized as an impairment loss.

We test long-lived assets and purchased intangible assets (other than goodwill) for impairment if we believe indicators of impairment exist. We determine whether the carrying value of an asset or asset group is recoverable, based on comparisons to undiscounted expected future cash flows the asset are expected to generate. If an asset is not recoverable, we record an impairment loss equal to the amount by which the carrying value of the asset exceeds its fair value. We primarily use the income valuation approach to determine the fair value of our long lived assets and purchased intangible assets.

Warranty. We generally 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 in the accompanying consolidated balance sheets. Should our actual experience of warranty returns be higher than anticipated, additional warranty reserves may be required, which would adversely affect our product gross profit and our operating results.

Income Taxes. We utilize the asset and liability method of accounting for income taxes, under which deferred taxes are determined based on the temporary differences between the financial statement and tax basis of assets and liabilities using tax rates expected to be in effect during the years in which the

basis differences reverse. A valuation allowance is recorded when it is more-likely-than-not that some or all of the deferred tax assets will not be realized, which increases 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, while also separately considering applicable discrete and other non-recurring items, 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 financial results during the year. This estimation process can result in significant changes to our expected effective tax rate. When this occurs, we adjust our income tax provision during the quarter in which our estimates are refined so that the year-to-date provision reflects the expected annual effective tax rate. These changes, along with adjustments to our deferred taxes, among others, may create fluctuations in our overall effective tax rate from quarter to quarter.

Income tax positions must meet a more-likely-than-not recognition threshold to be recognized. Income tax positions that previously failed to meet the more-likely-than-not threshold are recognized in the first subsequent financial reporting period in which that threshold is met. Previously recognized tax positions that no longer meet the more-likely-than-not threshold are derecognized in the first subsequent financial reporting period in which that threshold is no longer met.

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The application of tax laws and regulations is subject to legal and factual interpretation, judgment and uncertainty. Tax laws and regulations themselves are subject to change as a result of changes in fiscal policy, changes in legislation, the evolution of regulations and court rulings. Therefore, the actual liability for U.S. or foreign taxes may be materially different from our estimates, which could result in the need to record additional tax liabilities or potentially reverse previously recorded tax liabilities.

Stock-Based Compensation. We record stock-based compensation in the statements of operations as an expense, based on the estimated grant date fair value of our stock-based awards, whereby such fair values are amortized over the requisite service period. Our stock-based awards are currently comprised of common stock options and restricted stock units. The fair value of our common stock option awards is estimated on the grant date using the Black-Scholes-Merton option-pricing formula. While utilizing this model meets established requirements, the estimated fair values generated by it may not be indicative of the actual fair values of our common stock option awards as it does not consider certain factors important to those awards to employees, such as continued employment and periodic vesting requirements as well as limited transferability. The fair value of our restricted stock units is based on the closing market price of our common stock on the grant date. If there are any modifications or cancellations of the underlying unvested stock-based awards, we may be required to accelerate, increase or cancel any remaining unearned stock-based compensation expense.

Recent Accounting Pronouncements

Refer to Note 1 of Notes to Consolidated Financial Statements, included in Part IV, Item 15 of this report, for a discussion of recent accounting pronouncements.

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.

	Year Ended March 31,		
	2012	2011	2010
Net sales and contract revenues:			
Net sales	47.4%	54.3%	49.0%
Contract revenues	52.6	45.7	51.0
Total net sales and contract revenues	100.0%	100.0%	100.0%
Costs of net sales and contract revenues:			
Cost of net sales	22.9	25.9	23.8
Cost of contract revenues	37.6	30.1	33.6
Gross profit	39.5	44.0	42.6
Operating expenses:			
Selling, general and administrative	30.8	32.7	30.4
Research and development	5.4	4.7	5.1
Amortization of intangible assets	0.9	0.3	0.2
Change in fair value of contingent acquisition consideration	(1.1)	0.1	0.0
Impairment of goodwill	0.0	15.3	0.0
Total operating expenses	36.0	53.1	35.7
Operating income (loss)	3.5	(9.1)	6.9
Non-operating income (expense):			
Other income, net	0.0	0.0	0.1
Interest expense, net	(0.1)	(0.3)	(0.5)
Income (loss) from continuing operations before income taxes	3.4	(9.4)	6.5
Provision for income taxes	(1.1)	(0.5)	(1.9)
Income (loss) from continuing operations	2.3	(9.9)	4.6

Gain on sale of discontinued operation, net of tax	2.0	0.0	0.0
Income (loss) from discontinued operation, net of tax	0.0	(0.1)	(0.4)
Net income (loss)	4.3%	(10.0)%	4.2%

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Analysis of Fiscal 2012, Fiscal 2011 and Fiscal 2010 Results of Operations

Net Sales and Contract Revenues. Net sales are comprised of sales from our Roadway Sensors segment. Contract revenues consist of revenues from our Transportation Systems segment.

The following tables present details of our net sales and contract revenues for Fiscal 2012 compared to Fiscal 2011, and Fiscal 2011 compared to Fiscal 2010:

	Year Ended March 31,		Increase (Decrease)	% Change
	2012	2011		
(In thousands, except percentages)				
Net sales	\$ 27,679	\$ 28,208	\$ (529)	(1.9)%
Contract revenues	30,727	23,758	6,969	29.3
Total net sales and contract revenues	\$ 58,406	\$ 51,966	\$ 6,440	12.4

	Year Ended March 31,		Increase (Decrease)	% Change
	2011	2010		
(In thousands, except percentages)				
Net sales	\$ 28,208	\$ 25,341	\$ 2,867	11.3%
Contract revenues	23,758	26,413	(2,655)	(10.1)
Total net sales and contract revenues	\$ 51,966	\$ 51,754	\$ 212	0.4

We currently have a diverse customer base, and no individual customer represented greater than 10% of our total a net sales and contract revenues for Fiscal 2012, Fiscal 2011 or Fiscal 2010.

Net Sales

Net sales of Roadway Sensors products in Fiscal 2012 were marginally lower compared to Fiscal 2011 due primarily to certain international customer orders in Fiscal 2011 which did not recur in the current year. We believe we continued to gain domestic market share in Fiscal 2012, mainly as a result of new product introductions and other competitive advantages; however, our gains in market share were offset in part by lower prices due to competitive pressures. The increase in Roadway Sensors net sales in Fiscal 2011, as compared to Fiscal 2010, were driven by higher unit sales domestically from both our direct sales and dealer markets, which was offset in part by lower prices due to competitive pressures. We also saw particular strength, both domestically and internationally, in certain of our newer product lines which were introduced within the previous two fiscal years. Additionally, we believe we gained market share as a result of these new product introductions.

Contract Revenues

Our contract revenues are primarily dependent upon the continued availability of funding at the local, state and federal levels from the various agencies and departments of transportation. Contract revenues in Fiscal 2012 increased compared to Fiscal 2011 in part due to several significant project wins in the last two quarters of Fiscal 2012. Additionally in Fiscal 2012, we recognized \$5.1 million and \$936,000 of total contract revenues derived from our acquisitions of MET and BTS, respectively, which contributed to the overall increase. In Fiscal 2012, the Transportation System segment continued to experience similar general lengthening of overall sales cycles, government budget constraints and funding delays and/or reductions on various existing contracts that existed in Fiscal 2011. Our Transportation Systems contract revenues decreased in Fiscal 2011 compared to Fiscal 2010 primarily as a result of the ongoing weakness in the markets this segment serves, which has been aggravated by the general lengthening of the overall sales cycle, from the bid and proposal process, to the signing of a contract and commencement of work on a project. Government budgeting constraints and funding delays or reductions on various existing contracts, particularly in the Southeast region of the U.S., also contributed to the decline in our contract revenues. Our private planning group, which focuses on private development consulting, has likewise experienced particular weakness. Additionally, our Fiscal 2011 contract revenues included approximately \$1.5 million of revenues attributable to MET, which we acquired in January 2011.

Going forward, we plan to continue to pursue larger contracts that may contain significant sub-consulting content, which will likely contribute to variability in the timing and amount of our contract revenues and margins from period to period. We also intend to continue to expand our foreign operations by pursuing additional international opportunities in the Middle East and other regions. Among other factors, we believe the ability of our Transportation Systems segment to grow and successfully win and service new contracts will be highly dependent upon our continued success in recruiting and retaining qualified personnel, as well as upon the passage of a new Federal Highway Bill and other government funding initiatives in the markets we serve.

Gross Profit. The following tables present details of our gross profit for Fiscal 2012 compared to Fiscal 2011, and Fiscal 2011 compared to Fiscal 2010:

	Year Ended March 31,		Increase	% Change
	2012	2011		
	(In thousands, except percentages)			
Total gross profit	\$ 23,071	\$ 22,884	\$ 187	0.8%
Total gross profit as a % of total net sales and contract revenues	39.5%	44.0%		
Gross profit as a % of net sales	51.6%	52.3%		
Gross profit as a % of contract revenues	28.6%	34.2%		

	Year Ended March 31,		Increase	% Change
	2011	2010		
	(In thousands, except percentages)			
Total gross profit	\$ 22,884	\$ 22,042	\$ 842	3.8%
Total gross profit as a % of total net sales and contract revenues	44.0%	42.6%		
Gross profit as a % of net sales	52.3%	51.4%		
Gross profit as a % of contract revenues	34.2%	34.1%		

Our total gross profit as a percentage of total net sales and contract revenues decreased in Fiscal 2012 compared to Fiscal 2011 primarily as a result of our product and service mix, whereby Transportation Systems consulting revenues (discussed below) significantly increased as percentage of the total. Our net sales (derived from our Roadway Sensors segment) represented approximately 47% of our total net sales and contract revenues in Fiscal 2012 compared to 54% in Fiscal 2011. Our net sales generally carry higher margins than our contract revenues, which are derived primarily from our consulting services. Our total gross profit as a percent of total net sales and contract revenues increased in Fiscal 2011 compared to Fiscal 2010 primarily as a result of our product and service mix. In Fiscal 2011, our net sales represented approximately 54% of our total net sales and contract revenues as compared to 49% in Fiscal 2010.

The decrease in gross profit as a percent of net sales in Fiscal 2012 as compared to Fiscal 2011 was primarily a result of sales mix as well as certain manufacturing overhead costs previously absorbed by sales of Vehicle Sensors products. The Vehicle Sensors segment was divested in July 2011. Our gross margin on net sales can fluctuate in any specific quarter or year based on, among other factors, customer and product mix, competitive pricing requirements, product warranty costs and provisions for excess and obsolete inventories, as well as shifts of engineering resources from development activities to sustaining activities, which we record as cost of goods sold.

The increase in gross margin on net sales in Fiscal 2011 as compared to Fiscal 2010 was primarily a result of higher overall net sales and higher margins in Roadway Sensors during Fiscal 2011. Such higher margins were largely driven by our customer mix and lower costs for certain key materials. We generally enjoy higher gross margins on direct product sales as compared to sales through our dealer channel.

We recognize contract revenues and related gross profit using percentage of completion contract accounting when appropriate, while certain of our contract revenues are recognized as services are performed and amounts are earned, which is measured by time incurred or other contractual milestones or output measures. Therefore, the underlying mix of contract activity can affect the related gross profit recognized in any given period. Gross profit as a percent of contract revenues in Fiscal 2012 was lower than in Fiscal 2011 primarily due to the overall mix of contract revenues which in the current year contained a significant proportion of lower-margin sub-consulting content as well as lower margins stemming from seasonality due to the decrease in revenues from certain of our MDSS and weather forecasting services in the spring and summer time periods. Gross profit as percent of contract revenues in Fiscal 2011 were highly consistent with those of Fiscal 2010. We expect the variability and timing of contract mix and related sub-consulting content in our Transportation Systems segment in future periods, as well as factors such as paid holidays and our ability to efficiently utilize our workforce, will cause fluctuations in our margins from contract revenues from period to period.

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Selling, General and Administrative Expense

The following table presents selling, general and administrative expense for Fiscal 2012 and Fiscal 2011:

	Year Ended March 31,		Amount	% of Net Sales and Contract Revenues	Increase (Decrease)	% Change
	2012	2011				
	(In thousands, except percentages)					
Salary and personnel-related	\$ 12,434	21.3%	\$ 11,952	23.0%	\$ 482	4.0%
Facilities, insurance and supplies	1,853	3.2	1,379	2.7	474	34.4
Travel and conferences	1,568	2.7	1,205	2.3	363	30.1
Professional and outside services	1,778	3.0	2,150	4.1	(372)	(17.3)

Other	353	0.6	295	0.6	58	19.7
Selling, general and administrative	\$ 17,986	30.8%	\$ 16,981	32.7%	\$ 1,005	5.9

The increase in selling, general and administrative expenses in Fiscal 2012 as compared to Fiscal 2011 was primarily due to (i) higher salary, travel and headcount-related expenses as we added certain key sales and marketing personnel, (ii) added personnel as well as facilities and other related operating costs as a result of the MET and BTS acquisitions, (iii) legal and professional services related to the sale of our Vehicle Sensors segment and (iv) certain other corporate initiatives related to the development of our performance measurement software.

The following table presents selling, general and administrative expense for Fiscal 2011 and 2010:

	Year Ended March 31,					
	2011		2010		Increase (Decrease)	% Change
	Amount	% of Net Sales and Contract Revenues	Amount	% of Net Sales and Contract Revenues		
(In thousands, except percentages)						
Salary and personnel-related	\$ 11,952	23.0%	\$ 10,496	20.3%	\$ 1,456	13.9%
Facilities, insurance and supplies	1,379	2.7	1,320	2.6	59	4.5
Travel and conferences	1,205	2.3	908	1.8	297	32.7
Professional and outside services	2,150	4.1	2,280	4.4	(130)	(5.7)
Other	295	0.6	706	1.4	(411)	(58.2)
Selling, general and administrative	\$ 16,981	32.7%	\$ 15,710	30.5%	\$ 1,271	8.1

The increase in selling, general and administrative expenses in Fiscal 2011 as compared to Fiscal 2010 was primarily due to (i) higher selling and commission-related expenses for our Roadway Sensors segment, as total net sales increased approximately 11% from Fiscal 2010 levels, (ii) higher salary and headcount-related expenses as we have added certain key sales and marketing personnel in all of our business segments, including as a result of the acquisition of MET in January 2011, and (iii) additional legal and professional services related to our acquisition of MET, along with various other corporate initiatives. We also saw a shift from cost of sales to sales and marketing of certain of our headcount expenses in our Transportation Systems segment in Fiscal 2011 commensurate with the overall decline in this segment's revenues and the reallocation of existing personnel in an effort to expand our contract backlog and increase contract revenues. Additionally, during Fiscal 2011, we realized approximately \$250,000 in reversals of certain previously recorded bad debt expense (included in the "Other" category in the table above) as a result of collecting certain large accounts receivable balances. In prior periods, we had recorded an estimated allowance for doubtful accounts against these receivables given the uncertainty of collection at that time. In the future, our operating results in any given period may be favorably or adversely impacted as a result of our estimates of the realization of our accounts receivable.

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Research and Development Expense

The following table presents research and development expense for Fiscal 2012 and Fiscal 2011:

	Year Ended March 31,					
	2012		2011		Increase (Decrease)	% Change
	Amount	% of Net Sales and Contract Revenues	Amount	% of Net Sales and Contract Revenues		
(In thousands, except percentages)						
Salary and personnel-related	\$ 2,153	3.7%	\$ 1,736	3.3%	\$ 417	24.0%
Facilities, development and supplies	792	1.3	557	1.1	235	42.2
Other	238	0.4	151	0.3	87	57.6
Research and development	\$ 3,183	5.4%	\$ 2,444	4.7%	\$ 739	30.2

Research and development expenses for Fiscal 2012 were higher than Fiscal 2011 primarily due to (i) the allocation of additional resources to various development projects in our Roadway Sensors segment, including our Vantage Vector vehicle detection sensor, (ii) development costs related to our IterisPeMS information management solution, and (iii) additional headcount and other expenses in Fiscal 2012 related to the MET and BTS acquisitions.

The following table presents research and development expense for Fiscal 2011 and 2010:

	Year Ended March 31,					
	2011		2010		Increase (Decrease)	% Change
	Amount	% of Net Sales and Contract Revenues	Amount	% of Net Sales and Contract Revenues		
(In thousands, except percentages)						
Salary and personnel-related	\$ 1,736	3.3%	\$ 1,857	3.6%	\$ (121)	(6.5)%

Facilities, development and supplies	557	1.1	692	1.3	(135)	(19.5)
Other	151	0.3	96	0.2	55	57.3
Research and development	<u>\$ 2,444</u>	<u>4.7%</u>	<u>\$ 2,645</u>	<u>5.1%</u>	<u>\$ (201)</u>	<u>(7.6)</u>

Research and development expenses for Fiscal 2011 were generally consistent, in total, with those of Fiscal 2010. We believe research and development activities are crucial to our ability to continue to be a leader in our markets.

Impairment of Goodwill

In Fiscal 2012, we early adopted the new provisions issued by the FASB that are intended to simplify goodwill impairment testing. The updated guidance permits us to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If we conclude that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, we conduct a two-step goodwill impairment test. We performed the annual impairment assessment of the carrying value of goodwill for Fiscal 2012 in the fourth fiscal quarter. Based on our assessments, we determined that no impairment was indicated as the estimated fair value of each reporting unit exceeded its respective carrying value.

During Fiscal 2011, due primarily to lower than expected operating results in our Transportation Systems reporting unit, as well as ongoing weakness specifically in the Transportation Systems markets, we determined it was necessary to perform an interim test of impairment of the carrying value of goodwill in our Transportation Systems reporting unit as of December 31, 2010. In performing the first step in this analysis, we estimated the fair value of our Transportation Systems reporting unit using the income approach. As of December 31, 2010, we determined that the carrying value of our Transportation Systems reporting unit exceeded its estimated fair value and, accordingly, we performed the second step of the impairment analysis to estimate the implied fair value of the goodwill of this reporting unit.

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The implied fair value of goodwill was determined in the same manner utilized to estimate the amount of goodwill recognized in a business combination. To determine this value, we estimated the fair value of the assets and liabilities, including certain intangible assets, to be allocated to the Transportation Systems reporting unit as of December 31, 2010. The implied fair value of goodwill was measured as the difference between the estimated fair value of the reporting unit over the estimated fair value amounts of its assets and liabilities. The impairment loss for the Transportation Systems reporting unit was measured by the amount the carrying value of its goodwill exceeded the implied fair value of the goodwill. Accordingly, in order to write down Transportation Systems goodwill with a carrying value of \$14.9 million to its implied fair value of \$6.9 million, we recorded an impairment charge of \$8.0 million in the three months ended December 31, 2010, the third quarter of Fiscal 2011.

As a result of the impairment charge taken in Fiscal 2011, we believe we have no goodwill at risk, as the estimated fair values of our Roadway Sensors and Transportations Systems reporting units significantly exceeded their carrying values at March 31, 2012. If our actual financial results, or the plans and estimates used in future goodwill impairment analyses, are lower than the original estimates used to assess for impairment of our goodwill, we could incur future goodwill impairment charges.

Interest Expense, Net

Net interest expense was approximately \$72,000, \$152,000 and \$264,000 in Fiscal 2012, Fiscal 2011 and Fiscal 2010, respectively. The sequential decreases were primarily due to our lower overall level of borrowings, as we continue to make monthly principal payments on our term note. See "Liquidity and Capital Resources" below for additional details on our borrowings.

Income Taxes

The following table presents our provision for income taxes for Fiscal 2012, Fiscal 2011 and Fiscal 2010:

	Year Ended March 31,		
	2012	2011	2010
	(In thousands, except percentages)		
Provision for income taxes	<u>\$ 643</u>	<u>\$ 278</u>	<u>\$ 960</u>
Effective tax rate	<u>33.0%</u>	<u>-5.7%</u>	<u>28.6%</u>

Our effective tax rate for Fiscal 2012 was favorably impacted by the recognition of approximately \$276,000 of previously unrecognized tax benefits during the year due to the expiration of statutes limitation in various jurisdictions, by the recognition of tax credits of approximately \$246,000 for research and development activities, and by approximately \$211,000 of tax benefit from non-taxable favorable fair value adjustments recognized for financial statement purposes. These favorable impacts were partially offset by the impact of recognizing approximately \$466,000 of expense upon the expiration of a state net operating loss, net of federal benefit. Our effective tax rate for Fiscal 2011 was impacted unfavorably by a portion of the charge recorded for the impairment of goodwill, amounting to approximately \$2.2 million, for which there is no corresponding tax basis. This unfavorable impact was partially offset by the impact of the recognition of approximately \$327,000 of previously unrecognized tax benefits during the year due to expiration of certain federal and state statutes in various jurisdictions. Our effective tax rate for Fiscal 2010 was favorably impacted by the recognition of approximately \$414,000 of unrecognized tax benefits during the year due to the expiration of certain federal and state statutes in various jurisdictions.

As of March 31, 2012 and 2011, respectively, we determined that it was more likely than not that our deferred tax assets will be realized.

Accordingly, no valuation allowance has been recorded against our deferred tax assets as of either such dates. In making our determination as to the realizability of our deferred tax assets, we reviewed all available positive and negative evidence, including reversal of deferred tax liabilities, potential carrybacks, projected future taxable income, tax planning strategies and recent financial performance.

As we update our estimates in future periods, adjustments to our deferred tax asset and valuation allowance may be necessary. We anticipate this will cause our future overall effective tax rate in any given period to fluctuate from prior effective tax rates and statutory tax rates. We utilize the liability method of accounting for income taxes. We record net deferred tax assets to the extent that we believe these assets will more likely than not be realized. In making such determination, we consider all available positive and negative evidence, including, but not limited to, scheduled reversals of deferred tax liabilities, projected future taxable income, tax planning strategies and recent financial performance.

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At March 31, 2012, we had \$25.0 million of federal net operating loss carryforwards and \$10.9 million of state net operating loss carryforwards that begin to expire in 2021 and 2014, respectively. Although the impact cannot be precisely determined at this time, we believe that our net operating loss carryforwards will cause us to have future income tax payments that are substantially lower than the income tax liability calculated using statutory tax rates. Due to changes in stock ownership, our federal net operating loss carryforwards and other federal attributes are subject to a Section 382 annual limitation.

Liquidity and Capital Resources

Cash Flows

We have historically financed our operations with a combination of cash flows from operations, borrowings under credit facilities and the sale of equity securities. We currently rely on cash flows from operations and the availability of borrowings on a line of credit facility to fund our operations, which we believe to be sufficient to fund our operations for at least the next twelve months. However, we may need or choose to raise additional capital to fund potential future acquisitions and our future growth. We may raise such funds by selling equity or debt securities to the public or to selected investors or by borrowing money from financial institutions. If we raise additional funds by issuing equity or convertible debt securities, our existing stockholders may experience significant dilution and any equity securities that may be issued may have rights senior to our existing stockholders.

At March 31, 2012, we had \$28.4 million in working capital, which included no borrowings on our \$12.0 million line of credit and \$18.7 million in cash and cash equivalents. This compares to working capital of \$24.8 million at March 31, 2011, which included no borrowings on our line of credit and \$11.8 million in cash and cash equivalents.

The following table summarizes our cash flows for Fiscal 2012, Fiscal 2011 and Fiscal 2010:

	Year Ended March 31,		
	2012	2011	2010
	(In thousands)		
Net cash provided by (used in):			
Operating activities	\$ 668	\$ 5,346	\$ 6,484
Investing activities	10,002	(1,530)	(594)
Financing activities	(3,787)	(2,403)	(1,857)

Operating Activities. Cash provided by our operations in Fiscal 2012 was the result of (i) adding back to net income \$907,000 of depreciation expense, \$331,000 of stock-based compensation expense, \$504,000 of amortization expense and \$286,000 of deferred tax assets, (ii) deducting from net income \$619,000 in changes in the fair value of contingent consideration related to our recent acquisition of MET and BTS and \$1.2 million for the gain on sale of Vehicle Sensors and (iii) \$2.1 million in negative cash flows resulting from changes in our operating assets and liabilities during Fiscal 2012, all of which was partially offset by our net income of \$2.5 million for such fiscal year.

Our accounts receivable and net costs and estimated earnings in excess of billings increased approximately \$3.0 million, or 22%, during Fiscal 2012 mainly as a result of a 12% year-over-year increase in net sales and contract revenues as well as the timing of collection on certain receivables. In the future, our accounts receivable and net costs and estimated earnings in excess of billings accounts are likely to be determined based upon, among other factors, increases or decreases in net sales and contract revenues, the timing of collections of existing receivables and our ability to timely bill billings in excess of costs amounts. We try to offset significant increases in accounts receivables through increased and focused collection efforts; however, we cannot assure you that our efforts will be successful.

The increase in accounts payable by approximately \$1.1 million during Fiscal 2012 was largely driven by the general timing of payments to vendors and sub-consultants.

Cash provided by our operations in Fiscal 2011 was the result of (i) \$9.9 million in non-cash items within the statement of operations, primarily \$8.0 million for the impairment of goodwill, depreciation expense of \$1.0 million and stock-based compensation expense of \$382,000; and (ii) \$614,000 in positive cash flows resulting from changes in our operating assets and liabilities during Fiscal 2011, all of which was partially offset by our net loss of \$5.2 million for such fiscal year.

Our inventories increased approximately \$953,000, or 35%, during Fiscal 2011 as we built up certain inventories on hand in Fiscal 2011 to meet anticipated increases in our product net sales in our the Roadway Sensors segment. In the future, our inventory levels are likely to continue to be determined

based upon, among other factors, the level of purchase orders we receive from our customers, the stage at which our products are in their respective product life cycles, and competitive situations in the marketplace. We attempt to balance such considerations against risk of obsolescence and potentially excess inventory levels.

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The increase in accounts payable by approximately \$920,000 from March 31, 2010 to March 31, 2011 was primarily driven by our increased inventory levels and the general timing of payments to vendors.

Cash provided by our operations in Fiscal 2010 was primarily the result of (i) our Fiscal 2010 net income of \$2.2 million; (ii) \$2.5 million in non-cash items within the statement of operations, primarily consisting of adjustments to our deferred tax assets of \$1.0 million, depreciation expense of \$986,000 and stock-based compensation expense of \$375,000; and (iii) \$1.7 million in cash resulting from changes in our operating assets and liabilities during the year.

Investing Activities. Cash provided by our investing activities for Fiscal 2012 consisted of (i) \$11.4 million in proceeds from the sale of the Vehicle Sensors segment, (ii) \$1.0 million used for the acquisition of MET and BTS, which consisted of \$840,000 for the initial purchase of BTS and \$129,000 related to purchase price adjustments for the purchase of MET, (iii) purchases of property and equipment of \$337,000 and (iv) capitalized software of \$138,000 related to IterisPeMS. Cash used in our investing activities for Fiscal 2011 consisted of \$1.1 million used for the acquisition of MET and purchases of property and equipment of \$414,000. Our investing activities for Fiscal 2010 consisted of purchases of property and equipment of \$294,000, as well as \$300,000 representing the initial payment for the acquisition of certain assets of Hamilton Signal, Inc. For further information on our acquisitions, refer to Note 4 of Notes to Consolidated Financial Statements included in Part IV, Item 15 of this report.

Financing Activities. Net cash used in our financing activities during Fiscal 2012 primarily consisted of \$2.3 million in payments on our long-term debt, which consists of a bank term note, \$112,000 for the second anniversary payment for the Hamilton Signal acquisition, \$676,000 related to the first year deferred payment to MET and \$754,000 used to repurchase our common stock under our stock repurchase program announced in August 2011. Net cash used in our financing activities during Fiscal 2011 primarily consisted of \$2.4 million in payments on our term note and \$106,000 for the first anniversary payment for the Hamilton Signal acquisition. Net cash used in our financing activities during Fiscal 2010 consisted of net payments on our term note of \$2.0 million. The net payments on our term note during Fiscal 2010 were partially offset by \$143,000 in proceeds received from the exercise in Fiscal 2010 of outstanding stock options to purchase shares of our common stock.

Borrowings

In October 2008, we entered into a \$19.5 million credit facility with California Bank & Trust (the "Bank"), which provided for a two-year revolving line of credit with borrowings of up to \$12.0 million and a \$7.5 million term note (discussed below). In September 2010, we entered into a modification agreement with the Bank to extend the expiration date of our revolving line of credit to October 1, 2012. Interest on borrowed amounts under the revolving line of credit are payable monthly at a rate equal to the current stated prime rate (3.25% at March 31, 2012) up to the current stated prime rate plus 0.50%, depending on aggregate deposit balances maintained at the bank in relation to the total loan commitment under the credit facility. We are obligated to pay an unused line fee of 0.25% per annum applied to the average unused portion of the revolving line of credit during the preceding month. The revolving line of credit does not contain any early termination fees and is secured by substantially all of our assets. As of March 31, 2012, no amounts were outstanding under the revolving line of credit portion of the facility. Availability under this line of credit may be reduced or otherwise limited as a result of our obligations to comply with certain financial covenants, as described further below.

As of March 31, 2012, we had outstanding borrowings of approximately \$634,000 under our bank term note, which expires on May 1, 2013. Principal payments under this term note are required to be repaid in monthly installments of \$152,000. Additionally, beginning on November 1, 2009, and on November 1 of each year thereafter, we are required to repay additional principal of up to \$500,000, calculated based on certain financial measures, as further defined in the loan agreement. These additional principal payments effectively reduce the total number of monthly installments necessary to repay the term note. To date, we have made additional principal payments of \$500,000 on each of November 1, 2011, 2010 and 2009. Interest on the term note is payable monthly at a rate equal to the current stated prime rate plus 0.50% up to the current stated prime rate plus 1.00%, depending on aggregate deposit balances maintained at the bank in relation to the total loan commitment under the credit facility. The term note contains no early termination fees and, along with our revolving line of credit discussed above, is secured by substantially all of our assets. We currently expect the remaining outstanding balance of the term note will be paid off in full by June 30, 2012.

In connection with our credit facility and loan agreement with the Bank, we are also required to comply with certain quarterly financial covenants. These include achieving ratios for working capital and debt service, as well as maintaining a level of profitability, all of which are further defined in the agreement. While we believe we are currently in compliance with all such financial covenants, we cannot assure you that we will not violate one or more covenants in the future. If we were to be in violation of covenants under this agreement, our lender could choose to accelerate payment on all outstanding loan balances and pursue its security interest in our assets. In this event, we cannot assure you that we would be able to quickly obtain equivalent or suitable replacement financing on acceptable terms, on a timely basis, or at all. If we were not able to secure alternative sources of financing, such acceleration would have a material adverse impact on our business and financial condition.

Off-Balance Sheet Arrangements

Other than our operating leases, which are further described at Note 9 of Notes to Consolidated Financial Statements, included in Part IV, Item 15 of this report, we do not believe we have any other material off-balance sheet arrangements at March 31, 2012.

Seasonality

We have historically experienced seasonality, particularly with respect to our Roadway Sensors net sales in our third and fourth fiscal quarters due to a reduction in road construction and repairs during the winter months due to inclement weather conditions. With the addition of MET in January 2011, we have also experienced seasonality related to certain MDSS services in our first and second fiscal quarters mainly because these services are generally not required in the summer months.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate Risk

Our exposure to interest rate risk is limited to our line of credit and our bank term note. Our line of credit bears interest equal to the prevailing prime rate (3.25% at March 31, 2012) plus 0% to 1.0%. We do not believe that a 10% increase in the interest rate on our line of credit or term note would 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 under our credit facility 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

None.

ITEM 9A. CONTROLS AND PROCEDURES

(a) *Evaluation of disclosure controls and procedures.* In accordance with Rule 13a-15(b) of the Securities Exchange Act of 1934, as of the end of the period covered by this Annual Report on Form 10-K, management evaluated, with the participation of the our President and Chief Executive Officer and the Chief Financial Officer, the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act). Based upon their evaluation of these disclosure controls and procedures, the President and Chief Executive Officer and the Chief Financial Officer have concluded that our disclosure controls and procedures were effective as of the date of such evaluation in ensuring that information required to be disclosed in our Exchange Act reports is (1) recorded, processed, summarized and reported in a timely manner, and (2) accumulated and communicated to management, including the Company's President and Chief Executive Officer and the Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

(b) *Changes in internal control.* There was no change in our internal control over financial reporting that occurred during the fourth quarter of Fiscal 2012 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Inherent Limitations on Internal Control

A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, 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 management override or improper acts, if any, have been detected. These inherent limitations include the realities that judgments in decision making can be faulty, and that breakdowns can occur because of simple errors. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any system of controls is also based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Because of the inherent limitations in a cost-effective control system, misstatements due to management override, error or improper acts may occur and not be detected. Any resulting misstatement or loss may have an adverse and material effect on our business, financial condition and results of operations.

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Management's Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Our internal control system was designed to provide reasonable assurance to management and our Board of Directors regarding the effectiveness of our internal control processes over the preparation and fair presentation of published financial statements.

We have assessed the effectiveness of our internal controls over financial reporting as of March 31, 2012. In making this assessment, we used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in Internal Control—Integrated Framework. Based

on our assessment, we believe that, as of March 31, 2012, our internal control over financial reporting is effective based on those criteria.

This annual report does not include an attestation report of our independent registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by our independent registered public accounting firm pursuant to the rules of the SEC applicable to smaller reporting companies.

ITEM 9B. OTHER INFORMATION

None.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

(a) *Identification of Directors.* The information under the caption "Election of Directors," appearing in our proxy statement for the 2012 Annual Meeting of Stockholders, is incorporated herein by reference.

(b) *Identification of Executive Officers.* The information under the caption "Executive Compensation and Other Information - Executive Officers," appearing in our proxy statement for the 2012 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 2012 Annual Meeting of Stockholders, is incorporated herein by reference.

(d) *Corporate Governance.* The information under the caption "Corporate Governance," appearing in our proxy statement for the 2012 Annual Meeting of Stockholders, is incorporated herein by reference.

(e) *Audit Committee.* The information under the caption "Board Meetings and Committees — Audit Committee," appearing in our proxy statement for the 2012 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 2012 Annual Meeting of Stockholders, is incorporated herein by reference.

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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 2012 Annual Meeting of Stockholders, is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information under the captions "Corporate Governance — Director Independence" and "Certain Transactions," appearing in our proxy statement for the 2012 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 Registered Public Accounting Firm," appearing in our proxy statement for the 2012 Annual Meeting of Stockholders, is incorporated herein by reference.

PART IV

ITEM 15. EXHIBITS, 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	34
Consolidated Balance Sheets as of March 31, 2012 and 2011	35
Consolidated Statements of Operations for the fiscal years ended March 31, 2012, 2011 and 2010	36
Consolidated Statements of Stockholders' Equity and Comprehensive Income (Loss) for the fiscal years ended March 31, 2012.	

2. *Exhibits.*

The exhibits listed on the accompanying Exhibit Index immediately following the financial statements are filed as part of, or hereby incorporated by reference into, this report.

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SIGNATURES

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

Dated: June 11, 2012

ITERIS, INC.
(Registrant)

By /s/ ABBAS MOHADDES
Abbas Mohaddes
Chief Executive Officer
(Principal Executive Officer)

POWER OF ATTORNEY

We, the undersigned officers and directors of Iteris, Inc., do hereby constitute and appoint James S. Miele and Abbas Mohaddes, 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:

<u>Signature</u>	<u>Title</u>	<u>Date</u>
<u>/s/ ABBAS MOHADDES</u> Abbas Mohaddes	Director, President and Chief Executive Officer (principal executive officer)	June 11, 2012
<u>/s/ JAMES S. MIELE</u> James S. Miele	Chief Financial Officer (principal financial and accounting officer)	June 11, 2012
<u>/s/ GREGORY A. MINER</u> Gregory A. Miner	Chairman of the Board	June 11, 2012
<u>/s/ RICHARD CHAR</u> Richard Char	Director	June 11, 2012
<u>/s/ KEVIN C. DALY</u> Kevin C. Daly, Ph.D.	Director	June 11, 2012
<u>/s/ JOEL SLUTZKY</u> Joel Slutzky	Director	June 11, 2012
<u>/s/ THOMAS L. THOMAS</u> Thomas L. Thomas	Director	June 11, 2012
<u>/s/ MIKEL WILLIAMS</u> Mikel Williams	Director	June 11, 2012

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Iteris, Inc.

Index to Consolidated Financial Statements

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders
Iteris, Inc.

We have audited the accompanying consolidated balance sheets of Iteris, Inc. and subsidiaries as of March 31, 2012 and 2011, and the related consolidated statements of operations, stockholders' equity and comprehensive income (loss), and cash flows for each of the three years in the period ended March 31, 2012. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements 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. The Company is not required to have, nor were we engaged to perform, an audit of its 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, as well as evaluating the overall financial statement presentation. We believe that our audits provide 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. and subsidiaries as of March 31, 2012 and 2011, and the results of their operations and their cash flows for each of the three years in the period ended March 31, 2012, in conformity with U.S. generally accepted accounting principles.

/s/ McGladrey LLP
Irvine, California
June 11, 2012

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Iteris, Inc.
Consolidated Balance Sheets
(In thousands, except par value)

	<u>March 31,</u>	
	<u>2012</u>	<u>2011</u>
Assets		
Current assets:		
Cash and cash equivalents	\$ 18,701	\$ 11,818
Trade accounts receivable, net of allowance for doubtful accounts of \$379 and \$385 at March 31, 2012		

and 2011, respectively	11,081	9,419
Costs in excess of billings on uncompleted contracts	5,360	4,070
Inventories	2,454	2,392
Deferred income taxes	2,904	2,967
Prepaid expenses and other current assets	425	392
Assets of discontinued operation	—	7,672
Total current assets	40,925	38,730
Property and equipment, net	1,948	2,461
Deferred income taxes	6,761	10,807
Intangible assets, net	2,578	1,845
Goodwill	17,318	16,522
Other assets	210	203
Total assets	\$ 69,740	\$ 70,568

Liabilities and stockholders' equity

Current liabilities:		
Trade accounts payable	\$ 4,044	\$ 2,985
Accrued payroll and related expenses	3,398	3,523
Accrued liabilities	2,942	3,181
Billings in excess of costs and estimated earnings on uncompleted contracts	1,542	1,335
Current portion of long-term debt	634	2,324
Current liabilities of discontinued operation	—	611
Total current liabilities	12,560	13,959
Long-term debt	—	640
Deferred rent	700	1,058
Unrecognized tax benefits	351	587
Other non-current liabilities	657	1,028
Total liabilities	14,268	17,272
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, \$1.00 par value:		
Authorized shares - 2,000		
Issued and outstanding shares - none	—	—
Common stock, \$0.10 par value:		
Authorized shares - 70,000 at March 31, 2012 and 2011		
Issued and outstanding shares - 33,909 at March 31, 2012 and 34,364 at March 31, 2011	3,391	3,436
Additional paid-in capital	137,645	137,938
Accumulated deficit	(85,564)	(88,078)
Total stockholders' equity	55,472	53,296
Total liabilities and stockholders' equity	\$ 69,740	\$ 70,568

See accompanying notes.

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Iteris, Inc. Consolidated Statements of Operations (In thousands, except per share amounts)

	Year Ended March 31,		
	2012	2011	2010
Net sales and contract revenues:			
Net sales	\$ 27,679	\$ 28,208	\$ 25,341
Contract revenues	30,727	23,758	26,413
Total net sales and contract revenues	58,406	51,966	51,754
Costs of net sales and contract revenues:			
Cost of net sales	13,393	13,447	12,313
Cost of contract revenues	21,942	15,635	17,399
Gross profit	23,071	22,884	22,042
Operating expenses:			
Selling, general and administrative	17,986	16,981	15,709
Research and development	3,183	2,444	2,646
Amortization of intangible assets	504	176	113

Change in fair value of contingent acquisition consideration	(619)	55	—
Impairment of goodwill	—	7,970	—
Total operating expenses	21,054	27,626	18,468
Operating income (loss)	2,017	(4,742)	3,574
Non-operating income (expense):			
Other income, net	4	18	44
Interest expense, net	(72)	(152)	(264)
Income (loss) from continuing operations before income taxes	1,949	(4,876)	3,354
Provision for income taxes	(643)	(278)	(960)
Income (loss) from continuing operations	1,306	(5,154)	2,394
Gain on sale of discontinued operation, net of tax	1,180	—	—
Income (loss) from discontinued operation, net of tax	28	(55)	(191)
Net income (loss)	\$ 2,514	\$ (5,209)	\$ 2,203
Income (loss) per share from continuing operations - basic and diluted	\$ 0.04	\$ (0.15)	\$ 0.07
Gain per share from sale of discontinued operation - basic and diluted	\$ 0.03	\$ 0.00	\$ 0.00
Income (loss) per share from discontinued operation - basic and diluted	\$ 0.00	\$ 0.00	\$ (0.01)
Net income (loss) per share - basic and diluted	\$ 0.07	\$ (0.15)	\$ 0.06
Shares used in basic per share calculations	34,259	34,335	34,249
Shares used in diluted per share calculations	34,380	34,335	34,435

See accompanying notes.

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Iteris, Inc.
Consolidated Statements of Stockholders' Equity and Comprehensive Income (Loss)
(In thousands)

	Common Stock		Additional Paid-In Capital	Common Stock Held in Trust	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
	Shares	Amount					
Balance at March 31, 2009	34,205	\$ 3,420	\$ 136,997	\$ (31)	\$ (85,025)	\$ (3)	\$ 55,358
Cumulative effect of adoption of change in accounting for warrants	—	—	—	—	(47)	—	(47)
Stock option exercises	113	12	131	—	—	—	143
Stock-based compensation	—	—	375	—	—	—	375
Issuance of shares held in trust	—	—	—	31	—	—	31
Components of comprehensive income:							
Foreign currency translation	—	—	—	—	—	3	3
Net income	—	—	—	—	2,203	—	2,203
Comprehensive income	—	—	—	—	—	—	2,206
Balance at March 31, 2010	34,318	3,432	137,503	—	(82,869)	—	58,066
Stock option exercises	46	4	53	—	—	—	57
Stock-based compensation	—	—	382	—	—	—	382
Net loss and comprehensive loss	—	—	—	—	(5,209)	—	(5,209)
Balance at March 31, 2011	34,364	3,436	137,938	—	(88,078)	—	53,296
Stock option exercises	68	8	77	—	—	—	85
Stock-based compensation	—	—	331	—	—	—	331
Issuance of shares pursuant to vesting of restricted stock units	51	5	(5)	—	—	—	—
Repurchases of common stock	(574)	(58)	(696)	—	—	—	(754)
Net income and comprehensive income	—	—	—	—	2,514	—	2,514
Balance at March 31, 2012	33,909	\$ 3,391	\$ 137,645	\$ —	\$ (85,564)	\$ —	\$ 55,472

See accompanying notes.

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Iteris, Inc.
Consolidated Statements of Cash Flows
(In thousands)

	Year Ended March 31,		
	2012	2011	2010
Cash flows from operating activities			
Net income (loss)	\$ 2,514	\$ (5,209)	\$ 2,203
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Deferred income taxes	286	273	1,014
Depreciation of property and equipment	907	1,030	986
Stock-based compensation	331	382	375
Impairment of goodwill	—	7,970	—
Amortization of intangible assets	504	222	159
Change in fair value of contingent acquisition consideration	(619)	55	—
Loss on disposal of equipment	1	9	—
Gain on sale of Vehicle Sensors	(1,180)	—	—
Changes in operating assets and liabilities, net of effects of acquisitions and sale of Vehicle Sensors:			
Accounts receivable	(1,826)	1,052	1,137
Net costs and estimated earnings in excess of billings	(902)	(501)	917
Inventories	79	(953)	2,954
Prepaid expenses and other assets	284	211	(350)
Accounts payable and accrued expenses	289	805	(2,911)
Net cash provided by operating activities	668	5,346	6,484
Cash flows from investing activities			
Purchases of property and equipment	(337)	(414)	(294)
Capitalized software	(138)	—	—
Net cash paid for acquisitions	(969)	(1,116)	(300)
Net proceeds from sale of Vehicle Sensors	11,446	—	—
Net cash provided by (used in) investing activities	10,002	(1,530)	(594)
Cash flows from financing activities			
Payments on long-term debt	(2,330)	(2,354)	(2,750)
Borrowings on long-term debt	—	—	750
Repurchases of common stock	(754)	—	—
Deferred payment for prior business combinations	(788)	(106)	—
Proceeds from stock option exercises	85	57	143
Net cash used in financing activities	(3,787)	(2,403)	(1,857)
Increase in cash and cash equivalents	6,883	1,413	4,033
Cash and cash equivalents at beginning of year	11,818	10,405	6,372
Cash and cash equivalents at end of year	\$ 18,701	\$ 11,818	\$ 10,405
Supplemental cash flow information:			
Cash paid during the year for:			
Interest	\$ 111	\$ 200	\$ 306
Income taxes	439	455	159
Supplemental schedule of non-cash investing and financing activities:			
Liabilities incurred for business combinations	\$ 971	\$ 2,610	\$ 218
Issuance of common stock for vested restricted stock units	5	—	—
Fair value of common stock issued in settlement of liabilities	—	—	31

See accompanying notes.

Description of Business

Iteris, Inc. (referred to collectively with our subsidiaries in these consolidated financial statements as “Iteris,” the “Company,” “we,” “our” and “us”) is a leading provider of intelligent information solutions to the traffic management market. We are focused on the development and application of advanced technologies and software-based information systems that reduce traffic congestion, provide measurement, management and predictive traffic analytics and improve the safety of surface transportation systems infrastructure. We believe that our products, services and solutions, in conjunction with sound traffic management, minimize the environmental impact of traffic congestion. By combining image processing, traffic engineering, information technology, and other products and services, we offer a broad range of Intelligent Transportation Systems (“ITS”) solutions to customers worldwide. Iteris was originally incorporated in Delaware in 1987.

Basis of Presentation

Our consolidated financial statements include the accounts of Iteris and our subsidiaries and have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”). All significant intercompany accounts and transactions have been eliminated in consolidation.

The results of continuing operations for all periods presented in the consolidated financial statements exclude the financial impact of discontinued operations. See Note 3, “Sale of Vehicle Sensors”, for further discussion related to discontinued operations presentation.

Use of Estimates

The preparation of consolidated financial statements in conformity with GAAP requires our 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, projections of taxable income used to assess realizability of deferred tax assets, inventory and warranty reserves, costs to complete long-term contracts, indirect cost rates used in cost-plus contracts, contract reserves, the valuation of purchased intangible asset and goodwill, the valuation of debt and equity instruments and estimates of future cash flows used to assess the recoverability of long-lived assets and the impairment of goodwill.

Revenue Recognition

Net Sales

Product revenues and related costs of sales are recognized when all of the following criteria are met: (i) persuasive evidence of an arrangement exists, (ii) delivery has occurred, (iii) the price to the customer is fixed or determinable, and (iv) collection of the receivable is reasonably assured. These criteria are typically met at the time of product shipment, but in certain circumstances, may not be met until receipt or acceptance by the customer. Accordingly, at the date revenue is recognized, the significant obligations or uncertainties concerning the sale have been resolved.

We recognize revenue from the sale of deliverables that are part of a multiple-element arrangement in accordance with applicable accounting guidance that establishes a relative selling price hierarchy permitting the use of an estimated selling price to determine the allocation of arrangement consideration to a deliverable in a multiple-element arrangement where neither vendor specific objective evidence (“VSOE”) nor third-party evidence (“TPE”) of fair value is available for that deliverable. In the absence of VSOE or TPE of the standalone selling price for one or more delivered or undelivered elements in a multiple-element arrangement, we are required to estimate the selling prices of those elements. Overall arrangement consideration is allocated to each element (both delivered and undelivered items) that has stand-alone value based on their relative selling prices, regardless of whether those selling prices are evidenced by VSOE or TPE or are based on our estimated selling prices.

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We account for multiple-element arrangements that consist only of software and software-related services in accordance with applicable accounting guidance for software and software-related transactions. For such transactions, revenue on arrangements that include multiple elements is allocated to each element based on the relative fair value of each element, and fair value is determined by VSOE. If we cannot objectively determine the fair value of any undelivered element included in such multiple-element arrangements and the only undelivered element is post-contract customer support or maintenance, and VSOE of the fair value of such support or maintenance does not exist, revenue from the entire arrangement is recognized ratably over the support period. When the fair value of a delivered element has not been established but VSOE of fair value exists for the undelivered elements, we use the residual method to recognize revenue if the fair value of all undelivered elements is determinable. Under the residual method, the fair value of the undelivered elements is deferred and the remaining portion of the arrangement fee is allocated to the delivered elements and is recognized as revenue.

Contract Revenues

Contract revenues are derived primarily from long-term contracts with governmental agencies. When appropriate, contract revenues are recognized using the percentage of completion method of accounting, whereby revenue is recognized as contract performance progresses and is determined 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 contract revenues when their realization is

reasonably assured. Certain of our contract revenues are recognized as services are performed and amounts are earned, which is measured by time incurred or other contractual milestones or output measures. Contract revenues accounted for in this manner generally relate to certain cost-plus fixed fee or time-and-materials contracts for which no specific maximum contract values are stipulated.

Costs in Excess of Billings on Uncompleted Contracts

Costs in excess of billings on uncompleted contracts in the accompanying consolidated balance sheets represent unbilled amounts earned and reimbursable under services sales arrangements. At any given period-end, a large portion of the balance in this account represents the accumulation of labor, materials and other costs that have not been billed due to timing, whereby the accumulation of each month's costs and earnings are not administratively billed until the subsequent month. Also included in this account are amounts that will become billable according to contract terms, which usually require the consideration of the passage of time, achievement of milestones or completion of the project. Such unbilled amounts are expected to be billed and collected within the next twelve months.

Costs in excess of billings on uncompleted contracts at March 31, 2012 and 2011 include approximately \$944,000 and \$400,000, respectively, which were not billable because certain milestone objectives specified in the contracts had not been attained. The costs and estimated earnings in excess of billings at March 31, 2012 are expected to be billed and collected during the fiscal year ending March 31, 2013.

Billings in Excess of Costs and Estimated Earnings on Uncompleted Contracts

Billings in excess of costs and estimated earnings on uncompleted contracts in the accompanying consolidated balance sheets is comprised of cash collected from customers and billings to customers on contracts in advance of work performed, advance payments negotiated as a contract condition, estimated losses on uncompleted contracts, project-related legal liabilities and other project-related reserves. The unearned amounts are expected to be earned within the next twelve months.

We record provisions for estimated losses on uncompleted contracts in the period in which such losses become known. The cumulative effects of revisions to contract revenues and estimated completion costs are recorded in the accounting period in which the amounts become evident and can be reasonably estimated. These revisions can include such items as the effects of change orders and claims, warranty claims, liquidated damages or other contractual penalties, adjustments for audit findings on contract closeout settlements.

Concentration of Credit Risk

Financial instruments that potentially subject us to a concentration of credit risk consist principally of cash and cash equivalents and trade accounts receivable.

Cash and cash equivalents consist primarily of demand deposits and money market funds maintained with several financial institutions. Deposits held with banks may exceed the amount of insurance provided on such deposits. Generally, these deposits may be redeemed upon demand and are maintained with high credit quality financial institutions and therefore are believed to have minimal credit risk.

Our accounts receivable are primarily derived from billings with customers located throughout North America, as well as in Europe, Asia and South America. We generally do not require collateral or other security from customers. We maintain an allowance for doubtful accounts for potential credit losses, which losses have historically been within management's expectations.

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Fair Values of Financial Instruments

The fair value of cash and cash equivalents, receivables, accounts payable and accrued expenses approximate carrying value because of the short period of time to maturity. The fair value of line of credit agreements and long-term debt approximate carrying value because the related effective rates of interest approximate current market rates available to us for debt with similar terms and similar remaining maturities.

Cash and Cash Equivalents

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

Allowance for Doubtful Accounts

The collectability of our accounts receivable is evaluated through review of invoices outstanding greater than a certain period of time and ongoing credit evaluations of our customers' financial condition. In cases where we are aware of circumstances that may impair a specific customer's ability to meet its financial obligations subsequent to the original sale, we will record an allowance against amounts due, and thereby reduce the net recognized receivable to the amount we reasonably believe will be collected. We also maintain an allowance based on our historical collections experience. When we determine that collection is not likely, we write off accounts receivable against the allowance for doubtful accounts.

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 using the straight-line method over the estimated useful life ranging from three to eight years. Leasehold improvements are depreciated over the term of the related lease or the estimated useful life of the improvement, whichever is shorter.

Goodwill and Long-Lived Assets

We evaluate goodwill on an annual basis in our fourth fiscal quarter or more frequently if we believe indicators of impairment exist. We have determined that our reporting units for purposes of testing for goodwill impairment are identical to our reportable segments for financial reporting purposes. In the fiscal year ended March 31, 2012 ("Fiscal 2012") we early adopted the new provisions issued by the Financial Accounting Standards Board ("FASB") that are intended to simplify goodwill impairment testing. This guidance permits us to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If we conclude that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, we conduct a two-step goodwill impairment test. The first step of the impairment test involves comparing the fair values of the applicable reporting units with their carrying values. We determine the fair values of our reporting units using the income valuation approach, as well as other generally accepted valuation methodologies. If the carrying amount of a reporting unit exceeds the reporting unit's fair value, we perform the second step of the goodwill impairment test. The second step of the goodwill impairment test involves comparing the implied fair value of the affected reporting unit's goodwill with the carrying value of that goodwill. The amount by which the carrying value of the goodwill exceeds its implied fair value, if any, is recognized as an impairment loss. We performed an annual impairment assessment of the carrying value of goodwill for each of the fiscal years ended March 31, 2012, 2011 and 2010. Based on these assessments, we determined that no impairment as of each of these dates was indicated as the estimated fair value of each of our reporting units exceeded its respective carrying value. We monitor the indicators for goodwill impairment testing between annual tests. Certain adverse business conditions impacting one or more reporting units would cause us to test goodwill for impairment on an interim basis. Refer to Note 5 for additional discussion regarding our interim goodwill impairment analyses during Fiscal 2012 and the fiscal year ended March 31, 2011 ("Fiscal 2011").

We test long-lived assets and purchased intangible assets (other than goodwill) for impairment if we believe indicators of impairment exist. We determine whether the carrying value of an asset or asset group is recoverable, based on comparisons to undiscounted expected future cash flows the asset are expected to generate. If an asset is not recoverable, we record an impairment loss equal to the amount by which the carrying value of the asset exceeds its fair value. We primarily use the income valuation approach to determine the fair value of our long lived assets and purchased intangible assets.

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Income Taxes

We utilize the asset and liability method of accounting for income taxes, under which deferred taxes are determined based on the temporary differences between the financial statement and tax basis of assets and liabilities using tax rates expected to be in effect during the years in which the basis differences reverse. A valuation allowance is recorded when it is more-likely-than-not that some or all of the deferred tax assets will not be realized, which increases our income tax expense in the period such determination is made.

Income tax positions must meet a more-likely-than-not recognition threshold to be recognized. Income tax positions that previously failed to meet the more-likely-than-not threshold are recognized in the first subsequent financial reporting period in which that threshold is met. Previously recognized tax positions that no longer meet the more-likely-than-not threshold are derecognized in the first subsequent financial reporting period in which that threshold is no longer met.

Stock-Based Compensation

We record stock-based compensation in the consolidated statement of operations as an expense, based on the estimated grant date fair value of our stock-based awards, whereby such fair values are amortized over the requisite service period. Our stock-based awards are currently comprised of common stock options and restricted stock units. The fair value of our common stock option awards is estimated on the grant date using the Black-Scholes-Merton ("BSM") option-pricing formula. While utilizing this model meets established requirements, the estimated fair values generated by it may not be indicative of the actual fair values of our common stock option awards as it does not consider certain factors important to those awards to employees, such as continued employment and periodic vesting requirements as well as limited transferability. The fair value of our restricted stock units is based on the closing market price of our common stock on the grant date. If there are any modifications or cancellations of the underlying unvested stock-based awards, we may be required to accelerate, increase or cancel any remaining unearned stock-based compensation expense.

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.

Sales Taxes

Sales taxes are presented on a net basis (excluded from net sales and contract revenues) in the consolidated statements of operations.

Advertising Expenses

Advertising costs are expensed in the period incurred and totaled \$187,000, \$224,000 and \$153,000 in the fiscal years ended March 31, 2012, 2011 and 2010, respectively.

Warranty

We generally provide a one to three year warranty from the original invoice date on all products, materials and workmanship. Products sold to various original equipment manufacturer customers sometimes carry longer warranties. Defective products will be either repaired or replaced, usually 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 reserve is included within accrued liabilities in the accompanying consolidated balance sheets.

Repair and Maintenance Costs

We incur repair and maintenance costs in the normal course of business. Should the repair or maintenance result in a permanent improvement to one of our 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.

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Recent Accounting Pronouncements

In May 2011, the FASB issued Accounting Standards Update (“ASU”) No. 2011-04, *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs* (“ASU 2011-04”), which amends Accounting Standards Codification 820, *Fair Value Measurements*. ASU 2011-04 aims to eliminate certain differences that existed between U.S. and international fair value accounting concepts, and also clarifies existing guidance under GAAP. Additionally, among other disclosures, this ASU requires certain new quantitative and qualitative disclosures regarding unobservable fair value measurements. We will be required to adopt the amendments prescribed by ASU 2011-04 for our fiscal year ending March 31, 2013. We do not expect that the adoption of ASU 2011-04 will have a material impact on our consolidated financial statements.

In June 2011, the FASB issued ASU No. 2011-05, *Presentation of Comprehensive Income* (“ASU 2011-05”). ASU 2011-05 requires the presentation of comprehensive income, the components of net income and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The new standard also requires presentation of adjustments for items that are reclassified from other comprehensive income to net income in the statement where the components of net income and the components of other comprehensive income are presented; however, in December 2011, the FASB issued ASU No. 2011-12, *Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05*, which deferred this requirement, and the FASB plans to reconsider it during the first half of calendar 2012. The amendments prescribed by ASU 2011-05 are currently scheduled to become effective on a retrospective basis for financial statements issued for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2011. Early adoption is permitted. We do not expect that the adoption of ASU 2011-05 will have a material impact on our consolidated financial statements.

In September 2011, the FASB issued ASU No. 2011-08, *Testing for Goodwill Impairment* (“ASU 2011-08”). With respect to performing their required annual test for goodwill impairment, ASU 2011-08 gives companies the option to first perform a qualitative assessment to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If a company concludes that this is the case, it must perform the two-step test in accordance with previously existing guidance. Otherwise, a company can skip the two-step test. ASU 2011-08 is effective for fiscal years beginning after December 15, 2011. Early adoption is permitted and we chose to adopt ASU 2011-05 in Fiscal 2012, which did not result in a material impact on our consolidated financial statements.

2. Supplementary Financial Information

Inventories

The following table presents details regarding our inventories:

	March 31,	
	2012	2011
	(In thousands)	
Materials and supplies	\$ 1,513	\$ 1,734
Work in process	98	84
Finished goods	843	574
	<u>\$ 2,454</u>	<u>\$ 2,392</u>

Property and Equipment

The following table presents details of our property and equipment:

	March 31,	
	2012	2011
	(In thousands)	
Equipment	\$ 5,545	\$ 8,101
Leasehold improvements	1,946	1,985
Accumulated depreciation	(5,543)	(7,625)
	<u>\$ 1,948</u>	<u>\$ 2,461</u>

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Intangible Assets

The following table presents details regarding our intangible assets:

	March 31,			
	2012		2011	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
	(In thousands)			
Technology	\$ 1,856	\$ (935)	\$ 1,566	\$ (719)
Customer contracts / relationships	750	(122)	500	(21)
Other	1,110	(219)	550	(31)
Capitalized software development costs	138	—	—	—
Total	<u>\$ 3,854</u>	<u>\$ (1,276)</u>	<u>\$ 2,616</u>	<u>\$ (771)</u>

Amortization expense for intangible assets subject to amortization was approximately \$504,000, \$176,000 and \$113,000 for the fiscal years ended March 31, 2012, 2011 and 2010, respectively.

In Fiscal 2012, we capitalized approximately \$138,000 of internal costs incurred in developing software products to be sold. These costs related to the internal development of our performance measurement software offerings.

We do not have any intangible assets with indefinite useful lives. Future estimated amortization expense is as follows:

Year Ending March 31,	
(In thousands)	
2013	\$ 644
2014	627
2015	431
2016	360
2017	378
Thereafter	—
	<u>\$ 2,440</u>

Refer to Note 4 for additional information regarding intangible assets acquired during the last three fiscal years. If we acquire additional intangible assets in future periods, our amortization expense will increase.

Goodwill

The following table presents the activity related to the carrying value of our goodwill by reportable segment for Fiscal 2011 and Fiscal 2012:

	Roadway Sensors	Transportation Systems	Total
	(In thousands)		
Balance - March 31, 2010			
Goodwill	\$ 8,214	\$ 14,906	\$ 23,120
Accumulated impairment losses	—	—	—
	<u>8,214</u>	<u>14,906</u>	<u>23,120</u>
Acquisition of Meridian Environmental Technology, Inc. (Note 4)	—	1,372	1,372
Impairment loss	—	(7,970)	(7,970)
Balance - March 31, 2011			
Goodwill	8,214	16,278	24,492

Accumulated impairment losses	—	(7,970)	(7,970)
	<u>8,214</u>	<u>8,308</u>	<u>16,522</u>
Acquisition of Berkeley Transportation Systems, Inc. (Note 4)	—	796	796
Balance - March 31, 2012			
Goodwill	8,214	17,074	25,288
Accumulated impairment losses	—	(7,970)	(7,970)
	<u>\$ 8,214</u>	<u>\$ 9,104</u>	<u>\$ 17,318</u>

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The measurement period adjustments in the table above are due primarily to certain income tax-related adjustments pertaining to our acquisition of Meridian Environmental Technology, Inc. in January 2011 (see Note 4).

Warranty Reserve Activity

The following table presents activity with respect to the warranty reserve:

	Year Ended March 31,		
	2012	2011	2010
	(In thousands)		
Balance at beginning of fiscal year	\$ 279	\$ 297	\$ 247
Additions charged to cost of sales	86	137	218
Warranty claims	(134)	(155)	(168)
Balance at end of fiscal year	<u>\$ 231</u>	<u>\$ 279</u>	<u>\$ 297</u>

Earnings Per Share

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

	Year Ended March 31,		
	2012	2011	2010
	(In thousands, except per share amounts)		
Numerator:			
Income (loss) from continuing operations	<u>\$ 1,306</u>	<u>\$ (5,154)</u>	<u>\$ 2,394</u>
Denominator:			
Weighted average common shares used in basic computation	34,259	34,335	34,249
Dilutive stock options	96	—	185
Dilutive restricted stock units	25	—	—
Dilutive warrants	—	—	1
Weighted average common shares used in diluted computation	<u>34,380</u>	<u>34,335</u>	<u>34,435</u>
Income (loss) from continuing operations per share:			
Basic	<u>\$ 0.04</u>	<u>\$ (0.15)</u>	<u>\$ 0.07</u>
Diluted	<u>\$ 0.04</u>	<u>\$ (0.15)</u>	<u>\$ 0.07</u>

The following instruments were excluded for purposes of calculating weighted average common share equivalents in the computation of diluted income (loss) from continuing operations per share as their effect would have been anti-dilutive:

	Year Ended March 31,		
	2012	2011	2010
	(In thousands)		
Stock options	1,840	1,467	1,790
Restricted stock units	—	54	—
Warrants	15	272	371

3. Sale of Vehicle Sensors

On July 29, 2011, we completed the sale of substantially all of our assets used in connection with our Vehicle Sensors segment to Bendix Commercial Vehicle Systems LLC (“Bendix”), a member of Knorr-Bremse Group, pursuant to an Asset Purchase Agreement (the “Agreement”) signed on July 25, 2011 (the “Asset Sale”).

Under the terms of the Agreement, upon the closing of the Asset Sale, Bendix paid us \$14 million in cash, subject to a \$2 million holdback and

adjustments based upon the working capital of the Vehicle Sensors segment at closing, and Bendix assumed certain specified obligations and liabilities of the Vehicle Sensors segment. We are entitled to additional consideration in the form of the following performance and royalty-related earn-outs: Bendix is obligated to pay us an amount in cash equal to (i) 85% of revenue

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associated with royalties received under our license and distribution agreements with Audiovox Electronics Corporation and Valeo Schalter and Sensoren GmbH through December 31, 2017 and (ii) 30% of the amount, if any, by which the amount of revenue generated from the sale of our lane departure warning systems exceeds Bendix's projection for such revenue for the two years following closing, each subject to certain reductions and limitations set forth in the Agreement.

Upon the closing of the Asset Sale and resolution of working capital adjustments (as described above), we recorded aggregate proceeds received of approximately \$12.0 million. Legal and other professional fees of approximately \$0.6 million that were directly related to the sale transaction were offset against the proceeds to calculate net proceeds from the Asset Sale of approximately \$11.4 million.

The following table summarizes the assets and liabilities of the Vehicle Sensors segment as of the closing date of the Asset Sale (in thousands):

Cash	\$	105
Accounts receivable		1,850
Inventories		1,147
Other current assets		31
Property and equipment, net		133
Goodwill		4,671
Total assets		7,937
Current liabilities		(691)
Net assets	\$	7,246

In comparing the above net assets to the net proceeds received, we recorded a gain on the Asset Sale of \$4.3 million, or \$1.2 million after tax, in the accompanying consolidated statements of operations for Fiscal 2012. The effective tax rate applicable to the gain was impacted by goodwill of \$4.7 million for which there is no corresponding tax basis. We also recorded a gain on the sale of approximately \$189,000, or \$129,000 after tax, related to certain performance and royalty-related earn-outs (as described above) that were achieved through December 31, 2011.

In accordance with applicable accounting guidance, we determined that the Vehicle Sensors segment, which constituted one of our operating segments, qualified as a discontinued operation. The applicable financial results of the Vehicle Sensors segment have been reported as a discontinued operation in the consolidated statements of operations for all periods presented. For the fiscal years ended March 31, 2012, 2011 and 2010, Vehicle Sensors net sales classified as part of discontinued operation was \$3.2 million, \$7.5 million and \$6.3 million, respectively. We have elected not to allocate any interest expense to the discontinued operation. Additionally, the applicable net assets of the Vehicle Sensors segment are separately presented as assets and liabilities of discontinued operation in the accompanying consolidated balance sheet as of March 31, 2011.

We entered into a short-term transitional services agreement with Bendix that terminated at the end of February 2012, pursuant to which we provided them certain ongoing logistical and administrative support services. Bendix paid us a fixed monthly amount for such support services, and also paid us an hourly amount for providing certain development-related services during the transition period.

4. Acquisitions

Berkeley Transportation Systems, Inc.

In November 2011, we acquired all of the outstanding capital stock of Berkeley Transportation Systems, Inc. ("BTS"). BTS was a privately-held company based in Berkeley, California, which specializes in transportation performance measurement. BTS' Performance Measurement System leverages its real-time data collection, diagnostic, fusion and warehousing platform to aggregate and compute performance measures. This information is used to analyze how a transportation system is performing based on pre-determined measures of effectiveness such as stops, delays and travel time. Our primary reasons for the acquisition were to add key technologies to complement our iPerform solution and strengthen our performance measurement and management initiative as a whole.

Our consolidated financial statements for Fiscal 2012 include the results of operations of BTS commencing as of the acquisition date. BTS contributed approximately \$936,000 of Contract Revenues and approximately \$38,000 of operating income since the acquisition date included in the consolidated statement of operations for Fiscal 2012. On or shortly after the acquisition date, we paid a total of approximately \$840,000 in cash to BTS. Additionally, we are also scheduled to pay (i) up to \$250,000 at the 24-month anniversary of the closing of the acquisition, pursuant to a holdback provision, (ii) up to \$500,000 at the 36-month anniversary of the closing of the acquisition, pursuant to a deferred payment provision, and (iii) up to \$750,000 pursuant to an earn-out provision based on revenue and operating income achieved from BTS' operations during the 18 months ending June 30, 2013. Our potential obligation pertaining to the various contingent consideration payments ranges from zero to \$1.5 million. Acquisition-related costs were not significant and are included in selling, general and administrative expenses in the accompanying consolidated statement of operations for Fiscal 2012.

[Table of Contents](#)*Acquisition Accounting*

We have accounted for the acquisition of BTS as a business combination in accordance with applicable accounting guidance. We measured the fair value of the consideration transferred (including contingent consideration) to determine the purchase price of the acquisition. We allocated the fair value of consideration transferred to tangible assets acquired, liabilities assumed and identifiable intangible assets acquired based on their estimated fair values at the acquisition date.

The BTS acquisition is recorded as follows (in thousands):

Fair value of consideration transferred:	
Cash paid on or shortly after acquisition date	\$ 840
Estimated fair value of contingent consideration	971
Total	1,811
Allocation:	
Accounts receivable	(164)
Other tangible assets	(375)
Purchased intangible assets	(1,100)
Liabilities	624
Goodwill	\$ 796

The excess of the fair value of the BTS business over the aggregate fair values of identifiable assets acquired and liabilities assumed was recorded as goodwill. The primary factor that resulted in the recognition of goodwill was the acquisition of BTS' assembled workforce, which is not a separately identifiable intangible asset. The goodwill is not expected to be deductible for income tax purposes.

Purchased Intangible Assets

The following table presents details of the intangible assets acquired from BTS:

	Estimated Useful Life	Amount
	(In years)	(In thousands)
Backlog	3	\$ 330
Technology	6	290
Customer contracts / relationships	6	250
Other purchased intangible assets	5 - 7	230
		\$ 1,100

Meridian Environmental Technology, Inc.

In January 2011, we acquired all of the capital stock of Meridian Environmental Technology, Inc. ("MET"), a privately-held company based in Grand Forks, North Dakota. MET specializes in 511 advanced traveler information systems, as well as Maintenance Decision Support System management tools that allow users to create solutions to meet roadway maintenance decision needs. Our primary reasons for the acquisition were (i) to enhance our ability to provide travelers and traffic management authorities with more accurate and real-time information and network performance management tools and (ii) to provide Iteris with key capabilities in the emerging performance measurement and management market. From the date of acquisition through the end of Fiscal 2011, MET contributed approximately \$1.5 million of Contract Revenues and approximately \$77,000 of operating income included in the consolidated statement of operations for Fiscal 2011.

Our consolidated financial statements for the fiscal years ended March 31, 2012 and 2011 include the results of operations of MET commencing as of the acquisition date. On or shortly after the acquisition date, we paid approximately \$1.6 million in cash, exclusive of \$369,000 of cash acquired. We also agreed to pay up to \$1 million on each of the first two anniversaries of the acquisition date, subject to adjustments related to the retention of various key employees and certain other adjustments as further defined in the agreement. Additionally, we agreed to pay up to an additional \$1 million per year for two years pursuant to an earn-out provision, based on revenue and operating income achieved from MET's operations during the twelve months ending December 31, 2011 and 2012. Acquisition-related costs were not significant and are included in selling, general and administrative expenses in the accompanying consolidated statement of operations for Fiscal 2011. In January 2012, we made a cash payment of approximately \$676,000 related to the first deferred payment to the shareholders of MET and held back \$250,000 in

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accordance with certain provisions of the purchase agreement. We expect the contingencies related to the hold-back to be resolved sometime in the first fiscal quarter of the fiscal year ending March 31, 2013 at which time we may or may not release the hold-back. No amounts were earned by the shareholders of MET related to the first year earn-out provision. As a result of the first year deferred payment and that no amounts were earned related to the first year earn-out

provision, the potential outcomes pertaining to the remaining contingent consideration payments at March 31, 2012 range from zero to approximately \$1.8 million.

Acquisition Accounting

We have accounted for the acquisition of MET as a business combination in accordance with applicable accounting guidance. We measured the fair value of the consideration transferred (including contingent consideration) to determine the purchase price of the acquisition. We allocated the fair value of consideration transferred to tangible assets acquired, liabilities assumed and identifiable intangible assets acquired based on their estimated fair values at the acquisition date.

The acquisition is recorded as follows (in thousands):

Fair value of consideration transferred:	
Cash paid on or shortly after acquisition date	\$ 1,622
Estimated fair value of contingent consideration	2,473
Total	4,095
Allocation:	
Cash	(369)
Accounts receivable	(682)
Other tangible current assets	(531)
Property and equipment	(682)
Purchased intangible assets	(1,620)
Liabilities	1,161
Goodwill	\$ 1,372

The excess of the fair value of the business over the aggregate fair values of identifiable assets acquired and liabilities assumed was recorded as goodwill. The primary factor that resulted in the recognition of goodwill was the acquisition of MET's assembled workforce, which is not a separately identifiable intangible asset. The goodwill is not expected to be deductible for income tax purposes.

Purchased Intangible Assets

The following table presents details of the intangible assets acquired from MET:

	Estimated Useful Life	Amount
	(In years)	(In thousands)
Technology	6	\$ 570
Customer contracts / relationships	6	500
Other purchased intangible assets	3 - 7	550
		\$ 1,620

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Supplemental Pro Forma Data (Unaudited)

The unaudited pro forma data below presents selected details of our results of operations as if the acquisition of BTS had occurred on April 1, 2010 (the beginning of Fiscal 2011). The following data includes the amortization of purchased intangible assets. This pro forma data is presented for informational purposes only and does not purport to be indicative of the results of future operations or the results that would have occurred had the acquisition taken place on April 1, 2010.

	Year Ended March 31,	
	2012	2011
	(In thousands, except per share data)	
Pro forma net sales and contract revenues	\$ 59,553	\$ 53,722
Pro forma net income (loss)	\$ 2,383	\$ (5,433)
Pro forma net income (loss) per share - basic and diluted	\$ 0.07	\$ (0.16)

Hamilton Signal, Inc.

In April 2009, we completed the acquisition of certain assets of Hamilton Signal, Inc., a privately-held developer of video processing algorithms enabling state and local governments to conduct real-time analysis on fixed and pan-tilt-zoom camera feeds. Our primary reasons for the acquisition were to expand our product portfolio in the traffic management market and to integrate enhanced functionality into and complement our Roadway Sensors technologies.

The total purchase consideration was approximately \$518,000, of which we paid \$300,000 in cash upon execution of the purchase agreement and of which, pursuant to the purchase agreement, we paid \$106,000 on the first anniversary of the acquisition date and \$112,000 on the second anniversary of the acquisition date. Pursuant to the purchase agreement, the selling stockholder became an employee of Iteris and was eligible to receive compensation based on net sales of certain products during the three-year period ended March 31, 2012, subject to continued employment and other limitations.

We accounted for this acquisition as a business combination in accordance with applicable accounting guidance. We estimated the fair value of the assets acquired to allocate the purchase price, which is summarized as follows (in thousands):

Developed technology	\$	501
Goodwill		17
	<u>\$</u>	<u>518</u>

The purchased developed technology was determined to have an estimated useful life of five years.

Our consolidated financial statements for the fiscal years ended March 31, 2012, 2011 and 2010 include the results of operations of Hamilton Signal commencing as of the acquisition date. Disclosures required for material business combinations have been limited due to the immateriality of the acquisition of Hamilton Signal to our consolidated financial statements.

5. Impairment of Goodwill

As discussed in Note 1, goodwill is tested for impairment on an annual basis in our fourth fiscal quarter or more frequently if indicators of impairment exist.

In Fiscal 2012, we early adopted the new provisions issued by the FASB that are intended to simplify goodwill impairment testing. The updated guidance permits us to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If we conclude that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, we conduct a two-step goodwill impairment test. Based on our qualitative assessment for Fiscal 2012, we concluded that it is not more likely than not that the fair value of our reporting units are less than their carrying amount and therefore, we did not perform a two-step goodwill impairment test.

In Fiscal 2011, during the quarter ended December 31, 2010, due primarily to lower than expected operating results in our Transportation Systems reporting unit, as well as ongoing weakness specifically in the Transportation Systems markets, we performed an interim test of impairment of the carrying value of goodwill in our Transportation Systems reporting unit as of December 31, 2010. In performing the first step in this analysis, we estimated the fair value of our Transportation Systems reporting unit using the income approach. As of December 31, 2010, we determined that the carrying value of our Transportation Systems reporting unit exceeded its estimated fair value and, accordingly, we performed the second step of the impairment analysis to estimate the implied fair value of the goodwill of this reporting unit.

The implied fair value of goodwill was determined in the same manner utilized to estimate the amount of goodwill recognized in a business combination. To determine this value, we estimated the fair value of the assets and liabilities, including certain intangible assets, to be allocated to the Transportation Systems reporting unit as of December 31, 2010. The implied fair value of goodwill was measured as the difference between the estimated fair value of the reporting unit over the estimated fair value amounts of its assets and liabilities. The impairment loss for the Transportation Systems reporting unit was measured by the amount the carrying value of its goodwill exceeded the implied fair value of the goodwill. Accordingly, in order to write down Transportation Systems goodwill with a carrying value of \$14.9 million to its implied fair value of \$6.9 million, we recorded an impairment charge of \$8.0 million in the three months ended December 31, 2010.

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We estimated the fair value of the Transportation Systems reporting unit using the income approach, which was based on management's business plans and financial projections for the next five years, along with a perpetual growth rate thereafter of approximately 4%. The analysis also used a weighted average discount rate of approximately 14%, which we believe reflects our cost of capital, slightly adjusted for increased market risk.

6. Fair Value Measurements

We measure fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Fair value measurements are based on a three-tier hierarchy that prioritizes the inputs used to measure fair value. These tiers include: Level 1, defined as observable inputs such as quoted prices in active markets for identical assets and liabilities; Level 2, defined as observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities or prices quoted in inactive markets; and Level 3, defined as unobservable inputs that are significant to the fair value of the asset or liability, and for which little or no market data exists, therefore requiring management to utilize its own assumptions to provide its best estimate of what market participants would use in valuing the asset or liability.

The liability for the estimated fair value of the contingent consideration in connection with our acquisitions of MET and BTS was determined using Level 3 inputs based on a probabilistic calculation whereby we assigned estimated probabilities to achieving the earn-out targets and then discounted the total contingent consideration to net present value. The following table reconciles this liability measured at fair value on a recurring basis for Fiscal 2012 (in thousands):

Balance at March 31, 2011	\$ 2,528
Fair value of BTS contingent consideration assumed at acquisition date	971
Deferred payments made to MET shareholders	(676)
Change in fair value included in net income	(619)
Balance at March 31, 2012	<u>\$ 2,204</u>

The change in the estimated fair value of this liability during the current fiscal year resulted primarily from payments to the shareholders of MET related to the first year deferred payment and revisions to our estimates regarding both the probability of achieving certain earn-out targets and the amounts of certain future deferred payments.

The current portions of the liability at March 31, 2012 and 2011 were \$1.6 million and \$1.5 million, respectively, and were included within accrued liabilities in the accompanying consolidated balance sheets. The remaining non-current portions of the liability are included within non-current liabilities in the accompanying consolidated balance sheets.

Other than the above, we did not have any material financial assets or liabilities measured at fair value on a recurring basis using Level 3 inputs as of March 31, 2012.

Our non-financial assets, such as goodwill, intangible assets and property and equipment, are measured at fair value on a non-recurring basis, generally when there is a transaction involving those assets such as a purchase transaction, a business combination or an adjustment for impairment. See Notes 4 and 5 above for further discussion regarding certain of our intangible assets and goodwill balances (including goodwill impairment) that were measured at fair value, using certain Level 3 inputs, during the fiscal years ended March 31, 2012 and 2011.

7. Revolving Line of Credit and Long-Term Debt

Revolving Line of Credit

In October 2008, we entered into a \$19.5 million credit facility with California Bank & Trust ("CB&T"). This credit facility provided for a two-year revolving line of credit with borrowings of up to \$12.0 million and a \$7.5 million 48-month term note (discussed below). Interest on borrowed amounts under the revolving line of credit are payable monthly at a rate equal to the current stated prime rate (3.25% at March 31, 2012) up to the current stated prime rate plus 0.50%, depending on aggregate deposit balances maintained at the bank in relation to the total loan commitment under the credit facility. We are obligated to pay an unused line fee of 0.25% per annum applied to the average unused portion of the revolving line of credit during the preceding month. The revolving line of credit does not contain any early termination fees and is secured by substantially all of our assets. As of March 31, 2012, no amounts were borrowed under the revolving line of credit portion of the facility. Availability under this line of credit may be reduced or otherwise limited as a result of our obligations to comply with certain financial covenants. In September 2010, we entered into a modification agreement with CB&T to extend the expiration date of our revolving line of credit to October 1, 2012.

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Long-Term Debt — Bank Term Note

As of March 31, 2012, we had outstanding borrowings of approximately \$634,000 under the term note with our bank referenced above, which expires on May 1, 2013. Principal payments under this term note are required to be repaid in monthly installments of \$152,000. Additionally, beginning on November 1, 2009, and on November 1 of each year thereafter, we are required to repay additional principal of up to \$500,000, calculated based on certain financial measures, as further defined in the loan agreement. These additional principal payments effectively reduce the total number of monthly installments necessary to repay the term note. To date, we have made additional principal payments of \$500,000 on each of November 1, 2011, 2010 and 2009. Interest on the term note is payable monthly at a rate equal to the current stated prime rate plus 0.50% up to the current stated prime rate plus 1.00%, depending on aggregate deposit balances maintained at the bank in relation to the total loan commitment under the credit facility. The term note contains no early termination fees and, along with the revolving line of credit under the same credit agreement, is secured by substantially all of our assets. We currently expect the remaining outstanding balance of this term note will be repaid in full by June 2012.

8. Income Taxes:

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

	Year Ended March 31,		
	2012	2011	2010
	(In thousands)		
Income tax provision (benefit) at statutory rates	\$ 663	\$ (1,658)	\$ 1,140
State income taxes net of federal benefit	562	189	192
Impairment charges	—	2,044	—
Research credits	(246)	—	—
Change in fair value of contingent acquisition consideration	(211)	—	—
Compensation charges	59	94	(12)
Unrecognized tax benefits	(276)	(288)	(362)
Other	92	(103)	2

Provision for income taxes	\$ 643	\$ 278	\$ 960
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The components of deferred tax assets and liabilities are as follows:

	March 31,	
	2012	2011
(In thousands)		
Deferred tax assets:		
Net operating losses	\$ 8,246	\$ 12,315
Credit carry forwards	773	319
Deferred compensation and payroll	941	823
Bad debt allowance and other reserves	433	763
Deferred rent	435	—
Other, net	300	252
Total deferred tax assets	<u>11,128</u>	<u>14,472</u>
Deferred tax liabilities:		
Property and equipment	(517)	(66)
Deferred rent	—	(145)
Acquired intangibles	(754)	(527)
Goodwill	(193)	—
Total deferred tax liabilities	<u>(1,464)</u>	<u>(738)</u>
Net deferred tax assets	<u>\$ 9,664</u>	<u>\$ 13,734</u>

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

	Year Ended March 31,		
	2012	2011	2010
(In thousands)			
Current income tax provision (benefit):			
Federal	\$ (221)	\$ (186)	\$ (234)
State	208	264	127
Deferred income tax provision (benefit):			
Federal	12	251	903
State	644	(51)	164
Net income tax provision (benefit)	<u>\$ 643</u>	<u>\$ 278</u>	<u>\$ 960</u>

At March 31, 2012, we had approximately \$525,000 in federal alternative minimum tax credit carryforwards that can be carried forward indefinitely. We had \$25.0 million of federal net operating loss carryforwards at March 31, 2012 that begin to expire in 2021. We also had \$10.9 million of state net operating loss carryforwards at March 31, 2012, of which \$420,000 are scheduled to expire in 2014, \$10.2 million are scheduled to expire in 2015 and \$298,000 are scheduled to expire in 2031.

Due to changes in stock ownership, our federal net operating loss carryforwards of approximately \$25.0 million as of March 31, 2012 and other federal attributes are subject to an annual limitation under Section 382 of the Internal Revenue Code. As of March 31, 2012, based on the cumulative amount of tax attributes that have become available under the limitation imposed by Section 382, all of our net operating losses are now fully available for use. Our deferred tax assets at March 31, 2012 do not include approximately \$901,000 of excess tax benefits from employee stock option exercises that are a component of our net operating loss carryforwards. If and when such excess tax benefits are realized, stockholders' equity will be adjusted.

As of March 31, 2012 and 2011, we determined that it was more likely than not that our deferred tax assets will be realized. Accordingly, no valuation allowance has been recorded against our deferred tax assets as of either such dates. In making our determination as to the realizability of our deferred tax assets, we reviewed all available positive and negative evidence, including reversal of deferred tax liabilities, potential carrybacks, projected future taxable income, tax planning strategies and recent financial performance.

Unrecognized Tax Benefits

As of March 31, 2012 and 2011, our gross unrecognized tax benefits were \$1.7 million and \$1.9 million, respectively, of which \$1.3 million and \$1.5 million, respectively, if recognized, would affect our effective tax rate.

We recognize interest and/or penalties related to income tax matters in income tax expense. As of March 31, 2012 and 2011, we had accrued cumulatively \$56,000 and \$45,000, respectively, for the payment of potential interest and penalties.

A reconciliation of the beginning and ending balances of the total amounts of gross unrecognized tax benefits is as follows:

	Year Ended March 31,		
	2012	2011	2010
	(In thousands)		
Gross unrecognized tax benefits at beginning of year	\$ 1,941	\$ 2,153	\$ 2,525
Increases for tax positions taken in prior years	97	121	93
Decreases for tax positions taken in prior years	(10)	(15)	—
Increases for tax positions taken in the current year	20	17	—
Decreases for tax positions taken in the current year	—	—	(51)
Settlement with taxing authorities	—	(8)	—
Lapse in statute of limitations	(356)	(327)	(414)
Gross unrecognized tax benefits at March 31	<u>\$ 1,692</u>	<u>\$ 1,941</u>	<u>\$ 2,153</u>

We anticipate a decrease in gross unrecognized tax benefits of approximately \$60,000 within the next twelve months based on federal and state statute expirations in various jurisdictions.

We are subject to taxation in the U.S. and various states. We are subject to U.S. federal tax examination for fiscal tax years ended March 31, 2009 or later, and state and local income tax examination for fiscal tax years ended March 31, 2008 or later.

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9. Commitments and Contingencies

Litigation and Other Contingencies

From time to time, we have been involved in litigation relating to claims arising out of our operations in the normal course of business. We currently are not a party to any legal proceedings, the adverse outcome of which, in management's opinion, individually or in the aggregate, would have a material adverse effect on our consolidated results of operations, financial position or cash flows.

Operating Leases

In May 2007, we entered into an agreement to lease 52,000 square feet of office space in Santa Ana, California for a term of 88 months. In September 2007, we relocated our headquarters and principal operations into this space. The monthly lease rate was \$102,000 during the first year of the lease and increases each year thereafter, up to a maximum of \$120,000 during the last year of the lease. The lease may be extended for a period of five years, at our option, at a lease rate to be based on the market lease rate for comparable property determined as of the commencement date of the extension period. Additionally, the lease agreement provided for \$1.8 million in incentives in the form of tenant improvement allowances, which we recorded as deferred rent and capitalized leasehold improvements in our consolidated balance sheet. The deferred rent amount reduces monthly rent expense over the term of the lease, and the capitalized leasehold improvements amount are being depreciated over the initial term of the lease (the estimated useful life of the related leasehold improvements).

We have lease commitments for facilities in various locations throughout the U.S., as well as for certain equipment. Future minimum rental payments under these non-cancelable operating leases at March 31, 2012 were as follows:

Year Ending March 31,	
(In thousands)	
2013	\$ 2,111
2014	1,905
2015	1,430
2016	280
2017	175
Thereafter	339
	<u>\$ 6,240</u>

Rent expense totaled \$1.9 million for each of the fiscal years ended March 31, 2012, 2011 and 2010, respectively.

Related Party Transaction

We previously subleased office space to MAXxess Systems, Inc. ("MAXxess"), one of our former subsidiaries that we sold in September 2003. MAXxess is currently owned by an investor group that includes two of our directors, one of whom is the former Chief Executive Officer of MAXxess. The sublease terminated in September 2007, at which time MAXxess owed us an aggregate of \$274,000 related to this sublease and certain ancillary corporate services that we provided to MAXxess. We have previously fully reserved for amounts owed to us by MAXxess under the terms of this sublease. In August 2009, MAXxess executed a promissory note payable to Iteris in the original principal amount of \$274,000. The promissory note bears interest at a rate of 6% per annum, compounded annually, with accrued interest to be paid annually on the first business day of each calendar year. Payments under the note may be made in bona fide services rendered by MAXxess to Iteris to the extent such services and amounts are pre-approved in writing by us. All amounts outstanding under the note will become due and payable on the earliest of (i) August 10, 2014, (ii) a change of control in MAXxess, or (iii) a financing by MAXxess resulting in gross proceeds of at least \$10 million. As of March 31, 2012, approximately \$259,000 of the original principal balance is outstanding

and payable to Iteris, all of which remains fully reserved.

Inventory Purchase Commitments

At March 31, 2012, we had firm commitments to purchase approximately \$2.5 million of inventory, which are expected to occur primarily during the first and second quarters of our fiscal year ending March 31, 2013.

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10. Stockholders' Equity

Preferred Stock

Our certificate of incorporation provides for the issuance of up to 2,000,000 shares of preferred stock. Our 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. As of March 31, 2012 and 2011, there were no outstanding shares of preferred stock, and we do not currently have plans to issue any shares of preferred stock.

In August 2009, our Board of Directors adopted a stockholder rights plan, which calls for preferred stock purchase rights (each, a "Right") to be distributed, as a dividend, at the rate of one Right for each share of common stock held as of September 3, 2009. Each Right will entitle holders of common stock to buy one one-thousandth of one share of Series A Junior Participating Preferred Stock of Iteris. A further description and terms of the Rights are set forth in the Rights Agreement dated August 20, 2009 by and between Iteris and Computershare Trust Company, N.A., as rights agent. In connection with the stockholder rights plan, our Board of Directors approved the adoption of a Certificate of Designations, which created the Series A Junior Participating Preferred Stock, and likewise authorized the filing of a Certification of Elimination to eliminate the two series of junior participating preferred stock, which were originally created in April 1998 in connection with our previous stockholder rights plan which expired in 2008.

Common Stock Warrants

As of March 31, 2012, we had outstanding fully exercisable warrants to purchase 15,000 shares of our common stock. These warrants have an exercise price per share of \$1.42 and a remaining contractual life of 1.4 years. There was no activity with respect to these or any other warrants during Fiscal 2012.

In connection with our adoption of certain provisions of accounting for derivatives, which became effective for us on April 1, 2009, we determined that certain outstanding warrants to purchase shares of our common stock contained provisions that provide for a possible future adjustment to either the exercise price and/or number of shares to be issued upon exercise. As such, beginning April 1, 2009, we began recognizing these warrants as liabilities at their respective estimated fair values on each reporting date. The cumulative effect of the change in accounting for these warrants of \$47,000 was recognized as an adjustment to the opening balance of accumulated deficit at April 1, 2009. The amounts recognized in the consolidated balance sheet as a result of our adoption on April 1, 2009 were determined based on the amounts that would have been recognized if this accounting treatment had been applied from the issuance date of the warrants. By March 31, 2011, all such warrants had expired unexercised, and thus there was no remaining liability recorded on our consolidated balance sheet at that date or thereafter. We estimated the fair value of these warrants using the BSM option-pricing formula. The change in the estimated fair value of the warrants for the fiscal years ended March 31, 2011 and 2010 is included in "other income, net" in the accompanying consolidated statements of operations.

Common Stock Reserved for Future Issuance

The following summarizes common stock reserved for future issuance at March 31, 2012:

	<u>Number of Shares</u> <u>(In thousands)</u>
Stock options outstanding	2,493
Restricted stock units outstanding	235
Authorized for future issuance under stock incentive plans	335
Warrants outstanding	15
	<u>3,078</u>

11. Employee Benefit Plans

Stock Incentive Plans

In September 2007, our stockholders approved the 2007 Omnibus Incentive Plan (the "2007 Plan"), which provides that options to purchase shares of our unissued common stock may be granted to our employees, officers, consultants and directors at exercise prices which are equal to or greater than the market value of our common stock on the date of grant. Options expire no more than ten years after the date of grant and generally vest at the rate of 25% on each of the first four anniversaries of the grant date. The 2007 Plan also allows for the issuance of stock appreciation rights, restricted stock, restricted stock units ("RSUs") and other stock-based awards based on the value of our common stock. New shares are issued to satisfy stock option exercises and share issuances

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under the 2007 Plan. In September 2009, our stockholders approved an amendment to increase the number of shares of our common stock authorized and reserved for issuance under the 2007 Plan by 800,000 shares to a total of 1,650,000 shares. At March 31, 2012, there were approximately 335,000 shares of common stock available for grant under this plan. As of March 31, 2012, options to purchase approximately 1,022,000 shares of common stock, as well as 235,000 RSUs, were outstanding under the 2007 Plan.

Our 1997 Stock Incentive Plan (the “1997 Plan”) terminated in September 2007; however, all stock options outstanding under the 1997 Plan remain outstanding pursuant to the terms of such stock options. As of March 31, 2012, options to purchase approximately 1,061,000 shares of our common stock were outstanding under the 1997 Plan. No further options or other stock-based awards may be granted under the 1997 Plan.

In connection with our merger with our Iteris, Inc. subsidiary (the “Iteris Subsidiary”) in 2004, we assumed the 1998 Stock Incentive Plan (the “1998 Plan”) of the Iteris Subsidiary and all outstanding options granted thereunder. As of March 31, 2012, options to purchase approximately 410,000 shares of our common stock were outstanding under the 1998 Plan. No further options or other stock-based awards may be granted under the 1998 Plan.

Certain options granted under the 2007 Plan, the 1997 Plan and the 1998 Plan (collectively, the “Plans”) and the RSUs granted under the 2007 Plan provide for accelerated vesting of unvested options in the event of a change in control under certain circumstances.

Stock Options

A summary of activity in the Plans with respect to our stock options for Fiscal 2012 is as follows:

	Options (In thousands)	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Life (Years)	Aggregate Intrinsic Value (In thousands)
Options outstanding at March 31, 2011	3,111	\$ 1.59		
Granted	315	1.13		
Exercised	(68)	1.24		
Forfeited	(31)	1.54		
Expired	(834)	1.30		
Options outstanding at March 31, 2012	2,493	\$ 1.64	3.8	\$ 393
Options exercisable at March 31, 2012	1,986	\$ 1.73	2.5	\$ 267
Vested and expected to vest at March 31, 2012	2,431	\$ 1.65	3.6	\$ 374
Options exercisable at March 31, 2012 pursuant to a change-in-control	2,493	\$ 1.64	3.8	\$ 393

Restricted Stock Units

In August 2010, we began granting RSUs under the 2007 Plan to certain of our employees. RSUs awards are stock-based awards that entitle the holder to receive one share of our common stock for each RSU upon vesting. RSUs vest at the rate of 25% on each of the first four anniversaries of the grant date provided that the holder remains in service (as defined by the 2007 Plan) as of the vesting date. The fair value per RSU is determined based on the closing market price of our common stock on the grant date.

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A summary of activity with respect to our RSUs for Fiscal 2012 is as follows:

	# of Shares (In thousands)	Weighted Average Price Per Share	Weighted Average Remaining Life (Years)	Aggregate Intrinsic Value (In thousands)
RSUs outstanding at March 31, 2011	214	\$ 1.48		
Granted	100	1.10		
Vested	(51)	1.48		
Forfeited	(28)	1.48		
RSUs outstanding at March 31, 2012	235	\$ 1.32	2.8	\$ 40
Expected to vest at March 31, 2012	198	\$ 1.32	2.8	\$ 33
Common stock issuable (for RSUs) at				

March 31, 2012 upon a change-in-control	235	\$	1.32	\$	2.8	\$	40
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Stock-Based Compensation

The following table presents stock-based compensation expense that is included in each functional line item in our consolidated statements of operations:

	Year Ended March 31,		
	2012	2011	2010
	(In thousands)		
Cost of net sales	\$ 16	\$ 11	\$ 9
Cost of contract revenues	29	36	39
Selling, general and administrative expense	249	280	288
Research and development expense	31	25	21
Income from discontinued operation, net of tax	6	30	18
Total stock-based compensation	\$ 331	\$ 382	\$ 375

At March 31, 2012, there was approximately \$475,000 of unrecognized compensation expense related to unvested stock options and RSUs. This expense is currently expected to be recognized over a weighted average period of approximately 2.5 years. If there are any modifications or cancellations of the underlying unvested awards, we may be required to accelerate, increase or cancel any remaining unearned stock-based compensation expense. Future stock-based compensation expense and unearned stock-based compensation will increase to the extent that we grant additional stock options, RSUs or other stock-based awards.

The grant date fair value of stock options granted was estimated using the following weighted-average assumptions:

	Year Ended March 31,		
	2012	2011	2010
Expected life - years	7.0	7.0	7.0
Risk-free interest rate	1.6%	2.1%	3.2%
Expected volatility of common stock	52%	58%	74%
Dividend yield	—%	—%	—%

A summary of certain fair value and intrinsic value information pertaining to our stock options is as follows:

	Year Ended March 31,		
	2012	2011	2010
	(In thousands, except per share amounts)		
Weighted average grant date fair value per share of options granted	\$ 0.61	\$ 0.86	\$ 1.01
Intrinsic value of options exercised	\$ 7	\$ 23	\$ 28

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Employee Incentive Programs

Under the terms of a Profit Sharing Plan, we may contribute to a trust fund such amounts as determined annually by the Board of Directors. No contributions were made during the fiscal years ended March 31, 2012, 2011 and 2010.

We sponsor a defined contribution 401(k) Plan, adopted in 1990, under which eligible associates voluntarily contribute to the plan, up to IRS maximums, through payroll deductions. Under the provisions of the 401(k) Plan, associates have various investment choices, one of which is the purchase of Iteris common stock at market price. We match up to 90% of contributions, based on years of service, up to a stated limit. From July 1, 2009 through March 31, 2010, we temporarily suspended our matching contributions to the 401(k) Plan. Beginning in April 2010, we reinstated certain limited matching contributions to the 401(k) Plan. Our matching contributions under the 401(k) Plan were approximately \$475,000, \$491,000 and \$220,000 for the fiscal years ended March 31, 2012, 2011 and 2010, respectively.

12. Stock Repurchase Program

In August 2011, our Board of Directors approved a stock repurchase program pursuant to which we may acquire up to \$3 million of our outstanding common stock from time to time until August 2012. Under the program, we may repurchase shares in open-market and privately negotiated transactions and block trades and pursuant to a 10b5-1 trading plan during our closed trading windows. There is no guarantee as to the exact number of shares that will be repurchased. We may modify, terminate or extend the repurchase program at any time without prior notice. From inception of this program through March 31, 2012, we repurchased approximately 573,558 shares of our common stock at an average price per share of \$1.31. All repurchased shares have been retired and resumed their status as authorized and unissued shares of our common stock.

13. Business Segments, Significant Customer and Geographic Information

Business Segments

As a result of the sale of substantially all of the assets used in connection with our Vehicle Sensors segment to Bendix in July 2011 (see Note 3), along with a reevaluation and reorganization of our operating segments in the first quarter of our fiscal year ended March 31, 2012, we now operate in two reportable segments: Roadway Sensors and Transportation Systems.

The Roadway Sensors segment includes, among other products, our Vantage, Versicam, Pico, Vantage Vector and Abacus vehicle detection systems for traffic intersection control, incident detection and certain highway traffic data collection applications.

The Transportation Systems segment includes transportation engineering and consulting services and the development of transportation management and traveler information systems for the ITS industry. This segment includes the operations of MET, which specializes in 511 advanced traveler information systems and offers Maintenance Decision Support System management tools that allow users to create solutions to meet roadway maintenance decision needs. Also included in this segment are the operations of BTS, which specializes in transportation performance measurement.

The accounting policies of our reportable segments are the same as those described in the summary of significant accounting policies (Note 1). Certain corporate expenses, including interest and amortization of intangible assets, are not allocated to the segments. Unallocated corporate expenses in the current fiscal year also include costs related to the sale of our Vehicle Sensors segment and certain other corporate initiatives, as well as costs related to our recently announced iPerform information management solution. The reportable segments are each managed separately because they manufacture and distribute distinct products or provide services with different processes. All reported segment revenues are derived from external customers.

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Selected financial information for our reportable segments for the fiscal years ended March 31, 2012, 2011 and 2010 is as follows:

	Roadway Sensors	Transportation Systems	Total
	(In thousands)		
Year Ended March 31, 2012			
Product revenue	\$ 27,679	\$ —	\$ 27,679
Service and other revenue	—	30,727	30,727
Depreciation	194	393	587
Segment income	2,826	1,284	4,110
Year Ended March 31, 2011			
Product revenue	\$ 28,208	\$ —	\$ 28,208
Service and other revenue	—	23,758	23,758
Depreciation	217	250	467
Impairment of goodwill	—	7,970	7,970
Segment income (loss)	3,942	(7,540)	(3,598)
Year Ended March 31, 2010			
Product revenue	\$ 25,341	\$ —	\$ 25,341
Service and other revenue	—	26,413	26,413
Depreciation	234	221	455
Segment income	3,158	1,445	4,603

The following table reconciles total segment income (loss) to consolidated income (loss) from continuing operations before income taxes:

	Year Ended March 31,		
	2012	2011	2010
Segment income (loss):			
Total income (loss) from reportable segments	\$ 4,110	\$ (3,598)	\$ 4,603
Unallocated amounts:			
Corporate and other expenses	(2,208)	(913)	(916)
Amortization of intangible assets	(504)	(176)	(113)
Change in fair value of contingent acquisition consideration	619	(55)	—
Other income, net	4	18	44
Interest expense, net	(72)	(152)	(264)
Income (loss) from continuing operations before income taxes	\$ 1,949	\$ (4,876)	\$ 3,354

Fiscal 2012 corporate and other expense includes legal and accounting expenses related to the sale of the Vehicle Sensors segment in July 2011 as well as certain other costs incurred in connection with the development of IterisPeMS and certain corporate general and administrative expenses allocated to the Vehicle Sensors segment in prior fiscal years.

Significant Customer and Geographic Information

No single customer accounted for more than 10% of our total net sales and contract revenues for each of the fiscal years ended March 31, 2012, 2011 and 2010.

No individual customer or government agency had a receivable balance at March 31, 2012 or 2011 greater than 10% of our total trade accounts receivable balances as of March 31, 2012 and 2011, respectively.

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The following table sets forth the percentages of our total net sales and contract revenues, by geographic region, derived from shipments to, or contract, service and other revenues from, external customers located outside the U.S.:

	Year Ended March 31,		
	2012	2011	2010
Europe	—%	5%	4%
Asia	1	5	2
Other	1	3	2
	<u>2%</u>	<u>13%</u>	<u>8%</u>

Substantially all of our long-lived assets are held in the U.S.

14. Quarterly Financial Data (Unaudited)

Quarter Ended:	Total Net Sales and Contract Revenues	Gross Profit	Net Income (Loss)	Basic Net Income (Loss) per Share	Diluted Net Income (Loss) per Share
(In thousands, except per share amounts)					
June 30, 2011	\$ 13,892	\$ 5,869	\$ 97	\$ 0.00	\$ 0.00
September 30, 2011	14,393	6,005	1,310	0.04	0.04
December 31, 2011	14,881	5,464	747	0.02	0.02
March 31, 2012	15,240	5,733	360	0.01	0.01
	<u>\$ 58,406</u>	<u>\$ 23,071</u>	<u>\$ 2,514</u>	<u>\$ 0.07*</u>	<u>\$ 0.07*</u>
June 30, 2010	\$ 13,905	\$ 6,257	\$ 797	0.02	0.02
September 30, 2010	12,466	5,675	542	0.02	0.02
December 31, 2010	11,953	4,894	(7,027)	(0.20)	(0.20)
March 31, 2011	13,642	6,058	479	0.01	0.01
	<u>\$ 51,966</u>	<u>\$ 22,884</u>	<u>\$ (5,209)</u>	<u>\$ (0.15)*</u>	<u>\$ (0.15)*</u>

* 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.

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Exhibit Index

Exhibit Number	Description	Reference
2.1+	Stock Purchase Agreement dated December 23, 2010 by and among Iteris, Inc., Meridian Environmental Technology, Inc., (“MET”) the shareholders of MET and Kathy J. Osborne as the Shareholders Representative	<i>Exhibit 2.1 to the registrant’s Quarterly Report on Form 10-Q for the quarter ended December 31, 2010 as filed with the SEC on February 14, 2011</i>
2.2+	Asset Purchase Agreement by and between Iteris, Inc. and Bendix Commercial Vehicle Systems LLC, dated as of July 25, 2011	<i>Exhibit 2.1 to the registrant’s Current Report on Form 8-K/A as filed with the SEC on November 1, 2011</i>
3.1	Restated Certificate of Incorporation of the registrant	<i>Exhibit 3.1 to the registrant’s Quarterly Report on Form 10-O</i>

for the quarter ended September 30, 2009 as filed with the SEC on October 30, 2009

3.2	Certificate of Designations of Series A Junior Participating Preferred Stock	<i>Exhibit 3.2 to the registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2009 as filed with the SEC on October 30, 2009</i>
3.3	Bylaws of the registrant, as amended	<i>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</i>
3.4	Certificates of Amendment to Bylaws of the registrant dated April 24, 1998 and August 10, 2001	<i>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</i>
3.5	Certificate of Amendment to Bylaws of registrant dated September 9, 2004	<i>Exhibit 3.1 to the registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2004 as filed with the SEC on November 15, 2004</i>
3.6	Certificate of Amendment to Bylaws of registrant effective September 16, 2005	<i>Exhibit 3.5 to the registrant's Annual Report on Form 10-K for the year ended March 31, 2007</i>
3.7	Certificate of Amendment to Bylaws of registrant effective December 7, 2007	<i>Exhibit 3.1 to the registrant's Current Report on Form 8-K as filed with the SEC on December 13, 2007</i>
3.8	Certificate of Amendment to Bylaws of registrant, effective August 20, 2009	<i>Exhibit 3.3 to the registrant's Current Report on Form 8-K as filed with the SEC on August 21, 2009</i>
4.1	Specimen of common stock certificate	<i>Exhibit 4.1 to registrant's Registration Statement on Form 8-A as filed with the SEC on December 8, 2004</i>
4.2	Rights Agreement dated August 20, 2009 between the registrant and Computershare Trust Company, N.A., which includes the form of Certificate of Designations for the Series A Junior Participating Preferred Stock, the form of Right Certificate, and Summary of Rights to Purchase Preferred Stock as exhibits thereto	<i>Exhibit 4.1 to the registrant's Current Report on Form 8-K as filed with the SEC on August 21, 2009</i>
10.1	Form of Indemnity Agreement entered into by the registrant and certain of its officers and directors	<i>Exhibit 19.4 to the registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 1988</i>
10.2	Form of Indemnification Agreement entered into by the registrant and certain of its officers and directors	<i>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</i>

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10.3*	1997 Stock Incentive Plan (the "1997 Plan") as amended on May 3, 2003, as further amended on December 15, 2004	<i>Exhibit 10.32 to the registrant's Annual Report on Form 10-K for the year ended March 31, 2005 as filed with the SEC on July 14, 2005</i>
10.4*	Form of Notice of Grant of Stock Option for 1997 Plan	<i>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</i>
10.5*	Form of Stock Option Agreement for the 1997 Plan	<i>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</i>
10.6*	Form of Addendum to Stock Option Agreement for 1997 Plan—Involuntary Termination Following Corporate Transaction or Change in Control	<i>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</i>
10.7*	Form of Addendum to Stock Option Agreement for 1997 Plan—Limited Stock Appreciation Rights	<i>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</i>

10.8*	Form of Stock Issuance Agreement for 1997 Plan	<i>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</i>
10.9*	Form of Addendum to Stock Issuance Agreement for 1997 Plan—Involuntary Termination Following Corporate Transaction/Change in Control	<i>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</i>
10.10*	Form of Notice of Grant of Automatic Stock Option for 1997 Plan—Initial Grant	<i>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</i>
10.11*	Form of Notice of Grant of Automatic Stock Option for 1997 Plan—Annual Grant	<i>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</i>
10.12*	Form of Automatic Stock Option Agreement for 1997 Plan	<i>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</i>
10.13*	Iteris Inc. 1998 Stock Incentive Plan (as amended on February 7, 2000) ("1998 Plan")	<i>Exhibit 10.24 to the registrant's Annual Report on Form 10-K for the year ended March 31, 2005 as filed with the SEC on July 14, 2005</i>
10.14*	Form of Notice of Grant for 1998 Plan, including forms of Option Agreement and Stock Purchase Agreement for the following directors and executive officers: Gregory McKhann, James S. Miele and Abbas Mohaddes	<i>Exhibit 99.2 to the registrant's Registration Statement on Form S-8 (File No. 333-126834) as filed with the SEC on July 22, 2005</i>
10.15*	Form of Addendum to Stock Option Agreement for 1998 Plan	<i>Exhibit 99.3 to the registrant's Registration Statement on Form S-8 (File No. 333-126834) as filed with the SEC on July 22, 2005</i>
10.16*	Form of 1997 Stock Option Agreements	<i>Exhibit 99.4 to the registrant's Registration Statement on Form S-8 (File No. 333-126834) as filed with the SEC on July 22, 2005</i>

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10.17	Sublease Agreement, dated September 30, 2003, by and between Odetics, Inc. and Maij, Inc.	<i>Exhibit 10.1 to the registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2007 as filed with the SEC on August 14, 2007</i>
10.18	Office Lease Agreement, dated May 24, 2007, by and between Crown Carnegie Associates, LLC and Iteris, Inc.	<i>Exhibit 10.2 to the registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2007 as filed with the SEC on August 14, 2007</i>
10.19*	2007 Omnibus Incentive Plan	<i>Filed herewith</i>
10.20*	Forms of Stock Option Agreements under the 2007 Omnibus Incentive Plan	<i>Filed herewith</i>
10.21*	Change in Control Agreement dated June 11, 2008 by and between James S. Miele and Iteris, Inc.	<i>Exhibit 10.42 to the registrant's Annual Report on Form 10-K for the year ended March 31, 2008 as filed with the SEC on June 12, 2008</i>
10.22	Amended and Restated Loan and Security Agreement dated February 4, 2009 by and between California Bank & Trust and the registrant	<i>Exhibit 10.1 to the registrant's Quarterly Report on Form 10-Q for the quarter ended December 31, 2008 as filed with the SEC on February 13, 2009</i>
10.23	Unsecured Promissory Note dated August 10, 2009 executed by MAXxess Systems, Inc.	<i>Exhibit 10.1 to the registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2009 as filed with the SEC on August 11, 2009</i>
10.24*	Letter Agreement dated July 27, 2010 by and between the registrant and Abbas Mohaddes	<i>Exhibit 10.1 to the registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2010 as filed with the SEC on July</i>

10.25*	Change in Control Agreement dated July 27, 2010 by and between the registrant and Abbas Mohaddes	<i>Exhibit 10.2 to the registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2010 as filed with the SEC on July 28, 2010</i>
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10.26*	Form of Restricted Stock Unit Award Agreement under the 2007 Omnibus Incentive Plan	<i>Exhibit 10.3 to the registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2010 as filed with the SEC on July 28, 2010</i>
10.27	Modification Agreement dated September 30, 2010 by and between Iteris, Inc. and California Bank & Trust	<i>Exhibit 10.1 to the registrant's Current Report on Form 8-K as filed with the SEC on October 6, 2010</i>
21	Subsidiaries of the registrant	<i>Filed herewith</i>
23	Consent of Independent Registered Public Accounting Firm	<i>Filed herewith</i>
24	Power of Attorney	<i>Filed herewith (included on the Signature page)</i>
31.1	Certification of the Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	<i>Filed herewith</i>
31.2	Certification of the Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	<i>Filed herewith</i>
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	<i>Filed herewith</i>
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	<i>Filed herewith</i>
101.INS#	XBRL Instance Document	<i>Filed herewith</i>
101.SCH#	XBRL Taxonomy Extension Schema Document	<i>Filed herewith</i>
101.CAL#	XBRL Taxonomy Extension Calculation Linkbase Document	<i>Filed herewith</i>
101.LAB#	XBRL Taxonomy Extension Label Linkbase Document	<i>Filed herewith</i>
101.PRE#	XBRL Taxonomy Extension Presentation Linkbase Document	<i>Filed herewith</i>
101.DEF#	XBRL Taxonomy Definition Presentation Linkbase Document	<i>Filed herewith</i>

* Indicates a management contract or compensatory plan or arrangement

+ Confidential treatment has been requested for certain confidential portions of this exhibit pursuant to Rule 24b-2 of the Securities Exchange Act of 1934, as amended. In accordance with Rule 24b-2, these confidential portions have been omitted from the exhibit and filed separately with the SEC.

Pursuant to Rule 406T of Regulation S-T, these interactive data files i) are not deemed filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, are not deemed filed for purposes of Section 18 of the Securities Exchange Act of 1934, irrespective of any general incorporation language included in any such filings, and otherwise are not subject to liability under these sections; and ii) are deemed to have complied with Rule 405 of Regulation S-T ("Rule 405") and are not subject to liability under the anti-fraud provisions of the Section 17(a)(1) of the Securities Act of 1933, Section 10(b) of the Securities Exchange Act of 1934 or under any other liability provision if we have made a good faith attempt to comply with Rule 405 and, after we become aware that the interactive data files fail to comply with Rule 405, we promptly amend the interactive data files.

ITERIS, INC.
2007 OMNIBUS INCENTIVE PLAN
(amended and restated as of October 21, 2010)

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ITERIS, INC.
2007 OMNIBUS INCENTIVE PLAN
(amended and restated as of October 21, 2010)

Section 1. Purpose

The purpose of the Plan is to promote the interests of the Company and its stockholders by aiding the Company in attracting and retaining employees, officers, consultants, independent contractors, advisors and directors capable of assuring the future success of the Company, to offer such persons incentives to continue in the Company's employ or service and to afford such persons an opportunity to acquire a proprietary interest, or otherwise increase their proprietary interest, in the Company.

Section 2. Definitions

As used in the Plan, the following terms shall have the meanings set forth below:

- (a) "Affiliate" shall mean (i) any entity that, directly or indirectly through one or more intermediaries, is controlled by the Company and (ii) any entity in which the Company has a significant equity interest, in each case as determined by the Committee.
- (b) "Award" shall mean any Option, Stock Appreciation Right, Restricted Stock, Restricted Stock Unit, Performance Award, Dividend Equivalent, Other Stock Grant or Other Stock-Based Award granted under the Plan.
- (c) "Award Agreement" shall mean any written agreement, contract or other instrument or document evidencing an Award granted under the Plan. Each Award Agreement shall be subject to the applicable terms and conditions of the Plan and any other terms and conditions (not inconsistent with the Plan) determined by the Committee.
- (d) "Board" shall mean the Board of Directors of the Company.
- (e) "Change in Control" shall mean a change in ownership or control of the Company effected through any of the following transactions: (i) a merger, consolidation or other reorganization unless securities representing more than 50% of the total combined voting power of the voting securities of the successor corporation are immediately thereafter beneficially owned, directly or indirectly and in substantially the same proportion, by the persons who beneficially owned the Company's outstanding voting securities immediately prior to such transaction; (ii) a sale, transfer or other disposition of all or substantially all of the Company's assets; or (iii) the acquisition, directly or indirectly, by any person or related group of persons (other than the Company or a person that directly or indirectly controls, is controlled by, or is under common control with, the Company), of beneficial ownership (within the meaning of Rule 13d-3 of the Exchange Act) of securities possessing more than 50% of the total combined voting power of the Company's outstanding securities pursuant to a tender or exchange offer made directly to the Company's stockholders.
- (f) "Code" shall mean the Internal Revenue Code of 1986, as amended from time to time, and any regulations promulgated thereunder.
- (g) "Committee" shall mean one or more committees of Directors designated by the Board to administer the Plan, of which the Company's compensation committee shall initially be the primary committee. The primary Committee shall be comprised of at least two Directors but not less than such number of Directors as shall be required to permit Awards granted under the Plan to qualify under Rule 16b-3 and Section 162(m) of the Code, and each member of the primary Committee shall be a "Non-Employee Director" and an "Outside Director." Any secondary Committee shall be comprised of at least two Directors.
- (h) "Company" shall mean Iteris, Inc., a Delaware corporation, and any successor corporation.
- (i) "Director" shall mean a member of the Board, including any Non-Employee Director.
- (j) "Dividend Equivalent" shall mean any right granted under Section 6(e) of the Plan.
- (k) "Eligible Person" shall mean any employee, officer, consultant, independent contractor, advisor or director providing services to the Company or any Affiliate who the Committee determines to be an Eligible Person.

(l) “*Exchange Act*” shall mean the Securities Exchange Act of 1934, as amended.

(m) “*Fair Market Value*” shall mean, with respect to any property (including, without limitation, any Shares or other securities), the fair market value of such property determined by such methods or procedures as shall be established from time to time by the Committee. Notwithstanding the foregoing and unless otherwise determined by the Committee, if the Shares are at the time listed on any stock exchange in the United States, the Fair Market Value of a Share as of a given date shall be the closing sale price of one Share as reported on the principal United States exchange on which the Shares are listed on the date as of which Fair Market Value is being determined, or, if there is no closing sales price for the Shares on the date in question, then the Fair Market Value shall be the closing sales price on the last preceding date for which such price exists.

(n) “*Incentive Stock Option*” shall mean an option granted under Section 6(a) of the Plan that is intended to qualify as an “incentive stock option” in accordance with the terms of Section 422 of the Code or any successor provision.

(o) “*Non-Employee Director*” shall mean any Director who is not also an employee of the Company or an Affiliate within the meaning of Rule 16b-3.

(p) “*Non-Qualified Stock Option*” shall mean an option granted under Section 6(a) of the Plan that is not an Incentive Stock Option.

(q) “*Option*” shall mean an Incentive Stock Option or a Non-Qualified Stock Option.

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(r) “*Other Stock Grant*” shall mean any right granted under Section 6(f) of the Plan.

(s) “*Other Stock-Based Award*” shall mean any right granted under Section 6(g) of the Plan.

(t) “*Outside Director*” shall mean any Director who is an “outside director” within the meaning of Section 162(m) of the Code.

(u) “*Participant*” shall mean an Eligible Person designated to be granted an Award under the Plan.

(v) “*Performance Award*” shall mean any right granted under Section 6(d) of the Plan.

(w) “*Performance Goal*” shall mean one or more of the following performance goals, either individually, alternatively or in any combination, applied on a corporate, subsidiary or business unit basis: revenue, cash flow, gross profit, earnings before interest and taxes, earnings before interest, taxes, depreciation and amortization and net earnings, earnings per share, margins (including one or more of gross, operating and net income margins), returns (including one or more of return on assets, equity, investment, capital and revenue and total stockholder return), stock price, economic value added, working capital, market share, cost reductions, workforce satisfaction and diversity goals, employee retention, customer satisfaction, completion of key projects and strategic plan development and implementation. Such goals may reflect absolute entity or business unit performance or a relative comparison to the performance of a peer group of entities or other external measure of the selected performance criteria. Pursuant to rules and conditions adopted by the Committee on or before the 90th day of the applicable performance period for which Performance Goals are established, the Committee may appropriately adjust any evaluation of performance under such goals to exclude the effect of certain events, including any of the following events: asset write-downs; litigation or claim judgments or settlements; changes in tax law, accounting principles or other such laws or provisions affecting reported results; severance, contract termination and other costs related to exiting certain business activities; and gains or losses from the disposition of businesses or assets or from the early extinguishment of debt.

(x) “*Person*” shall mean any individual or entity, including a corporation, partnership, limited liability company, association, joint venture or trust.

(y) “*Plan*” shall mean the Iteris, Inc. 2007 Omnibus Incentive Plan, as amended from time to time, the provisions of which are set forth herein.

(z) “*Qualified Performance Based Award*” shall have the meaning set forth in Section 6(d) of the Plan.

(aa) “*Restricted Stock*” shall mean any Share granted under Section 6(c) of the Plan.

(bb) “*Restricted Stock Unit*” shall mean any unit granted under Section 6(c) of the Plan evidencing the right to receive a Share (or evidencing the right to receive a cash payment equal to the Fair Market Value of a Share if explicitly so provided in the Award Agreement) at some future date.

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(cc) “*Rule 16b-3*” shall mean Rule 16b-3 promulgated by the Securities and Exchange Commission under the Exchange Act, or any successor rule or regulation.

(dd) “*Section 162(m)*” shall mean Section 162(m) of the Code and the applicable Treasury Regulations promulgated thereunder.

(ee) “*Securities Act*” shall mean the Securities Act of 1933, as amended.

(ff) “*Service*” shall mean the performance of services for the Company (or any Affiliate) by a person in the capacity of an employee, a member of the board of directors or a consultant, except to the extent otherwise specifically provided in the Award Agreement.

(gg) “*Share*” or “*Shares*” shall mean a share or shares of common stock, \$0.10 par value per share, of the Company or such other securities or property as may become subject to Awards pursuant to an adjustment made under Section 4(c) of the Plan.

(hh) “*Stock Appreciation Right*” shall mean any right granted under Section 6(b) of the Plan.

Section 3. Administration

(a) Power and Authority of the Committee. The Plan shall be administered by the Board and the primary Committee. The Board may designate a secondary Committee to have concurrent authority to administer the Plan, provided that the secondary Committee shall not have any authority (i) with regard to grants of Options to be made to officers or directors of the Company or any Affiliate who are subject to Section 16 of the Exchange Act, (ii) in such a manner as would cause the Plan not to comply with the requirements of Section 162(m) of the Code or (iii) in such a manner as would contravene Section 157 of the Delaware General Corporation Law. Any Awards made to members of the Committee, however, should be authorized by a disinterested majority of the Board. Subject to the express provisions of the Plan and to applicable law, the Committee (or the Board, as applicable) shall have full power and authority to: (i) designate Participants; (ii) determine the type or types of Awards to be granted to each Participant under the Plan; (iii) determine the number of Shares to be covered by (or the method by which payments or other rights are to be determined in connection with) each Award; (iv) determine the terms and conditions of any Award or Award Agreement; (v) amend the terms and conditions of any Award or Award Agreement and accelerate the exercisability of any Option or waive any restrictions relating to any Award; (vi) determine whether, to what extent and under what circumstances Awards may be exercised in cash, Shares, other securities, other Awards or other property, or canceled, forfeited or suspended; (vii) interpret and administer the Plan and any instrument or agreement, including an Award Agreement, relating to the Plan; (viii) establish, amend, suspend or waive such rules and regulations and appoint such agents as it shall deem appropriate for the proper administration of the Plan; and (ix) make any other determination and take any other action that the Committee deems necessary or desirable for the administration of the Plan. Unless otherwise expressly provided in the Plan, all designations, determinations, interpretations and other decisions under or with respect to the Plan or any Award or Award Agreement shall be within the sole discretion of the Committee, may be made at any time and shall be final, conclusive and binding upon any Eligible Person and any holder or beneficiary of any Award.

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(b) Power and Authority of the Board. Notwithstanding anything to the contrary contained herein, the Board may, at any time and from time to time, without any further action of the Committee, exercise the powers and duties of the Committee under the Plan.

Section 4. Shares Available for Awards

(a) Shares Available. Subject to adjustment as provided in Section 4(c) of the Plan, the aggregate number of Shares that may be issued under the Plan shall be One Million Six Hundred Fifty Thousand (1,650,000). Shares to be issued under the Plan may be either authorized but unissued Shares or Shares re-acquired and held in treasury. Notwithstanding the foregoing, (x) the number of Shares available for granting Incentive Stock Options under the Plan shall not exceed One Million Six Hundred Fifty Thousand (1,650,000), subject to adjustment as provided in Section 4(c) of the Plan and subject to the provisions of Section 422 or 424 of the Code or any successor provision and (y) the number of Shares available for granting Restricted Stock and Restricted Stock Units shall not exceed One Million Six Hundred Fifty Thousand (1,650,000), subject to adjustment as provided in Section 4(c) of the Plan.

(b) Accounting for Awards. For purposes of this Section 4, if an Award entitles the holder thereof to receive or purchase Shares, the number of Shares covered by such Award or to which such Award relates shall be counted on the date of grant of such Award against the aggregate number of Shares available for granting Awards under the Plan. In addition, if any Shares covered by an Award or to which an Award relates are not purchased or are forfeited, or if an Award otherwise terminates without delivery of any Shares, then the number of Shares counted against the aggregate number of Shares available under the Plan with respect to such Award, to the extent of any such forfeiture or termination, shall again be available for granting Awards under the Plan.

(c) Adjustments. In the event any dividend or other distribution (whether in the form of cash, Shares, other securities or other property), recapitalization, stock split, reverse stock split, reorganization, merger, consolidation, split-up, spin-off, combination, repurchase or exchange of Shares or other securities of the Company, issuance of warrants or other rights to purchase Shares or other securities of the Company or other similar corporate transaction or event affects the Shares such that an adjustment is necessary in order to prevent dilution or enlargement of the benefits or potential benefits intended to be made available under the Plan, then the Committee shall, in such manner as it may deem equitable, adjust any or all of (i) the number and type of Shares (or other securities or other property) that thereafter may be made the subject of Awards, (ii) the number and type of Shares (or other securities or other property) subject to outstanding Awards, (iii) the purchase price or exercise price with respect to any Award and (iv) the limitations contained in Section 4(d) of the Plan; *provided, however*, that the number of Shares covered by any Award or to which such Award relates shall always be a whole number.

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(d) Section 162(m) Award Limitations Under the Plan. Notwithstanding any other provision of the Plan other than Section 4(c), if the Committee provides that this Section 4(d) is applicable to a particular Award, no Participant receiving such an Award shall be granted: (i) Options or SARs with respect to more than 500,000 Shares in the aggregate within any fiscal year of the Company; or (ii) Qualified Performance Based Awards which could

result in such Participant receiving more than \$1,500,000 in cash or the equivalent Fair Market Value of Shares determined at the date of grant for each full or partial fiscal year of the Company contained in the performance period of a particular Qualified Performance Based Award; *provided, however*, that, if any other Qualified Performance Based Awards are outstanding for such Participant for a given fiscal year, such dollar limitation shall be reduced for each such given fiscal year by the amount that could be received by the Participant under all such Qualified Performance Based Awards, divided, for each such Qualified Performance Based Award, by the number of full or partial fiscal years of the Company contained in the performance period of each such outstanding Qualified Performance Based Award; *provided, however*, that the limitations set forth in this Section 4(d) shall be subject to adjustment under Section 4(c) of the Plan only to the extent that such adjustment does not affect the status of any Award intended under Section 6(d) to qualify as “performance based compensation” under Section 162(m) of the Code.

Section 5. Eligibility

Any Eligible Person shall be eligible to be designated a Participant. In determining which Eligible Persons shall receive an Award and the terms of any Award, the Committee may take into account the nature of the services rendered by the respective Eligible Persons, their present and potential contributions to the success of the Company or such other factors as the Committee, in its discretion, shall deem relevant. Notwithstanding the foregoing, an Incentive Stock Option may only be granted to full-time or part-time employees (which term as used herein includes, without limitation, officers and directors who are also employees), and an Incentive Stock Option shall not be granted to an employee of an Affiliate unless such Affiliate is also a “subsidiary corporation” of the Company within the meaning of Section 424(f) of the Code or any successor provision.

Section 6. Awards

(a) Options. The Committee is hereby authorized to grant Options to Eligible Persons with the following terms and conditions and with such additional terms and conditions not inconsistent with the provisions of the Plan as the Committee shall determine:

(i) Exercise Price. The purchase price per Share purchasable under an Option shall be determined by the Committee; *provided, however*, that such purchase price shall not be less than 100% of the Fair Market Value of a Share on the date of grant of such Option.

(ii) Option Term. The term of each Option shall be fixed by the Committee at the time of grant, but shall not be longer than 10 years from the date of grant.

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(iii) Time and Method of Exercise. The Committee shall determine the time or times at which an Option may be exercised in whole or in part and the method or methods by which, and the form or forms (including, without limitation, cash, Shares, other securities, other Awards or other property, or any combination thereof, having a Fair Market Value on the exercise date equal to the applicable exercise price) in which, payment of the exercise price with respect thereto may be made or deemed to have been made. The Committee shall have the discretion to grant Options that are exercisable for unvested Shares. Should the Participant’s Service cease while the Shares issued upon the early exercise of the Participant’s Options are still unvested, the Company shall have the right to repurchase any or all of those unvested Shares at a price per share determined by the Committee. 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 Committee and set forth in the Award Agreement. Any repurchases must be made in compliance with the relevant provisions of Delaware law.

(iv) Incentive Stock Options. Notwithstanding anything in the Plan to the contrary, the following additional provisions shall apply to the grant of stock options which are intended to qualify as Incentive Stock Options:

(A) The Committee will not grant Incentive Stock Options in which the aggregate Fair Market Value (determined as of the time the option is granted) of the Shares with respect to which Incentive Stock Options are exercisable for the first time by any Participant during any calendar year (under this Plan and all other plans of the Company and its Affiliates) shall exceed \$100,000.

(B) All Incentive Stock Options must be granted within ten years from the earlier of the date on which this Plan was adopted by the Board or the date this Plan was approved by the stockholders of the Company.

(C) Unless sooner exercised, all Incentive Stock Options shall expire and no longer be exercisable no later than 10 years after the date of grant; *provided, however*, that in the case of a grant of an Incentive Stock Option to a Participant who, at the time such Option is granted, owns (within the meaning of Section 422 of the Code) stock possessing more than 10% of the total combined voting power of all classes of stock of the Company or of its Affiliate, such Incentive Stock Option shall expire and no longer be exercisable no later than 5 years from the date of grant.

(D) The purchase price per Share for an Incentive Stock Option shall be not less than 100% of the Fair Market Value of a Share on the date of grant of the Incentive Stock Option; *provided, however*, that, in the case of the grant of an Incentive Stock Option to a Participant who, at the time such Option is granted, owns (within the meaning of Section 422 of the Code) stock possessing more than 10% of the total combined voting power of all classes of stock of the Company or of its Affiliate, the purchase price per Share purchasable under an Incentive Stock Option shall be not less than 110% of the Fair Market Value of a Share on the date of grant of the Incentive Stock Option.

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(E) Any Incentive Stock Option authorized under the Plan shall contain such other provisions as the Committee shall deem advisable, but shall in all events be consistent with and contain all provisions required in order to qualify the Option as an Incentive Stock Option.

(b) Stock Appreciation Rights. The Committee is hereby authorized to grant Stock Appreciation Rights to Eligible Persons subject to the terms of the Plan and any applicable Award Agreement. Each Stock Appreciation Right granted under the Plan shall confer on the holder upon exercise the right to receive a number of Shares equal to the excess of (a) the Fair Market Value of one Share on the date of exercise (or, if the Committee shall so determine, at any time during a specified period before or after the date of exercise) over (b) the grant price of the Stock Appreciation Right as determined by the Committee, which grant price shall not be less than 100% of the Fair Market Value of one Share on the date of grant of the Stock Appreciation Right. Subject to the terms of the Plan, the grant price, term, methods of exercise, dates of exercise and any other terms and conditions (including conditions or restrictions on the exercise thereof) of any Stock Appreciation Right shall be as determined by the Committee.

(c) Restricted Stock and Restricted Stock Units. The Committee is hereby authorized to grant Restricted Stock and Restricted Stock Units to Eligible Persons with the following terms and conditions and with such additional terms and conditions not inconsistent with the provisions of the Plan as the Committee shall determine:

(i) Restrictions. Shares of Restricted Stock and Restricted Stock Units shall be subject to such restrictions as the Committee may impose (including, without limitation, a restriction on or prohibition against the right to receive any dividend or other right or property with respect thereto), which restrictions may lapse separately or in combination at such time or times, in such installments or otherwise as the Committee may deem appropriate.

(ii) Issuance of Shares. Any Restricted Stock granted under the Plan may be evidenced in such manner as the Board may deem appropriate, including book-entry registration or issuance of a stock certificate or certificates which certificate or certificates shall be held by the Company. Such certificate or certificates shall be registered in the name of the Participant and shall bear an appropriate legend referring to the restrictions applicable to such Restricted Stock.

(iii) Forfeiture. Except as otherwise determined by the Committee, upon a Participant's termination of Service (as determined under criteria established by the Committee) during the applicable restriction period, all Shares of Restricted Stock and Restricted Stock Units at such time subject to restriction shall be forfeited and reacquired by the Company; *provided, however*, that the Committee may, when it finds that a waiver would be in the best interest of the Company, waive in whole or in part any or all remaining restrictions with respect to Shares of Restricted Stock or Restricted Stock Units.

(d) Performance Awards. The Committee is hereby authorized to grant Performance Awards to Eligible Persons subject to the terms of the Plan. A Performance Award granted under the Plan (i) may be denominated or payable in cash, Shares (including, without limitation, Restricted Stock and Restricted Stock Units), other securities, other Awards or other property and (ii) shall confer on the holder thereof the right to receive payments, in whole or in part, upon the achievement of such performance goals during such performance periods as the Committee shall establish. Subject to the terms of the Plan, the performance goals to be achieved during any performance period, the length of any performance period, the amount of any Performance Award granted, the amount of any payment or transfer to be made pursuant to any Performance Award and any other terms and conditions of any Performance Award shall be determined by the Committee. From time to time, the Committee may designate an Award granted pursuant to the Plan as an award of "qualified performance-based compensation" within the meaning of Section 162(m) of the Code (a "*Qualified Performance Based Award*"). Qualified Performance Based Awards shall, to the extent required by Section 162(m), be conditioned solely on the achievement of one or more objective Performance Goals, and such Performance Goals shall be established by the Committee within the time period prescribed by, and shall otherwise comply with the requirements of, Section 162(m). The Committee shall also certify in writing that such Performance Goals have been met prior to payment of the Qualified Performance Based Awards to the extent required by Section 162(m).

(e) Dividend Equivalents. The Committee is hereby authorized to grant Dividend Equivalents to Eligible Persons under which the Participant shall be entitled to receive payments (in cash, Shares, other securities, other Awards or other property as determined in the discretion of the Committee) equivalent to the amount of cash dividends paid by the Company to holders of Shares with respect to a number of Shares determined by the Committee. Subject to the terms of the Plan, such Dividend Equivalents may have such terms and conditions as the Committee shall determine.

(f) Other Stock Grants. The Committee is hereby authorized, subject to the terms of the Plan, to grant to Eligible Persons Shares without restrictions thereon ("*Other Stock Grants*") as are deemed by the Committee to be consistent with the purpose of the Plan. Subject to the terms of the Plan and any applicable Award Agreement, such Other Stock Grant may have such terms and conditions as the Committee shall determine.

(g) Other Stock-Based Awards. The Committee is hereby authorized to grant to Eligible Persons, subject to the terms of the Plan, such other Awards that are denominated or payable in, valued in whole or in part by reference to, or otherwise based on or related to, Shares (including, without limitation, securities convertible into Shares), as are deemed by the Committee to be consistent with the purpose of the Plan. Shares or other securities delivered pursuant to a purchase right granted under this Section 6(g) shall be purchased for such consideration, which may be paid by such method or methods and in such form or forms (including, without limitation, cash, Shares, other securities, other Awards or other property or any combination thereof), as the Committee shall determine, the value of which consideration, as established by the Committee, shall not be less than 100% of the Fair Market Value of such Shares or other securities as of the date such purchase right is granted.

(h) General.

(i) Consideration for Awards. Awards may be granted for no cash consideration or for any cash or other consideration as determined by the Committee and required by applicable law.

(ii) Awards May Be Granted Separately or Together. Awards may, in the discretion of the Committee, be granted either alone or in addition to, in tandem with or in substitution for any other Award or any award granted under any plan of the Company or any Affiliate. Awards granted in addition to or in tandem with other Awards or in addition to or in tandem with awards granted under any such other plan of the Company or any Affiliate may be granted either at the same time as or at a different time from the grant of such other Awards or awards.

(iii) Forms of Payment under Awards. Subject to the terms of the Plan and of any applicable Award Agreement, payments or transfers to be made by the Company or an Affiliate upon the grant, exercise or payment of an Award may be made in such form or forms as the Committee shall determine (including, without limitation, cash, Shares, other securities, other Awards or other property or any combination thereof), and may be made in a single payment or transfer, in installments or on a deferred basis, in each case in accordance with rules and procedures established by the Committee. Such rules and procedures may include, without limitation, provisions for the payment or crediting of reasonable interest on installment or deferred payments or the grant or crediting of Dividend Equivalents with respect to installment or deferred payments.

(iv) Limits on Transfer of Awards. No Award (other than Other Stock Grants) and no right under any such Award shall be transferable by a Participant other than by will or by the laws of descent and distribution and the Company shall not be required to recognize any attempted assignment of such rights by any Participant; *provided, however*, that, if so determined by the Committee, a Participant may, in the manner established by the Committee, designate a beneficiary or beneficiaries to exercise the rights of the Participant and receive any property distributable with respect to any Award upon the death of the Participant; *provided, further*, that, if so determined by the Committee, a Participant may, at any time that such Participant holds such Option, transfer a Non-Qualified Stock Option to any "Family Member" (as such term is defined in the General Instructions to Form S-8, or any successor to such Instructions or such Form), or to an *inter vivos* or testamentary trust in which Family Members have a beneficial interest of more than 50% and which provides that such Option is to be transferred to the beneficiaries upon the Participant's death, *provided* that the Participant may not receive any consideration for such transfer, the Family Member may not make any subsequent transfers other than by will or by the laws of descent and distribution and the Company receives written notice of such transfer, *provided, further*, that, if so determined by the Committee and except in the case of an Incentive Stock Option, Awards may be transferable as determined by the Committee. Except as otherwise determined by the Committee, each Award (other than an Incentive Stock Option) or right under any such Award shall be exercisable during the Participant's lifetime only by the Participant or, if permissible under applicable law, by the Participant's guardian or legal representative.

Except as otherwise determined by the Committee, no Award (other than an Incentive Stock Option) or right under any such Award may be pledged, alienated, attached or otherwise encumbered, and any purported pledge, alienation, attachment or other encumbrance thereof shall be void and unenforceable against the Company or any Affiliate.

(v) Term of Awards. The term of each Award shall be fixed by the Committee at the time of grant, but shall not be longer than 10 years from the date of grant.

(vi) Restrictions; Securities Exchange Listing. All Shares or other securities delivered under the Plan pursuant to any Award or the exercise thereof shall be subject to such stop transfer orders and other restrictions as the Committee may deem advisable under the Plan, applicable federal or state securities laws and regulatory requirements, and the Committee may direct appropriate stop transfer orders and cause other legends to be placed on the certificates for such Shares or other securities to reflect such restrictions. If the Shares or other securities are traded on a securities exchange, the Company shall not be required to deliver any Shares or other securities covered by an Award unless and until such Shares or other securities have been and continue to be admitted for trading on such securities exchange. No Shares or other assets shall be issued or delivered pursuant to the Plan unless and until there shall have been compliance with all applicable requirements of applicable securities laws, including the filing and effectiveness of the Form S-8 registration statement for the Shares issuable pursuant to the Plan, and all applicable listing requirements of any stock exchange or trading system on which Common Stock is then traded. No Shares shall be issued or delivered pursuant to the Plan if doing so would violate any internal policies of the Company.

(vii) Prohibition on Repricing. Except as provided in Section 4(c) of the Plan, no Option or Stock Appreciation Right may be amended to reduce its initial exercise or grant price and no Option or Stock Appreciation Right shall be canceled and replaced with Options or Stock Appreciation Rights having a lower exercise or grant price, without the approval of the stockholders of the Company or unless there would be no material adverse effect on the Company's financial statements as prepared in accordance with generally accepted accounting principles in the United States.

(i) Directors' Automatic Option Grant Program.

(i) Annual Grant. Beginning with the 2011 Annual Stockholders Meeting, each Non-Employee Director shall receive annually on the date of each annual stockholders' meeting a Non-Qualified Stock Option to purchase Ten Thousand (10,000) Shares, provided that such Non-

Employee Director has served as a Non-Employee Director for at least six (6) months and is to continue to serve as a Non-Employee Director, whether or not he or she is standing for reelection at that particular Annual Meeting. The exercise price for the Shares shall be 100% of the Fair Market Value of the Shares on the date of grant. Each Option shall be exercisable immediately upon grant, shall be exercisable for ten (10) years following the date of grant and shall be generally subject to the terms and conditions set forth in the Plan. Each such Option shall initially

be unvested and shall vest in full upon the Non-Employee Director's completion of one (1) year of Board service measured from the grant date. There shall be no limit on the number of such automatic Option grants any one Non-Employee Director may receive over his or her period of Board service, and Non-Employee Directors who have previously been employees of the Company (or any Affiliate) or who have received one or more Option grants from the Company prior to becoming a Non-Employee Director shall be eligible to receive one or more such automatic Option grants over their period of continued Board service.

(ii) Initial Grant. Upon appointment or initial election to the Board, each Non-Employee Director shall receive a Non-Qualified Stock Option to purchase Twenty Thousand (20,000) Shares, provided such individual was not previously in the Company's employ. The exercise price for such Shares shall be 100% of the Fair Market Value of the Shares on the date of grant. Each Option shall be exercisable immediately upon grant, shall be exercisable for 10 years following the date of grant and shall be generally subject to the terms and conditions set forth in the Plan. Each such Option shall initially be unvested and shall vest in full upon the Non-Employee Director's completion of one (1) year of Board service measured from the grant date.

(iii) Termination of Board Service. The following provisions shall govern the exercise of any options granted to Non-Employee Directors pursuant to the Automatic Option Grant Program that are outstanding at the time the Non-Employee Director ceases to serve as a Board member:

(A) Should the Non-Employee Director's service as a Board member cease for any reason while one or more Options granted pursuant to this Automatic Option Grant Program are outstanding, then each such Option shall remain exercisable, for any or all of the vested Shares for which the Option is exercisable at the time of such cessation of Board service, until the earlier of (i) the termination date of the Option or (ii) the expiration of the one-year period measured from the date the Non-Employee Director's Board service ceases. Upon the expiration of the one-year post-termination exercise period, or (if earlier) upon the termination date of the Option, the Option shall terminate with respect to any vested Shares for which the Option has not been exercised.

(B) Should the Non-Employee Director cease to serve as a Board member by reason of death or Permanent Disability, then all shares at the time subject to the Option granted pursuant to this Automatic Option Grant Program 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. "*Permanent Disability*" for purposes of this section shall mean the inability of the Non-Employee Director 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.

(C) Each Option granted pursuant to this Automatic Option Grant Program that is outstanding at the time of the Non-Employee Director's cessation of Board service shall immediately terminate and cease to remain outstanding with respect to any and all unvested Shares for which the Option is not otherwise at that time exercisable.

(iv) Change in Control. In the event of a Change in Control effected during the Non-Employee Director's period of Board service, the vesting, if any, of each Option granted pursuant to this Automatic Option Grant Program at the time held by such Non-Employee Director shall automatically accelerate so that each such Option shall, immediately prior to the specified effective date for the Change in Control, become exercisable for all of the Shares at the time subject to such Option and may be exercised for all or any portion of such Shares. Upon the consummation of the Change in Control, all Options granted pursuant to this Automatic Option Grant Program shall terminate and cease to be outstanding.

(v) Remaining Terms. The remaining terms and conditions of each Option granted pursuant to this Automatic Option Grant Program shall be substantially the same as the terms in effect for Options made under the Plan and shall be set forth in an Option Agreement.

Section 7. Amendment and Termination; Adjustments

(a) Amendments to the Plan. The Board may amend, alter, suspend, discontinue or terminate the Plan at any time; *provided, however*, that, notwithstanding any other provision of the Plan or any Award Agreement, without the approval of the stockholders of the Company, no such amendment, alteration, suspension, discontinuation or termination shall be made that, absent such approval:

(i) violates the rules or regulations of the Financial Industry Regulatory Authority, Inc. or any other regulatory organization or securities exchange that are applicable to the Company;

(ii) causes the Company to be unable, under the Code, to grant Incentive Stock Options under the Plan;

- (iii) increases the number of shares authorized under the Plan as specified in Section 4(a);
- (iv) permits the award of Options or Stock Appreciation Rights at a price less than 100% of the Fair Market Value of a Share on the date of grant of such Option or Stock Appreciation Right, as prohibited by Sections 6(a)(i) and 6(b) of the Plan or the repricing of Options or Stock Appreciation Rights, as prohibited by Section 6(h)(vii) of the Plan; or
- (v) would prevent the grant of Options or Stock Appreciation Rights that would qualify under Section 162(m) of the Code.

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(b) Amendments to Awards. The Committee may waive any conditions of or rights of the Company under any outstanding Award, prospectively or retroactively. Except as otherwise provided herein or in an Award Agreement, the Committee may not amend, alter, suspend, discontinue or terminate any outstanding Award, prospectively or retroactively, if such action would adversely affect the rights of the holder of such Award, without the consent of the Participant or holder or beneficiary thereof. Notwithstanding the foregoing, the Committee shall not waive any conditions or rights of the Company, or otherwise amend or alter any outstanding Qualified Performance Based Awards in such a manner as to cause such Award not to qualify as performance based compensation within the meaning of Section 162(m) of the Code.

(c) Correction of Defects, Omissions and Inconsistencies. The Committee may correct any defect, supply any omission or reconcile any inconsistency in the Plan or in any Award or Award Agreement in the manner and to the extent it shall deem desirable to implement or maintain the effectiveness of the Plan.

Section 8. Income Tax Withholding

In order to comply with all applicable federal, state or local income tax laws or regulations, the Company may take such action as it deems appropriate to ensure that all applicable federal, state or local payroll, withholding, income or other taxes, which are the sole and absolute responsibility of a Participant, are withheld or collected from such Participant. In order to assist a Participant in paying all or a portion of the federal, state and local taxes to be withheld or collected upon exercise or receipt of (or the lapse of restrictions relating to) an Award, the Committee, in its discretion and subject to such additional terms and conditions as it may adopt, may permit the Participant to satisfy such tax obligation by (i) electing to have the Company withhold a portion of the Shares otherwise to be delivered upon exercise or receipt of (or the lapse of restrictions relating to) such Award with a Fair Market Value equal to the amount of such taxes or (ii) delivering to the Company Shares other than Shares issuable upon exercise or receipt of (or the lapse of restrictions relating to) such Award with a Fair Market Value equal to the amount of such taxes. The election, if any, must be made on or before the date that the amount of tax to be withheld is determined.

Section 9. General Provisions

(a) No Rights to Awards. No Eligible Person or other Person shall have any claim to be granted any Award under the Plan, and there is no obligation for uniformity of treatment of Eligible Persons or holders or beneficiaries of Awards under the Plan. The terms and conditions of Awards need not be the same with respect to any Participant or with respect to different Participants.

(b) Award Agreements. No Participant will have rights under an Award granted to such Participant unless and until an Award Agreement shall have been duly executed on behalf of the Company and, if requested by the Company, signed by the Participant.

(c) Plan Provisions Control. In the event that any provision of an Award Agreement conflicts with or is inconsistent in any respect with the terms of the Plan as set forth herein or subsequently amended, the terms of the Plan shall control.

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(d) No Rights of Stockholders. Except with respect to Shares of Restricted Stock as to which the Participant has been granted the right to vote, neither a Participant nor the Participant's legal representative shall be, or have any of the rights and privileges of, a stockholder of the Company with respect to any Shares issuable to such Participant upon the exercise or payment of any Award, in whole or in part, unless and until such Shares have been issued in the name of such Participant or such Participant's legal representative without restrictions thereto.

(e) No Limit on Other Compensation Arrangements. Nothing contained in the Plan shall prevent the Company or any Affiliate from adopting or continuing in effect other or additional compensation arrangements, and such arrangements may be either generally applicable or applicable only in specific cases.

(f) No Right to Employment. The grant of an Award shall not be construed as giving a Participant the right to be retained in the employ, or as giving a director of the Company or an Affiliate the right to continue as a director or an Affiliate of the Company or any Affiliate, nor will it affect in any way the right of the Company or an Affiliate to terminate a Participant's employment or Service at any time, with or without cause. In addition, the Company or an Affiliate may at any time dismiss a Participant from employment, or terminate the term of a director of the Company or an Affiliate, free from any liability or any claim under the Plan or any Award, unless otherwise expressly provided in the Plan or in any Award Agreement. Nothing in this Plan shall confer on any person any legal or equitable right against the Company or any Affiliate, directly or indirectly, or give rise to any cause of action at law or in equity against the Company or an Affiliate. The Awards granted hereunder shall not form any part of the wages or salary of any Eligible Person for purposes of severance pay or termination indemnities, irrespective of the reason for termination of employment. Under no circumstances shall any person ceasing to be an employee of

the Company or any Affiliate be entitled to any compensation for any loss of any right or benefit under the Plan which such employee might otherwise have enjoyed but for termination of employment, whether such compensation is claimed by way of damages for wrongful or unfair dismissal, breach of contract or otherwise. By participating in the Plan, each Participant shall be deemed to have accepted all the conditions of the Plan and the terms and conditions of any rules and regulations adopted by the Committee and shall be fully bound thereby.

(g) Governing Law. The validity, construction and effect of the Plan or any Award, and any rules and regulations relating to the Plan or any Award, shall be determined in accordance with the internal laws, and not the law of conflicts, of the State of Delaware.

(h) Severability. If any provision of the Plan or any Award is or becomes or is deemed to be invalid, illegal or unenforceable in any jurisdiction or would disqualify the Plan or any Award under any law deemed applicable by the Committee, such provision shall be construed or deemed amended to conform to applicable laws, or if it cannot be so construed or deemed amended without, in the determination of the Committee, materially altering the purpose or intent of the Plan or the Award, such provision shall be stricken as to such jurisdiction or Award, and the remainder of the Plan or any such Award shall remain in full force and effect.

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(i) No Trust or Fund Created. Neither the Plan nor any Award shall create or be construed to create a trust or separate fund of any kind or a fiduciary relationship between the Company or any Affiliate and an Eligible Person or any other Person. To the extent that any Person acquires a right to receive payments from the Company or any Affiliate pursuant to an Award, such right shall be no greater than the right of any unsecured general creditor of the Company or any Affiliate.

(j) Other Benefits. No compensation or benefit awarded to or realized by any Participant under the Plan shall be included for the purpose of computing such Participant's compensation under any compensation-based retirement, disability, or similar plan of the Company unless required by law or otherwise provided by such other plan.

(k) No Fractional Shares. No fractional Shares shall be issued or delivered pursuant to the Plan or any Award, and the Committee shall determine whether cash shall be paid in lieu of any fractional Shares or whether such fractional Shares or any rights thereto shall be canceled, terminated or otherwise eliminated.

(l) Headings. Headings are given to the Sections and subsections of the Plan solely as a convenience to facilitate reference. Such headings shall not be deemed in any way material or relevant to the construction or interpretation of the Plan or any provision thereof.

(m) Section 16 Compliance; Section 162(m) Administration. The Plan is intended to comply in all respects with Rule 16b-3 or any successor provision, as in effect from time to time, and in all events the Plan shall be construed in accordance with the requirements of Rule 16b-3. If any Plan provision does not comply with Rule 16b-3 as hereafter amended or interpreted, the provision shall be deemed inoperative. The Board of Directors, in its absolute discretion, may bifurcate the Plan so as to restrict, limit or condition the use of any provision of the Plan with respect to persons who are officers or directors subject to Section 16 of the Exchange Act without so restricting, limiting or conditioning the Plan with respect to other Eligible Persons. With respect to Options and Stock Appreciation Rights, the Company intends to have the Plan administered in accordance with the requirements for the award of "qualified performance-based compensation" within the meaning of Section 162(m) of the Code.

(n) Conditions Precedent to Issuance of Shares. Shares shall not be issued pursuant to the exercise or payment of the purchase price relating to an Award unless such exercise or payment and the issuance and delivery of such Shares pursuant thereto shall comply with all relevant provisions of law, including, without limitation, the Securities Act, the Exchange Act, the rules and regulations promulgated thereunder, the requirements of any applicable Stock Exchange and the Delaware General Corporation Law. As a condition to the exercise or payment of the purchase price relating to such Award, the Company may require that the person exercising or paying the purchase price represent and warrant that the Shares are being purchased only for investment and without any present intention to sell or distribute such Shares if, in the opinion of counsel for the Company, such a representation and warranty is required by law.

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Section 10. Effective Date of the Plan

The Plan became effective on September 21, 2007, the date of approval of the Plan by the Company's stockholders.

Section 11. Term of the Plan

No Award shall be granted under the Plan after (i) July 19, 2017 or (ii) any earlier date of discontinuation or termination established pursuant to Section 7(a) of the Plan. However, unless otherwise expressly provided in the Plan or in an applicable Award Agreement, any Award theretofore granted may extend beyond such date, and the authority of the Committee provided for hereunder with respect to the Plan and any Awards, and the authority of the Board to amend the Plan, shall extend beyond the termination of the Plan.

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ITERIS, INC.
INCENTIVE STOCK OPTION AGREEMENT

This **INCENTIVE STOCK OPTION AGREEMENT** (the “*Agreement*”) is made this _____ day of _____, by and between Iteris, Inc., a Delaware corporation (the “*Company*”), and _____, an individual resident of _____, (“*Optionee*”). Capitalized terms used but not otherwise defined herein shall have the meaning ascribed to such terms in the Iteris, Inc. 2007 Omnibus Incentive Plan (the “*Plan*”).

1. Grant of Option. The Company hereby grants Optionee the option (the “*Option*”) to purchase all or any part of an aggregate of shares (the “*Shares*”) of common stock, \$0.10 par value (“*Common Stock*”), of the Company at the exercise price of \$ _____ per share according to the terms and conditions set forth in this Agreement and in the Plan. The Option will be treated as an incentive stock option within the meaning of Section 422 of the Internal Revenue Code of 1986, as amended (the “*Code*”). The Option is issued under the Plan and is subject to its terms and conditions. A copy of the Plan will be furnished upon request of Optionee.

The Option shall terminate at the close of business ten (10) years from the date hereof; *provided, however*, that if Optionee owns (within the meaning of Section 422 of the Code) as of the date hereof stock possessing more than 10% of the total combined voting power of all classes of stock of the Company or of its Affiliates, the Option shall terminate at the close of business five (5) years from the date hereof.

2. Vesting of Option Rights.

(a) Except as otherwise provided in this Agreement, the Option may be exercised by Optionee in accordance with the following schedule:

On or after each of the following dates	Number of Shares with respect to which the Option is exercisable

(b) During the lifetime of Optionee, the Option shall be exercisable only by Optionee and shall not be assignable or transferable by Optionee, other than by will or the laws of descent and distribution.

(c) Optionee understands that to the extent that the aggregate fair market value (determined at the time the option was granted) of the shares of Common Stock of the Company with respect to which all options that are incentive stock options within the meaning of Section 422 of the Code are exercisable for the first time by Optionee during any calendar year exceed \$100,000, in accordance with Section 422(d) of the Code, such options shall be treated as options that do not qualify as incentive stock options.

3. Exercise of Option after Death or Termination of Employment or Service. The Option shall terminate and may no longer be exercised if Optionee ceases to be employed by or provide Service to the Company or its Affiliates, except that:

(a) If Optionee’s employment shall be terminated for any reason, voluntary or involuntary, other than for “Cause” (as defined in Section 3(e)) or Optionee’s death or disability (within the meaning of Section 22(e)(3) of the Code), Optionee may at any time within a period of 3 months after such termination exercise the Option to the extent the Option was exercisable by Optionee on the date of the termination of Optionee’s employment.

(b) If Optionee’s employment is terminated for Cause, the Option shall be terminated as of the date of the act giving rise to such termination.

(c) If Optionee shall die while the Option is still exercisable according to its terms or if employment is terminated because Optionee has become disabled (within the meaning of Section 22(e)(3) of the Code) while in the employ of the Company and Optionee shall not have fully exercised the Option, such Option may be exercised at any time within 12 months after Optionee’s death or date of termination of employment for disability by Optionee, personal representatives or administrators or guardians of Optionee, as applicable or by any person or persons to whom the Option is transferred by will or the applicable laws of descent and distribution, to the extent of the full number of Shares Optionee was entitled to purchase under the Option on (i) the earlier of the date of death or termination of employment or (ii) the date of termination for such disability, as applicable.

(d) Notwithstanding the above, in no case may the Option be exercised to any extent by anyone after the termination date of the Option.

(e) “Cause” shall mean shall mean the commission of any act of fraud, embezzlement or dishonesty by the Optionee, any unauthorized use or disclosure by such person of confidential information or trade secrets of the Company (or any Affiliate), or any other intentional misconduct by such person adversely affecting the business or affairs of the Company (or any Affiliate) in a material manner. The foregoing definition shall not be deemed to be inclusive of all the acts or omissions which the Company (or any Affiliate) may consider as grounds for the dismissal or discharge of any Optionee in the Service of the Company (or any Affiliate). However, if the term or concept has been defined in an

employment agreement between the Company and Optionee, then Cause shall have the definition set forth in such employment agreement. For purposes of this paragraph, no action or failure to act on Optionee's part shall be considered "willful" unless done or omitted to be done, by Optionee in bad faith and without reasonable belief that his or her action or omission was in the best interests of the Company.

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4. Method of Exercise of Option. Subject to the foregoing, the Option may be exercised in whole or in part from time to time by serving written notice of exercise on the Company at its principal office within the Option period. The notice shall state the number of Shares as to which the Option is being exercised and shall be accompanied by payment of the exercise price. Payment of the exercise price shall be made (i) in cash (including bank check, personal check or money order payable to the Company), (ii) with the approval of the Company (which may be given in its sole discretion), by delivering to the Company for cancellation shares of the Company's Common Stock already owned by Optionee having a Fair Market Value equal to the full exercise price of the Shares being acquired, (iii) with the approval of the Company (which may be given in its sole discretion) and subject to Section 402 of the Sarbanes-Oxley Act of 2002, by delivering to the Company the full exercise price of the Shares being acquired in a combination of cash and Optionee's full recourse liability promissory note with a principal amount not to exceed eighty percent (80%) of the exercise price and a term not to exceed five (5) years, which promissory note shall provide for interest on the unpaid balance thereof which at all times is not less than the minimum rate required to avoid the imputation of income, original issue discount or a below-market rate loan pursuant to Sections 483, 1274 or 7872 of the Code or any successor provisions thereto, (iv) subject to Section 402 of the Sarbanes-Oxley Act of 2002, to the extent this Option is exercised for vested shares, through a special sale and remittance procedure pursuant to which Optionee shall concurrently provide irrevocable instructions (1) to Optionee's brokerage firm to effect the immediate sale of the purchased Shares and remit to the Company, 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 income and employment taxes required to be withheld by the Company by reason of such exercise and (2) to the Company to deliver the certificates for the purchased shares directly to such brokerage firm in order to complete the sale, or (v) with the approval of the Company (which may be given in its sole discretion) and subject to Section 402 of the Sarbanes-Oxley Act of 2002, by delivering to the Company a combination of any of the forms of payment described above. This Option may be exercised only with respect to full shares and no fractional share of stock shall be issued.

5. Change in Control.

(a) Immediately prior to the effective date of a "Change in Control" (as defined in Section 5(e)), this Option shall vest and become exercisable for all of the Shares and may be exercised for any or all of those Shares. However, this Option shall not vest and become exercisable on an accelerated basis if and to the extent: (i) this Option is to be assumed by the successor corporation (or parent thereof) or is otherwise to be continued in full force and effect pursuant to the terms of the Change in Control transaction or (ii) this Option is to be replaced with a cash incentive program of the successor corporation which preserves the spread existing at the time of the Change in Control on the Shares for which this Option is not otherwise at that time exercisable (the excess of the Fair Market Value of those Shares over the aggregate exercise price payable for such Shares) and provides for subsequent payout of that spread no later than the time this Option would have vested and become exercisable for those Shares.

(b) Immediately following the consummation of the Change in Control, this Option shall terminate, except to the extent assumed by the successor corporation (or parent thereof) or otherwise continued in effect pursuant to the terms of the Change in Control transaction.

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(c) If this Option is assumed or otherwise continued in effect in connection with a Change in Control, then this Option shall be appropriately adjusted, upon such Change in Control, to apply to the number and class of securities which would have been issuable to Optionee in consummation of such Change in Control had this Option been exercised immediately prior to such Change in Control, and appropriate adjustments shall also be made to the exercise price, provided the aggregate exercise price shall remain the same. To the extent that the holders of Common Stock receive cash consideration for their Common Stock in consummation of the Change in Control, the successor corporation (or its parent) may, in connection with the assumption of this Option, 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 Change in Control.

(d) This Agreement shall not in any way affect the right of the Company 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.

(e) For purposes of this Agreement, "*Change in Control*" shall mean a change in ownership or control of the Company effected through any of the following transactions: (i) a merger, consolidation or other reorganization unless securities representing more than 50% of the total combined voting power of the voting securities of the successor corporation are immediately thereafter beneficially owned, directly or indirectly and in substantially the same proportion, by the persons who beneficially owned the Company's outstanding voting securities immediately prior to such transaction; (ii) a sale, transfer or other disposition of all or substantially all of the Company's assets; or (iii) the acquisition, directly or indirectly, by any person or related group of persons (other than the Company or a person that directly or indirectly controls, is controlled by, or is under common control with, the Company), of beneficial ownership (within the meaning of Rule 13d-3 of the Exchange Act) of securities possessing more than 50% of the total combined voting power of the Company's outstanding securities pursuant to a tender or exchange offer made directly to the Company's stockholders.

6. Capital Adjustments and Reorganization. Should any change be made to the Common Stock by reason of any stock split, reverse stock split, stock dividend, recapitalization, combination of shares, exchange of shares or other change affecting the outstanding Common Stock as a class without the Company's receipt of consideration, appropriate adjustments shall be made to (a) the number and/or class of securities subject to this Option and (b) the exercise price in order to reflect such change and thereby preclude a dilution or enlargement of benefits hereunder.

7. Miscellaneous.

(a) Entire Agreement; Plan Provisions Control. This Agreement (and any addendum hereto) and the Plan constitute the entire agreement between the parties hereto with regard to the subject matter hereof. In the event that any provision of the Agreement conflicts with or is inconsistent in any respect with the terms of the Plan, the terms of the Plan shall control. All decisions of the Committee with respect to any question or issue arising under the Plan or this Agreement shall be and binding on all persons having an interest in this Option. All capitalized terms used in this Agreement and not otherwise defined in this Agreement shall have the meaning assigned to them in the Plan.

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(b) No Rights of Stockholders. Neither Optionee, Optionee's legal representative nor a permissible assignee of this Option shall have any of the rights and privileges of a stockholder of the Company with respect to the Shares, unless and until such Shares have been issued in the name of Optionee, Optionee's legal representative or permissible assignee, as applicable, without restrictions thereto.

(c) No Right to Employment. The grant of the Option shall not be construed as giving Optionee the right to be retained in the employ of, or if Optionee is a director of the Company or an Affiliate as giving the Optionee the right to continue as a director of, the Company or an Affiliate, nor will it affect in any way the right of the Company or an Affiliate to terminate such employment or position at any time, with or without cause. In addition, the Company or an Affiliate may at any time dismiss Optionee from employment, or terminate the term of a director of the Company or an Affiliate, free from any liability or any claim under the Plan or the Agreement. Nothing in the Agreement shall confer on any person any legal or equitable right against the Company or any Affiliate, directly or indirectly, or give rise to any cause of action at law or in equity against the Company or an Affiliate. The Option granted hereunder shall not form any part of the wages or salary of Optionee for purposes of severance pay or termination indemnities, irrespective of the reason for termination of employment. Under no circumstances shall any person ceasing to be an employee of the Company or any Affiliate be entitled to any compensation for any loss of any right or benefit under the Agreement or Plan which such employee might otherwise have enjoyed but for termination of employment, whether such compensation is claimed by way of damages for wrongful or unfair dismissal, breach of contract or otherwise. By participating in the Plan, Optionee shall be deemed to have accepted all the conditions of the Plan and the Agreement and the terms and conditions of any rules and regulations adopted by the Committee and shall be fully bound thereby.

(d) Governing Law. The validity, construction and effect of the Plan and the Agreement, and any rules and regulations relating to the Plan and the Agreement, shall be determined in accordance with the internal laws, and not the law of conflicts, of the State of Delaware.

(e) Severability. If any provision of the Agreement is or becomes or is deemed to be invalid, illegal or unenforceable in any jurisdiction or would disqualify the Agreement under any law deemed applicable by the Committee, such provision shall be construed or deemed amended to conform to applicable laws, or if it cannot be so construed or deemed amended without, in the determination of the Committee, materially altering the purpose or intent of the Plan or the Agreement, such provision shall be stricken as to such jurisdiction or the Agreement, and the remainder of the Agreement shall remain in full force and effect.

(f) No Trust or Fund Created. Neither the Plan nor the Agreement shall create or be construed to create a trust or separate fund of any kind or a fiduciary relationship between the Company or any Affiliate and Optionee or any other person.

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(g) Headings. Headings are given to the Sections and subsections of the Agreement solely as a convenience to facilitate reference. Such headings shall not be deemed in any way material or relevant to the construction or interpretation of the Agreement or any provision thereof.

(h) Notices. Any notice required to be given or delivered to the Company under the terms of this Agreement shall be addressed to the Company at its principal corporate offices. Any notice required to be given or delivered to Optionee shall be addressed to Optionee at the address of record provided to the Company by Optionee in connection with Optionee's employment with or Services provided to the Company or such other address as Optionee may designate by ten (10) days' advance written notice to the Company. Any notice required to be given under this Agreement shall be in writing and shall be deemed effective upon personal delivery or upon the third (3rd) day following deposit in the U.S. mail, registered or certified, postage prepaid and properly addressed to the party entitled to such notice.

(i) Conditions Precedent to Issuance of Shares. Shares shall not be issued pursuant to the exercise of the Option unless such exercise and the issuance and delivery of the applicable Shares pursuant thereto shall comply with all relevant provisions of law, including, without limitation, the Securities Act of 1933, as amended, the Exchange Act of 1934, as amended, the rules and regulations promulgated thereunder, state blue sky laws, the requirements of any applicable Stock Exchange or the Nasdaq Stock Market and the Delaware General Corporation Law. As a condition to the exercise of the purchase price relating to the Option, the Company may require that the person exercising or paying the purchase price represent and warrant that the Shares are being purchased only for investment and without any present intention to sell or distribute such Shares if, in the opinion of counsel for the Company, such a representation and warranty is required by law.

(j) Withholding. If Optionee shall dispose of any of the shares of Common Stock acquired upon exercise of the Option within two (2) years from the date the Option was granted or within one (1) year after the date of exercise of the Option, then, in order to provide the Company with the opportunity to claim the benefit of any income tax deduction, Optionee shall promptly notify the Company of the dates of acquisition and disposition of such shares, the number of shares so disposed of, and the consideration, if any, received for such shares. In order to comply with all applicable federal or state income tax

laws or regulations, the Company may take such action as it deems appropriate to assure (i) notice to the Company of any disposition of the shares of the Company within the time periods described above, and (ii) that, if necessary, all applicable federal or state payroll, withholding, income or other taxes are withheld or collected from Optionee.

(k) Consultation With Professional Tax and Investment Advisors. Optionee acknowledges that the grant, exercise and vesting with respect to this Option, and the sale or other taxable disposition of the Shares, may have tax consequences pursuant to the Code or under local, state or international tax laws. Optionee further acknowledges that Optionee is relying solely and exclusively on Optionee’s own professional tax and investment advisors with respect to any and all such matters (and is not relying, in any manner, on the Company or any of its employees or representatives). Optionee understands and agrees that any and all tax consequences resulting from the Option and its grant, exercise and vesting, and the sale or other taxable disposition of the Shares, is solely and exclusively the responsibility of Optionee without any expectation or understanding that the Company or any of its employees or representatives will pay or reimburse Optionee for such taxes or other items.

(l) Acceptance of Option. By accepting this Agreement, Optionee hereby agrees to the terms and conditions set forth in this Agreement and the Plan with respect to the Option and any Shares issued as a result of the exercise of the Option, in whole or in part.

IN WITNESS WHEREOF, the Company has executed this Agreement and caused this Option to be issued to Optionee on the date set forth in the first paragraph above.

ITERIS, INC.

By: _____

Name: _____

Title: _____

**ITERIS, INC.
NON-INCENTIVE STOCK OPTION AGREEMENT**

This NON-INCENTIVE STOCK OPTION AGREEMENT (the “*Agreement*”) is made this _____ day of _____, by and between Iteris, Inc., a Delaware corporation (the “*Company*”), and _____, an individual resident of _____, (“*Optionee*”). Capitalized terms used but not otherwise defined herein shall have the meaning ascribed to such terms in the Iteris, Inc. 2007 Omnibus Incentive Plan (the “*Plan*”).

1. Grant of Option. The Company hereby grants Optionee the option (the “*Option*”) to purchase all or any part of an aggregate of _____ shares (the “*Shares*”) of common stock, \$0.10 par value (“*Common Stock*”), of the Company at the exercise price of \$ _____ per share according to the terms and conditions set forth in this Agreement and in the Plan. The Option will **not** be treated as an incentive stock option within the meaning of Section 422 of the Internal Revenue Code of 1986, as amended (the “*Code*”). The Option is issued under the Plan and is subject to its terms and conditions. A copy of the Plan will be furnished upon request of Optionee.

The Option shall terminate at the close of business ten (10) years from the date hereof.

2. Vesting of Option Rights.

(a) Except as otherwise provided in this Agreement, the Option may be exercised by Optionee in accordance with the following schedule:

On or after each of the following dates	Number of Shares with respect to which the Option is exercisable

(b) During the lifetime of Optionee, the Option shall be exercisable only by Optionee and shall not be assignable or transferable by Optionee, other than by will or the laws of descent and distribution. Notwithstanding the foregoing, Optionee may transfer the Option to any Family Member (as such term is defined in the General Instructions to Form S-8 (or successor to such Instructions or such Form)); *provided, however*, that (i) Optionee may not receive any consideration for such transfer, (ii) the Family Member must agree in writing not to make any subsequent transfers of the Option other than by will or the laws of the descent and distribution and (iii) the Company receives prior written notice of such transfer.

3. Exercise of Option after Death or Termination of Employment or Service. The Option shall terminate and may no longer be exercised if

Optionee ceases to be employed by or provide Service to the Company or its Affiliates, except that:

(a) If Optionee's employment shall be terminated for any reason, voluntary or involuntary, other than for "Cause" (as defined in Section 3(e)) or Optionee's death or disability (within the meaning of Section 22(e)(3) of the Code), Optionee may at any time within a period of 3 months after such termination exercise the Option to the extent the Option was exercisable by Optionee on the date of the termination of Optionee's employment.

(b) If Optionee's employment is terminated for Cause, the Option shall be terminated as of the date of the act giving rise to such termination.

(c) If Optionee shall die while the Option is still exercisable according to its terms or if employment is terminated because Optionee has become disabled (within the meaning of Section 22(e)(3) of the Code) while in the employ of the Company and Optionee shall not have fully exercised the Option, such Option may be exercised at any time within 12 months after Optionee's death or date of termination of employment for disability by Optionee, personal representatives or administrators or guardians of Optionee, as applicable or by any person or persons to whom the Option is transferred by will or the applicable laws of descent and distribution, to the extent of the full number of Shares Optionee was entitled to purchase under the Option on (i) the earlier of the date of death or termination of employment or (ii) the date of termination for such disability, as applicable.

(d) Notwithstanding the above, in no case may the Option be exercised to any extent by anyone after the termination date of the Option.

(e) "Cause" shall mean the commission of any act of fraud, embezzlement or dishonesty by the Optionee, any unauthorized use or disclosure by such person of confidential information or trade secrets of the Company (or any Affiliate), or any other intentional misconduct by such person adversely affecting the business or affairs of the Company (or any Affiliate) in a material manner. The foregoing definition shall not be deemed to be inclusive of all the acts or omissions which the Company (or any Affiliate) may consider as grounds for the dismissal or discharge of any Optionee in the Service of the Company (or any Affiliate). However, if the term or concept has been defined in an employment agreement between the Company and Optionee, then Cause shall have the definition set forth in such employment agreement. For purposes of this paragraph, no action or failure to act on Optionee's part shall be considered "willful" unless done or omitted to be done, by Optionee in bad faith and without reasonable belief that his or her action or omission was in the best interests of the Company.

4. Method of Exercise of Option. Subject to the foregoing, the Option may be exercised in whole or in part from time to time by serving written notice of exercise on the Company at its principal office within the Option period. The notice shall state the number of Shares as to which the Option is being exercised and shall be accompanied by payment of the exercise price. Payment of the exercise price shall be made (i) in cash (including bank check, personal check or money order payable to the Company), (ii) with the approval of the Company (which may be given in its sole discretion), by delivering to the Company for cancellation shares of the Company's Common Stock already owned by Optionee having a Fair Market Value equal

to the full exercise price of the Shares being acquired, (iii) with the approval of the Company (which may be given in its sole discretion) and subject to Section 402 of the Sarbanes-Oxley Act of 2002, by delivering to the Company the full exercise price of the Shares being acquired in a combination of cash and Optionee's full recourse liability promissory note with a principal amount not to exceed eighty percent (80%) of the exercise price and a term not to exceed five (5) years, which promissory note shall provide for interest on the unpaid balance thereof which at all times is not less than the minimum rate required to avoid the imputation of income, original issue discount or a below-market rate loan pursuant to Sections 483, 1274 or 7872 of the Code or any successor provisions thereto, (iv) subject to Section 402 of the Sarbanes-Oxley Act of 2002, to the extent this Option is exercised for vested shares, through a special sale and remittance procedure pursuant to which Optionee shall concurrently provide irrevocable instructions (1) to Optionee's brokerage firm to effect the immediate sale of the purchased Shares and remit to the Company, 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 income and employment taxes required to be withheld by the Company by reason of such exercise and (2) to the Company to deliver the certificates for the purchased shares directly to such brokerage firm in order to complete the sale, or (v) with the approval of the Company (which may be given in its sole discretion) and subject to Section 402 of the Sarbanes-Oxley Act of 2002, by delivering to the Company a combination of any of the forms of payment described above. This Option may be exercised only with respect to full shares and no fractional share of stock shall be issued.

5. Change in Control.

(a) Immediately prior to the effective date of a "Change in Control" (as defined in Section 5(e)), this Option shall vest and become exercisable for all of the Shares and may be exercised for any or all of those Shares. However, this Option shall not vest and become exercisable on an accelerated basis if and to the extent: (i) this Option is to be assumed by the successor corporation (or parent thereof) or is otherwise to be continued in full force and effect pursuant to the terms of the Change in Control transaction or (ii) this Option is to be replaced with a cash incentive program of the successor corporation which preserves the spread existing at the time of the Change in Control on the Shares for which this Option is not otherwise at that time exercisable (the excess of the Fair Market Value of those Shares over the aggregate exercise price payable for such Shares) and provides for subsequent payout of that spread no later than the time this Option would have vested and become exercisable for those Shares.

(b) Immediately following the consummation of the Change in Control, this Option shall terminate, except to the extent assumed by

the successor corporation (or parent thereof) or otherwise continued in effect pursuant to the terms of the Change in Control transaction.

(c) If this Option is assumed or otherwise continued in effect in connection with a Change in Control, then this Option shall be appropriately adjusted, upon such Change in Control, to apply to the number and class of securities which would have been issuable to Optionee in consummation of such Change in Control had this Option been exercised immediately prior to such Change in Control, and appropriate adjustments shall also be made to the exercise price, provided the aggregate exercise price shall remain the

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same. To the extent that the holders of Common Stock receive cash consideration for their Common Stock in consummation of the Change in Control, the successor corporation (or its parent) may, in connection with the assumption of this Option, 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 Change in Control.

(d) This Agreement shall not in any way affect the right of the Company 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.

(e) For purposes of this Agreement, "*Change in Control*" shall mean a change in ownership or control of the Company effected through any of the following transactions: (i) a merger, consolidation or other reorganization unless securities representing more than 50% of the total combined voting power of the voting securities of the successor corporation are immediately thereafter beneficially owned, directly or indirectly and in substantially the same proportion, by the persons who beneficially owned the Company's outstanding voting securities immediately prior to such transaction; (ii) a sale, transfer or other disposition of all or substantially all of the Company's assets; or (iii) the acquisition, directly or indirectly, by any person or related group of persons (other than the Company or a person that directly or indirectly controls, is controlled by, or is under common control with, the Company), of beneficial ownership (within the meaning of Rule 13d-3 of the Exchange Act) of securities possessing more than 50% of the total combined voting power of the Company's outstanding securities pursuant to a tender or exchange offer made directly to the Company's stockholders.

6. Capital Adjustments and Reorganization. Should any change be made to the Common Stock by reason of any stock split, reverse stock split, stock dividend, recapitalization, combination of shares, exchange of shares or other change affecting the outstanding Common Stock as a class without the Company's receipt of consideration, appropriate adjustments shall be made to (a) the number and/or class of securities subject to this Option and (b) the exercise price in order to reflect such change and thereby preclude a dilution or enlargement of benefits hereunder.

7. Miscellaneous.

(a) Entire Agreement; Plan Provisions Control. This Agreement (and any addendum hereto) and the Plan constitute the entire agreement between the parties hereto with regard to the subject matter hereof. In the event that any provision of the Agreement conflicts with or is inconsistent in any respect with the terms of the Plan, the terms of the Plan shall control. All decisions of the Committee with respect to any question or issue arising under the Plan or this Agreement shall be and binding on all persons having an interest in this Option. All capitalized terms used in this Agreement and not otherwise defined in this Agreement shall have the meaning assigned to them in the Plan.

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(b) No Rights of Stockholders. Neither Optionee, Optionee's legal representative nor a permissible assignee of this Option shall have any of the rights and privileges of a stockholder of the Company with respect to the Shares, unless and until such Shares have been issued in the name of Optionee, Optionee's legal representative or permissible assignee, as applicable, without restrictions thereto.

(c) No Right to Employment. The grant of the Option shall not be construed as giving Optionee the right to be retained in the employ of, or if Optionee is a director of the Company or an Affiliate as giving the Optionee the right to continue as a director of, the Company or an Affiliate, nor will it affect in any way the right of the Company or an Affiliate to terminate such employment or position at any time, with or without cause. In addition, the Company or an Affiliate may at any time dismiss Optionee from employment, or terminate the term of a director of the Company or an Affiliate, free from any liability or any claim under the Plan or the Agreement. Nothing in the Agreement shall confer on any person any legal or equitable right against the Company or any Affiliate, directly or indirectly, or give rise to any cause of action at law or in equity against the Company or an Affiliate. The Option granted hereunder shall not form any part of the wages or salary of Optionee for purposes of severance pay or termination indemnities, irrespective of the reason for termination of employment. Under no circumstances shall any person ceasing to be an employee of the Company or any Affiliate be entitled to any compensation for any loss of any right or benefit under the Agreement or Plan which such employee might otherwise have enjoyed but for termination of employment, whether such compensation is claimed by way of damages for wrongful or unfair dismissal, breach of contract or otherwise. By participating in the Plan, Optionee shall be deemed to have accepted all the conditions of the Plan and the Agreement and the terms and conditions of any rules and regulations adopted by the Committee and shall be fully bound thereby.

(d) Governing Law. The validity, construction and effect of the Plan and the Agreement, and any rules and regulations relating to the Plan and the Agreement, shall be determined in accordance with the internal laws, and not the law of conflicts, of the State of Delaware.

(e) Severability. If any provision of the Agreement is or becomes or is deemed to be invalid, illegal or unenforceable in any jurisdiction or would disqualify the Agreement under any law deemed applicable by the Committee, such provision shall be construed or deemed amended to conform to applicable laws, or if it cannot be so construed or deemed amended without, in the determination of the Committee, materially altering the purpose or intent of

the Plan or the Agreement, such provision shall be stricken as to such jurisdiction or the Agreement, and the remainder of the Agreement shall remain in full force and effect.

(f) No Trust or Fund Created. Neither the Plan nor the Agreement shall create or be construed to create a trust or separate fund of any kind or a fiduciary relationship between the Company or any Affiliate and Optionee or any other person.

(g) Headings. Headings are given to the Sections and subsections of the Agreement solely as a convenience to facilitate reference. Such headings shall not be deemed in any way material or relevant to the construction or interpretation of the Agreement or any provision thereof.

(h) Notices. Any notice required to be given or delivered to the Company under the terms of this Agreement shall be addressed to the Company at its principal corporate offices. Any notice required to be given or delivered to Optionee shall be addressed to Optionee at the address of record provided to the Company by Optionee in connection with Optionee's employment with or Services provided to the Company or such other address as Optionee may designate by ten (10) days' advance written notice to the Company. Any notice required to be given under this Agreement shall be in writing and shall be deemed effective upon personal delivery or upon the third (3rd) day following deposit in the U.S. mail, registered or certified, postage prepaid and properly addressed to the party entitled to such notice.

(i) Conditions Precedent to Issuance of Shares. Shares shall not be issued pursuant to the exercise of the Option unless such exercise and the issuance and delivery of the applicable Shares pursuant thereto shall comply with all relevant provisions of law, including, without limitation, the Securities Act of 1933, as amended, the Exchange Act of 1934, as amended, the rules and regulations promulgated thereunder, state blue sky laws, the requirements of any applicable Stock Exchange or the Nasdaq Stock Market and the Delaware General Corporation Law. As a condition to the exercise of the purchase price relating to the Option, the Company may require that the person exercising or paying the purchase price represent and warrant that the Shares are being purchased only for investment and without any present intention to sell or distribute such Shares if, in the opinion of counsel for the Company, such a representation and warranty is required by law.

(j) Withholding. In order to provide the Company with the opportunity to claim the benefit of any income tax deduction which may be available to it upon the exercise of the Option and in order to comply with all applicable federal or state income tax laws or regulations, the Company may take such action as it deems appropriate to insure that, if necessary, all applicable federal or state payroll, withholding, income or other taxes are withheld or collected from Optionee.

(k) Consultation With Professional Tax and Investment Advisors. Optionee acknowledges that the grant, exercise and vesting with respect to this Option, and the sale or other taxable disposition of the Shares, may have tax consequences pursuant to the Code or under local, state or international tax laws. Optionee further acknowledges that Optionee is relying solely and exclusively on Optionee's own professional tax and investment advisors with respect to any and all such matters (and is not relying, in any manner, on the Company or any of its employees or representatives). Optionee understands and agrees that any and all tax consequences resulting from the Option and its grant, exercise and vesting, and the sale or other taxable disposition of the Shares, is solely and exclusively the responsibility of Optionee without any expectation or understanding that the Company or any of its employees or representatives will pay or reimburse Optionee for such taxes or other items.

(l) Acceptance of Option. By accepting this Agreement, Optionee hereby agrees to the terms and conditions set forth in this Agreement and the Plan with respect to the Option and any Shares issued as a result of the exercise of the Option, in whole or in part.

IN WITNESS WHEREOF, the Company has executed this Agreement and caused this Option to be issued to Optionee on the date set forth in the first paragraph above.

ITERIS, INC.

By: _____

Name: _____

Title: _____

LIST OF SUBSIDIARIES

<u>Subsidiary</u>	<u>Jurisdiction of Incorporation</u>
Meridian Environmental Technology, Inc.	North Dakota
Berkeley Transportation Systems, Inc.	Delaware

Consent of Independent Registered Public Accounting Firm

We consent to the incorporation by reference in Registration Statements (Nos. 333-121942, 333-136739, and 333-138735) on Form S-3 and (Nos. 333-162807, 333-146459, 333-126834, 333-75728, 333-44907 and 333-30396) on Form S-8 of Iteris, Inc. of our report dated June 11, 2012, relating to our audit of the consolidated financial statements, which appears in this Annual Report on Form 10-K of Iteris, Inc. for the year ended March 31, 2012.

/s/ McGladrey LLP

Irvine, California

June 11, 2012

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

I, Abbas Mohaddes, 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's Board of Directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: June 11, 2012

/s/ ABBAS MOHADDES

Abbas Mohaddes
Chief Executive Officer
(Principal Executive Officer)

**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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's Board of Directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: June 11, 2012

/s/ JAMES S. MIELE

James S. Miele
Chief Financial Officer
(Principal Financial Officer)

**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, 2012, as filed with the Securities and Exchange Commission (the "Report"), I, Abbas Mohaddes, 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.

Date: June 11, 2012

/s/ ABBAS MOHADDES

Abbas Mohaddes
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.

**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, 2012 as filed with the Securities and Exchange Commission (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: June 11, 2012

/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.
