

**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, 2018

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**

**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**  
(Address of Principal Executive Offices)

**92705**  
(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	The NASDAQ Stock Market LLC

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 of 1933, as amended (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, as amended (the "Exchange Act") 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, a smaller reporting company, or an emerging growth company. See definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☐ Accelerated filer ☒ Non accelerated filer ☐  
(Do not check if a smaller reporting company) Smaller reporting company ☐ Emerging growth company ☐

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

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

The aggregate market value of the registrant's common stock held by nonaffiliates of the registrant as of September 30, 2017 was approximately \$147,100,000. 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 May 29, 2018, there were 33,203,740 shares of our common stock outstanding.

#### **DOCUMENTS INCORPORATED BY REFERENCE**

Part III of this report incorporates by reference certain information from the registrant's definitive proxy statement for the 2018 Annual Meeting of Stockholders, which will be filed with the Securities and Exchange Commission.

---

---

**ITERIS, INC.**  
**ANNUAL REPORT ON FORM 10-K**  
**FOR THE FISCAL YEAR ENDED MARCH 31, 2018**  
**TABLE OF CONTENTS**

<b><u>PART I</u></b>		
<u>ITEM 1.</u>	<u>BUSINESS</u>	<u>3</u>
<u>ITEM 1A.</u>	<u>RISK FACTORS</u>	<u>11</u>
<u>ITEM 1B.</u>	<u>UNRESOLVED STAFF COMMENTS</u>	<u>23</u>
<u>ITEM 2.</u>	<u>PROPERTIES</u>	<u>23</u>
<u>ITEM 3.</u>	<u>LEGAL PROCEEDINGS</u>	<u>23</u>
<u>ITEM 4.</u>	<u>MINE SAFETY DISCLOSURES</u>	<u>23</u>
<b><u>PART II</u></b>		
<u>ITEM 5.</u>	<u>MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES</u>	<u>24</u>
<u>ITEM 6.</u>	<u>SELECTED FINANCIAL DATA</u>	<u>26</u>
<u>ITEM 7.</u>	<u>MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u>	<u>27</u>
<u>ITEM 7A.</u>	<u>QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	<u>39</u>
<u>ITEM 8.</u>	<u>FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA</u>	<u>40</u>
<u>ITEM 9.</u>	<u>CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE</u>	<u>77</u>
<u>ITEM 9A.</u>	<u>CONTROLS AND PROCEDURES</u>	<u>77</u>
<u>ITEM 9B.</u>	<u>OTHER INFORMATION</u>	<u>78</u>
<b><u>PART III</u></b>		
<u>ITEM 10.</u>	<u>DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE</u>	<u>78</u>
<u>ITEM 11.</u>	<u>EXECUTIVE COMPENSATION</u>	<u>78</u>
<u>ITEM 12.</u>	<u>SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS</u>	<u>78</u>
<u>ITEM 13.</u>	<u>CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE</u>	<u>78</u>
<u>ITEM 14.</u>	<u>PRINCIPAL ACCOUNTING FEES AND SERVICES</u>	<u>78</u>
<b><u>PART IV</u></b>		
<u>ITEM 15.</u>	<u>EXHIBITS, FINANCIAL STATEMENT SCHEDULES</u>	<u>79</u>

Unless otherwise indicated in this report, the "Company," "we," "us" and "our" refer to Iteris, Inc. and its wholly-owned subsidiary, ClearAg, Inc. CheckPoint™, ClearAg®, ClearPath Weather®, CVIEW-Plus™, Edge®, EdgeConnect™, EMPower®, EvapoSmart™, IMFocus™, inspect™, iPeMS®, Iteris®, Next®, P10™, P100™, PedTrax®, Pegasus™, SmartCycle®, SmartSpan®, TransitHelper®, UCRLink™, Vantage®, VantageLive!™, VantageNext®, VantagePegasus®, VantageRadius™, Vantage Vector®, VantageView™, Velocity®, VersiCam™ and WeatherPlot™ are among, but not all of, the trademarks of Iteris, Inc. Any other trademarks or trade names mentioned herein are the property of their respective owners.

## Cautionary Statement

*This report, including the following discussion and analysis, contains forward-looking statements (within the meaning of the Private Securities Litigation Reform Act of 1995) that are based on our current expectations, estimates and projections about our business and our industry, and reflect management's beliefs and certain assumptions made by us based upon information available to us as of the date of this report. When used in this report and the information incorporated herein by reference, the words "expect(s)," "feel(s)," "believe(s)," "intend(s)," "plan(s)," "should," "will," "may," "anticipate(s)," "estimate(s)," "could," "should," 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 growth, sales, revenue, expenses, profitability, capital needs, backlog, manufacturing capabilities, the market acceptance of our products, competition, the impact of any current or future litigation, the impact of recent accounting pronouncements, the applications for and acceptance of our products and services, and the status of our facilities and product development. These statements are not guarantees of future performance and are subject to certain risks and uncertainties that could cause our 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 encourage you to carefully review and consider the various disclosures made by us which describe certain factors which could affect our business, including in "Risk Factors" set forth in Part I, 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, including to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.*

## PART I

### ITEM 1. BUSINESS

#### Overview

Iteris, Inc. (referred to collectively with its wholly-owned subsidiary, ClearAg, Inc., in this report as "Iteris," the "Company," "we," "our," and "us") is a provider of essential applied informatics that enable smart transportation and digital agriculture. Municipalities, government agencies, crop science companies, farmers and agronomists use our solutions to make roads safer and travel more efficient, as well as farmlands more sustainable, healthy and productive.

As a pioneer in intelligent transportation systems ("ITS") technology for more than two decades, our intellectual property, products, software-as-a-service offerings and weather forecasting systems offer a comprehensive range of ITS solutions to our customers throughout the U.S. and internationally.

In the agribusiness markets, we have combined our intellectual property with enhanced atmospheric, land surface and agronomic modeling techniques to offer smart content solutions that provide analytical support to large enterprises in the agriculture industry, such as seed and crop protection companies, integrated food companies, and agricultural equipment manufacturers and service providers.

We believe our products, solutions and services improve and safely optimize mobility within our communities, while minimizing environmental impact on the roads we travel and the lands we farm.

We continue to make significant investments to leverage our existing technologies and further expand both our advanced detection sensors and performance analytics systems in the transportation infrastructure market, while supporting the entire value chain in the agriculture market with our smart content and digital farming platform.

Iteris was 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 website address is [www.iteris.com](http://www.iteris.com). The inclusion of our website address in this report does not include or incorporate by reference into this report any information on, or accessible through, our website. 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 "Investor Relations" section of our website, free of charge, as soon as reasonably practicable after such material is electronically filed with, or furnished to, the U.S. Securities and Exchange Commission ("SEC").

## Recent Developments

### *ClearAg, Inc.*

In April 2017, Iteris, Inc. formed a wholly-owned subsidiary, ClearAg, Inc., a Delaware corporation, to provide ClearAg solutions in the agribusiness markets.

## Products and Services

We currently operate in three reportable segments: Roadway Sensors, Transportation Systems, and Agriculture and Weather Analytics.

The Roadway Sensors segment provides various advanced detection sensors and systems for traffic intersection management, communication systems and roadway traffic data collection applications. The Transportation Systems segment provides engineering and consulting services, performance measurement, regulatory compliance, and traffic analytics solutions, as well as the development of traveler information systems for the ITS industry. The Agriculture and Weather Analytics segment includes ClearPath Weather, our road maintenance applications, and ClearAg, our digital agriculture platform.

See Note 13 of Notes to Consolidated Financial Statements, included in Part II, Item 8 of this report, for further details on our reportable segments.

### *Roadway Sensors*

Our Roadway Sensors segment product line uses advanced image and signal processing technology and other techniques to capture and analyze sensor data through sophisticated algorithms, enabling vehicle, bicycle and pedestrian detection, as well as the transmission of both video images and data using various communication technologies. Our Roadway Sensors products include, among others, Vantage, VantageLive!, VantageNext, VantageRadius, VantagePegasus, Vantage Vector, Velocity, SmartCycle, SmartCycle Bike Indicator, SmartSpan, VersiCam, PedTrax and P-Series products.

- Our Vantage detection systems detect vehicle presence at intersections, as well as vehicle count, speed and other traffic data used in traffic management systems. Vantage detection systems typically include up to four of our advanced cameras or radar devices. Our Vantage systems give traffic managers the tools to mitigate roadway congestion by visualizing and analyzing traffic patterns allowing them to modify traffic signal timing to improve traffic flow. Our various software components complement our Vantage detection systems by providing integrated platforms to manage and view detection assets remotely over a network connection, as well as mobile application for viewing anywhere.
- Our Vantage Vector video/radar hybrid product is an all-in-one detection sensor with a wide range of capabilities, including stop bar and advanced zone detection, which enable advanced safety and adaptive control applications. Vantage Vector includes all of the benefits of Iteris video detection, including high accuracy, high-availability remote viewing of video images, bicycle and pedestrian detection capability, and dilemma-zone detection.

- VantageLive! is a cloud-based platform that allows users to collect, process and analyze advanced intersection data, as well as to view and understand intersection activity.
- All of our Vantage systems are available with SmartCycle capability, which can effectively differentiate between bicycles and other vehicles with a single video detection camera, enabling more efficient signalized intersections, improved traffic throughput and increased bicyclist safety. Agencies using bicycle timing can now benefit from bicycle-specific virtual detection zones that can be placed anywhere within the approaching traffic lanes, eliminating the need for separate bicycle-only detection systems.
- The SmartCycle Bike Indicator, which leverages the SmartCycle bicycle detection algorithm, is a device that mounts onto traffic signals and illuminates when cyclists waiting at an intersection have been detected, allowing cyclists to avoid interacting with vehicle traffic to push pole-mounted buttons.
- Our Vantage systems are also available with the PedTrax capability, which provides bi-directional counting and speed tracking of pedestrians within the crosswalk to help improve signal timing efficiency, as well as providing an additional data stream to existing vehicle and bicycle counts.
- 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.

We believe that future growth domestically and internationally, 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 also sell certain complementary original equipment manufacturer ("OEM") products for the traffic intersection market, which include, among other things, traffic signal controllers and traffic signal equipment cabinets.

#### *Transportation Systems*

Our Transportation Systems segment includes engineering and consulting services focused on the planning, design, development and implementation of software and hardware-based ITS 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, implementation, operation and management of surface transportation infrastructure systems. We perform analysis and study goods movement, commercial vehicle operations, provide travel demand forecasting and systems engineering, and identify mitigation measures to reduce traffic congestion.

The Transportations Systems segment also includes our performance measurement and management solution, iPeMS—a state-of-the-art information management software suite that provides prescriptive data insights to help determine current and future traffic patterns, permitting the effective performance analysis and management of traffic infrastructure resources. iPeMS utilizes a wide range of data resources and analytical techniques to determine current and future traffic patterns, permitting the effective performance analysis and management of traffic infrastructure resources. This information can then be analyzed by traffic professionals to measure how a transportation network is performing and to identify potential areas of improvement. iPeMS is also capable of providing users with predictive traffic analytics, and easy-to-use visualization and animation features based on historical traffic conditions.

This segment also includes our commercial vehicle operations and vehicle safety compliance platforms, known as "CVIEW-Plus," "CheckPoint," "UCRLink" and "inspect."

Our Transportation Systems segment is largely dependent upon state and local governmental funding, and to a lesser extent federal governmental funding. As such, our Transportation Systems business has been adversely affected by governmental budgetary issues. In addition, various other funding mechanisms exist to support transportation infrastructure and related projects, including, but not limited to, bonds, dedicated sales and gas tax measures, and other alternative funding sources. We believe the overall expansion of our Transportation Systems segment in the future will continue to be dependent at least in part on the federal and local government's use of funds. Delays in the allocation of funds may prolong uncertainty regarding the allotment of transportation funds in federal, state and local budgets.

#### *Agriculture and Weather Analytics*

Our Agriculture and Weather Analytics segment, which we formed during the first quarter of our fiscal year ended March 31, 2013, consists of our ClearPath Weather and Clear Ag solutions.

Our ClearPath Weather is a web-based system that has a suite of tools that enable users to assess historical weather conditions and analyze short-term and long-range weather forecasts, to customize route/site weather and pavement forecast tools, which provide winter road maintenance recommendations for state agencies, municipalities and enable commercial companies to create solutions for the management of roadway maintenance.

Our Weather Analytics business is a market leader in performance management solutions for federal and state organizations. We intend to use our strong brand and deep experience in the traffic management market, as well as our market-specific intellectual property, to expand our leadership in data aggregation and analytics in this market.

Beginning in late 2013, we undertook the development of "ClearAg solutions" for the digital agricultural market. These new products utilize and expand the intellectual property, technology base and product suites of our ClearPath Weather solutions. For our ClearAg solutions, we developed additional scientific and agronomic models and forecasts, expanded our computing infrastructure for additional big data acquisition and processing, and designed distributed delivery vehicles and products.

Our ClearAg solutions combine weather and agronomic data with proprietary land-surface modeling and analytics to solve complex agricultural problems, which results in the increased efficiency and sustainability of farmlands. The ClearAg Platform delivers product validation, irrigation and harvest solutions giving growers, researchers and other agribusinesses access to a comprehensive database of historical, real-time and forecasted weather, soil and plant health information, as well as other information on crop growth. Companies use the ClearAg Platform to simulate field conditions and determine how new products may perform on a crop given certain weather and soil conditions. Growers leverage the ClearAg Platform to determine the best times to plant, spray, fertilize, irrigate, and harvest crops.

We currently offer our ClearAg solutions on an enterprise basis combining our modeling solutions with ClearAg application programming interfaces ("APIs"). These APIs facilitate the integration of ClearAg's analytics and insights with the offerings of large enterprise customers in the agriculture market. We commenced commercial sales of the ClearAg solutions and related APIs in the first quarter of our fiscal year ended March 31, 2015 ("Fiscal 2015"). We also developed the ClearAg WeatherPlot and ClearAg Insights applications, which provide analytics on forecasted historical weather, water and soil temperatures to help agronomists and crop consultants identify and make recommendations for treatments at ideal environmental conditions to maximize crop quality and yield.

We expect market acceptance of our ClearAg solutions to continue to increase in upcoming quarters. We plan to continue to fund the investments in our ClearAg solutions, through cash flow generated from our Roadway Sensors and Transportation Systems operations, revenues from our

Agriculture and Weather Analytics segment, and our available cash on hand, as needed. We may also elect to raise additional equity for these investments.

## **Sales and Marketing**

We currently sell our Roadway Sensors products through both direct and indirect sales channels. In the territories where we sell direct, we use a combination of our own sales personnel and outside sales organizations to sell, oversee installations and set-up issues, and support our products. Our indirect sales channel is comprised of a network of independent distributors in the U.S. and select international locations, which sell integrated systems and related products to the traffic management market. In the fourth quarter of our fiscal year ended March 31, 2018 ("Fiscal 2018"), we entered into a distribution agreement to expand our northern European sales coverage in the U.K. and Ireland. Our independent distributors are trained in, and primarily responsible for, sales, installation, set-up and support of our products, maintain an inventory of demonstration traffic products from various manufacturers, and sell directly to government agencies and installation contractors. These distributors 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 various high-quality ITS products to the traffic management market. We periodically hold technical training classes for our distributors 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 distributor network to accommodate the needs of the market and our customer base.

We market and sell our Transportation Systems services and solutions, and our ClearPath Weather services primarily to government agencies pursuant to negotiated contracts that involve competitive bidding and specific qualification requirements. Most of our contracts are with federal, state and local 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 Transportation Systems contracts generally involve long lead times and require extensive specification development, evaluation and price negotiations.

We currently market and sell our ClearAg solutions as a subscription-based service to seed and crop protection companies, allied providers and agriculture integrators, as well as to growers and retailers. Due to the recent consolidation of certain large companies in the agriculture market, sales to such companies typically involve long lead times. We generally sell directly to customers interested in the ClearAg API products, but typically sell through selling partners for our ClearAg applications. Mobile versions of WeatherPlot are currently available in the Apple app store and on Google Play.

We have historically had a diverse customer base. For Fiscal 2018, one individual customer represented greater than 10% of our total revenues. For the fiscal year ended March 31, 2017 ("Fiscal 2017"), one individual customer represented greater than 10% of our total revenues.

## **Manufacturing and Materials**

We use contract manufacturers to build subassemblies that are used in our Roadway Sensors products. Additionally, we procure certain components for our Roadway Sensors products from qualified suppliers, both in the U.S. and internationally, and generally use multi-sourcing strategies when technically and economically feasible to mitigate supply risk. These subassemblies and components are typically 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 Veris Manufacturing, MoboTrex, Inc. and Sony Electronics, Inc. Our manufacturing activities are conducted in approximately 9,000 square feet of space at our Santa Ana, California 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 revenues for Fiscal 2018, Fiscal 2017 and the fiscal year ended March 31, 2016 ("Fiscal 2016"). We believe customer support is a key competitive factor for our company.

Our ClearAg solutions are primarily sold as annual subscription services with recurring monthly revenue. As an element of these services, we provide full-time support and customer service for such ClearAg solutions.

## **Backlog**

Our total backlog of unfulfilled firm orders was approximately \$47.5 million as of March 31, 2018, which included \$37.7 million related to Transportation Systems. We typically recognize approximately 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 for both Transportation Systems and Agriculture and Weather Analytics. Substantially the entire backlog for Roadway Sensors as of March 31, 2018 is expected to be recognized as revenue in the fiscal year ending March 31, 2019. At March 31, 2017, we had backlog of approximately \$64.5 million, which included \$54.4 million related to Transportation Systems. The decline in backlog in the current fiscal year was largely due to the completion of a large Transportation Systems contract in the current fiscal year.

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. In addition, pursuant to the customary terms of our agreements with government contractors and other customers, our 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**

Our product development activities are mostly conducted at our Agriculture and Weather Analytics facilities in Grand Forks, North Dakota and Oakland, California, as well as at our principal facility in Santa Ana, California. Our research and development costs and expenses were approximately \$7.9 million for Fiscal 2018 and \$6.9 million for both Fiscal 2017 and Fiscal 2016. We expect to continue to pursue various product development programs and incur research and development expenditures, primarily in our Agriculture and Weather Analytics and Roadway Sensors segments, in future periods.

We believe our engineering and product development capabilities are a competitive strength. We strive to continuously develop new products, technologies, features and functionalities to meet the needs of our ever-changing markets, as well as to enhance, improve upon, and refine our existing product lines. We plan to focus our development efforts in the near future in our Agriculture and Weather Analytics segment on our ClearAg solutions and to developing further enhancements and functionality in our Vantage products family. We believe that developing new and enhanced product

offerings across our segments and enhancing, refining and marketing our existing products are key components for 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.

The markets in which our Agriculture and Weather Analytics segment operates vary from the commercial sector customers for ClearAg solutions to public sector customers for ClearPath Weather solutions. Our competitors vary in number, scope and breadth of the products and services they offer. In the public sector, we compete with some of the same transportation engineering, planning and design firms that also compete with our Transportation Systems segment. In the commercial sector, we compete with a variety of entities that currently provide weather-related data to that market, such as IBM/The Weather Company, MeteoGroup and agronomic analytics companies such as FBN and Farmer's Edge.

In the market for our Roadway Sensors detection products, we compete with manufacturers and distributors of other above-ground video camera detection systems such as Econolite, and manufacturers and distributors of other non-intrusive detection devices, including microwave, infrared, radar, ultrasonic and magnetic detectors, as well as manufacturers and installers of in-pavement inductive loop products, which have historically been, and currently continue to be, the predominant vehicle detection system in this market. Additionally, products such as Velocity and VantagePegasus compete against various competitors in the travel-time and data communications markets, respectively.

The markets in which our Transportation Systems segment operate are 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 large, national corporations that generally offer expertise in traveler information, integration and transportation management. Our competitors in transportation engineering, planning and design include major regional ITS engineering 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.

## **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 have a total of

40 issued U.S. patents, including: (i) 10 relating to our Roadway Sensors technologies, one of which was issued in Fiscal 2018, (ii) 23 relating to our Agriculture and Weather Analytics technologies, six of which were issued in Fiscal 2018, and (iii) seven relating specifically to our Transportation Systems technologies, one of which was issued in Fiscal 2018. We have a total of 22 pending patent applications in the U.S. and 15 pending foreign patent applications. The expiration dates of our patents range from 2026 to 2037. We intend to pursue additional patent protection to the extent we believe it would be beneficial and cost-effective.

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, rapidly evolving technology makes our future success dependent largely upon our ability to successfully achieve 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**

As of March 31, 2018, we employed 414 full-time employees and 33 part-time employees, for a total of 447 employees. None of our employees are represented by a labor union, and we have never experienced a work stoppage. We believe our relations with our employees 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; however, as we expand internationally, foreign laws and regulations could have a material impact on our business in the 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.*

***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 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 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, delays in the expenditures from the federal highway bill and delays or reductions in other state and local funding dedicated for transportation and ITS projects;
- other government budgetary constraints, cut-backs, delays or reallocation of government funding, including without limitation, changes in the new administration;
- performance bond requirements;
- long purchase cycles or approval processes;
- competitive bidding and qualification requirements, as well as our ability to replace large contracts once they have been completed;
- changes in government policies and political agendas;
- maintenance of relationships with key government entities from whom a substantial portion of our revenue is derived;
- milestone requirements and liquidated damage and/or contract termination provisions for failure to meet contract milestones;
- adverse weather conditions may cause delays, such as, evacuations and flooding due to hurricanes can result in our inability to perform work in affected areas; 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, and the ongoing uncertainty as to the timing and accessibility to government funding could cause our 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 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.

***We recently expanded our Agriculture and Weather Analytics capabilities to address a new market segment, the agricultural market, which may not broadly accept our technologies and new products.*** The application of digital analytics to the agricultural market is a relatively new development that has required us to invest, and is expected to continue to require us to invest, in additional research and development, and sales and marketing without any guarantee of a commensurate increase in revenues. The introduction of any new Agriculture and Weather Analytics products and services could have longer than expected sales cycles, which could adversely impact our operating results. We cannot assure you that growers or other companies in this market will perceive the value proposition of our Agriculture and Weather Analytics or that our new ClearAg products for this market will achieve broad market acceptance in the near future or at all. If the agricultural market fails to understand and appreciate the benefit of our Agriculture and Weather Analytics products or chooses not to adopt our technologies, our business, financial condition and results of operations will be adversely affected.

***We may not be able to achieve profitability on a quarterly or annual basis in the future.*** For Fiscal 2018 and Fiscal 2017, we had net losses of \$3.5 million and \$4.8 million, respectively, and we cannot assure you that we will be profitable in the future. Our ability to become profitable in future periods could be impacted by governmental budgetary constraints, government and political agendas, economic instability and other items that are not in our control. Furthermore, we rely on operating profits from certain of our business segments to fund investments in sales and marketing and research and development initiatives. We cannot assure you that our financial performance will sustain a sufficient level to completely support those investments. 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 or increases in planned investments. As a result, we may continue to 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.

***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;
- the timing of new contract awards or the completion of large contract;
- availability of funding or other budget issues;

- 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.

An inability to properly and fully utilize our Transportation Systems workforce could have an adverse effect on our results of operations.

***We recently entered into the software development market and may be subject to additional challenges and additional costs and delays.*** We have only been in the business of software development for a few years and may experience development and technical challenges. Our business and results of operations could also be seriously harmed by any significant delays in our software development and updates. Despite testing and quality control, we cannot be certain that errors will not be found in our software after its release. 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 or our reputation, any of which could adversely affect our business and competitive position. In addition, the software development industry frequently experiences litigation concerning intellectual property disputes, which could be costly and distract our management.

***If we do not keep pace with rapid technological changes and evolving industry standards, we will not be able to remain competitive, and the demand for our products will likely decline.*** 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.

***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. During the past two fiscal years, we have introduced both new and enhanced products across all segments. 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 develop new or enhanced products and software to remain competitive. We need to continue to develop and introduce new products that incorporate the latest technological advancements in outdoor image processing hardware, camera technologies, software and analysis 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.

***If our security measures are breached and unauthorized access is obtained to our customer's personal and/or proprietary data in connection with our web-based and mobile application services, we may incur significant liabilities, our services may be perceived as not being secure and customers may curtail or stop using our services, we could incur significant liability to our customers and to individuals or businesses whose information was being stored, our business may suffer and our reputation will be damaged.*** Because techniques used to obtain unauthorized access to, or to sabotage, systems change frequently and generally are not recognized until launched against a target, we may be unable to anticipate these techniques or to implement adequate preventive measures. If an actual or perceived breach of our security occurs, the market perception of the effectiveness of our security measures could be harmed and we could lose sales and customers.

***The markets in which we operate are highly competitive and have many more established competitors than us, which could adversely affect our revenues or the market acceptance of our products.*** We compete with numerous other companies in our target markets including, but not limited to, large, multi-national corporations and many smaller regional engineering firms.

We compete with existing, well-established companies and technologies in our Roadway Sensors segment, both domestically and abroad. Only a portion of the traffic intersection market has adopted advanced above-ground detection technologies, and our future success will depend in part upon gaining broader market acceptance for such technologies. 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.

The markets in which our Agriculture and Weather Analytics segment operates vary from public sector customers who focus on snow and ice management for state and county roadways, to commercial sector customers who employ our environmental content and agronomic models. Our competitors include divisions of large, international weather companies, as well as a variety of small providers in the road weather market. In the commercial agriculture sector, we compete with a variety of public and private entities that currently market software, agronomic analytics and weather forecast capabilities to the agribusiness.

In each of our operating 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 our competitors 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 and services 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 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 may 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. We have in the past, and may in the future, be subject to litigation regarding our intellectual property rights. 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. Our recent expansion into software development activities may subject us to increased possibility of litigation. Any of the foregoing 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.

***Our failure to successfully secure new contracts and renew existing contracts could reduce our revenues and profitability.*** 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 continue to be subject to traffic related litigation.*** The traffic industry in general is subject to litigation claims due to the nature of personal injuries that result from traffic accidents. As a provider of traffic engineering services, products and solutions, we are, and could from time to time in the future continue to be, subject to litigation for traffic related accidents, even if our products or services did not cause the particular accident. While we generally carry insurance against these types of claims, some claims may not be covered by insurance or the damages resulting from such litigation could exceed our insurance coverage limits. In the event that we are required to pay significant damages as a result of one or more lawsuits that are not covered by insurance or exceed our coverage limits, it could materially harm our business, financial condition or cash flows. Even defending against unsuccessful claims could cause us to incur significant expenses and result in a diversion of management's attention.

***We may be unable to attract and retain key personnel, including senior management, 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. We believe that our success will depend on the continued employment of a highly qualified and experienced senior management team and our ability to retain existing business and generate new business. 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 (e.g., loss of customers or loss of new business opportunities). 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. Particularly in highly specialized areas, it has become more difficult to retain employees and meet all of our needs for employees in a timely manner, which may adversely affect our growth in the current fiscal year and in future years. Although we intend to continue to devote significant resources to recruit, train and retain qualified skilled personnel, we may not be able to attract and retain these employees and therefore could impair our ability to perform our contractual obligations efficiently and timely meet our customers' needs and win new business, which could adversely affect our future results. The future success of our Transportation Systems segment will depend on our ability to hire additional qualified engineers, planners and technical personnel. The future success of our Agriculture and Weather Analytics segment will depend on our ability to hire additional software developers, qualified engineers and technical personnel. Competition for qualified employees, particularly development engineers and software developers, 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 management information systems and databases could be disrupted by system security failures, cyber threats or by the failure of, or lack of access to, our Enterprise Resource Planning system. These disruptions could negatively impact our sales, increase our expenses and/or harm our reputation.*** Internal users and computer programmers may be able to penetrate, aka "hack", our network security and create system disruptions, cause shutdowns and/or misappropriate our confidential information or that of our employees and third parties. Therefore, we could incur significant expenses addressing problems created by security breaches to our network. We must, and do, take precautions to secure customer information and prevent unauthorized access to our databases and systems containing confidential information. Any data loss or information security lapses resulting in the compromise of personal information or the improper use or disclosure of confidential, sensitive or classified information could result in claims, remediation costs, regulatory sanctions against us, loss of current and future contracts and serious harm to our reputation. We operate our Enterprise Resource Planning system on a software-as-a-service platform, and we use this system for reporting, planning, sales, audit, customer relationship management, inventory control, loss prevention, purchase order management and business intelligence. Accordingly, we depend on this system, and the third-party provide of this service, for a number of aspects of our operations. If this service provider or this system fails, or if we are unable to continue to have access to this system on commercially reasonable terms, or at all, operations would be severely disrupted until an equivalent system could be identified, licensed or developed, and integrated into our operations. This disruption would have a material adverse effect on our business.

***If we experience declining or flat revenues and we fail to manage such declines 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.

***Our use of estimates in conjunction with the percentage of completion method of accounting for our Transportation Systems revenues could result in a reduction or reversal of previously recorded revenues and profits.*** A portion of Transportation Systems 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 proportionally 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.

***Uncertainties in the interpretation and application of the new revenue recognition standard ASC 606 could materially affect our revenue recognition.*** As discussed in Note 1 to the Consolidated Financial Statements (Description of Business and Summary of Significant Accounting Policies—Recent Accounting Pronouncements), effective March 1, 2018, we adopted the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-09, Revenue from Contracts with Customers ("ASC 606"). We believe that ASC 606 and related revenue recognition policies will not result in a material change to our consolidated financial statements, and will not cause any significant changes to the amount and timing of our recognition of future revenue and cost. However, uncertainties in future guidance of the interpretation and application of ASC 606 could materially affect our revenue and cost recognition.

***Uncertainties in the interpretation and application of the 2017 Tax Cuts and Jobs Act could materially affect our tax obligations and effective tax rate.*** The 2017 Tax Cuts and Jobs Act (the "Tax Act") was enacted on December 22, 2017, and significantly affected U.S. tax law by changing how the U.S. imposes income tax on multinational corporations. The U.S. Department of Treasury has broad authority to issue regulations and interpretative guidance that may significantly impact how we will apply the law and impact our results of operations in the period issued. The Tax Act requires complex computations not previously provided in U.S. tax law. As such, the application of accounting guidance for such items is currently uncertain. Further, compliance with the Tax Act and the accounting for such provisions require accumulation of information not previously required or regularly produced. As a result, we have provided a provision on the effect of the Tax Act in our financial statements. As additional regulatory guidance is issued by the applicable taxing authorities, and the accounting treatment is clarified, we plan to perform additional analysis on the application of the law, and may need to refine our estimates in calculating the impact of such further guidance. As such, our final analysis may be different from our current provisional amounts, which could materially affect our tax obligations and effective tax rate.

***Declines in the value of securities held in our investment portfolio can affect us negatively.*** As of March 31, 2018, the value of securities available for sale and held to maturity within our investment portfolio was \$9.0 million, which is generally determined based upon market values available from third-party sources, may fluctuate as a result of market volatility and economic or financial market conditions. Declines in the value of securities held in our investment portfolio negatively impact our levels of capital and liquidity. Further, to the extent that we experience unrealized losses in our portfolio of investment securities from declines in securities values that management determines to be other than temporary, the book value of those securities will be adjusted to their estimated recovery value and we will recognize a charge to earnings in the quarter during which we make that determination. Although we have policies and procedures in place to assess and mitigate potential impacts of market risks, including hedging-related strategies, those policies and procedures are inherently limited because they cannot anticipate the existence or future development of currently

unanticipated or unknown risks. Accordingly, we could suffer adverse effects as a result of our failure to anticipate and manage these risks properly.

***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. We are required to obtain our auditors' attestation pursuant to Section 404(b) of the Sarbanes-Oxley Act. Going forward, 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.

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. If we are not able to maintain effective internal controls over financial reporting, we may lose the confidence of investors and analysts and our stock price could decline.

***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 the federal highway bill or other government 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 ClearPath Weather 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;
- decrease in revenues derived from key or significant customers;
- deferrals of customer orders in anticipation of new products, applications or product enhancements;
- risks and uncertainties associated with our international business;
- market condition changes such as industry structure consolidations that could slow down our ability to procure new business;
- general economic and political conditions;
- international conflicts and acts of terrorism; and
- other factors beyond our control, including but not limited to, natural disasters.

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 rely on outside suppliers that could experience supply shortages or may experience production gaps that could materially and adversely impact our sales and financial results.*** 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, and have had to reengineer products from time to time to address obsolete components, especially in our Roadway Sensors products. Should any such delay or disruption occur, or should a key supplier discontinue operations, 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.

***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 two acquisitions since November 2011 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;
- 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.

***Our international business operations may be threatened by many factors that are outside of our control.*** While we historically have had limited international sales, revenues and operational experience, we previously had Transportation Systems contracts in the United Arab Emirates ("UAE"), for which approximately \$130,000 in performance bonds have not yet been released by the UAE Department of Transportation. We also have been expanding our distribution capabilities for our Roadway Sensors segment internationally, particularly in Canada, Australia, New Zealand, Europe and in South America. We plan to continue to expand our international efforts, but we cannot assure you that we will be successful in such efforts. International operations subject us to various inherent risks including, among others:

- political, social and economic instability, as well as international conflicts and acts of terrorism;
- bonding requirements for certain international projects;
- longer accounts receivable payment cycles;
- import and export license requirements and restrictions of the U.S. and each other country in which we operate;
- currency fluctuations and restrictions, and our ability to repatriate currency from certain foreign regions;

- unexpected changes in regulatory requirements, tariffs and other trade barriers or restrictions;
- required compliance with existing and new foreign regulatory requirements and laws, more restrictive labor laws and obligations, including but not limited to the U.S. Foreign Corrupt Practices Act;
- 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 product 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.

Any of the factors mentioned above may adversely affect our future international 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 certain other parts of the world.

***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. On September 1, 2017, we filed a registration statement on a Form S-3, utilizing a "shelf" registration process, and may consider a new equity financing in the future. Should the credit markets further tighten or our business declines, we may need or choose to raise additional capital to fund our operations, 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 economic slowdowns 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.

***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. From August 1, 2015 through May 31, 2018, our common stock has traded at prices as low as \$1.77 per share and as high as \$8.17 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 stock market analyst recommendations regarding our common stock, other comparable companies or our industry in general;
- changes in earnings estimates or investment recommendations by securities analysts; and
- international conflicts, political unrest and acts of terrorism.

The stock market has from time to time experienced volatility, which has often affected and may continue to affect 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 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 other acquisition of the company more difficult.

#### **ITEM 1B. UNRESOLVED STAFF COMMENTS**

None.

#### **ITEM 2. PROPERTIES**

Our headquarters and principal operations are housed in approximately 41,000 square feet of leased office, manufacturing and warehouse space located in Santa Ana, California, pursuant to a lease which terminates in March 2022. For additional information regarding our lease obligations, see Note 8 of Notes to Consolidated Financial Statements, included in Part II, Item 8 of this report.

#### **ITEM 3. LEGAL PROCEEDINGS**

The information set forth under the heading "Litigation and Other Contingencies" under Note 8 of Notes to Consolidated Financial Statements, included in Part II, Item 8 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 NASDAQ Capital Market under the symbol "ITI" since February 8, 2016. Prior to that, our common stock traded on the NYSE MKT under the same symbol. The following table sets forth, for the periods indicated, the highest and lowest sales prices for our common stock:

	<u>High</u>	<u>Low</u>
<b>Fiscal 2018</b>		
Quarter Ended June 30, 2017	\$ 6.50	\$ 4.88
Quarter Ended September 30, 2017	6.91	5.68
Quarter Ended December 31, 2017	8.17	5.30
Quarter Ended March 31, 2018	7.88	4.43
<b>Fiscal 2017</b>		
Quarter Ended June 30, 2016	\$ 2.99	\$ 2.20
Quarter Ended September 30, 2016	4.04	2.81
Quarter Ended December 31, 2016	3.79	3.20
Quarter Ended March 31, 2017	5.64	3.52

On May 29, 2018, the last reported sales price of our common stock on the NASDAQ Capital Market was \$5.16. As of May 29, 2018, we had 331 holders of record of our common stock according to information furnished by our transfer agent. The actual number of stockholders is greater than this number of record holders, and includes stockholders who are beneficial owners but whose shares are held in street name by brokers and other nominees.

**Securities Authorized for Issuance under Equity Compensation Plans**

Information regarding securities authorized for issuance can be found under Part III, "Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters."

**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**

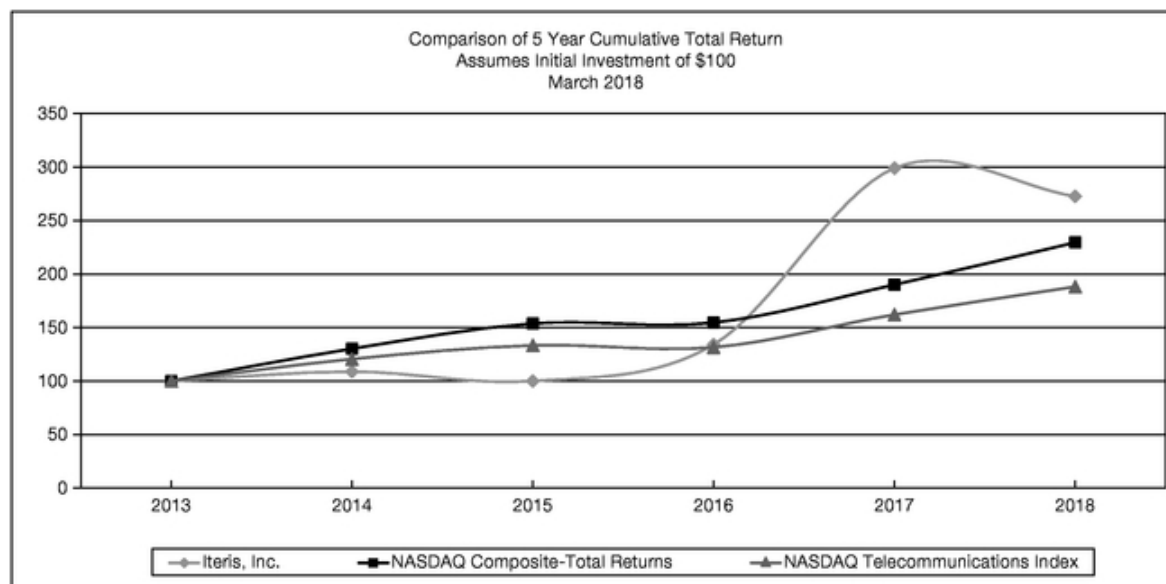
In August 2011, our Board of Directors approved a stock repurchase program pursuant to which we were authorized to acquire up to \$3.0 million of our outstanding common stock from time to time through August 2012. We repurchased approximately 964,000 shares under this original program for a total purchase price of \$1.3 million. On August 9, 2012, our Board of Directors cancelled the initial stock repurchase program and the approximate \$1.7 million of remaining funds, and approved a new stock repurchase program pursuant to which we may acquire up to \$3 million of our outstanding common stock for an unspecified length of time. Under the new program, we may repurchase shares

from time to time in open market and privately negotiated transactions and block trades, and may also repurchase shares 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 or terminate the repurchase program at any time without prior notice. On November 6, 2014, our Board of Directors approved a \$3.0 million increase to the Company's existing stock repurchase program, pursuant to which the Company may continue to acquire shares of its outstanding common stock from time to time for an unspecified length of time.

For our fiscal years ended March 31, 2018 and 2017, we did not repurchase any shares. For our fiscal year ended March 31, 2016, we repurchased approximately 656,000 shares of our common stock. From inception of the program in August 2011 through March 31, 2018, we repurchased approximately 3,422,000 shares of our common stock for an aggregate price of approximately \$5.6 million, at an average price per share of \$1.63. As of March 31, 2018, all repurchased shares have been retired and returned to their status as authorized and unissued shares of our common stock. As of March 31, 2018, approximately \$1.7 million remains available for the repurchase of our common stock under our current program.

## Performance Graph

The following performance graph compares the cumulative total stockholder return of the Company's common stock for the five-year period ended March 31, 2018 to the total returns of (i) the NASDAQ Composite Index and (ii) the NASDAQ Telecommunications Index. This comparison assumes in each case that \$100 was invested at the close of market on March 29, 2013, the last trading day immediately preceding the Company's fifth preceding fiscal year, and that any dividends were reinvested. Stockholder returns over the indicated period should not be considered indicative of future stockholder returns.



	2013	2014	2015	2016	2017	2018
Iteris	\$ 100.00	\$ 108.79	\$ 100.00	\$ 134.07	\$ 298.90	\$ 272.53
NASDAQ Composite	\$ 100.00	\$ 130.18	\$ 153.76	\$ 154.62	\$ 189.99	\$ 229.43
NASDAQ Telecommunications	\$ 100.00	\$ 120.57	\$ 133.29	\$ 131.52	\$ 162.03	\$ 188.13

The foregoing performance graph shall not be deemed "filed" for purposes of Section 18 of the Exchange Act, or otherwise subject to the liabilities under that section and shall not be deemed to be incorporated by reference into any of our filings under the Securities Act or the Exchange Act.

## ITEM 6. SELECTED FINANCIAL DATA

The selected consolidated financial data for the five-year period ended March 31, 2018 has been derived from our consolidated financial statements. The historical results are not necessarily indicative of the results to be expected in any future period. The following selected consolidated financial data should be read in conjunction with, and are qualified in their entirety by reference to, the section entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated audited financial statements and the related notes included elsewhere in this Annual Report. The consolidated statements of operations data for the years ended March 31, 2015 and 2014 and the consolidated balance sheet data as of March 31, 2016, 2015 and 2014 have been derived from consolidated financial statements not included herein

In July 2011, we completed the sale of substantially all of the assets used in connection with our prior Vehicle Sensors business. As a result, the results of operations of this business are all reflected as a discontinued operation for all periods presented below. See Note 3 (Sale of Vehicle Sensors) of the Notes to Consolidated Financial Statements included in this Annual Report.

	For the Years Ended March 31,				
	2018	2017	2016	2015	2014
(in thousands except share and per share data)					
<b>Selected Consolidated Statement of Operations Data:</b>					
Total revenues	\$ 103,729	\$ 95,982	\$ 77,748	\$ 72,251	\$ 68,228
Gross profit	39,831	37,402	30,669	28,182	25,974
Income (loss) from continuing operations	(3,768)	(5,187)	(12,535)	(1,277)	1,320
Gain on sale of discontinued operation, net of tax	242	361	214	207	89
Net income (loss)	(3,526)	(4,826)	(12,321)	(1,070)	1,409
<b>Earnings (loss) per share (basic and diluted):</b>					
(Loss) income per share from continuing operations	\$ (0.12)	\$ (0.16)	\$ (0.39)	\$ (0.04)	\$ 0.04
Gain per share on sale of discontinued operation, net of tax	\$ 0.01	\$ 0.01	\$ 0.01	\$ 0.01	\$ 0.00
Net (loss) income per share	\$ (0.11)	\$ (0.15)	\$ (0.38)	\$ (0.03)	\$ 0.04
<b>Weighted average common shares used in basic per share calculations</b>					
	32,776	32,174	32,049	32,595	32,665
<b>Weighted average common shares used in diluted per share calculations</b>					
	32,776	32,174	32,049	32,595	32,847
<b>Selected Consolidated Balance Sheet Data:</b>					
Total assets	\$ 62,886	\$ 62,345	\$ 60,020	\$ 70,632	\$ 70,607
Long-term liabilities	871	1,542	1,631	1,009	199
Stockholders' equity	39,521	40,224	43,462	55,968	57,490

- (1) See Note 2 to our accompanying consolidated financial statements in Part II, Item 8 of this Annual Report for a description of the method used to compute basic and diluted net loss per common share

## 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 II, Item 8 of this report and the "Risk Factors" section in Item 1A, as well as the 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 provider of essential applied informatics that enable smart transportation and digital agriculture. Municipalities, government agencies, crop science companies, farmers and agronomists use our solutions to make roads safer and travel more efficient, as well as farmlands more sustainable, healthy and productive.

**Sale of Vehicle Sensors.** On July 29, 2011, we completed the sale of substantially all of our assets used in connection with our former 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"). In connection with the Asset Sale, we were entitled to additional consideration in the form of certain performance and royalty-related earn-outs through December 31, 2017. From the date of the Asset Sale through March 31, 2018, we received approximately \$2.6 million in connection with such royalty-related earn-out provisions. We also had approximately \$106,000 in royalty-related receivables included in the prepaid expenses and other current assets in the accompanying consolidated balance sheet as of March 31, 2018. We do not anticipate any further payments from Bendix.

As a result of the Asset Sale, we no longer operate in the Vehicle Sensors segment. We determined that the Vehicle Sensors segment, which previously constituted one of our operating segments, qualified as a discontinued operation. The applicable financial results of our former Vehicle Sensors segment through the closing of the Asset Sale have been reclassified as a discontinued operation for all periods presented in this report. Refer to Note 3 of Notes to Consolidated Financial Statements, included in Part II, Item 8 of this report, for additional discussion regarding the Asset Sale.

**Business Segments.** We currently operate in three reportable segments: Roadway Sensors, Transportation Systems and Agriculture and Weather Analytics.

The Roadway Sensors segment provides various advanced detection sensors and systems for traffic intersection management, communication systems and roadway traffic data collection applications. The Roadways Sensors product line uses advanced image processing technology and other techniques to capture and analyze sensor data through sophisticated algorithms, enabling vehicle, bicycle and pedestrian detection, as well as the transmission of both video images and data using various communication technologies. Our Roadway Sensors products include, among others, Vantage, VantageLive!, VantageNext, VantagePegasus, Vantage Vector, Velocity, SmartCycle, SmartCycle Bike Indicator, SmartSpan, VersiCam, PedTrax and P-Series products.

The Transportation Systems segment includes engineering and consulting services, performance measurement and traffic analytics solutions, as well as the development of transportation management and traveler information systems for the ITS industry. Our Transportation Systems services include planning, design, implementation, operation and management of surface transportation infrastructure systems. We perform analysis and study goods movement, commercial vehicle operations, provide travel demand forecasting and systems engineering, and identify mitigation measures to reduce traffic congestion. Our Transportation Systems product line includes: iPeMS, our performance measurement and information management solution, as well as our commercial vehicle operations and vehicle safety compliance platforms, known as "CVIEW-Plus," "CheckPoint," "UCRLink," and "inspect."

The Agriculture and Weather Analytics segment includes ClearPath Weather, our road maintenance applications, and ClearAg, our digital agriculture platform. Our ClearPath Weather suite of tools, such as tools for assessing historical weather conditions to both short-term and long-range weather forecasts and customizable route/site weather and pavement forecast tools, provide winter road maintenance recommendations for state agencies, municipalities and for commercial companies that allow such users to create solutions to meet roadway maintenance decision needs. Our ClearAg solutions combine weather and agronomic data with proprietary land-surface modeling and analytics to solve complex agricultural problems. Our ClearAg solutions include our ClearAg applications, ClearAg APIs and components, WeatherPlot mobile application and ClearAg Insights applications.

## Critical Accounting Policies and Estimates

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

Transportation Systems revenues are derived primarily from long-term contracts with governmental agencies. Certain Agriculture and Weather Analytics revenues are also derived from long-term contracts with governmental agencies, as well as contracts with commercial companies. ClearAg revenues that are derived from contracts with commercial companies are from subscription revenue that we typically invoice our customers at the beginning of the term, in multiyear, annual, semi-annual or quarterly installments, and revenue is recognized ratably over the period of the subscription beginning once all requirements for revenue recognition have been met, including provisioning the service so that it is available to our customers. When appropriate, 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 revenues when their realization is reasonably assured. Certain of our revenues are recognized as services are performed and amounts are earned, which is measured by time incurred or other contractual milestones or output measures. Revenues accounted for in this manner generally relate to certain fixed fee professional services, cost-plus fixed fee or time-and-materials contracts. Revenues for ongoing operations and maintenance services contracts are generally accounted for ratably as the services are performed throughout the term of the contract. Payments received in advance of services performed are deferred and recognized when the related services are performed.

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 stand-alone 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.

**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 internally developed and 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 perform an annual qualitative assessment of our goodwill during the fourth fiscal quarter, or more frequently, to determine if any events or circumstances exist, such as an adverse change in business climate or a decline in overall industry demand, that would indicate that it would more likely than not reduce the fair value of a reporting unit below its carrying amount, including goodwill. If events or circumstances do not indicate that the fair value of a reporting unit is below its carrying amount, then goodwill is not considered to be impaired and no further testing is required. If further testing is required, we perform a two-step process. The first step involves comparing the fair value of our reporting unit to its carrying value, including goodwill. If the carrying value of the reporting unit exceeds its fair value, the second step of the test is performed by comparing the carrying value of the goodwill in the reporting unit to its implied fair value. An impairment charge is recognized for the excess of the carrying value of goodwill over its implied fair value. We determine the fair values of our reporting units using the income valuation approach, as well as other generally accepted valuation methodologies.

In Fiscal 2017, we adopted the provisions issued by the FASB that were intended to simplify goodwill impairment testing. This guidance permits us to eliminate the second step of the goodwill impairment test, and eliminate the requirements for any reporting unit with a zero or negative carrying amount to perform a qualitative assessment. If the carrying amount of a reporting unit exceeds the reporting unit's fair value, the amount by which the carrying value of the goodwill exceeds its implied fair value, if any, is recognized as an impairment loss. We monitor the indicators for goodwill impairment testing between annual tests.

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 or asset group is 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.

**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 reversed in the first subsequent financial reporting period in which that threshold is no longer met.

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.

In relation to the Tax Act, we determine reasonable provisional estimate on our existing deferred tax balances and the one-time transition tax under the SEC Staff Accounting Bulletin No. 118, Income Tax Accounting Implications of the Tax Cuts and Jobs Act ("SAB 118"). Actual future operating results and the underlying amount and type of income could differ materially from our estimates, assumptions and judgments, thereby impacting our consolidated financial position and results of operations.

**Stock-Based Compensation.** We record stock-based compensation in the statements of operations as an expense, based on the grant date estimated 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 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 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 the limited transferability of the awards. 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 II, Item 8 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 revenues for the periods indicated.

	Year Ended March 31,		
	2018	2017	2016
Product revenues	44.8%	45.6%	53.7%
Service revenues	55.2	54.4	46.3
Total revenues	100.0	100.0	100.0
Cost of product revenues	25.7	24.8	30.0
Cost of service revenues	35.9	36.2	30.5
Cost of revenues	61.6	61.0	60.6
Gross profit	38.4	39.0	39.4
Operating expenses:			
Selling, general and administrative	36.0	34.6	34.4
Research and development	7.7	7.2	8.9
Amortization of intangible assets	0.1	0.3	0.5
Loss on impairment of goodwill	—	2.3	—
Total operating expenses	43.8	44.4	43.8
Operating loss	(5.4)	(5.4)	(4.4)
Non-operating income (expense):			
Other (expense) income, net	(0.0)	(0.0)	0.0
Interest income, net	0.0	0.0	0.0
Loss from continuing operations before income taxes	(5.4)	(5.4)	(4.4)
Benefit (provision) for income taxes	1.8	0.0	(11.7)
Loss from continuing operations	(3.6)	(5.4)	(16.1)
Gain on sale of discontinued operation, net of tax	0.2	0.4	0.3
Net loss	(3.4)%	(5.0)%	(15.8)%

## Analysis of Fiscal 2018, Fiscal 2017 and Fiscal 2016 Results of Operations

**Total Revenues.** Total revenues are comprised of sales from our Roadway Sensors, Transportation Systems and Agriculture and Weather Analytics segments. The following table's present details of total revenues for Fiscal 2018 compared to Fiscal 2017, and Fiscal 2017 compared to Fiscal 2016:

	Year Ended March 31,		\$	%
	2018	2017	Increase	Change
	(In thousands, except percentages)			
Product revenues	\$ 46,464	\$ 43,735	\$ 2,729	6.2%
Service revenues	57,265	52,247	5,018	9.6%
Total revenues	\$ 103,729	\$ 95,982	\$ 7,747	8.1%



	Year Ended March 31,		\$ Increase	% Change
	2017	2016		
	(in thousands, except percentages)			
Product revenues	\$ 43,735	\$ 41,733	\$ 2,002	4.8%
Service revenues	52,247	36,015	16,232	45.1%
Total revenues	<u>\$ 95,982</u>	<u>\$ 77,748</u>	<u>\$ 18,234</u>	<u>23.5%</u>

Product revenues for Fiscal 2018 increased approximately 6.2% to \$46.5 million, compared to \$43.7 million in Fiscal 2017, primarily due to increases in unit sales of our core Roadway Sensors products, Roadway Sensors OEM sales, as well as our Transportation Systems third-party product sales. Service revenues for Fiscal 2018 increased approximately 9.6% to \$57.3 million, compared to \$52.2 million in Fiscal 2017, primarily due to higher Transportation Systems traffic engineering service revenue for government agencies. Total revenues for Fiscal 2018 increased approximately 8.1% to \$103.7 million, compared to \$96.0 million in Fiscal 2017, primarily due to an approximate 11% increase in Transportation Systems revenues, an approximate 5% increase in Roadway Sensors revenues, and an approximate 8% increase in Agriculture and Weather Analytics revenues.

Roadway Sensors revenues in Fiscal 2018 included approximately \$44.2 million in product revenues and approximately \$194,000 of service revenues, reflecting an increase in total revenues of approximately \$2.2 million or 5%, compared to Fiscal 2017. The increase was primarily due to higher unit sales of our core Roadway Sensors video detection products aided by a corresponding increase of in our distribution of certain OEM products for the traffic intersection market. Revenue generated through the distribution of certain third party products was approximately \$5.3 million and approximately \$4.8 million for Fiscal 2018 and Fiscal 2017, respectively. Roadway Sensors revenues in Fiscal 2017 included approximately \$42.1 million in product revenues and \$111,000 of service revenues, reflecting an increase in total revenues of approximately \$1.9 million or 5%, compared to Fiscal 2016. The increase was primarily due to higher unit sales of our Roadway Sensors products, slightly offset by a decrease in our distribution of OEM products for the traffic intersection market. Revenue generated through the distribution of certain third party products was approximately \$4.8 million and approximately \$5.3 million for Fiscal 2017 and Fiscal 2016, respectively. Going forward, we plan to grow revenues by focusing on our core domestic intersection market, and refine and deliver products that address the needs of this market, primarily our Vantage processors and camera systems, and our Vantage Vector video/radar hybrid sensor, as well as our SmartCycle, Velocity, PedTrax and SmartSpan products.

Transportation revenues in Fiscal 2018 included approximately \$52.2 million of service revenues and approximately \$2.3 million of sales of third-party products purchased for installation under certain construction-type contracts, reflecting an increase in total revenues of approximately \$5.2 million or 11%, compared to Fiscal 2017. The increase was primarily a result of extensions granted on certain large contracts, new contract awards, and the timing of backlog fulfilment on certain other projects. Transportation revenues in Fiscal 2017 included approximately \$47.6 million of service revenues and approximately \$1.7 million of sales of third-party products purchased for installation under certain construction-type contracts, reflecting an increase in total revenues of approximately \$15.2 million or 45%, compared to Fiscal 2016. The increase was primarily due as a result of one large contract win during the fourth quarter of Fiscal 2017 and two large contract wins during the third quarter of Fiscal 2016, which was a key contributor to positively impacting revenue growth in Fiscal 2017, as well as timing of backlog fulfilment on certain other projects. While one of the aforementioned large contracts is expected to be near completion by the first quarter of our fiscal year ending March 31, 2019, we plan to continue to pursue larger contracts that may contain significant sub-consulting content. While we believe larger contacts will contribute to overall revenue growth, the mix of sub-consulting content will

likely affect the related gross profit from period to period, as revenues derived from sub-consultants generally have lower gross margins than revenues generated by our professional services.

Agriculture and Weather Analytics revenues in Fiscal 2018 included no product revenue and approximately \$4.9 million of service revenues, largely consisting of subscription revenues, reflecting an increase in total revenues of approximately \$351,000 or 8%, compared to Fiscal 2017. The increase was primarily due to an increase in ClearAg solutions under newly signed contracts during Fiscal 2018 and Fiscal 2017. Agriculture and Weather Analytics revenues in Fiscal 2017 included no product revenue and approximately \$4.5 million of service revenues, largely consisting of subscription revenues, reflecting an increase in total revenues of approximately \$1.1 million or 34%, compared to Fiscal 2016. The increase was primarily due to increases in both ClearPath Weather and ClearAg solutions under newly signed contracts during Fiscal 2017. Going forward, we plan to continue investing in this segment, particularly in the research and development and sales and marketing of the ClearAg and ClearPath Weather solutions. We also plan to pursue commercial opportunities in the precision agriculture technology markets by offering software applications, content, and modeling services that provide analytics and decision support services that leverage our precision weather, soil and agronomic content and applications.

**Gross Profit.** The following tables present details of our gross profit for Fiscal 2018 compared to Fiscal 2017, and Fiscal 2017 compared to Fiscal 2016:

	Year Ended March 31,		\$ Increase (Decrease)	% Change
	2018	2017		
	(In thousands, except percentages)			
Product gross margin	\$ 19,831	\$ 19,858	\$ (27)	(0.1)%
Service gross margin	20,000	17,544	2,456	14.0%
Total gross margin	<u>\$ 39,831</u>	<u>\$ 37,402</u>	<u>\$ 2,429</u>	<u>6.5%</u>
Product gross margin as a % of product revenues	42.7%	45.4%		
Service gross margin as a % of service revenues	34.9%	33.6%		
Total gross margin as a % of total revenues	38.4%	39.0%		

	Year Ended March 31,		\$	%
	2017	2016	Increase	Change
	(in thousands, except percentages)			
Product gross margin	\$ 19,858	\$ 18,393	\$ 1,465	8.0%
Service gross margin	17,544	12,276	5,268	42.9%
Total gross margin	<u>\$ 37,402</u>	<u>\$ 30,669</u>	<u>\$ 6,733</u>	<u>22.0%</u>
Product gross margin as a % of product revenues	45.4%	44.1%		
Service gross margin as a % of service revenues	33.6%	34.1%		
Total gross margin as a % of total revenues	39.0%	39.4%		

Our product gross profit as a percentage of product revenues for Fiscal 2018 decreased approximately 270 basis points compared to Fiscal 2017 primarily due an increase in our Roadway Sensors OEM sales, as well as our Transportation Systems third-party product sales, both of which typically yield lower gross margins than our Roadway Sensors core video detection products. Our service gross profit as a percentage of service revenues for Fiscal 2018 increased 130 basis points compared to Fiscal 2017 primarily due to the timing of certain extension contracts, the contract mix and a decrease in the amount of related sub-consulting content of such contracts. Sub-consulting content generally results in lower gross margins than our workforce. Our total gross profit as a percentage of total revenues for Fiscal 2018 decreased 60 basis points compared to Fiscal 2017

primarily as a result of the revenue mix between the Roadway Sensors and Transportation Systems segments, as Roadway Sensors revenues generally yield higher total gross margins than our other segments. As such, the increase in our Transportation Systems total revenues from approximately 51% of total revenues for Fiscal 2017 to approximately 53% of total revenues for Fiscal 2018 was a primary contributor to our decline in total gross margin. Roadway Sensors revenue decreased as a percentage of total revenues from approximately 44% for Fiscal 2017 to approximately 43% for Fiscal 2018.

Our product gross profit as a percentage of product revenues for Fiscal 2017 increased approximately 130 basis points compared to Fiscal 2016 primarily due an increase in unit sales of our core Roadway Sensors products, coupled with a decrease in our Transportation Systems third-party product sales in Fiscal 2017, both of which typically yield lower gross margins than our Roadway Sensors core video detection products. Our service gross profit as a percentage of service revenues for Fiscal 2017 decreased 50 basis points compared to Fiscal 2016 primarily due to the timing of certain extension contracts, the contract mix and an increase in the amount of related sub-consulting content of such contracts. Sub-consulting content generally results in lower gross margins than our workforce. Our total gross profit as a percentage of total revenues for Fiscal 2017 decreased approximately 40 basis points compared to Fiscal 2016 primarily due to higher revenues derived from our Transportation Systems segment in Fiscal 2017, which has generally experienced lower gross profits than our other segments and which increased to approximately 51% of our total revenues for Fiscal 2017, as compared to 44% for Fiscal 2016. Therefore, the increase in Transportation Systems revenues, as a percentage of our overall revenue mix, decreased our overall margin.

Roadway Sensors gross profit can fluctuate in any specific quarter or year based on, among other factors, customer and product mix between core products and third party OEM products, competitive pricing requirements, product warranty costs and provisions for our 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.

We recognize a portion of our Transportation Systems revenues and related gross profit using percentage of completion contract accounting, and the underlying mix of contract activity affects the related gross profit recognized in any given period. For the Transportation Systems segment, we expect to experience gross profit variability in future periods due to our contract mix and the amount of related sub-consulting content of such contracts, as well as factors such as our ability to efficiently utilize our internal workforce, which could cause fluctuations in our margins from period to period.

### ***Selling, General and Administrative Expense***

Selling, general and administration expense for Fiscal 2018 increased approximately 12.3% to \$37.4 million, compared to \$33.3 million in Fiscal 2017. The overall increase was primarily due to an increase in business development costs aimed at the pursuit of large contracts in the Transportations Systems segment. In addition, there were higher personnel compensation costs driven by higher revenues. This increase in personnel also drove an increase in facilities costs. The overall increase was also attributable to an increase in other selling, general and administrative expenses, primarily due to a reversal of certain bad debt reserves on specific accounts receivable that were subsequently collected during Fiscal 2017, which did not reoccur in Fiscal 2018.

Selling, general and administration expense for Fiscal 2017 increased approximately 24.1% to \$33.3 million, compared to \$26.8 million in Fiscal 2016. The overall increase was primarily due to planned headcount increases in corporate headquarters general and administrative positions, as well as planned investments in Agriculture and Weather Analytics sales and marketing, including an increase in the salesforce headcount, which resulted in higher salary and personnel-related costs. The increases in general and administrative expense were also due to legal costs incurred (i) to reach a proxy contest settlement during our second quarter of Fiscal 2018 and (ii) for recent stockholder litigation which was

settles in the first half of Fiscal 2018 (see Note 8 of Notes to Consolidated Financial Statements). The increases in general and administrative were also attributable to additional costs for internal control framework to comply with Sarbanes-Oxley standards as an accelerated filer. These increases were partially offset by a reversal of certain bad debt reserves that were placed on specific accounts receivable that were collected during Fiscal 2017.

### ***Research and Development Expense***

Research and development expense for Fiscal 2018 increased approximately 15.5% to \$7.9 million, compared to \$6.9 million in Fiscal 2017. The overall increase was primarily due to continued investment in research, discovery, and development largely focused on our software related product offerings.

We continued to invest in the development of our iPeMS software offering as well as our ClearAg and ClearPath Weather solutions. In addition, we invested in further enhancements and functionality in our Vantage products family. During Fiscal 2018, we successfully released Iteris SPM, our cloud-based signal performance measures application. During Fiscal 2017, we released our VantageLive! platform as well as a number of generally available advisory applications, including our Harvest Advisory and Nitrogen Advisory. Certain development costs were capitalized into intangible assets in the consolidated balance sheets; however, certain costs did not meet the criteria for capitalization under GAAP and are included in research and development expense. Going forward, we expect to continue to invest in our solutions. This continued investment may result in increases in research and development costs in future periods.

Research and development for Fiscal 2017 and Fiscal 2016 was relatively consistent at \$6.9 million for both periods as the Company continued to invest in research, discovery, and development.

### ***Impairment of Goodwill***

Based on our goodwill impairment testing for Fiscal 2018, we believe the carrying value of our goodwill was not impaired, as the estimated fair values of our reporting units exceeded their carrying values at the end of Fiscal 2018. Based on our goodwill impairment testing for Fiscal 2017, we determined the fair value of the Agriculture and Weather Analytics reporting unit was less than its carrying amount and resulted in approximately \$2.2 million impairment charge in the consolidated statement of operations for Fiscal 2017. We also determined our Roadway Sensors and Transportation Systems reporting units had no impairment, as their estimated fair values exceeded their respective carrying values. Based on our goodwill impairment testing for Fiscal 2016, we believe the carrying value of our goodwill was not impaired, as the estimated fair values of our reporting units exceeded their carrying values at the end of such fiscal year. If our actual financial results, or the plans and estimates used in future goodwill impairment analyses, are lower than our original estimates used to assess impairment of our goodwill, we could incur goodwill impairment charges in the future.

### ***Amortization of Intangible Assets***

Amortization of intangible assets was approximately \$88,000, \$281,000 and \$360,000 in Fiscal 2018, Fiscal 2017 and Fiscal 2016, respectively. The decrease in amortization was primarily due to the completion of amortization on certain older intangible assets.

### ***Interest Income, Net***

Net interest income was approximately \$32,000, \$13,000 and \$12,000 in Fiscal 2018, Fiscal 2017 and Fiscal 2016, respectively.

**Income Taxes**

The following table presents our (benefit) provision for income taxes for Fiscal 2018, Fiscal 2017 and Fiscal 2016:

	Year Ended March 31,		
	2018	2017	2016
	(In thousands, except percentages)		
(Benefit) provision for income taxes	\$ (1,818)	\$ (44)	\$ 9,079
Effective tax rate	32.5%	0.8%	(262.6)%

For Fiscal 2018, the difference between the statutory and the effective tax rate was primarily attributable to an increase in tax expense resulting from the impact of the change in the U.S. federal tax rate on the Company's deferred tax assets, offset by a corresponding change to the valuation allowance maintained against the deferred tax assets and a benefit for research tax credits generated during the current fiscal year. The effective tax rate for Fiscal 2018 was also favorably impacted by the reversal of the valuation allowance related to Alternative Minimum Tax credit carryforwards, which were made refundable by the tax legislation discussed below.

For Fiscal 2017 and 2016, the difference between the statutory and the effective tax rate was primarily attributable to the valuation allowance recorded against the Company's deferred tax assets.

In assessing the realizability of our deferred tax assets, we review 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 the Company has sustained a cumulative pre-tax loss over the trailing three years, we considered it appropriate to maintain valuation allowances of \$9.8 million and \$11.7 million against our deferred tax assets at March 31, 2018 and 2017, respectively. We will continue to reassess the appropriateness of maintaining a valuation allowance.

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.

At March 31, 2018, we had \$6.8 million of federal net operating loss carryforwards that do not expire as a result of recent tax law changes and \$5.6 million of federal net operating loss carryforwards that begin to expire in 2022. We also had \$4.4 million of state net operating loss carryforwards that begin to expire in 2031. Although the impact cannot be precisely determined at this time, we believe that our net operating loss carryforwards will provide reductions in our future income tax payments, that would otherwise be higher using statutory tax rates.

The Tax Act was enacted on December 22, 2017 and reduced U.S. corporate income tax rates to 21.0% as of January 1, 2018. The rate change became effective during Fiscal 2018 resulting in a blended statutory tax rate of 30.8% for Fiscal 2018. As a consequence of the tax legislation, the Company recorded a decrease in its net deferred tax assets of \$4.1 million and a decrease in the valuation allowance maintained against its deferred tax assets of \$5.8 million. The estimated impact of the tax legislation was an income tax benefit of \$1.7 million, of which \$1.1 million was due to the release of valuation allowance that had been maintained against Alternative Minimum Tax credit carryforwards, which were made refundable by the tax legislation, and \$640,000 was due to the remeasurement of a deferred tax liability related to indefinite-lived assets.

On December 22, 2017, the SEC issued guidance under SAB 118 directing taxpayers to consider the impact of the tax legislation as "provisional" when it does not have the necessary information available, prepared or analyzed (including computations) in reasonable detail to complete its accounting for the change in tax law. In accordance with SAB 118, the income tax effects discussed above represent the Company's best estimate based on its current interpretation of this tax legislation. The Company is accumulating data to finalize the underlying calculations and evaluate other aspects of this tax legislation, or in certain cases, the U.S. Treasury is expected to issue further guidance on the application of certain provisions of the tax legislation. In accordance with SAB 118, the income tax effects of the tax legislation discussed above are considered provisional and will be finalized in Fiscal 2019.

## Liquidity and Capital Resources

### Cash Flows

We have historically financed our operations with a combination of cash flows from operations and the sale of equity securities. We have historically relied, and expect to continue to rely on cash flows from operations and our cash reserves 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. There is no assurance that we will be able to secure additional funding on a timely basis, on terms acceptable to us, or at all.

At March 31, 2018, we had \$17.4 million in working capital, which included \$10.2 million in cash and cash equivalents, as well as \$5.3 million in short term investments. This compares to working capital of \$22.7 million at March 31, 2017, which included \$18.2 million in cash and cash equivalents.

The following table summarizes our cash flows for Fiscal 2018, Fiscal 2017 and Fiscal 2016:

	Year Ended March 31,		
	2018	2017	2016
	(In thousands)		
<b>Net cash provided by (used in):</b>			
Operating activities	\$ (268)	\$ 2,903	\$ (4,110)
Investing activities	(8,823)	(1,343)	(978)
Financing activities	1,042	612	(844)

**Operating Activities.** Cash used in our operations during Fiscal 2018 was primarily the result of our net loss of approximately \$3.5 million, adjusted by approximately \$2.4 million in non-cash items for deferred income taxes, depreciation, stock-based compensation, amortization, gain on sales of discontinued operations, and loss on disposal of equipment. The net loss was offset in part by approximately \$819,000 of working capital provided in Fiscal 2018.

Cash provided by our operations during Fiscal 2017 was primarily the result of approximately \$3.6 million of working capital provided and offset by our net loss of approximately \$4.8 million, adjusted by approximately \$4.2 million in non-cash items for deferred income taxes, depreciation, stock-based compensation, amortization, gain on sales of discontinued operations, loss on disposal of equipment and loss on impairment of goodwill.

Cash used in our operations during Fiscal 2016 was primarily the result of our net loss of approximately \$12.3 million, adjusted by approximately \$10.5 million in non-cash items, of which

approximately \$9.0 million related to the change in our deferred income taxes and related valuation allowance recorded against our federal net operating loss carryforwards. Such non-cash items also included higher stock-based compensation primarily due to the recent large equity grant to our new CEO, as well as depreciation, amortization, gain on the sale of discontinued operation and loss on disposal of equipment. Cash used in our operations was also driven by approximately \$2.3 million used in working capital.

**Investing Activities.** Cash used in our investing activities during Fiscal 2018 consisted of approximately \$5.3 million in investment purchases, approximately \$1.1 million for purchases of property and equipment primarily related to leasehold improvement to our corporate headquarters, and \$2.9 million of capitalized software development primarily related to the development of our new Oracle ERP system, and to a lesser extent, in the Agriculture and Weather Analytics and Roadway Sensors business segments related to ClearAg assets and VantageLive! developments. These investments were partially offset by approximately \$511,000 in proceeds from the earn-out provision included in the sale of the Vehicle Sensors segment.

Cash used in our investing activities during Fiscal 2017 consisted of approximately \$1.2 million of capitalized software development in the Agriculture and Weather Analytics and Roadway Sensors business segments related to ClearAg assets and VantageLive! development, respectively, and approximately \$668,000 for purchases of property and equipment, primarily related to computers and related equipment which were offset by approximately \$495,000 in proceeds from the sale of the Vehicle Sensors segment.

Cash used in our investing activities during Fiscal 2016 consisted of approximately \$856,000 for purchases of property and equipment, primarily related to computers and related equipment and approximately \$490,000 of capitalized software development in the Agriculture and Weather Analytics business segment related to ClearAg assets, which were offset by approximately \$368,000 in proceeds from the sale of the Vehicle Sensors segment.

**Financing Activities.** Net cash provided by financing activities during Fiscal 2018 and Fiscal 2017 was primarily the result of approximately \$1.0 million and \$612,000, respectively, of cash proceeds received from the exercises of stock options.

Net cash used in financing activities during Fiscal 2016 was primarily the result of approximately \$1.2 million in cash used to repurchase shares of our common stock under our stock repurchase program, which was offset in part by approximately \$383,000 of cash proceeds received from the exercises of stock options.

### ***Borrowings***

We previously had a \$12.0 million revolving line of credit with California Bank & Trust ("CB&T"), which expired on October 1, 2016. We were obligated to pay an unused line fee of 0.15% per annum applied to the average unused portion of the revolving line of credit. We chose not to renew our line of credit as we do not foresee a need to utilize credit within the next twelve months, and we will avoid paying an unused line fee.

### **Off-Balance Sheet Arrangements**

Other than our operating leases, which are further described at Note 8 of Notes to Consolidated Financial Statements, included in Part II, Item 8 of this report, we do not have any other material off-balance sheet arrangements at March 31, 2018.

## Seasonality

We have historically experienced seasonality, particularly with respect to our Roadway Sensors segment, which adversely affects such sales in our third and fourth fiscal quarters due to a reduction in intersection construction and repairs during the winter months due to inclement weather conditions, with the third fiscal quarter generally impacted the most by inclement weather. We have also experienced seasonality, particularly with respect to our Transportation Systems segment, which adversely impacts our third fiscal quarter due to the increased number of holidays, causing a reduction in available billable hours. In addition, we have experienced seasonality related to certain ClearPath Weather services, which adversely impacts such sales in our first and second fiscal quarters, mainly because these services are generally not required during Spring and Summer when weather conditions are comparatively milder.

## ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

### Interest Rate Risk

Our exposure to market rate risk for changes in interest rates relates primarily to our investment portfolio. The primary objective of our investment activities is to preserve principal and liquidity while at the same time maximizing yields without significantly increasing risk. To achieve this objective, we maintain our investments portfolio in a variety of available-for-sale fixed debt securities, including both government and corporate obligations and money market funds. Investments in fixed rate interest bearing instruments carry a degree of interest rate risk. Fixed rate securities may have their fair market value adversely impacted due to a rise in prevailing interest rates. Due in part to these factors, we may suffer losses in principal if we need the funds prior to maturity and choose to sell securities that have declined in market value due to changes in interest rates or perceived credit risk related to the securities' issuers.



**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

**Iteris, Inc.  
Index to Consolidated Financial Statement**

<a href="#">Report of Independent Registered Public Accounting Firm</a>	<a href="#">41</a>
<a href="#">Consolidated Balance Sheets as of March 31, 2018 and 2017</a>	<a href="#">43</a>
<a href="#">Consolidated Statements of Operations for the fiscal years ended March 31, 2018, 2017 and 2016</a>	<a href="#">44</a>
<a href="#">Consolidated Statements of Stockholders' Equity for the fiscal years ended March 31, 2018, 2017 and 2016</a>	<a href="#">45</a>
<a href="#">Consolidated Statements of Cash Flows for the fiscal years ended March 31, 2018, 2017 and 2016</a>	<a href="#">46</a>
<a href="#">Notes to Consolidated Financial Statements</a>	<a href="#">47</a>

## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the stockholders and the Board of Directors of Iteris, Inc.

### Opinions on the Financial Statements and Internal Control over Financial Reporting

We have audited the accompanying consolidated balance sheets of Iteris, Inc. and subsidiary (the "Company") as of March 31, 2018 and 2017, the related consolidated statements of operations, stockholders' equity, and cash flows, for each of the three years in the period ended March 31, 2018, and the related notes (collectively referred to as the "financial statements"). We also have audited the Company's internal control over financial reporting as of March 31, 2018, based on criteria established in *Internal Control—Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of March 31, 2018 and 2017, and the results of their operations and their cash flows for each of the three years in the period ended March 31, 2018, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of March 31, 2018, based on criteria established in *Internal Control—Integrated Framework (2013)* issued by COSO.

### Basis for Opinions

The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on these financial statements and an opinion on the Company's internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud, and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the financial statements included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures to respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

## **Definition and Limitations of Internal Control over Financial Reporting**

A company's internal control over financial reporting is a process designed 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. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Deloitte & Touche LLP  
Costa Mesa, CA  
June 7, 2018

We have served as the Company's auditor since fiscal 2016.

**Iteris, Inc.**

**Consolidated Balance Sheets**

**(In thousands, except par value)**

	<b>March 31,</b>	
	<b>2018</b>	<b>2017</b>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 10,152	\$ 18,201
Short-term investments	5,319	—
Trade accounts receivable, net of allowance for doubtful accounts of \$333 and \$389 at March 31, 2018 and March 31, 2017, respectively	12,866	14,299
Unbilled accounts receivable	7,473	6,456
Inventories	2,921	2,250
Prepaid expenses and other current assets	1,165	2,108
Total current assets	<u>39,896</u>	<u>43,314</u>
Property and equipment, net	2,333	2,064
Intangible assets, net	3,751	1,498
Goodwill	15,150	15,150
Other assets	1,756	319
Total assets	<u>\$ 62,886</u>	<u>\$ 62,345</u>
<b>Liabilities and stockholders' equity</b>		
Current liabilities:		
Trade accounts payable	\$ 7,838	\$ 7,886
Accrued payroll and related expenses	7,398	6,443
Accrued liabilities	2,358	2,201
Deferred revenue	4,900	4,049
Total current liabilities	<u>22,494</u>	<u>20,579</u>
Deferred rent	638	649
Deferred income taxes	65	707
Unrecognized tax benefits	168	186
Total liabilities	<u>23,365</u>	<u>22,121</u>
Commitments and contingencies (Note 9)		
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, 2018 and March 31, 2017		
Issued and outstanding shares—33,186 at March 31, 2018 and 32,488 at March 31, 2017	3,318	3,249
Additional paid-in capital	139,722	136,968
Accumulated deficit	<u>(103,519)</u>	<u>(99,993)</u>
Total stockholders' equity	<u>39,521</u>	<u>40,224</u>
Total liabilities and stockholders' equity	<u>\$ 62,886</u>	<u>\$ 62,345</u>

See accompanying notes.

**Iteris, Inc.**

**Consolidated Statements of Operations**

**(In thousands, except per share amounts)**

	<b>Year Ended March 31,</b>		
	<b>2018</b>	<b>2017</b>	<b>2016</b>
Product revenues	\$ 46,464	\$ 43,735	\$ 41,733
Service revenues	57,265	52,247	36,015
Total revenues	103,729	95,982	77,748
Cost of product revenues	26,633	23,877	23,340
Cost of service revenues	37,265	34,703	23,739
Cost of revenues	63,898	58,580	47,079
Gross profit	39,831	37,402	30,669
Operating expenses:			
Selling, general and administrative	37,400	33,313	26,846
Research and development	7,945	6,877	6,933
Amortization of intangible assets	88	281	360
Loss on impairment of goodwill	—	2,168	—
Total operating expenses	45,433	42,639	34,139
Operating loss	(5,602)	(5,237)	(3,470)
Non-operating income (expense):			
Other (expense) income, net	(16)	(7)	2
Interest income, net	32	13	12
Loss from continuing operations before income taxes	(5,586)	(5,231)	(3,456)
Benefit (provision) for income taxes	1,818	44	(9,079)
Loss from continuing operations	(3,768)	(5,187)	(12,535)
Gain on sale of discontinued operation, net of tax	242	361	214
Net loss	\$ (3,526)	\$ (4,826)	\$ (12,321)
Loss per share from continuing operations—basic and diluted	\$ (0.12)	\$ (0.16)	\$ (0.39)
Gain per share from sale of discontinued operation—basic and diluted	\$ 0.01	\$ 0.01	\$ 0.01
Net loss per share—basic and diluted	\$ (0.11)	\$ (0.15)	\$ (0.38)
Shares used in basic per share calculations	32,776	32,174	32,049
Shares used in diluted per share calculations	32,776	32,174	32,049

See accompanying notes.

**Iteris, Inc.**

**Consolidated Statements of Stockholders' Equity**

**(In thousands)**

	<b>Common Stock</b>		<b>Additional Paid-In Capital</b>	<b>Accumulated Deficit</b>	<b>Total Stockholders' Equity</b>
	<b>Shares</b>	<b>Amount</b>			
Balance at March 31, 2015	32,411	\$ 3,242	\$ 135,572	\$ (82,846)	\$ 55,968
Stock option exercises	243	24	359	—	383
Stock-based compensation	—	—	659	—	659
Issuance of shares pursuant to vesting of restricted stock units, net of payroll withholding taxes	50	5	(37)	—	(32)
Repurchases of common stock	(656)	(66)	(1,129)	—	(1,195)
Net loss				(12,321)	(12,321)
Balance at March 31, 2016	32,048	\$ 3,205	\$ 135,424	\$ (95,167)	\$ 43,462
Stock option exercises	388	40	628	—	668
Stock-based compensation	—	—	976	—	976
Issuance of shares pursuant to vesting of restricted stock units, net of payroll withholding taxes	52	4	(60)	—	(56)
Net loss				(4,826)	(4,826)
Balance at March 31, 2017	32,488	\$ 3,249	\$ 136,968	\$ (99,993)	\$ 40,224
Stock option exercises	591	59	1,131	—	1,190
Stock-based compensation	—	—	1,781	—	1,781
Issuance of shares pursuant to vesting of restricted stock units, net of payroll withholding taxes	107	10	(158)	—	(148)
Net loss				(3,526)	(3,526)
Balance at March 31, 2018	33,186	\$ 3,318	\$ 139,722	\$ (103,519)	\$ 39,521

See accompanying notes.

**Iteris, Inc.**

**Consolidated Statements of Cash Flows**

(In thousands)

	Year Ended March 31,		
	2018	2017	2016
<b>Cash flows from operating activities</b>			
Net loss	\$ (3,526)	\$ (4,826)	\$ (12,321)
Adjustments to reconcile net loss to net cash (used in) provided by operating activities:			
Deferred income taxes	(660)	12	8,859
Depreciation of property and equipment	819	729	649
Stock-based compensation	1,781	976	659
Amortization of intangible assets	726	623	526
Gain on sale of discontinued operation, net of tax	(242)	(361)	(214)
Loss on disposal of equipment	16	14	58
Loss on impairment of goodwill	—	2,168	—
Changes in operating assets and liabilities, net of effects of discontinued operation:			
Accounts receivable	1,433	(1,058)	(2,035)
Unbilled accounts receivable and deferred revenue, net	(166)	549	(239)
Inventories	(671)	903	(91)
Prepaid expenses and other assets	(693)	(408)	(407)
Accounts payable and accrued expenses	915	3,582	446
Net cash (used in) provided by operating activities	(268)	2,903	(4,110)
<b>Cash flows from investing activities</b>			
Purchases of property and equipment	(1,079)	(668)	(856)
Capitalized software development costs	(2,936)	(1,170)	(490)
Purchase of short term investments	(5,319)	—	—
Net proceeds from sale of business segment	511	495	368
Net cash used in investing activities	(8,823)	(1,343)	(978)
<b>Cash flows from financing activities</b>			
Repurchases of common stock	—	—	(1,195)
Proceeds from stock option exercises	1,190	668	383
Tax withholding payments for net share settlements of restricted stock units	(148)	(56)	(32)
Net cash provided by (used in) financing activities	1,042	612	(844)
(Decrease) increase in cash and cash equivalents	(8,049)	2,172	(5,932)
Cash and cash equivalents at beginning of period	18,201	16,029	21,961
Cash and cash equivalents at end of period	<u>\$ 10,152</u>	<u>\$ 18,201</u>	<u>\$ 16,029</u>
<b>Supplemental cash flow information:</b>			
Cash paid during the year for:			
Interest	\$ —	\$ 14	\$ 18
Income taxes	130	166	177
<b>Supplemental schedule of non-cash investing and financing activities:</b>			
Capitalized software development costs included in accounts payable and accrued expenses	\$ 102	\$ —	\$ —
Issuance of common stock for vested restricted stock units	10	5	5
Landlord contribution for tenant improvements	145	—	—

See accompanying notes.

**Iteris, Inc.**

**Notes to Consolidated Financial Statements**

**March 31, 2018**

**1. Description of Business and Summary of Significant Accounting Policies**

**Description of Business**

Iteris, Inc. (referred to collectively with its wholly-owned subsidiary, ClearAg, Inc., in this report as "Iteris", the "Company", "we", "our", and "us") is a provider of essential applied informatics that enable smart transportation and digital agriculture. Municipalities, government agencies, crop science companies, farmers and agronomists use our solutions to make roads safer and travel more efficient, as well as farmlands more sustainable, healthy and productive.

We offer a comprehensive range of intelligent transportation systems ("ITS") technology solutions to our customers throughout the U.S. and internationally through a combination intellectual property, products, and decades of experience in traffic management, weather forecasting solutions and information technologies.

In the agribusiness markets, we have combined our intellectual property with enhanced atmospheric, land surface and agronomic modeling techniques to offer smart content solutions that provide analytical support to large enterprises in the agriculture industry, such as seed and crop protection companies, integrated food companies, and agricultural equipment manufacturers and service providers.

We believe our products, solutions and services improve and safely optimize mobility within our communities, while minimizing environmental impact on the roads we travel and the lands we farm.

We continue to make significant investments to leverage our existing technologies and further expand both our advanced detection sensors and performance analytics systems in the transportation infrastructure market, while supporting the entire value chain in the agriculture market with our smart content and digital farming platform.

Iteris was incorporated in Delaware in 1987.

**Recent Developments**

*ClearAg, Inc.*

In April 2017, Iteris, Inc. formed a wholly-owned subsidiary, ClearAg, Inc., a Delaware corporation, to provide ClearAg solutions in the agribusiness markets.

**Basis of Presentation**

Our consolidated financial statements include the accounts of Iteris, Inc. and its subsidiary and have been prepared in accordance with generally accepted accounting principles in the United States of America ("GAAP"). All 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 a discontinued operation. See Note 3, "Sale of Vehicle Sensors," for further discussion related to the discontinued operation presentation.



**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2018****1. Description of Business and Summary of Significant Accounting Policies (Continued)****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 collectability of accounts receivable and related allowance for doubtful accounts, projections of taxable income used to assess realizability of deferred tax assets, warranty reserves, costs to complete long-term contracts, indirect cost rates used in cost plus contracts, the valuation of purchased intangible assets and goodwill, the valuation of equity instruments, estimates of future cash flows used to assess the recoverability of long-lived assets and the impairment of goodwill, and fair value of our stock option awards used to calculate the stock-based compensation.

**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 under the terms of the arrangement 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.

Transportation Systems revenues are derived primarily from long-term contracts with governmental agencies. Certain Agriculture and Weather Analytics revenues are also derived from long-term contracts with governmental agencies, as well as contracts with commercial companies. Agriculture and Weather Analytics revenues that are derived from contracts with commercial companies are generally from subscription revenue that we typically invoice our customers at the beginning of the term, in multiyear, annual, semi-annual or quarterly installments, and revenue is recognized ratably over the period of the subscription beginning once all requirements for revenue recognition have been met, including provisioning the service so that it is available to our customers. When appropriate, 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. 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 revenues, when their realization is reasonably assured. Certain of our revenues are recognized as services are performed and amounts are earned, which is measured by time incurred or other contractual milestones or output measures. Revenues accounted for in this manner generally relate to certain fixed fee professional services, cost plus fixed fee, or time and materials contracts. Revenues for ongoing operations and maintenance services contracts are generally accounted for ratably as the services are performed throughout the term of the contract. Payments received in advance of services performed are deferred and recognized when the related services are performed.

**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2018****1. Description of Business and Summary of Significant Accounting Policies (Continued)**

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 stand-alone 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.

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 and adjustments for contract closeout settlements.

**Unbilled Accounts Receivable**

Unbilled accounts receivable in the accompanying audited consolidated balance sheets represent unbilled amounts earned and reimbursable under services sales arrangements, including approximately \$1.5 million of costs and estimated earnings in excess of billings on uncompleted contracts as of March 31, 2018, accounted for under Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 605-35, *Construction-Type and Production-Type Contracts* ("ASC 605-35"). 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.

**Deferred Revenue**

Deferred revenue 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, including approximately \$1.5 million of billings in excess of costs and estimated earnings on uncompleted contracts accounted for under FASB ASC 605-35. The unearned amounts are expected to be earned within the next twelve months.

**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.

**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2018****1. Description of Business and Summary of Significant Accounting Policies (Continued)**

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 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 the Middle East, Europe, South America and Asia. We generally do not require collateral or other security from our domestic customers. We maintain an allowance for doubtful accounts for potential credit losses, which losses have historically been within management's expectations.

We currently have, and historically have had, a diverse customer base. For the fiscal years ended March 31, 2018 ("Fiscal 2018") and March 31, 2017 ("Fiscal 2017"), one individual customer represented approximately 22% of our total revenues, respectively, and no other individual customer represented greater than 10% of our total revenues. . For the fiscal year ended March 31, 2016 ("Fiscal 2016"), no individual customer represented greater than 10% of our total revenues.

**Fair Values of Financial Instruments**

The fair value of cash equivalents, receivables, accounts payable and accrued expenses approximate carrying value because of the short period of time to maturity. Our investments are measured at fair value on a recurring basis.

The framework for measuring fair value and related disclosure requirements about fair value measurements are provided in ASC 820, *Fair Value Measurements* ("ASC 820"). This pronouncement defines fair value as the price that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The fair value hierarchy proscribed by ASC 820 contains three levels as follows:

Level 1—Quoted prices in active markets for identical assets or liabilities.

Level 2—Observable inputs other than quoted prices in active markets for identical assets or liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3—Inputs that are generally unobservable and typically reflect management's estimate of assumptions that market participants would use in pricing the asset or liability.

**Cash and Cash Equivalents**

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

**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2018****1. Description of Business and Summary of Significant Accounting Policies (Continued)****Investments**

The Company's investments are classified as either held-to-maturity, available-for-sale or trading, in accordance with FASB ASC 320. Held-to-maturity securities are those securities that the Company has the positive intent and ability to hold until maturity. Trading securities are those securities that the Company intends to sell in the near term. All other securities not included in the held-to-maturity or trading category are classified as available-for-sale. Held-to-maturity securities are recorded at amortized cost which approximates fair market value. Trading securities are carried at fair value with unrealized gains and losses charged to earnings. Available-for-sale securities are carried at fair value with unrealized gains and losses recorded within accumulated other comprehensive loss as a separate component of stockholders' equity. FASB ASC 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. FASB ASC 820 also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs, where available (see Note 5). Under FASB ASC 320-10-35, a security is considered to be other-than-temporarily impaired if the present value of cash flows expected to be collected are less than the security's amortized cost basis (the difference being defined as the "Credit Loss") or if the fair value of the security is less than the security's amortized cost basis and the investor intends, or will be required, to sell the security before recovery of the security's amortized cost basis. If an other-than-temporary impairment exists, the charge to earnings is limited to the amount of Credit Loss if the investor does not intend to sell the security, and will not be required to sell the security, before recovery of the security's amortized cost basis. Any remaining difference between fair value and amortized cost is recognized in other comprehensive loss, net of applicable taxes. The Company evaluates whether the decline in fair value of its investments is other-than-temporary at each quarter-end. This evaluation consists of a review by management, and includes market pricing information and maturity dates for the securities held, market and economic trends in the industry and information on the issuer's financial condition and, if applicable, information on the guarantors' financial condition. Factors considered in determining whether a loss is temporary include the length of time and extent to which the investment's fair value has been less than its cost basis, the financial condition and near-term prospects of the issuer and guarantors, including any specific events which may influence the operations of the issuer and the Company's intent and ability to retain the investment for a reasonable period of time sufficient to allow for any anticipated recovery of fair value.

**Prepaid Expenses and Other Current Assets**

Prepaid expenses and other current assets were \$1.2 million as of March 31, 2018 and \$2.1 million as of March 31, 2017 and included approximately \$130,000 of cash designated as collateral on performance bonds, as required under certain of our Transportation Systems contracts in the Middle East. The performance bonds require us to maintain 100% cash value of the bonds as collateral in a bank that is local to the purchasing agency. The performance bond collateral is required throughout the delivery of our services and is maintained in the local bank until the contract is closed by the purchasing agency. We expect these requirements, and the related cash collateral restrictions, to be released during calendar year 2018.

**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2018****1. Description of Business and Summary of Significant Accounting Policies (Continued)****Allowance for Doubtful Accounts**

The collectability of our accounts receivable is evaluated through review of outstanding invoices 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 accounts 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 consist of finished goods, work-in-process and raw materials and are stated at the lower of cost or net realizable value. 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 perform an annual qualitative assessment of our goodwill during the fourth fiscal quarter, or more frequently, to determine if any events or circumstances exist, such as an adverse change in business climate or a decline in overall industry demand, that would indicate that it would more likely than not reduce the fair value of a reporting unit below its carrying amount, including goodwill. If events or circumstances do not indicate that the fair value of a reporting unit is below its carrying amount, then goodwill is not considered to be impaired and no further testing is required. If further testing is required, we perform a two-step process. The first step involves comparing the fair value of our reporting unit to its carrying value, including goodwill. If the carrying value of the reporting unit exceeds its fair value, the second step of the test is performed by comparing the carrying value of the goodwill in the reporting unit to its implied fair value. An impairment charge is recognized for the excess of the carrying value of goodwill over its implied fair value. We determine the fair values of our reporting units using the income valuation approach, as well as other generally accepted valuation methodologies.

In Fiscal 2017, we adopted the provisions issued by the FASB that were intended to simplify goodwill impairment testing. This guidance permits us to eliminate the second step of the goodwill impairment test, and eliminate the requirements for any reporting unit with a zero or negative carrying amount to perform a qualitative assessment. If the carrying amount of a reporting unit exceeds the reporting unit's fair value, the amount by which the carrying value of the goodwill exceeds its implied fair value, if any, is recognized as an impairment loss. We monitor the indicators for goodwill impairment testing between annual tests. As of March 31, 2018, we determined that no adjustments to the carrying value of goodwill and intangible assets were required. As of March 31, 2017, we

**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2018****1. Description of Business and Summary of Significant Accounting Policies (Continued)**

determined the carrying amount of the goodwill in the Agriculture and Weather Analytics reporting unit exceeded its implied fair value, and as a result, recognized an approximate \$2.2 million impairment loss in the accompanying consolidated financial statements. We also determined that no adjustments to the carrying value of goodwill and intangible assets were required in the Roadway Sensors and Transportation Systems reporting units for any year presented.

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 or asset group is 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. As of March 31, 2018, there was no impairment to our long-lived and intangible assets.

**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. As such, we determined it was appropriate to record a valuation allowance of approximately \$10.1 million in the third quarter of Fiscal 2016 against our deferred tax assets. We will continuously reassess the appropriateness of maintaining a valuation allowance.

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 our consolidated 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.

**Iteris, Inc.**

**Notes to Consolidated Financial Statements (Continued)**

**March 31, 2018**

**1. Description of Business and Summary of Significant Accounting Policies (Continued)**

**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 revenues in the period during which the products ship.

**Sales Taxes**

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

**Advertising Expenses**

Advertising costs are expensed in the period incurred and totaled \$148,000, \$146,000, and \$164,000 in Fiscal 2018, Fiscal 2017 and Fiscal 2016, 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.

**Comprehensive Loss**

The difference between net loss and comprehensive loss was de minimis for Fiscal 2018. Comprehensive loss equaled net loss for Fiscal 2017 and Fiscal 2016.

**Recent Accounting Pronouncements**

In May 2014, the FASB issued Accounting Standards Update ("ASU") No. 2014-09, *Revenue from Contracts with Customers* ("ASU 2014-09"). The new revenue recognition standard ("ASC 606") provides a five-step analytical framework for transactions to determine when and how revenue is recognized. The core principle is that a company should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the

**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2018****1. Description of Business and Summary of Significant Accounting Policies (Continued)**

entity expects to be entitled in exchange for those goods or services. The two permitted transition methods under the new standard are the full retrospective method or the modified retrospective method. We are required to adopt this standard effective April 1, 2018.

We plan to adopt this standard using the modified retrospective method with an immaterial adjustment to accumulative deficit for the cumulative effect of adoption. Our assessment process has consisted of reviewing current accounting policies and practices to identify potential differences that would result from applying the requirements of the new standard to our revenue contracts. We have reviewed individual customer contracts and purchase orders related to these revenues streams as well as identified appropriate changes to our business processes, systems and controls to support the revenue recognition and disclosure requirements under the new standard. We believe that the new standard and related revenue recognition policies will not result in a material change to our consolidated financial statements, but will require additional disclosures in our financial statements as to the nature, amount and timing of revenue and cash flows arising from contracts with customers.

In December 2016, the FASB issued ASU No. 2016-20, *Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers* ("ASU 2016-20"), which allows entities not to make quantitative disclosures about remaining performance obligations in certain cases and requires entities that use any of the new or previously existing optional exemptions to expand their qualitative disclosures. The new standard is effective for fiscal years, and interim periods within those years, beginning after December 15, 2017, with early adoption permitted. The adoption of ASU 2016-20 is not expected to have a material impact on our consolidated financial statements.

In January 2016, the FASB issued ASU No. 2016-01, *Financial Instruments—Overall: Recognition and Measurement of Financial Assets and Financial Liabilities* ("ASU 2016-01"). This standard revises an entity's accounting related to (1) the classification and measurement of investments in equity securities and (2) the presentation of certain fair value changes for financial liabilities measured at fair value. It also amends certain disclosure requirements associated with the fair value of financial instruments. Under the new guidance, entities will have to measure certain equity investments at fair value and recognize any changes in fair value in net income unless the investments qualify for a new practicality exception. ASU 2016-01 is effective for financial statements issued for fiscal years beginning after December 15, 2017 and interim periods within those fiscal years. We are currently evaluating the impact of ASU 2016-01 on our consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases* ("ASU 2016-02"). The pronouncement requires an entity to recognize assets and liabilities for the rights and obligations created by leases on the entity's balance sheet for both finance and operating leases. For leases with a term of 12 months or less, an entity can elect to not recognize lease assets and lease liabilities and expense the lease over a straight-line basis for the term of the lease. ASU 2016-02 will require new disclosures that depict the amount, timing, and uncertainty of cash flows pertaining to an entity's leases. Companies are required to adopt the new standard using a modified retrospective approach for annual and interim periods beginning after December 15, 2018. Early adoption of ASU 2016-02 is permitted. The Company expects adoption to increase the assets and liabilities recorded on its consolidated balance sheet and increase the level of disclosures related to leases. We are currently evaluating the impact of ASU 2016-02 on our consolidated financial statements.



## Iteris, Inc.

## Notes to Consolidated Financial Statements (Continued)

March 31, 2018

## 1. Description of Business and Summary of Significant Accounting Policies (Continued)

In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments* ("ASU 2016-15"), which clarifies how certain cash receipts and cash payments are presented and classified in the statement of cash flows. The new standard is effective for fiscal years, and interim periods within those years, beginning after December 15, 2017, and early adoption is permitted. The adoption of ASU 2016-15 is not expected to have a material impact on our consolidated financial statements.

In November 2016, the FASB issued ASU No. 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash* ("ASU 2016-18"), requiring restricted cash and cash equivalents to be included with cash and cash equivalents on the statement of cash flows. The new standard is effective for fiscal years, and interim periods within those years, beginning after December 15, 2017, with early adoption permitted. The adoption of ASU 2016-18 is not expected to have a material impact on our consolidated financial statements.

In May 2017, the FASB issued ASU No. 2017-09, *Compensation—Stock Compensation: Scope of Modification Accounting* ("ASU 2017-09"). The amendments in ASU 2017-09 provide guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in ASC 718 Compensation—Stock Compensation. The adoption of ASU 2017-09, which will become effective for annual periods beginning after December 15, 2017, is not expected to have a material impact on our consolidated financial statements.

In March 2018, the FASB issued ASU 2018-05, *Income Taxes (Topic 740), Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118* ("ASU 2018-05"). ASU 2018-05 adds various Securities and Exchange Commission ("SEC") paragraphs pursuant to the issuance of the December 2017 SEC Staff Accounting Bulletin No. 118, *Income Tax Accounting Implications of the Tax Cuts and Jobs Act* ("SAB 118"), which was effective immediately. The SEC issued SAB 118 to address concerns about reporting entities' ability to timely comply with the accounting requirements to recognize all of the effects of the Tax Cuts and Jobs Act in the period of enactment. SAB 118 allows disclosure that timely determination of some or all of the income tax effects from the Tax Cuts and Jobs Act are incomplete by the due date of the financial statements and if possible to provide a reasonable estimate. The Company has accounted for the tax effects of the Tax Cuts and Jobs Act under the guidance of SAB 118, on a provisional basis. The Company's accounting for certain income tax effects is incomplete, but the Company has determined reasonable estimates for those effects and has recorded provisional amounts in its consolidated financial statements as of March 31, 2018.

## 2. Supplementary Financial Information

## Inventories

The following table presents details regarding our inventories:

	March 31,	
	2018	2017
	(In thousands)	
Materials and supplies	\$ 1,745	\$ 887
Work in process	232	298
Finished goods	944	1,065
	<u>\$ 2,921</u>	<u>\$ 2,250</u>

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

2. Supplementary Financial Information (Continued)

Property and Equipment, net

The following table presents details of our property and equipment, net:

	March 31,	
	2018	2017
	(In thousands)	
Equipment	\$ 6,053	\$ 7,078
Leasehold improvements	2,880	2,494
Accumulated depreciation	(6,600)	(7,508)
	<u>\$ 2,333</u>	<u>\$ 2,064</u>

Depreciation expense was approximately \$819,000, \$729,000, and \$649,000 in Fiscal 2018, Fiscal 2017 and Fiscal 2016, respectively. Approximately \$288,000, \$269,000, and \$252,000 of the depreciation expense was recorded to cost of revenues, and approximately \$531,000, \$397,000 and \$300,000 was recorded to operating expenses in Fiscal 2018, Fiscal 2017 and Fiscal 2016, respectively, in the consolidated statements of operations.

Intangible Assets

The following table presents details regarding our intangible assets:

	March 31,			
	2018		2017	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
	(In thousands)			
Technology	\$ 1,856	\$ (1,856)	\$ 1,856	\$ (1,828)
Customer contracts / relationships	750	(750)	750	(726)
Trade names and non-compete agreements	1,110	(1,102)	1,110	(1,066)
Capitalized software development costs	5,108	(1,365)	2,158	(756)
Total	<u>\$ 8,824</u>	<u>\$ (5,073)</u>	<u>\$ 5,874</u>	<u>\$ (4,376)</u>

Amortization expense for intangible assets subject to amortization was approximately \$726,000, \$623,000, and \$526,000 for Fiscal 2018, Fiscal 2017 and Fiscal 2016, respectively. Approximately \$638,000, \$342,000, and \$166,000 of the intangible asset amortization was recorded to cost of revenues, and approximately \$88,000, \$281,000, and \$360,000 was recorded to amortization expense for Fiscal 2018, Fiscal 2017 and Fiscal 2016, respectively, in the consolidated statements of operations.

We do not have any intangible assets with indefinite useful lives. As of March 31, 2018, our net capitalized software development costs of approximately \$3.8 million is associated with our Oracle ERP development of approximately \$2.3 million, which has a useful life of 10 years beginning Fiscal 2019; as

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

2. Supplementary Financial Information (Continued)

well as our Agriculture and Weather Analytics and Roadway Sensors segments, which have an average useful life of three years. The future estimated amortization expense is as follows:

<u>Year Ending March 31,</u> <u>(In thousands)</u>	
2019	\$ 1,076
2020	807
2021	339
2022	244
2023	244
Thereafter	1,041
	<u>\$ 3,751</u>

Goodwill

The following table presents the activity related to the carrying value of our goodwill by reportable segment for Fiscal 2016, Fiscal 2017 and Fiscal 2018:

	<u>Roadway Sensors</u>	<u>Transportation Systems</u>	<u>Ag &amp; Weather Analytics</u>	<u>Total</u>
	<u>(In thousands)</u>			
Balance—March 31, 2016				
Goodwill	\$ 8,214	\$ 14,906	\$ 2,168	\$ 25,288
Accumulated impairment losses	—	(7,970)	—	(7,970)
	<u>\$ 8,214</u>	<u>\$ 6,936</u>	<u>\$ 2,168</u>	<u>\$ 17,318</u>
Balance—March 31, 2017				
Goodwill	\$ 8,214	\$ 14,906	\$ 2,168	\$ 25,288
Accumulated impairment losses	—	(7,970)	(2,168)	(10,138)
	<u>8,214</u>	<u>6,936</u>	<u>—</u>	<u>15,150</u>
Balance—March 31, 2018				
Goodwill	\$ 8,214	\$ 14,906	\$ 2,168	\$ 25,288
Accumulated impairment losses	—	(7,970)	(2,168)	(10,138)
	<u>\$ 8,214</u>	<u>\$ 6,936</u>	<u>\$ —</u>	<u>\$ 15,150</u>

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

2. Supplementary Financial Information (Continued)

Warranty Reserve Activity

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

	Year Ended March 31,		
	2018	2017	2016
	(In thousands)		
Balance at beginning of fiscal year	\$ 278	\$ 193	\$ 181
Additions charged to cost of sales	623	382	236
Warranty claims	(498)	(297)	(224)
Balance at end of fiscal year	<u>\$ 403</u>	<u>\$ 278</u>	<u>\$ 193</u>

Earnings Per Share

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

	Year Ended March 31,		
	2018	2017	2016
	(In thousands, except per share amounts)		
Numerator:			
Loss from continuing operations	<u>\$ (3,768)</u>	<u>\$ (5,187)</u>	<u>\$ (12,535)</u>
Denominator:			
Weighted average common shares used in basic computation	32,776	32,174	32,049
Dilutive stock options	—	—	—
Dilutive restricted stock units	—	—	—
Dilutive warrants	—	—	—
Weighted average common shares used in diluted computation	<u>32,776</u>	<u>32,174</u>	<u>32,049</u>
Loss from continuing operations per share:			
Basic	<u>\$ (0.12)</u>	<u>\$ (0.16)</u>	<u>\$ (0.39)</u>
Diluted	<u>\$ (0.12)</u>	<u>\$ (0.16)</u>	<u>\$ (0.39)</u>

**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2018****2. Supplementary Financial Information (Continued)**

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

	<b>Year Ended March 31,</b>		
	<b>2018</b>	<b>2017</b>	<b>2016</b>
	<b>(In thousands)</b>		
Stock options	3,917	3,491	3,220
Restricted stock units	228	179	186

**3. Sale of Vehicle Sensors**

On July 29, 2011, we completed the sale of substantially all of our assets used in connection with our prior Vehicle Sensors segment to Bendix Commercial Vehicle Systems LLC ("Bendix"), a member of Knorr-Bremse Group. In connection with the asset sale, 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 85% of revenue associated with royalties received under our license and distribution agreements with Audiovox Electronics Corporation and Valeo Schalter and Sensoren GmbH through December 31, 2017, subject to certain reductions and limitations set forth in the asset purchase agreement. From the date of the asset sale, through March 31, 2018, we received approximately \$2.6 million in connection with royalty-related earn-outs provisions for a total of \$17.9 million in cash from the asset sale.

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. For the fiscal year ended March 31, 2018, 2017 and 2016, we recorded a gain on sale of discontinued operation of approximately \$242,000, \$361,000, and \$214,000, respectively, net of tax, related to the earn-out provisions of the asset purchase agreement.

**4. 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.

Based on our goodwill impairment testing for Fiscal 2018, we determined our Roadway Sensors and Transportation Systems reporting units were not impaired as of March 31, 2018, as the estimated fair values of our reporting units exceeded their carrying values at the end of such fiscal years. Based on our goodwill impairment testing for Fiscal 2017, we believe the carrying value of our goodwill in our Agriculture and Weather Analytic reporting unit was impaired as of March 31, 2017, and resulted in approximately \$2.2 million impairment charge. We also determined our Roadway Sensors and Transportation Systems reporting units were not impaired as of March 31, 2017. Based on our goodwill impairment testing for Fiscal 2016, we believe the carrying value of our goodwill was not impaired. If our actual financial results, or the plans and estimates used in future goodwill impairment analyses, are lower than our original estimates used to assess impairment of our goodwill, we could incur goodwill impairment charges in the future.

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

5. 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—Quoted prices in active markets for identical assets or liabilities.

Level 2—Observable inputs other than quoted prices in active markets for identical assets or liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3—Inputs that are generally unobservable and typically reflect management's estimate of assumptions that market participants would use in pricing the asset or liability.

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, 2018 or 2017. 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. In Fiscal 2018, Level 3 inputs were used to evaluate the fair value of our goodwill in our two reporting units that had goodwill balances. In Fiscal 2017, Level 3 inputs were used to evaluate the fair value of our goodwill in our three reporting units. As a result of our impairment testing, we recorded an adjustment for impairment of approximately \$2.2 million in our Agriculture and Weather Analytics reporting unit. No other non-financial assets were measured at fair value during the fiscal years ended March 31, 2018, 2017, and 2016.

The following tables present the Company's financial assets that are recorded at fair value on a recurring basis, segregated among the appropriate levels within the fair value hierarchy:

	As of March 31, 2018			
	Amortized Cost	Gross Unrealized Loss	Gross Unrealized Gain	Estimated Fair Value
	(In thousands)			
Level 1:				
Money market funds	666	—	—	666
Subtotal	666	—	—	666
Level 2:				
Commercial paper	1,891	—	—	1,891
Corporate notes and bonds	2,008	(2)	—	2,006
US Treasuries	1,500	(1)	—	1,499
US Government agencies	2,950	(1)	—	2,949
Subtotal	8,349	(4)	—	8,345
Total	9,015	(4)	—	9,011

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

6. Credit Facility

We had a \$12.0 million revolving line of credit with California Bank & Trust ("CB&T"), which expired on October 1, 2016. We chose not to renew our line of credit as we do not foresee a need to utilize credit within the next twelve months.

7. Income Taxes

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

	Year Ended March 31,		
	2018	2017	2016
	(In thousands)		
Loss from continuing operations before income taxes	\$ (5,586)	\$ (5,231)	\$ (3,456)
Current income tax provision:			
Federal	\$ 3	\$ 71	\$ 170
State	45	62	50
Total current tax provision	48	133	220
Deferred income tax (benefit) provision:			
Federal	(1,849)	(166)	8,289
State	(17)	(11)	570
Total deferred tax (benefit) provision	(1,866)	(177)	8,859
(Benefit) provision for income taxes on continuing operations	(1,818)	(44)	9,079
Loss from continuing operations, net of tax	<u>\$ (3,768)</u>	<u>\$ (5,187)</u>	<u>\$ (12,535)</u>

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

	Year Ended March 31,		
	2018	2017	2016
	(In thousands)		
(Benefit) for income taxes at statutory rates	\$ (1,720)	\$ (1,778)	\$ (1,175)
Change in federal tax rate	4,134	—	—
State income taxes net of federal benefit	(255)	(124)	(184)
Impairment charges	—	737	—
Tax credits	(567)	(125)	(258)
Compensation charges	(324)	29	91
Change in valuation allowance	(3,153)	1,148	10,557
Other	67	69	48
(Benefit) provision for income taxes	<u>\$ (1,818)</u>	<u>\$ (44)</u>	<u>\$ 9,079</u>

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

7. Income Taxes (Continued)

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

	March 31,	
	2018	2017
	(In thousands)	
Deferred tax assets:		
Net operating losses	\$ 2,853	\$ 830
Capitalized R&D	2,734	5,003
Credit carry forwards	2,043	2,387
Deferred compensation and payroll	1,603	2,064
Bad debt allowance and other reserves	567	820
Deferred rent	235	313
Property and equipment	844	521
Other, net	203	255
Total deferred tax assets	11,082	12,193
Valuation allowance	(9,814)	(11,726)
Total deferred tax assets, net of valuation allowance	1,268	467
Deferred tax liabilities:		
Acquired intangibles	(866)	(467)
Goodwill	(467)	(707)
Total deferred tax liabilities	(1,333)	(1,174)
Net deferred tax liabilities	\$ (65)	\$ (707)

At March 31, 2018, we had \$1.1 million in federal Alternative Minimum Tax credit carryforwards that were reclassified from a deferred tax asset to a noncurrent income tax receivable as we expect this amount to be refunded over the next four years. We also had \$1.5 million in federal research credits that begin to expire in 2031 and \$703,000 in state tax credits that begin to expire in 2023. We had \$6.8 million of federal net operating loss carryforwards at March 31, 2018 that do not expire as a result of recent tax law changes. We had \$5.6 million of federal net operating loss carryforwards at March 31, 2018 that begin to expire in 2022. We also had \$4.4 million of state net operating loss carryforwards at March 31, 2018 that begin to expire in 2031.

Our deferred tax assets at March 31, 2017 did not include approximately \$1.1 million of excess tax benefits from employee stock option exercises that were a component of our net operating loss carryforwards. Due to the adoption of ASU 2016-09 in Fiscal 2018, this amount was recognized through accumulated deficit, offset by a corresponding amount of valuation allowance, resulting in no net impact to accumulated deficit.

In assessing the realizability of our deferred tax assets, we review 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 the Company has sustained a cumulative pre-tax loss over the trailing three years, we considered it appropriate to maintain valuation allowances of \$9.8 million and \$11.7 million against our deferred tax assets at March 31, 2018 and



**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2018****7. Income Taxes (Continued)**

2017, respectively. We will continuously reassess the appropriateness of maintaining a valuation allowance.

The Tax Cuts and Jobs Act ("tax legislation") was enacted on December 22, 2017 and reduced U.S. corporate income tax rates to 21.0% as of January 1, 2018. The rate change became effective during Fiscal 2018 resulting in a blended statutory tax rate of 30.8% for Fiscal 2018. As a consequence of the tax legislation, the Company recorded a decrease in its net deferred tax assets of \$4.1 million and a decrease in the valuation allowance maintained against its deferred tax assets of \$5.8 million. The estimated impact of the tax legislation was an income tax benefit of \$1.7 million, of which \$1.1 million was due to the release of valuation allowance that had been maintained against Alternative Minimum Tax credit carryforwards, which were made refundable by the tax legislation, and \$640,000 was due to the remeasurement of a deferred tax liability related to indefinite-lived assets.

On December 22, 2017, the SEC issued guidance under Staff Accounting Bulletin No. 118, Income Tax Accounting Implications of the Tax Cuts and Jobs Act ("SAB 118") directing taxpayers to consider the impact of the tax legislation as "provisional" when it does not have the necessary information available, prepared or analyzed (including computations) in reasonable detail to complete its accounting for the change in tax law. In accordance with SAB 118, the income tax effects discussed above represent the Company's best estimate based on its current interpretation of this tax legislation. The Company is accumulating data to finalize the underlying calculations and evaluate other aspects of this tax legislation, or in certain cases, the U.S. Treasury is expected to issue further guidance on the application of certain provisions of the tax legislation. In accordance with SAB 118, the income tax effects of the tax legislation discussed above are considered provisional and will be finalized in Fiscal 2019.

**Unrecognized Tax Benefits**

As of March 31, 2018 and 2017, our gross unrecognized tax benefits were \$586,000 and \$426,000, respectively, of which \$461,000 and \$286,000, respectively, are netted against certain noncurrent deferred tax assets. The amounts that would affect our effective tax rate if recognized are \$513,000 and \$359,000, respectively.

We recognize interest and/or penalties related to income tax matters in income tax expense. As of March 31, 2018 and 2017, we had accrued cumulatively \$43,000 and \$46,000, respectively, for the payment of potential interest and penalties. The total amount of interest and penalties recognized in the consolidated statements of operations for the fiscal years ended March 31, 2018 and 2017 was \$(3,000) and \$(6,000), respectively.

**Iteris, Inc.**

**Notes to Consolidated Financial Statements (Continued)**

**March 31, 2018**

**7. Income Taxes (Continued)**

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

	<b>Year Ended March 31,</b>		
	<b>2018</b>	<b>2017</b>	<b>2016</b>
	<b>(In thousands)</b>		
Gross unrecognized tax benefits at beginning of year	\$ 426	\$ 394	\$ 319
Increases for tax positions taken in prior years	62	18	22
Decreases for tax positions taken in prior years	—	(8)	—
Increases for tax positions taken in the current year	122	59	68
Lapse in statute of limitations	(24)	(37)	(15)
Gross unrecognized tax benefits at March 31	<u>\$ 586</u>	<u>\$ 426</u>	<u>\$ 394</u>

We do not anticipate a significant change in gross unrecognized tax benefits within the next twelve months. We are subject to taxation in the U.S. and various state tax jurisdictions. We are subject to U.S. federal tax examination for fiscal tax years ended March 31, 2015 or later, and state and local income tax examination for fiscal tax years ended March 31, 2014 or later. However, if NOL carryforwards that originated in earlier tax years are utilized in the future, the amount of such NOLs from such earlier years remain subject to review by tax authorities.

**8. Commitments and Contingencies**

**Litigation and Other Contingencies**

As a provider of traffic engineering services, hardware products, software and other various solutions for the traffic and agricultural industries, the Company is, and may in the future from time to time, be involved in litigation relating to claims arising out of its operations in the normal course of business. While the Company cannot accurately predict the outcome of any such litigation, except as described below, the Company is not a party to any legal proceeding, the outcome of which, in management's opinion, individually or in the aggregate, would have a material effect on the Company's consolidated results of operations, financial position or cash flows.

On September 15, 2016, a stockholder class action and derivative action (captioned *Ionni v. Bergera, et al.*, Case No. 16-cv00807-RGA) was filed in the United States District Court for the District of Delaware (the "Court") against certain of the Company's current and former directors and officers (the "Individual Defendants") and the Company as a nominal defendant (together with the Individual Defendants, the "Defendants"). The complaint asserted claims for breach of fiduciary duty and unjust enrichment. Plaintiff contended that, in 2014 and 2015, the Individual Defendants caused the Company to issue purportedly false and misleading proxy statements in connection with the Company's annual meeting of stockholders in 2014 and 2015 (collectively, the "Proxy Statements"). In those Proxy Statements, the Company's stockholders were asked to approve amendments (the "Amendments") to increase the number of shares of the Company's common stock reserved for issuance under the Iteris, Inc. 2007 Omnibus Incentive Plan (the "2007 Plan"). Among other things, Plaintiff alleged that the Proxy Statements were materially false and misleading because they affirmatively represented that no person could receive more than 500,000 stock options or SARs under the 2007 Plan in any fiscal

**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2018****8. Commitments and Contingencies (Continued)**

year (the "Share Limit") and failed to disclose that the Compensation Committee had the discretion to approve an annual grant to a 2007 Plan participant in excess of that amount. Plaintiff contended that, the Amendments were not valid and sought rescission of any stock options granted pursuant to the Amendments, including the option to purchase up to 1,350,000 shares of the Company's common stock that was granted in September 2015 to Mr. Bergera (the "CEO Option") in connection with his appointment to serve as President and Chief Executive Officer of the Company.

The Individual Defendants denied that they breached their fiduciary duties and the Company believed (and still believes) the Amendments were properly approved and that all of the options granted pursuant to the Amendments, including the CEO Option, were valid. Nonetheless, to eliminate the burden, expense and uncertainty of the litigation, on November 8, 2016, the parties entered into a Memorandum of Understanding setting forth their agreement in principle to resolve the litigation. In consideration for a release of claims and dismissal of this litigation with prejudice, the Company agreed to submit a proposal at its 2016 Annual Meeting of Stockholders seeking stockholder approval for that portion of the CEO Option that exceeds the Share Limit (i.e., the 850,000 options above the Share Limit (the "Excess Shares")). The Company submitted a proposal of the Excess Shares for approval by the Company stockholders at the 2016 Annual Meeting of Stockholders. On December 15, 2016, the Company's stockholders approved the Excess Shares.

On April 28, 2017, the parties entered into a Stipulation of Settlement and Compromise (the "Stipulation") that provides for, among other things, a release of claims against Defendants. Under the Stipulation, Defendants agreed not to oppose any award of attorneys' fees and expenses to Plaintiff up to \$215,000. The Court approved the settlement and entered a final judgment dismissing the action with prejudice on September 8, 2017, and the settlement became effective on October 10, 2017. Pursuant to the settlement terms, Defendants paid \$215,000 in October 2017. An immaterial accrued liability for the settlement was included in the accompanying consolidated balance sheet as of March 31, 2017, which was sufficient to cover the settlement payment.

**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 increased each year thereafter, to \$120,000 per month during the last year of the lease. In February 2014, we entered into an amendment to the lease, which reduced our office space by approximately 11,000 square feet and changed the lease term to 96 months, commencing on April 1, 2014. The monthly lease rate is approximately \$76,000 during the first year of the amended term and increases each year thereafter, up to a maximum of approximately \$90,000 during the last year of the term. Additionally, the lease amendment provided for approximately \$328,000 in incentives in the form of tenant improvement allowances, which we recorded as fixed assets and deferred rent in our consolidated balance sheet. The leasehold improvements were capitalized into fixed assets during Fiscal 2015 and will be depreciated over the estimated useful life of the improvements, or the term of the lease amendment, whichever is shorter. The corresponding deferred rent amount will reduce monthly rent expense over the term of the lease amendment. On January 23, 2017, we entered into an amendment to the lease, which added approximately 5,980 square feet and will expire after 60 months,

**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2018****8. Commitments and Contingencies (Continued)**

commencing on April 1, 2017. The monthly lease rate is approximately \$14,000 during the first year of the term and increase each year thereafter, up to a maximum of approximately \$16,000 during the last year of the term. Additionally, the lease amendment provided for approximately \$119,000 in incentives in the form of tenant improvement allowances.

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, 2018 were as follows:

<u>Year Ending March 31,</u> <u>(In thousands)</u>	
2019	\$ 2,185
2020	1,936
2021	1,836
2022	1,725
2023	295
Thereafter	—
	<u>\$ 7,977</u>

Rent expense totaled approximately \$1.8 million for Fiscal 2018, and \$1.7 million for each of Fiscal 2017 and Fiscal 2016.

**Related Party Transaction**

We previously subleased office space to Maxxess Systems, Inc. ("Maxxess"), one of our former subsidiaries that we sold in September 2003. The sublease terminated in September 2007, at which time Maxxess owed us an aggregate of \$274,000. Maxxess executed a promissory note for such amount, which was subsequently amended and restated on July 23, 2013 and on August 11, 2016. The amended and restated note bears interest at a rate of 6% per annum, compounded annually, with accrued interest payable annually on the first business day of each calendar year. When authorized by the Company, Maxxess may pay down the balance of this note by providing consulting services to Iteris. We have previously fully reserved for amounts owed to us by Maxxess and the outstanding principal balance remains fully reserved. As of March 31, 2018, approximately \$146,000 of the original principal balance was outstanding and payable to Iteris. Maxxess is currently owned by an investor group that includes, among others, one former Iteris director, who has not been a director of Iteris since September 2013, and one existing director of Iteris, who currently owns less than 2% of Maxxess' capital stock.

**9. 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

**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2018****9. Stockholders' Equity (Continued)**

dividend, conversion, voting, redemption and liquidation rights. As of March 31, 2018 and 2017, 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 (as amended in August 2012) 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 Reserved for Future Issuance**

The following summarizes common stock reserved for future issuance at March 31, 2018:

	<u>Number of Shares</u> <u>(In thousands)</u>
Stock options outstanding	4,124
Restricted stock units outstanding	144
Authorized for future issuance under stock incentive plans	1,496
	<u>5,764</u>

**10. 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. 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 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. In September 2012, 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 2,450,000 shares. In October 2014, our stockholders approved an amendment of the 2007 Plan to increase the number of shares of common stock authorized for issuance under the 2007 Plan by an additional 1,500,000 shares to a total of 3,950,000 shares. In September 2015, our stockholders approved an

**Iteris, Inc.**

**Notes to Consolidated Financial Statements (Continued)**

**March 31, 2018**

**10. Employee Benefit Plans (Continued)**

amendment of the 2007 Plan to increase the number of shares of common stock authorized for issuance under the 2007 Plan by an additional 1,000,000 shares to a total of 4,950,000 shares. In December 2016, our stockholders approved the 2016 Omnibus Incentive Plan (the "2016 Plan") which allows for the issuance of stock options, stock appreciation rights, restricted stock, RSUs", cash incentive awards and other stock-based awards 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. Stock appreciation rights, restricted stock, RSUs and other stock-based awards are based on the value of our common stock. New shares are issued to satisfy stock option exercises and share issuances under the 2016 Plan.

We currently maintain both the 2007 Plan and the 2016 Plan. Of these plans, we may only grant future awards from the 2016 Plan. As of the 2016 Annual Meeting of Stockholders, no future shares could be granted under the 2007 Plan. At March 31, 2018, there were approximately 1.5 million shares of common stock available for grant under the 2016 plan. As of March 31, 2018, options to purchase approximately 2,309,000 shares of common stock, as well as 45,000 RSUs, were outstanding under the 2007 Plan and options to purchase approximately 1,816,000 shares of common stock, as well as 99,000 RSUs, were outstanding under the 2016 Plan.

**Stock Options**

A summary of activity in the Plans with respect to our stock options for Fiscal 2018 is as follows:

	<b>Options</b>	<b>Weighted</b>	<b>Weighted</b>	<b>Aggregate</b>
	<b>(In thousands)</b>	<b>Average</b>	<b>Average</b>	<b>Intrinsic</b>
		<b>Exercise</b>	<b>Remaining</b>	<b>Value</b>
		<b>Price Per</b>	<b>Contractual</b>	<b>(In thousands)</b>
		<b>Share</b>	<b>Life</b>	
			<b>(Years)</b>	
Options outstanding at March 31, 2017	3,776	\$ 2.76		
Granted	1,103	5.59		
Exercised	(591)	2.02		
Forfeited	(164)	4.00		
Expired	—	—		
Options outstanding at March 31, 2018	4,124	\$ 3.58	8.1	\$ 6,394
Options exercisable at March 31, 2018	1,616	\$ 2.45	7.0	\$ 4,049
Vested and expected to vest at March 31, 2018	4,124	\$ 3.58	8.1	\$ 6,394
Options exercisable at March 31, 2018 pursuant to a change-in-control	4,124	\$ 3.58	8.1	\$ 6,394

**Restricted Stock Units**

RSU awards are stock-based awards that entitle the holder to receive one share of our common stock for each RSU upon vesting. RSUs granted under the 2007 Plan 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

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

10. Employee Benefit Plans (Continued)

by the 2007 Plan) as of the vesting date. RSUs granted under the 2016 Plan vest at varying terms between one and four anniversaries of the grant date provided that the holder remains in service (as defined by the 2016 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.

A summary of activity with respect to our RSUs for Fiscal 2018 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, 2017	232	\$ 3.84		
Granted	73	6.40		
Vested	(134)	4.06		
Forfeited	(27)	4.88		
RSUs outstanding at March 31, 2018	144	\$ 4.72	1.9	\$ 167
Expected to vest at March 31, 2018	144	\$ 4.72	1.9	\$ 167
Common stock issuable (for RSUs) at March 31, 2018 upon a change-in-control	144	\$ 4.72	1.9	\$ 167

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,		
	2018	2017	2016
	(In thousands)		
Cost of revenues	\$ 71	\$ 51	\$ 42
Selling, general and administrative expense	1,558	858	567
Research and development expense	152	67	50
Total stock-based compensation	\$ 1,781	\$ 976	\$ 659

At March 31, 2018, there was approximately \$4.6 million and \$578,000 of unrecognized compensation expense related to unvested stock options and RSUs, respectively. This expense is currently expected to be recognized over a weighted average period of approximately 2.8 years for stock options and 1.8 years for RSUs. 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.

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

10. Employee Benefit Plans (Continued)

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

	Year Ended March 31,		
	2018	2017	2016
Expected life—years	6.5	6.5	7.2
Risk-free interest rate	2.7%	2.2%	1.9%
Expected volatility of common stock	43%	40%	47%
Dividend yield	—%	—%	—%

*Expected Life:* The Company's expected life represents the weighted-average period that the Company's stock options are expected to be outstanding. The expected life is based on expected time to post-vesting exercise of options by employees. The Company uses historical exercise patterns of previously granted options to derive employee behavioral patterns used to forecast expected exercise patterns.

*Risk-Free Interest Rate:* The risk-free interest rate is based on the U.S. Treasury zero coupon yield curve in effect at the time of grant for the expected term of the option.

*Expected Volatility:* The Company uses historical volatility as it provides a reasonable estimate of the expected volatility. Historical volatility is based on the most recent volatility of the stock price over a period of time equivalent to the expected term of the option.

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

	Year Ended March 31,		
	2018	2017	2016
	(In thousands, except per share amounts)		
Weighted average grant date fair value per share of options granted	\$ 2.59	\$ 2.11	\$ 1.19
Intrinsic value of options exercised	\$ 2,469	\$ 1,061	\$ 135

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, 2018, 2017 and 2016.

We sponsor a defined contribution 401(k) plan (the "401(k) Plan"), adopted in 1990, under which eligible associates voluntarily contribute to the plan, up to IRS maximums, through payroll deductions. We match up to 50% of contributions, up to a stated limit, with all matching contributions being fully vested after three years of service. Our matching contributions under the 401(k) Plan were approximately \$1,067,000, \$881,000, and \$716,000 for the fiscal years ended March 31, 2018, 2017 and 2016, respectively.



**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2018****10. Employee Benefit Plans (Continued)****Other Stock-Based Compensation Plans**

Beginning January 1, 2018, the Company offers an Employee Stock Purchase Plan ("ESPP") which allows employees to have a percentage of their base compensation withheld to purchase the Company's common stock at 95% of the fair market on the last trading day of the offering period. There are two offering periods during a calendar year, which consist of the six months beginning each January 1 and July 1. Employees may contribute 1-15% of their eligible gross pay up to a \$25,000 annual stock value limit. There were no share purchases in Fiscal 2018. The ESPP is considered a non-compensatory plan and accordingly no compensation expense is recorded in connection with this benefit.

**11. Stock Repurchase Program**

In August 2011, our Board of Directors approved a stock repurchase program pursuant to which we were authorized to acquire up to \$3 million of our outstanding common stock from time to time through August 2012. We repurchased approximately 964,000 shares under this original program for a total purchase price of \$1.3 million. On August 9, 2012, our Board of Directors cancelled the initial stock repurchase program and the approximate \$1.7 million of remaining funds, and approved a new stock repurchase program pursuant to which we may acquire up to \$3 million of our outstanding common stock for an unspecified length of time. Under the new program, we may repurchase shares from time to time in open market and privately negotiated transactions and block trades, and may also repurchase shares 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 or terminate the repurchase program at any time without prior notice. On November 6, 2014, our Board of Directors approved a \$3.0 million increase to the Company's existing stock repurchase program, pursuant to which the Company may continue to acquire shares of its outstanding common stock from time to time for an unspecified length of time.

For our fiscal years ended March 31, 2018 and 2017, we did not repurchase any shares. For our fiscal year ended March 31, 2016, we repurchased approximately 656,000 shares of our common stock. From inception of the program in August 2011 through March 31, 2018, we repurchased approximately 3,422,000 shares of our common stock for an aggregate price of approximately \$5.6 million, at an average price per share of \$1.63. As of March 31, 2018, all repurchased shares have been retired and returned to their status as authorized and unissued shares of our common stock. As of March 31, 2018, approximately \$1.7 million remains available for the repurchase of our common stock under our current program.

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

12. Investments

Our investments consisted of the following:

	As of March 31, 2018			
	Amortized Cost	Gross Unrealized Loss	Gross Unrealized Gain	Estimated Fair Value
	(In thousands)			
Cash and cash equivalents	\$ 3,692	\$ —	\$ —	\$ 3,692
Short term investments	5,323	(4)	—	5,319
Long term investments	—	—	—	—
Total	\$ 9,015	\$ (4)	\$ —	\$ 9,011

Unrealized losses related to these investments are due to interest rate fluctuations as opposed to credit quality. In addition, we do not intend to sell, and it is not more likely than not that we would be required to sell, these investments before recovery of their cost basis. As a result, there is no other-than-temporary impairment for these investments as of March 31, 2018.

The following table summarizes the contractual maturities of our investments at March 31, 2018:

Maturity break out:	As of March 31, 2018	
	Amortized Cost	Fair Value
(In thousands)		
Due within one year	\$ 9,015	\$ 9,011
Due within two years	—	—
Total	<u>\$ 9,015</u>	<u>\$ 9,011</u>

13. Business Segments, Significant Customer and Geographic Information

Business Segments

We currently operate in three reportable segments: Roadway Sensors, Transportation Systems, and Agriculture and Weather Analytics.

The Roadway Sensors segment provides various advanced detection sensors and systems for traffic intersection management, communication systems and roadway traffic data collection applications. The Roadways Sensors product line uses advanced image processing technology and other techniques to capture and analyze sensor data through sophisticated algorithms, enabling vehicle, bicycle and pedestrian detection, as well as the transmission of both video images and data using various communication technologies. Our Roadway Sensors products include, among others, Vantage, VantageLive!, VantageNext, VantagePegasus, VantageRadius, Vantage Vector, Velocity, SmartCycle, SmartCycle Bike Indicator, SmartSpan, VersiCam, PedTrax and P-Series products.

The Transportation Systems segment provides engineering and consulting services, performance measurement and traffic analytics solutions, as well as the development of transportation management and traveler information systems for the ITS industry. Our Transportation Systems services include planning, design, implementation, operation and management of surface transportation infrastructure

**Iteris, Inc.**

**Notes to Consolidated Financial Statements (Continued)**

**March 31, 2018**

**13. Business Segments, Significant Customer and Geographic Information (Continued)**

systems. We perform analysis and study goods movement, commercial vehicle operations, provide travel demand forecasting and systems engineering, and identify mitigation measures to reduce traffic congestion. Our Transportation Systems product line includes: iPeMS, our performance measurement and information management solution as well as our commercial vehicle operations and vehicle safety compliance platforms known as CVIEW Plus, CheckPoint, UCRLink and inspect.

The Agriculture and Weather Analytics segment includes ClearPath Weather, our road maintenance applications, and ClearAg, our digital agriculture platform. Our ClearPath Weather suite of tools, such as tools for assessing historical weather conditions to both short-term and long-range weather forecasts and customizable route/site weather and pavement forecast tools, provide winter road maintenance recommendations for state agencies, municipalities and for commercial companies that allow such users to create solutions to meet roadway maintenance decision needs. Our ClearAg solutions combine weather and agronomic data with proprietary land-surface modeling and analytics to solve complex agricultural problems. Our ClearAg solutions include our ClearAg applications, ClearAg APIs and components, WeatherPlot mobile application, and ClearAg Insights applications.

The accounting policies of our reportable segments are the same as those described in the summary of significant accounting policies (Note 1). Certain corporate general and administrative expenses, including general overhead functions such as information systems, accounting, human resources, marketing, compliance costs and certain administrative expenses, as well as interest and amortization of intangible assets, are not allocated to the segments. The reportable segments are each managed separately because they manufacture and distribute distinct products or provide services with different processes. All reported segment revenues are derived from external customers. Our Chief Executive Officer, who is our chief operating decision maker ("CODM"), reviews financial information at the operating segment level. Our CODM does not review assets by segment in his resource allocation, and therefore, assets by segment are not disclosed below.

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

13. Business Segments, Significant Customer and Geographic Information (Continued)

Selected financial information for our reportable segments for the fiscal years ended March 31, 2018, 2017 and 2016 is as follows:

	Roadway Sensors	Transportation Systems	Agriculture and Weather Analytics	Total
	(In thousands)			
<b>Year Ended March 31, 2018</b>				
Product revenues	\$ 44,163	\$ 2,301	\$ —	\$ 46,464
Service revenues	194	52,180	4,891	57,265
Revenues	44,357	54,481	4,891	103,729
Depreciation	221	204	109	534
Segment income (loss)	8,825	8,639	(8,048)	9,416
<b>Year Ended March 31, 2017</b>				
Product revenues	42,059	1,676	—	43,735
Service revenues	111	47,594	4,542	52,247
Revenues	42,170	49,270	4,542	95,982
Depreciation	180	191	131	502
Loss from continuing operations before income taxes	—	—	2,168	2,168
Segment income (loss)	9,799	8,482	(9,557)	8,724
<b>Year Ended March 31, 2016</b>				
Product revenues	39,923	1,810	—	41,733
Service revenues	336	32,286	3,393	36,015
Revenues	40,259	34,096	3,393	77,748
Depreciation	152	175	122	449
Segment income (loss)	\$ 8,401	\$ 4,170	\$ (6,140)	\$ 6,431

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

	Year Ended March 31,		
	2018	2017	2016
	(In thousands)		
<b>Segment income:</b>			
Total income from reportable segments	\$ 9,416	\$ 8,724	\$ 6,431
<b>Unallocated amounts:</b>			
Corporate and other expenses	(14,930)	(13,680)	(9,541)
Amortization of intangible assets	(88)	(281)	(360)
Other (expense) income, net	(16)	(7)	2
Interest income, net	32	13	12
Loss from continuing operations before income taxes	\$ (5,586)	\$ (5,231)	\$ (3,456)

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

13. Business Segments, Significant Customer and Geographic Information (Continued)

Significant Customer and Geographic Information

One individual customer who is also a government agency had a receivable balance of 13% of our total trade accounts receivable balance as of March 31, 2018. No individual customer or government agency had a receivable balance at March 31, 2017 or 2016 greater than 10% of our total trade accounts receivable balances as of March 31, 2017 and 2016, respectively.

The following table sets forth the percentages of our 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,		
	2018	2017	2016
Canada	1%	1%	—%
Europe	1	1	—
Middle East	—	—	1
	<u>2%</u>	<u>2%</u>	<u>1%</u>

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

14. Quarterly Financial Data (Unaudited)

Quarter Ended:	Revenues	Gross Profit	Net (Loss) Income	Basic Net Income/Loss per Share	Diluted Net Income/Loss per Share
	(In thousands, except per share amounts)				
June 30, 2017	\$ 27,183	\$ 9,905	\$ (470)	\$ (0.02)	\$ (0.02)
September 30, 2017	25,248	9,968	(984)	(0.03)	(0.03)
December 31, 2017	26,025	9,943	343	0.01	0.01
March 31, 2018	25,273	10,015	(2,415)	(0.07)	(0.07)
	<u>\$ 103,729</u>	<u>\$ 39,831</u>	<u>\$ (3,526)</u>	<u>\$ (0.11)**</u>	<u>\$ (0.11)**</u>
June 30, 2016	\$ 23,927	\$ 9,409	\$ (38)	\$ (0.00)	\$ (0.00)
September 30, 2016	24,060	9,455	(40)	(0.00)	(0.00)
December 31, 2016	22,691	8,620	(1,380)	(0.04)	(0.04)
March 31, 2017	25,304	9,918	(3,368)*	(0.10)	(0.10)
	<u>\$ 95,982</u>	<u>\$ 37,402</u>	<u>\$ (4,826)</u>	<u>\$ (0.15)**</u>	<u>\$ (0.15)**</u>

\* Net Loss includes a goodwill impairment charge of approximately \$2.2 million related to our Agriculture and Weather Analytics reporting unit. Refer to Note 4 for additional discussion regarding the goodwill impairment charge.

\*\* 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.

## 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 Exchange Act, as of the end of the period covered by this Annual Report on Form 10-K, management evaluated, with the participation of our President and Chief Executive Officer, and our 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 significant change in our internal controls over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during the fourth quarter of Fiscal 2018 that has materially affected, or is reasonably likely to materially affect, our internal controls 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.

### Management's Report on Internal Control Over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f) and 15d-15(f). Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in Internal Control—Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our evaluation under the framework in *Internal Control—Integrated Framework (2013)*, our management concluded that our internal control over financial reporting was effective as of March 31, 2018. The effectiveness of

our internal control over financial reporting as of March 31, 2018 has been audited by Deloitte & Touche LLP, an independent registered public accounting firm, as stated in their report, which is included herein.

## **ITEM 9B. OTHER INFORMATION**

On June 5, 2018, the Board of Directors amended the Bylaws by adding a Section 5 to Article VI (General Provisions) in order to adopt the necessary provisions relating to professional engineers required by the state of Washington.

The information set forth above is included herewith for the purpose of providing the disclosure required under "Item 5.03—Amendments to Articles of Incorporation or Bylaws; Change in Fiscal Year" of Form 8-K. The foregoing description of the amendment to the Bylaws is only a summary and is qualified in its entirety by reference to the full Restated Bylaws, which are filed as Exhibit 3.3 to this Annual Report on Form 10-K and incorporated by reference herein.

## **PART III**

## **ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

The information required by Item 10 will be either (i) included in an amendment to this Annual Report on Form 10-K ("the Form 10-K Amendment) or (ii) incorporated by reference to our Definitive Proxy Statement to be filed with the SEC in connection with our 2018 Annual Meeting of Stockholders (the "2018 Proxy Statement") under the headings "Executive Compensation and Other Information—Executive Officers," "Election of Directors," "Corporate Governance," and "Section 16(a) Beneficial Ownership Reporting Compliance."

## **ITEM 11. EXECUTIVE COMPENSATION**

The information required by Item 11 will be either included in the Form 10-K Amendment or is incorporated by reference to our 2018 Proxy Statement under the heading "Executive Compensation and Other Information—Executive Officers."

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

The information required by Item 12 will be either included in the Form 10-K Amendment or is incorporated by reference to our 2018 Proxy Statement under the heading "Equity Compensation Plan Information" and "Principal Stockholders and Common Stock Ownership of Certain Beneficial Owners and Management."

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

The information required by Item 13 will be either included in the Form 10-K Amendment or is incorporated by reference to our 2018 Proxy Statement under the heading "Corporate Governance" and "Certain Transactions."

## **ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES**

The information required by Item 14 will be either included in the Form 10-K Amendment or is incorporated by reference to our 2018 Proxy Statement under the heading "Fees Paid to Independent Registered Public Accounting Firm."

**PART IV****ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES**

(a) Documents filed as part of this report:

1. *Financial Statements.*

Our consolidated financial statements are listed in the "Index to Consolidated Financial Statements" under Part II, Item 8, of this Annual Report.

2. *Financial Statement Schedules.*

All financial statement schedules have been omitted because they are not required or are not applicable, or the required information is shown in our consolidated financial statements or the notes thereto.

3. *Exhibits.*

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:

**Exhibit Index**

<b>Exhibit Number</b>	<b>Description</b>	<b>Reference</b>
2.2+	<a href="#">Asset Purchase Agreement by and between Iteris, Inc. and Bendix Commercial Vehicle Systems LLC, dated as of July 25, 2011</a>	<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	<a href="#">Restated Certificate of Incorporation of the registrant</a>	<i>Exhibit 3.1 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>
3.2	<a href="#">Certificate of Designations of Series A Junior Participating Preferred Stock</a>	<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	<a href="#">Restated Bylaws of the registrant, as amended through June 5, 2018</a>	<i>Filed herewith</i>
4.1	<a href="#">Specimen of common stock certificate</a>	<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	<a href="#">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</a>	<i>Exhibit 4.1 to the registrant's Current Report on Form 8-K as filed with the SEC on August 21, 2009</i>



Exhibit Number	Description	Reference
4.3	<a href="#">Amendment No. 1 to Rights Agreement, entered into as of August 8, 2012 by and between Iteris, Inc. and Computershare Trust Company, N.A.</a>	Exhibit 4.1 to the registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2012 as filed with the SEC on August 10, 2012
10.1	Form of Indemnity Agreement entered into by the registrant and certain of its officers and directors	Exhibit 19.4 to the registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 1988
10.2	<a href="#">Form of Indemnification Agreement entered into by the registrant and certain of its officers and directors</a>	Exhibit 10.5 to the registrant's Annual Report on Form 10-K for the year ended March 31, 2004 as filed with the SEC on June 29, 2004
10.3	<a href="#">Office Lease, dated May 24, 2007, by and between the registrant and Realty Associates Fund X, L.P. (as the successor to Crown Carnegie Associates, LLC)</a>	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
10.4*	<a href="#">Iteris, Inc. Employee Stock Purchase Plan</a>	Filed herewith
10.5*	<a href="#">2007 Omnibus Incentive Plan</a>	Exhibit 10.19 to the registrant's Annual Report on Form 10-K for the year ended March 31, 2012 as filed with the SEC on June 11, 2012
10.6*	<a href="#">Forms of Stock Option Agreements under the 2007 Omnibus Incentive Plan</a>	Exhibit 10.20 to the registrant's Annual Report on Form 10-K for the year ended March 31, 2012 as filed with the SEC on June 11, 2012
10.7*	<a href="#">Form of Restricted Stock Unit Award Agreement under the 2007 Omnibus Incentive Plan</a>	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
10.8*	<a href="#">2016 Omnibus Incentive Plan</a>	Filed herewith
10.9*	<a href="#">Form of Restricted Stock Unit Issuance Agreement for use with 2016 Omnibus Incentive Plan</a>	Exhibit 99.2 to the registrant's Registration Statement on Form S-8 (File No.333-216407) as filed with the SEC on March 2, 2017
10.10*	<a href="#">Form of Form of Notice of Grant of Stock Option and form of Stock Option Agreement for use with 2016 Omnibus Incentive Plan</a>	Exhibit 99.3 to the registrant's Registration Statement on Form S-8 (File No.333-216407) as filed with the SEC on March 2, 2017
10.11	<a href="#">Amended and Restated Promissory Note, effective July 23, 2013, by and between Maxxess Systems, Inc. in favor of Iteris, Inc.</a>	Exhibit 10.1 to the registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2013 as filed with the SEC on August 1, 2013
10.12	<a href="#">First Amendment to Lease, dated February 21, 2014, by and between RREF II Freeway Acquisitions, LLC and Iteris, Inc.</a>	Exhibit 10.29 to the registrant's Annual Report on Form 10-K for the year ended March 31, 2014 as filed with the SEC on September 4, 2014.

Exhibit Number	Description	Reference
10.13	<a href="#">Second Amendment to Lease, dated September 29, 2014, by and between Realty Associates Fund X, L.P. and Iteris, Inc. (as the successor to Realty Associate RREF II Freeway Acquisitions, LLC) and Iteris, Inc.</a>	<i>Filed herewith</i>
10.14	<a href="#">Third Amendment to Lease, dated December 15, 2016, by and between Realty Associates Fund X, L.P. and Iteris, Inc.</a>	<i>Filed herewith</i>
10.15*	<a href="#">Employment Agreement dated March 9, 2015 between Iteris, Inc. and Andrew Schmidt</a>	<i>Exhibit 10.1 to the registrant's Current Report on Form 8-K as filed with the SEC on March 15, 2015</i>
10.16*	<a href="#">Amendment 1 to Employment Agreement dated June 12, 2017 between Iteris, Inc. and Andrew Schmidt</a>	<i>Exhibit 10.33 to the registrant's Annual Report on Form 10-K for the year ended March 31, 2016 as filed with the SEC on June 13, 2017.</i>
10.17*	<a href="#">Employment Agreement dated September 8, 2015 between Iteris, Inc. and Joe Bergera</a>	<i>Exhibit 10.1 to the registrant's Current Report on Form 8-K as filed with the SEC on September 22, 2015</i>
10.18	<a href="#">Seperation Agreement and General Release dated March 29, 2018 between Iteris, Inc. and Thomas N. Blair</a>	<i>Exhibit 99.1 to Amendment No. 1 to the registrant's Current Report on Form 8-K as filed with the SEC on April 5, 2018</i>
21	<a href="#">List of Subsidiaries</a>	<i>Filed herewith</i>
23	<a href="#">Consent of Independent Registered Public Accounting Firm, dated June 7, 2018</a>	<i>Filed herewith</i>
24	<a href="#">Power of Attorney</a>	<i>Filed herewith (included on the Signature page)</i>
31.1	<a href="#">Certification of the Chief Executive Officer, as required pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</a>	<i>Filed herewith</i>
31.2	<a href="#">Certification of the Chief Financial Officer, as required pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</a>	<i>Filed herewith</i>
32.1	<a href="#">Certification of the Chief Executive Officer, as required pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</a>	<i>Filed herewith</i>
32.2	<a href="#">Certification of the Chief Financial Officer, as required pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</a>	<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>

Exhibit Number	Description	Reference
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 contract, compensatory plan or arrangement in which directors or executive officers of the registrant are eligible to participate.

+ Confidential treatment has been previously granted by the SEC for certain portions of the referenced 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.

## 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 7, 2018

ITERIS, INC.  
(Registrant)

By /s/ JOE BERGERA

JOE BERGERA  
Chief Executive Officer  
(Principal Executive Officer)

## POWER OF ATTORNEY

We, the undersigned officers and directors of Iteris, Inc., do hereby constitute and appoint Joe Bergera and Andrew C. Schmidt, 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, as amended, 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>
<div>/s/ JOE BERGERA</div> <div>Joe Bergera</div>	Director, President and Chief Executive Officer (principal executive officer)	June 7, 2018
<div>/s/ ANDREW C. SCHMIDT</div> <div>Andrew C. Schmidt</div>	Chief Financial Officer (principal financial and accounting officer)	June 7, 2018
<div>/s/ THOMAS L. THOMAS</div> <div>Thomas L. Thomas</div>	Chairman of the Board	June 7, 2018
<div>/s/ LAURA L. SIEGAL</div> <div>Laura L. Siegal</div>	Director	June 7, 2018

<u>Signature</u>	<u>Title</u>	<u>Date</u>
<div>/s/ KEVIN C. DALY, PH.D</div> <div>_____ Kevin C. Daly, Ph.D</div>	Director	June 7, 2018
<div>/s/ GERARD M. MOONEY</div> <div>_____ Gerard M. Mooney</div>	Director	June 7, 2018
<div>/s/ SCOTT E. DEETER</div> <div>_____ Scott E. Deeter</div>	Director	June 7, 2018
<div>/s/ MIKEL WILLIAMS</div> <div>_____ Mikel Williams</div>	Director	June 7, 2018



**RESTATED BYLAWS  
OF  
ITERIS, INC.**  
(hereinafter called the "Corporation")  
(As amended through June 5, 2018)

**ARTICLE I  
OFFICES**

**Section 1.**        **Registered Office.**

The Board of Directors shall fix the location of the principal executive office of the Corporation at any place within or outside the State of Delaware. The registered office of the Corporation shall be in the City of Wilmington, County of New Castle, State of Delaware.

**Section 2.**        **Other Offices.**

The Corporation may also have offices at such other places both within and without the State of Delaware as the Board of Directors may from time to time determine.

**ARTICLE II  
MEETINGS OF STOCKHOLDERS**

**Section 1.**        **Place of Meetings.**

Meetings of stockholders shall be held at any place within or outside the State of Delaware designated by the Board of Directors. In the absence of any such designation, meetings of stockholders shall be held at the principal executive office of the Corporation.

**Section 2.**        **Annual Meeting.**

The annual meeting of stockholders shall be held at such date and time as the Board of Directors may determine. The annual meeting shall be held at the Corporation's principal executed office, or at any other location as may be determined by the Board of Directors. At each annual meeting, directors shall be elected and any other proper business may be transacted.

**Section 3.**        **Special Meetings.**

Special meetings of the stockholders may be called at any time by the Board of Directors, by the chairman of the board, by the president or by one or more stockholders holding shares in the aggregate entitled to cast not less than 10% of the votes at that meeting.

If a special meeting is called by any person or persons other than the Board of Directors, the request shall be in writing, specifying the time of such meeting and the general nature of the business proposed to be transacted, and shall be delivered personally or sent by registered mail or by telegraphic or other facsimile transmission to the chairman of the board, the president, any vice-president, or the secretary of the Corporation. The officer receiving the request shall promptly cause notice to be given to the stockholders entitled to vote, in accordance with the provisions of Sections 4 and 5 of this Article II, that a meeting will be held at the time requested

by the person or persons calling the meeting, not fewer than 35 or more than 60 days after the receipt of the request. If such notice is not given within 20 days after the receipt of the request, the person or persons requesting the meeting may give the notice. Nothing contained in this paragraph of this Section 3 shall be construed as limiting, fixing or affecting the time when a meeting of stockholders called by action of the Board of Directors may be held.

**Section 4.**        **Notice of Meetings of Stockholders.**

All notices of meetings of stockholders shall be sent or otherwise given in accordance with Section 5 of this Article II not fewer than ten or more than 60 days before the date of the meeting. Such notice shall specify the place, date and hour of the meeting and (i) in the case of a special meeting, the general nature of the business to be transacted, or (ii) in the case of the annual meeting, those matters that the Board of Directors, at the time of giving the notice, intends to present for action by the stockholders. The notice of any meeting at which directors are to be elected shall include the name of any nominee or nominees whom, at the time of the notice, management intends to present for election.

If action is proposed to be taken at any meeting for approval of (i) a contract or transaction in which a director has a direct or indirect financial interest, pursuant to Section 144 of the General Corporation Law of the State of Delaware (the "Delaware GCL"), (ii) an amendment of the Certificate of Incorporation, pursuant to Section 242 of the Delaware GCL, (iii) a reorganization of the Corporation pursuant to Section 251 of the Delaware GCL, (iv) a voluntary dissolution of the Corporation pursuant to Section 275 of the Delaware GCL, or (v) a distribution in dissolution, other than in accordance with the rights of outstanding preferred shares, pursuant to Section 275 of the Delaware GCL, the notice shall also state the general nature of that proposal.

**Section 5.**        **Manner of Giving Notice; Affidavit of Notice.**

Notice of any meeting of stockholders shall be given either personally or by mail or telegraphic or other written communication, charges prepaid, addressed to each stockholder at the address of such stockholder appearing on the books of the Corporation or given by the stockholder to the Corporation for the purpose of notice. If no such address appears on the books of the Corporation or is given, notice shall be deemed to have been given if sent to a stockholder by first-class mail or telegraphic or other written communication to the Corporation's principal executive office, or if published at least-once in a

newspaper of general circulation in the county where such office is located. Notice shall be deemed to have been given at the time when delivered personally or deposited in the mail or sent by telegram or other means of written communication.

If any notice addressed to a stockholder at the address of such stockholder appearing on the books of the Corporation is returned to the Corporation by the United States Postal Service marked to indicate that the United States Postal Service is unable to deliver such notice to such stockholder at such address, each future notice and report shall be deemed to have been duly given without further mailing if it shall be available to the stockholder on written demand by the shareholder at the principal executive office of the Corporation for a period of one year from the date of the giving of such notice or report.

An affidavit of the mailing or other means of giving any notice of any meeting of stockholders shall be executed by the secretary, assistant secretary or any transfer agent of the Corporation giving the notice and shall be filed and maintained in the minute book of the Corporation.

Section 6. Quorum.

The presence in person or by proxy of the holders of a majority of the shares entitled to vote at a meeting of stockholders shall constitute a quorum for the transaction of business at such meeting. The stockholders present at a duly called or held meeting at which a quorum is present may continue to do business until adjournment, notwithstanding the withdrawal of enough stockholders to leave less than a quorum, if any action taken (other than adjournment) is approved by at least a majority of the shares required to constitute a quorum.

Section 7. Adjourned Meeting; Notice.

Any meeting of stockholders, annual or special, whether or not a quorum is present, may be adjourned from time to time by the vote of the majority of the shares represented at such meeting, either in person or by proxy; but in the absence of a quorum, no other business may be transacted at such meeting, except as provided in Section 6 of this Article II.

When any meeting of stockholders, annual or special, is adjourned to another time or place, notice need not be given of the adjourned meeting if the time and place are announced at a meeting at which the adjournment is taken, unless a new record date for the adjourned meeting is fixed or unless the adjournment is for more than 45 days from the date set for the original meeting, in which case the Board of Directors shall set a new record date. Notice of any such adjourned meeting shall be given to each stockholder of record entitled to vote at the adjourned meeting in accordance with the provisions of Sections 4 and 5 of this Article II. At any adjourned meeting any business may be transacted that might have been transacted at the original meeting.

Section 8. Voting.

The stockholders entitled to vote at any meeting of the stockholders shall be determined in accordance with the provisions of Article V, Section 5, subject to the provisions of Section 217 of the Delaware GCL (relating to voting shares held by a fiduciary, or in joint ownership). Unless otherwise required by law, the Certificate of Incorporation or these Bylaws, any question brought before any meeting of stockholders at which a quorum is present shall be decided by the vote of the holders of a majority of the stock represented and entitled to vote thereat. Unless otherwise required by law, the Certificate of Incorporation or these Bylaws, each stockholder represented at a meeting of stockholders shall be entitled to cast one vote for each share of the capital stock entitled to vote thereat held by such stockholder [and shall not be entitled to cumulate votes in the election of directors](1).

---

(1) The bracketed language was approved by the Corporation's Board of Directors on May 15, 2018, but such language will not become effective unless and until the Corporation's stockholders approve the removal of cumulative voting from the Corporation's Certificate of Incorporation.

Every person entitled to vote for directors or on any other matter shall have the right to do so either in person or by one or more agents authorized by a written proxy signed by the person and filed with the secretary of the Corporation. A proxy shall be deemed signed if the stockholder's name is placed on the proxy (whether by manual signature, typewriting, telegraphic transmission, or otherwise) by the stockholder or the stockholder's attorney in fact. A validly executed proxy which does not state that it is irrevocable shall continue in full force and effect unless (i) revoked by the person executing it, before the vote pursuant to that proxy, by a writing delivered to the Corporation stating that the proxy is revoked, or by a subsequent proxy executed by, or attendance at the meeting and voting in person by, the person executing the proxy; or (ii) written notice of the death or incapacity of the maker of that proxy is received by the Corporation before the vote pursuant to that proxy is counted; provided, however, that no proxy shall be valid after the expiration of three years from the date of the proxy, unless otherwise provided in the proxy. The revocability of a proxy that states on its face that it is irrevocable shall be governed by the provisions of Section 212 of the Delaware GCL.

At any meeting of stockholders, the stockholders' vote may be by voice vote or by ballot; provided, however, that any election for directors must be by ballot if demanded by any stockholder before the voting has begun. On any matter other than elections of directors, any stockholder may vote part of the shares in favor of the proposal and refrain from voting the remaining shares or vote them against the proposal, but, if the stockholder fails to specify the number of shares which the stockholder is voting affirmatively, it will be conclusively presumed that the stockholder's approving vote is with respect to all shares that the stockholder is entitled to vote.

Section 9. Consent of Stockholders in Lieu Meeting.

Unless otherwise provided in the Certificate of Incorporation, any action required or permitted to be taken at any meeting of stockholders of the Corporation, may be taken without a meeting, without prior notice and without a vote, if a consent in writing, setting forth the action so taken, shall be signed by the holders of outstanding shares having not less than the minimum number of votes that would be necessary to authorize or take such action at a meeting at which all shares entitled to vote thereon were present and voted. In the case of election of directors, such a consent shall be effective only if signed by the holders of all outstanding shares entitled to vote for the election of directors; provided, however, that a director may be elected at any time to fill a vacancy on the Board of Directors that has not been filled by the directors, by the written consent of the holders of a majority of the outstanding shares entitled to vote for the election of directors. All such consents shall be filed with the secretary of the Corporation and shall be maintained in the corporate records. Any



stockholder giving a written consent, or the stockholder's proxy holders, or a transferee of the shares or a personal representative of the stockholder or their respective proxy holders, may revoke the consent by a writing received by the secretary of the Corporation before written consents of the number of shares required to authorize the proposed action have been filed with the secretary. Prompt notice of the taking of the corporate action without a meeting by less than unanimous written consent shall be given to those stockholders who have not consented in writing. This notice shall be given in the manner specified in Section 5 of this Article II.

Section 10. List of Stockholders Entitled to Vote.

The officer of the Corporation who has charge of the stock ledger of the Corporation shall prepare and make, at least ten days before every meeting of stockholders, a complete list of the stockholders entitled to vote at the meeting, arranged in alphabetical order, and showing the address of each stockholder and the number of shares registered in the name of each stockholder. Such list shall be open to the examination of any stockholder, for any purpose germane to the meeting, during ordinary business hours, for a period of at least ten days prior to the meeting, either at a place within the city where the meeting is to be held, which place shall be specified in the notice of the meeting, or, if not so specified, at the place where the meeting is to be held. The list shall also be produced and kept at the time and place of the meeting, during the whole time thereof, and may be inspected by any stockholder of the Corporation who is present.

Section 11. Stock Ledger.

The stock ledger of the Corporation shall be the only evidence as to who are the stockholders entitled to examine the stock ledger, the list required by Section 10 of this Article II or the books of the Corporation, or to vote in person or by proxy at any meeting of stockholders.

Section 12. Waiver of Notice or Consent by Absent Stockholders.

The transactions of any meeting of stockholders, annual or special, however called and noticed and wherever held, shall be as valid as though had at a meeting duly held after regular call and notice, if a quorum be present either in person or by proxy, and if, either before or after such meeting, each person entitled to vote, who was not present in person or by proxy, signs a written waiver of notice or a consent to a holding of such meeting or an approval of the minutes thereof. Such waiver of notice or consent need not specify either the business to be transacted or the purpose of any annual or special meeting of stockholders except that, if action is taken or proposed to be taken for approval of any of those matters specified in the second paragraph of Section 4 of this Article II, the waiver of notice or consent shall state the general nature of the proposal. All such waivers, consents or approvals shall be filed with the corporate records or made a part of the minutes of the meeting.

Attendance by a person at a meeting shall also constitute a waiver of notice of such meeting, except that when the person objects at the beginning of the meeting to the transaction of any business thereat because such meeting is not lawfully called or convened, and except that attendance at a meeting is not a waiver of any right to object to the consideration of matters not included in the notice of such meeting if an objection is expressly made at such meeting.

Section 13. Inspectors of Election.

Before any meeting of stockholders, the Board of Directors may appoint any persons other than nominees for office to act as inspectors of election at the meeting or its adjournment. If no inspectors of election are so appointed, the chairman of the meeting may, and on the request of any stockholder or a stockholder's proxy shall, appoint inspectors of election at the meeting. The number of such inspectors shall be either one or three. If such inspectors are appointed at a meeting on the request of one or more stockholders or proxies, the holders of a majority of shares or their proxies present at the meeting shall determine whether one or three inspectors are to be appointed. If any person appointed as inspector fails to appear or fails or

refuses to act, the chairman of the meeting may, and upon the request of any stockholder or a stockholder's proxy shall, appoint a person to fill that vacancy.

Such inspectors shall:

- (a) Determine the number of shares outstanding and the voting power of each, the shares represented at the meeting, the existence of a quorum, and the authenticity, validity, and effect of proxies;
- (b) Receive votes, ballots or consents;
- (c) Hear and determine all challenges and questions in any way arising in connection with the right to vote;
- (d) Count and tabulate all votes or consents;
- (e) Determine when the polls shall close;
- (f) Determine the result; and
- (g) Do any other acts that may be proper to conduct the election or vote with fairness to all stockholders.

Section 14. Advance Notice of Stockholder Business

Only business that has been properly brought before the stockholders meeting may be conducted at an annual meeting of the stockholders. To be properly brought before an annual stockholders meeting, business must be:

- (i) specified in the notice of meeting (or any supplement thereto) given by or at the direction of the Board of Directors;

(ii) otherwise properly brought before the stockholders meeting by or at the direction of the Board of Directors; or

(iii) a proper matter for stockholder action under the Delaware General Corporation Law that has been properly brought before the stockholders meeting by a stockholder (A) who is a stockholder of record on the date of the giving of the notice provided for in this Section 14 and on the record date for the determination of stockholders entitled to vote at such annual meeting of the stockholders and (B) who complies with the notice procedures set forth in this Section 14.

For such business to be considered properly brought before the meeting by a stockholder, such stockholder must, in addition to any other applicable requirements, have given timely notice in proper form of such stockholder's intent to bring such business before such meeting. To be timely, such stockholder's notice must:

(i) in the case of a proposal submitted for inclusion in the Corporation's proxy statement and form of proxy pursuant to Rule 14a-8 under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), meet the deadline for proposals submitted under such rule, or

6

---

(ii) in the case of all other matters, be delivered to or mailed and received by the secretary of the Corporation at the Corporation's principal executive offices not later than the close of business on the 90th day, nor earlier than the close of business on the 120th day, prior to the anniversary date of the immediately preceding annual meeting of the stockholders; provided, however, that in the event that no annual meeting of the stockholders was held in the previous year or the annual meeting of the stockholders is called for a date that is not within 30 days before or after such anniversary date, notice by the stockholder to be timely must be so received not later than the close of business on the 10th day following the day on which such notice of the date of the meeting was mailed or public disclosure of the date of the meeting was made, whichever occurs first.

To be in proper form, a stockholder's notice shall be in writing and shall set forth:

(i) the name and record address of the stockholder who intends to propose the business, the class or series and number of shares of capital stock of the Corporation which are owned beneficially or of record by such stockholder or any Associated Person (as defined below) of such stockholder and any other direct or indirect positions, agreements or understandings to which such stockholder or any Associated Person of such stockholder is a party (including hedged positions, short positions, options, derivatives, convertible securities and any other stock appreciation or voting interests) which provide the opportunity to profit or share in any profit derived from any increase or decrease in the value of the shares of the Corporation;

(ii) a representation that the stockholder is a holder of record of stock of the Corporation entitled to vote at such meeting and intends to appear in person or by proxy at the meeting to introduce the business specified in the notice;

(ii) a complete description of the business desired to be brought before the annual meeting of the stockholders and the reasons for conducting such business at the annual meeting of the stockholders;

(iv) any material interest of the stockholder or any Associated Person of such stockholder in such business including any agreements the stockholder or any Associated Person of such stockholder may have with others in connection with such business; and

(v) any other information that is required to be provided by the stockholder pursuant to Regulation 14A under the Exchange Act.

If any of the foregoing information changes in any material respect from the date the notice is received through the date of the meeting, the stockholder shall promptly supplement such information to reflect such change by notice in writing and delivered to or mailed and received by the secretary of the Corporation at the Corporation's principal executive offices.

For purposes of this Section 14 and Section 15, an "**Associated Person**" of any stockholder or proposed nominee shall mean (i) any member of the immediate family of such stockholder or proposed nominee sharing the same household with such stockholder or proposed nominee; (ii) any person controlling, controlled by, or under common control with, such stockholder or proposed nominee; (iii) any person acting in concert or as part of a group (within the meaning of the Exchange Act and the regulations promulgated thereunder) with such

7

---

stockholder or proposed nominee; or (iv) any beneficial owner of shares of stock of the Corporation owned of record or beneficially by such stockholder or proposed nominee.

In order to include information with respect to a stockholder proposal in the Corporation's proxy statement and form of proxy for a stockholders' meeting, stockholders must provide notice as required by, and otherwise comply with the requirements of, the Exchange Act and the regulations promulgated thereunder in addition to the requirements of this Section 14.

No business shall be conducted at the annual meeting of the stockholders except business brought before the annual meeting of the stockholders in accordance with the procedures set forth in this Section 14. The chairperson of the meeting may refuse to acknowledge the proposal of any business not made in compliance with the foregoing procedure.

#### Section 15. Advance Notice of Director Nominations.

Only persons who are nominated in accordance with the following procedures shall be eligible for election as directors, except as may be otherwise provided in the certificate of incorporation with respect to the right of holders of a class of preferred stock of the Corporation to nominate and elect a specified number of directors. To be properly brought before an annual meeting of the stockholders, or any special meeting of the stockholders called for the purpose of electing directors, nominations for the election of a director must be (i) specified in the notice of meeting (or any supplement thereto), (ii) made by or at the direction of the Board of Directors (or any duly authorized committee thereof) or (iii) made by any stockholder of the Corporation (A) who is a stockholder of

record on the date of the giving of the notice provided for in this Section 15 and on the record date for the determination of stockholders entitled to vote at such meeting and (B) who complies with the notice procedures set forth in this Section 15.

In addition to any other applicable requirements, for a nomination to be made by a stockholder, such stockholder must have given timely notice thereof in proper written form to the secretary of the Corporation. To be timely, a stockholder's notice to the secretary must be delivered to or mailed and received at the Corporation's principal executive offices, in the case of an annual meeting of the stockholders, in accordance with the provisions set forth in Section 14, and, the case of a special meeting of the stockholders called for the purpose of electing directors, not later than the close of business on the 10th day following the day on which notice of the date of the special meeting was mailed or public disclosure of the date of the special meeting was made, whichever occurs first.

To be in proper form, a stockholder's notice shall be in writing and shall set forth:

(i) as to each person whom the stockholder proposes to nominate for election as a director (A) the name, age, business address and residence address of the person, (B) the principal occupation or employment of the person, (C) the class or series and number of shares of capital stock of the Corporation which are owned beneficially or of record by the person or any Associated Person of the person, (D) any other direct or indirect positions, agreements or understandings to which such person or any Associated Person of such person is a party (including hedged positions, short positions, options, derivatives, convertible securities and any other stock appreciation or voting interests) which provide the opportunity to profit or share in any profit derived from any increase or decrease in the value of the shares of the Corporation, (E)

8

---

a description of all arrangements, understandings or material relationships between the stockholder and each nominee and any other person or persons (naming such person or persons) pursuant to which the nominations are to be made by the stockholder, and (F) any other information relating to such person that is required to be disclosed in solicitations of proxies for elections of directors, or is otherwise required, in each case pursuant to Regulation 14A under the Exchange Act (including without limitation such person's written consent to being named in the proxy statement, if any, as a nominee and to serving as a director if elected and a completed questionnaire concerning such person's business experience, beneficial ownership, relationships and transactions with the Corporation, independence and other matters typically contained in the Corporation's questionnaire for directors and officers); and

(ii) as to such stockholder giving notice, the information required to be provided pursuant to Section 14.

If any of the foregoing information changes in any material respect from the date the notice is received through the date of the meeting, the stockholder shall promptly supplement such information to reflect such change by notice in writing and delivered to or mailed and received by the secretary of the Corporation at the Corporation's principal executive offices.

Subject to the rights of any holders of a class of preferred stock of the Corporation, no person shall be eligible for election as a director of the Corporation unless nominated in accordance with the procedures set forth in this Section 15. If the chairperson of the meeting properly determines that a nomination was not made in accordance with the foregoing procedures, the chairperson shall declare to the meeting that the nomination was defective and such defective nomination shall be disregarded.

### ARTICLE III DIRECTORS

#### Section 1. Number, Election and Term of Directors.

The Board of Directors shall consist of not less than six (6) nor more than eleven (11) members, the exact number of which shall be six (6) until changed, within the limits specified above by a resolution duly adopted by the Board of Directors. The indefinite number of directors may be changed, or a definite number fixed without provisions for an indefinite number, by a bylaw amending this Section 1; provided, however, that an amendment reducing the number of directors to a number less than five cannot be adopted if the votes cast against its adoption at a meeting, or the shares not consenting in the case of action by written consent, are equal to more than 16-2/3% of the outstanding shares entitled to vote. At any meeting of stockholders at which directors may be elected, each director nominee shall be elected by an affirmative vote of a majority of the votes cast with respect to such director nominee by the stockholders entitled to vote in the election at a meeting at which a quorum is present, unless the number of nominees exceeds the number of directors to be elected, in which case each director nominee shall be elected by a plurality of the votes of the shares properly represented and entitled to vote in the election at such meeting. In the event that a nominee is already a director of the Corporation and does not receive a majority of the votes cast with respect to such nominee in an election where the number of nominees equals the number of directors to be elected, such nominee shall promptly tender his or her resignation to the Board of Directors for consideration.

9

---

Any director may resign at any time upon notice to the Corporation. Directors need not be stockholders.

#### Section 2. Vacancies.

Unless otherwise required by law or the Certificate of Incorporation, vacancies in the Board of Directors may be filled by a majority vote or written consent of the directors then in office, through less than a quorum, or by a sole remaining director, except that a vacancy created by the removal of a director by the vote or written consent of the shareholders or by court order may be filled only by the vote of a majority of the shares entitled to vote for such director represented at a duly held meeting at which a quorum is present, or by the written consent of holders of all shares entitled to vote for the election of such director. The directors so chosen shall hold office until the next annual election and until their successors are duly elected and qualified, or until their earlier resignation or removal.

The Board of Directors may increase the number of directors within the limits specified in Section 1 of this Article and any vacancy so created may be filled by the Board of Directors in accordance with the provisions of Article Ninth of the Certificate of Incorporation unless otherwise required by law.

A vacancy or vacancies in the Board of Directors shall be deemed to exist in the event of the death, resignation, or removal of any director, or if the Board of Directors by resolution declares vacant the office of a director who has been declared of unsound mind by an order of court or convicted of a felony, or if the authorized number of directors is increased, or if the stockholders fail, at any meeting of stockholders at which any director or directors are elected, to elect the number of directors to be voted for at that meeting.

Any director may resign effective on giving written notice to the chairman of the board, the president, the secretary, or the Board of Directors, unless the notice specifies a later time for that resignation to become effective. If the resignation of a director is effective at a future time, the Board of Directors may elect a successor to take office when the resignation becomes effective.

No reduction of the authorized number of directors shall have the effect of removing any director before that director's term of office expires.

### Section 3. Duties and Powers.

The business of the Corporation shall be managed by or under the direction of the Board of Directors which may exercise all such powers of the Corporation and do all such lawful acts and things as are not by statute or by the Certificate of Incorporation or by these Bylaws directed or required to be exercised or done by the stockholders,

### Section 4. Meetings.

The Board of Directors of the Corporation may hold meetings, both regular and special, either within or without the State of Delaware. Regular meetings of the Board of Directors may be held without notice at such time and at such place as may from time to time be determined by the Board of Directors. In the absence of such a determination, regular meetings shall be held at

10

---

the principal executive office of the Corporation. Special meetings of the Board of Directors may be called by the chairman, if there be one, the president, or a majority of the directors. Notice of special meetings stating the place, date and hour of the meeting shall be delivered personally or by telephone to each director or sent by first-class mail or telegram, charges prepaid, addressed to each director at that director's address as it is shown on the records of the Corporation. In case the notice is mailed, it shall be deposited in the United States mail at least four days before the time of the holding of the meeting. In case the notice is delivered personally, or by telephone or telegram, it shall be delivered personally or by telephone or to the telegraph company at least 48 hours before the time of the holding of the meeting. Any oral notice given personally or by telephone may be communicated either to the director or to a person at the office of the director who the person giving notice has reason to believe will promptly communicate it to the director. The notice need not specify the purpose of the meeting nor the place if the meeting is to be held at the principal executive office of the corporation.

Immediately following each annual meeting of shareholders, the Board of Directors shall hold a regular meeting for the purpose of organization, any desired election of officers, and the transaction of other business. Notice of this meeting shall not be required.

### Section 5. Quorum.

Except as may be otherwise specifically provided by law, the Certificate of Incorporation or these Bylaws, at all meetings of the Board of Directors, a majority of the entire Board of Directors shall constitute a quorum for the transaction of business and the act of a majority of the directors present at any meeting at which there is a quorum shall be the act of the Board of Directors. If a quorum shall not be present at any meeting of the Board of Directors, the directors present thereat may adjourn the meeting from time to time, without notice other than announcement at the meeting, until a quorum shall be present.

### Section 6. Actions of Board.

Unless otherwise provided by the Certificate of Incorporation or these Bylaws, any action required or permitted to be taken at any meeting of the Board of Directors or of any committee thereof may be taken without a meeting, if all the members of the Board of Directors or committee, as the case may be, consent thereto in writing, and the writing or writings are filed with the minutes of proceedings of the Board of Directors or committee.

### Section 7. Waiver of Notice.

The transactions of any meeting of the Board of Directors, however called and noticed or wherever held, shall be as valid as though had at a meeting duly held after regular call and notice if a quorum is present and if, either before or after the meeting, each of the directors not present signs a written waiver of notice, a consent to holding the meeting or an approval of the minutes. The waiver of notice or consent need not specify the purpose of the meeting. All such waivers, consents, and approvals shall be filed with the corporate records or made a part of the minutes of the meeting. Notice of a meeting shall also be deemed given to any director who attends the meeting without protesting before or at its commencement, the lack of notice to that director.

11

---

### Section 8. Meetings by Means of Conference Telephone.

Unless otherwise provided by the Certificate of Incorporation or these Bylaws, members of the Board of Directors of the Corporation, or any committee designated by the Board of Directors, may participate in a meeting of the Board of Directors or such committee by means of a conference telephone or similar communications equipment by means of which all persons participating in the meeting can hear each other, and participation in a meeting pursuant to this Section 8 shall constitute presence in person at such meeting.

### Section 9. Committees.

The Board of Directors may, by resolution passed by a majority of the entire Board of Directors, designate one or more committees, each committee to consist of two or more of the directors of the Corporation. The Board of Directors may designate one or more directors as alternate members of any committee, who may replace any absent or disqualified member at any meeting of any such committee. In the absence or disqualification of a member of a committee, and in the absence of a designation by the Board of Directors of an alternate member, the member or members thereof present at any meeting and

not disqualified from voting, whether or not he or they constitute a quorum, may unanimously appoint another member of the Board of Directors to act at the meeting in the place of any absent or disqualified member. Each committee shall keep regular minutes and report to the Board of Directors when required. Any committee, to the extent provided in the resolution of the board, shall have all the authority of the board, except with respect to:

- (a) the approval of any action which, under the Delaware GCL, also requires stockholders' approval or approval of the outstanding shares;
- (b) the filling of vacancies on the Board of Directors or in any committee;
- (c) the fixing of compensation of the directors for serving on the board or on any committee;
- (d) the amendment or repeal of bylaws or the adoption of new bylaws;
- (e) the amendment or repeal of any resolution of the Board of Directors which by its express terms is not so amendable or repealable;
- (f) a distribution to the stockholders of the Corporation, except at a rate or in a periodic amount or within a price range determined by the Board of Directors;
- (g) the appointment of any other committees of the Board of Directors or the members of these committees.

Meetings and action of committees shall be governed by, and held and taken in accordance with, the provisions of Article III of these Bylaws, Sections 4 (Meetings), 5 (Quorum), 6 (Actions of Board), and 7 (Waiver of Notice) with such changes in the context of those bylaws as are necessary to substitute the committee and its members for the Board of Directors and its members, except that the time of regular meetings of committees may be determined either by resolution of the Board of Directors or by resolution of the committee; special meetings of committees may also be called by resolution of the Board of Directors; and notice of special meetings of committees shall also be given to all alternate members, who shall

12

---

have the right to attend all meetings of the committee. The Board of Directors may adopt rules for the government of any committee not inconsistent with the provisions of these Bylaws.

#### Section 10. Compensation.

The directors may be paid their expenses, if any, of attendance at each meeting of the Board of Directors and may be paid a fixed sum for attendance at each meeting of the Board of Directors or a stated salary as director. No such payment shall preclude any director from serving the Corporation in any other capacity and receiving compensation therefor. Members of special or standing committees may be allowed like compensation for attending committee meetings.

#### Section 11. Interested Directors.

No contract or transaction between the Corporation and one or more of its directors or officers, or between the Corporation and any other corporation, partnership, association, or other organization in which one or more of its directors or officers are directors or officers, or have a for interest, shall be void or voidable solely for this reason, or solely because the director or officer is present at or participates in the meeting of the Board of Directors or committee thereof which authorizes the contract or transaction, or solely because his or their votes are counted for such purpose if (i) the material facts as to his or their relationship or interest and as to the contract or transaction are disclosed or are known to the Board of Directors or the committee, and the Board of Directors or committee in good faith authorizes the contract or transaction by the affirmative votes of a majority of the disinterested directors, even though the disinterested directors be less than a quorum; or (ii) the material facts as to his or their relationship or interest and as to the contract or transaction are disclosed or are known to the stockholders entitled to vote thereon, and the contract or transaction is specifically approved in good faith by vote of the stockholders; or (iii) the contract or transactions fair as to the Corporation as of the time it is authorized, approved or ratified, by the Board of Directors, a committee thereof or the stockholders. Common or interested directors may be counted in determining the presence of a quorum at a meeting of the Board of Directors or of a committee which authorizes the contract or transaction.

13

---

### ARTICLE IV OFFICERS

#### Section 1. General.

The officers of the Corporation shall be chosen by the Board of Directors and shall be a president, a secretary and a chief financial officer. The Board of Directors, in its discretion, may also choose a chairman of the Board of Directors (who must be a director) and one or more vice-presidents, assistant secretaries, assistant treasurers and other officers. Any number of offices may be held by the same person, unless otherwise prohibited by law, the Certificate of Incorporation or these Bylaws. The officers of the Corporation need not be stockholders of the Corporation nor, except in the case of the chairman of the Board of Directors, need such officers be directors of the Corporation. Except as otherwise provided herein, the officers of the Corporation shall perform such duties as the Board of Directors shall determine.

#### Section 2. Election.

The Board of Directors at its first meeting held after each Annual Meeting of Stockholders shall appoint the officers of the Corporation who shall hold their offices for such terms and shall exercise such powers and perform such duties as shall be determined from time to time by the Board of Directors; and all officers of the Corporation shall hold office until their successors are chosen and qualified, or until their earlier resignation or removal. The salaries of all officers of the Corporation shall be fixed by the Board of Directors.

Section 3.        Voting Securities Owned by the Corporation.

Powers of attorney, proxies, waivers of notice of meeting, consents and other instruments relating to securities owned by the Corporation may be executed in the name of an on behalf of the Corporation by the president or any vice-president and any such officer may, in the name of and on behalf of the Corporation, take all such action as any such officer may deem advisable to vote in person or by proxy at any meeting or security holders of any corporation in which the Corporation may own securities and at any such meeting shall possess and may exercise any and all rights and power incident to the ownership of such securities and which, as the owner thereof the Corporation might have exercised and possessed if present. The Board of Directors may, by resolution, from time to time confer like powers upon any other person or persons.

Section 4.        Chairman of the Board.

The chairman of the board shall be the chief executive officer of the Corporation and shall, subject to the control of the Board of Directors, have general supervision, direction and control of the business and officers of the Corporation. He shall preside at all meetings of the stockholders and at all meetings of the Board of Directors. He shall be ex officio a member of all of the committees of the board, including the executive committee, if any, and shall have the general powers and duties of management usually vested in the chief executive officer of a Corporation, and shall have such other powers and duties as may be prescribed by the Board of Directors or the Bylaws.

14

---

Section 5.        President.

The president shall, subject to the control of the Board of Directors and, if there be one, the chairman of the Board of Directors, have general supervision of the business of the Corporation and shall see that all orders and resolutions of the Board of Directors are carried into effect. He shall execute all bonds, mortgages, contracts and other instruments of the Corporation requiring a seal, under the seal of the Corporation, except where required or permitted by law to be otherwise signed and executed and except that the other officers of the Corporation may sign and execute documents when so authorized by these Bylaws, the Board of Directors or the president. In the absence or disability of the chairman of the Board of Directors, or if there be none, the president shall preside at all meetings of the stockholders and the Board of Directors. If there be no chairman of the Board of Directors, the president shall be the chief executive officer of the Corporation. The president shall also perform such other duties and may exercise such other powers as from time to time may be assigned to him by these Bylaws or by the Board of Directors.

Section 6.        Vice Presidents.

In the absence or disability of the president, the vice presidents, if any, in order of their rank as fixed by the Board of Directors or, if not ranked, a vice president designated by the Board of Directors, shall perform all the duties of the president, and when so acting shall have all the powers of, and be subject to all the restrictions upon, the president. The vice presidents shall have such other powers and perform such other duties as from time to time may be prescribed for them respectively by the Board of Directors or the bylaws, and the president, or the chairman of the board.

Section 7.        Secretary.

The secretary shall keep or cause to be kept, at the principal office or such other place as the Board of Directors may direct, a book of minutes of all meetings and actions of directors, committees of directors, and stockholders, with the time and place of holding, whether regular or special, and, if special, how authorized, the notice given, the names of those present at directors' meetings or committee meetings, the number of shares present or represented at stockholders' meetings, and the proceedings.

The secretary shall keep, or cause to be kept, at the principal executive office or at the office of the Corporations transfer agent or registrar, as determined by resolution of the Board of Directors, a share register, or a duplicate share register, showing the names of all stockholders and their addresses, the number and classes of shares held by each, the number and date of certificates issued for the same, and the number and date of cancellation of every certificate surrendered for cancellation.

The secretary shall give, or cause to be given, notice of all meetings of the stockholders and of the Board of Directors required by the bylaws or by law to be given, and he shall keep the seal of the Corporation if one be adopted, in safe custody, and shall have such other powers and perform such other duties as may be prescribed by the Board of Directors or by the Bylaws.

15

---

Section 8.        Chief Financial Officer.

The chief financial officer shall keep and maintain, or cause to be kept and maintained, adequate and correct books and records of accounts of the properties and business transactions of the Corporation, including accounts of its assets, liabilities, receipts, disbursements, gains, losses, capital, retained earnings, and shares. The books of account shall at all reasonable times be open to inspection by any director.

The chief financial officer shall deposit all moneys and other valuables in the name and to the credit of the Corporation with such depositaries as may be designated by the Board of Directors. He, shall disburse the funds of the Corporation as may be ordered by the Board of Directors, shall render to the president and directors, whenever they request it, an account of all of his transactions as chief financial officer and of the financial condition of the Corporation, and shall have other powers and perform such other duties as may be prescribed by the Board of Directors of the Bylaws.

Section 9.        Removal and Resignation of Officers.

Subject to the rights; if any, of an officer under any contract of employment, any officer may be removed, either with or without cause, by the Board of Directors at any regular or special meeting of the Board or, except in the case of any officer chosen by the Board of Directors, by any officer upon whom such power of removal may be conferred by the Board of Directors.

Any officer may resign at any time by giving written notice to the Corporation. Any resignation shall take effect at the date of the receipt of such notice or at any later time specified in such notice; and, unless otherwise specified in such notice, the acceptance of such resignation shall not be necessary to make it effective. Any resignation is without prejudice to the rights, if any, of the Corporation under any contract to which the resigning officer is a party.

Section 10.        Vacancies in Offices.

A vacancy in any office because of death, resignation, removal, disqualification or any other cause shall be filled in the manner prescribed in these Bylaws for regular appointments to such office.

ARTICLE V  
STOCK

Section 1.        Form of Certificates.

The shares of stock of the Corporation shall be represented by certificates, provided that the Board of Directors of the Corporation may, subject to the limits imposed by law, provide by resolution or resolutions that some or all of any or all classes or series of the stock of the Corporation shall be uncertificated shares. Any such resolution shall not apply to shares represented by a certificate until such certificate is surrendered to the Corporation. Every holder of stock represented by certificates shall be entitled to have a certificate signed, in the name of the Corporation (i) by the chairperson or vice-chairperson of the Board of Directors, or the president or a vice-president, and (ii) by the treasurer or an assistant treasurer, or the secretary or an assistant secretary, of the Corporation, representing the number of shares registered in

16

---

certificate form. Certificates shall be in such form as the Board of Directors may from time to time prescribe, to the extent consistent with applicable law, provided that the Corporation shall not have the power to issue a certificate in bearer form.

Section 2.        Signatures.

Where a certificate is countersigned by (i) a transfer agent other than the Corporation or its employee, or (ii) a registrar other than the Corporation or its employee, any other signature on the certificate may be a facsimile. In case any officer, transfer agent or registrar who has signed or whose facsimile signature has been placed upon a certificate shall have ceased to be such officer, transfer agent or registrar before such certificate is issued, it may be issued by the Corporation with the same effect as if he were such officer, transfer agent or registrar at the date of issue.

Section 3.        Lost Certificates.

The Board of Directors may direct a new certificate to be issued in place of any certificate theretofore issued by the Corporation alleged to have been lost, stolen or destroyed, upon the making of an affidavit of that fact by the person claiming the certificate of stock to be lost, stolen or destroyed. When authorizing such issue of a new certificate, the Board of Directors may, in its discretion and as a condition precedent to the issuance thereof, require the owner of such lost, stolen or destroyed certificate, or his legal representative, to advertise the same in such manner as the Board of Directors shall require and/or to give the Corporation a bond in such sum as it may direct as indemnity against any claim that may be made against the Corporation with respect to the certificate alleged to have been lost, stolen or destroyed.

Section 4.        Transfers.

Stock of the Corporation shall be transferable in the manner prescribed by applicable law and in these Bylaws. Transfers of stock shall be made on the books of the Corporation only by the registered holder thereof in person or by his or her attorney lawfully constituted in writing, (i) with regard to certificated shares, upon surrender for cancellation of certificates therefor properly endorsed for transfer and payment of all necessary transfer taxes, and (ii) with regard to uncertificated shares, upon delivery of proper transfer instructions and payment of all necessary transfer taxes and compliance with appropriate procedures for transferring shares in uncertificated form; provided, however, that such surrender and endorsement, compliance or payment of taxes shall not be required in any case in which the officers of the Corporation shall determine to waive such requirement.

Section 5.        Record Date.

In order that the Corporation may determine the stockholders entitled to notice of or to vote at any meeting of stockholders or any adjournment thereof, or entitled to express consent to corporate action in writing without a meeting, or entitled to receive payment of any dividend or other distribution or allotment of any rights, or entitled to exercise any rights in respect of any change, conversion or exchange of stock, or for the purpose of any other lawful action, the Board of Directors may fix, in advance, a record date, which shall not be more than 60 days nor less than ten days before the date of such meeting, nor more than 60 days prior to any other action. A

17

---

determination of stockholders of record entitled to notice of or to vote at a meeting of stockholders shall apply to any adjournment of the meeting of stockholders shall apply to any adjournment of the meeting; provided, however, that the Board of Directors may fix a new record date for the adjourned meeting.

If the Board of Directors does not so fix a record date:

(a)        The record date for determining stockholders entitled to notice of or to vote at a meeting of stockholders shall be at the close of business on the business day next preceding the day on which notice is given or, if notice is waived, at the close of business on the business day next preceding the day on which the meeting is held.

(b) The record date for determining stockholders entitled to give consent to corporate action in writing without a meeting, (i) when no prior action by the board has been taken, shall be the day on which the first written consent is given or (ii) when prior action of the board has been taken, shall be at the close of business on the day on which the board adopts the resolution relating to such prior action, or the sixtieth (60th) day before the date of such prior action, whichever is later.

Section 6. Beneficial Owners.

The Corporation shall be entitled to recognize the exclusive right of a person registered on its books as the owner of shares to receive dividends, and to vote as such owner, and to hold liable for calls and assessments a person registered on its books as the owner of shares, and shall not be bound to recognize any equitable or other claim to or interest in such share or shares on the part of any other person, whether or not it shall have express or other notice thereof, except as otherwise provided by law.

ARTICLE VI  
GENERAL PROVISIONS

Section 1. Dividends.

Dividends upon the capital stock of the Corporation, subject to applicable law and the provisions of the Certificate of Incorporation, if any, may be declared by the Board of Directors at any regular or special meeting, and may be paid in cash, in property, or in shares of the capital stock. Before payment of any dividend, there may be set aside out of any funds of the Corporation available for dividends such sum or sums as the Board of Directors from time to time, in its absolute discretion, deems proper as a reserve or reserves to meet contingencies, or for equalizing dividends, or for repairing or maintaining any property of the Corporation, or for any proper purpose, and the Board of Directors may modify or abolish any such reserve.

Section 2. Disbursements.

All checks or demands for money and notes of the Corporation shall be signed by such officer or officers or such other person or persons as the Board of Directors may from time to time designate.

18

---

Section 3. Fiscal Year.

The fiscal year of the Corporation shall be fixed by resolution of the Board of Directors.

Section 4. Corporate Seal.

The corporate seal shall have inscribed thereon the name of the Corporation, the year of its organization and the words "Corporate Seal, Delaware." The seal may be used by causing it or a facsimile thereof to be impressed or affixed or reproduced or otherwise.

Section 5. Designated Engineer in the State of Washington.

The Board of Directors, as required by the Revised Code of Washington, has appointed a licensed professional engineer in the state of Washington as the Designated Engineer being in responsible charge of the Corporation's engineering decisions pertaining to engineering activities in that state. The Designated Engineer named in a resolution as being in responsible charge, or an engineer under the Designated Engineer's direct supervision, shall make all engineering or land surveying decisions pertaining to engineering or land surveying activities in the state of Washington.

ARTICLE VII  
INDEMNIFICATION

Section 1. Power to Indemnify in Actions, Suits or Proceedings Other Than Those by or in the Right of the Corporation.

Subject to Section 3 of this Article VII, the Corporation shall indemnify any person who was or is a party or is threatened to be made a party to any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative (other than an action by or in the right of the Corporation) by reason of the fact that he is or was a director, officer, employee or agent of the Corporation, or is or was serving at the request of the Corporation as director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise, against expenses (including attorneys' fees), judgments, fines and amounts paid in settlement actually and reasonably incurred by him in connection with such action, suit or proceeding if he acted in good faith and in a manner he reasonably believed to be in or not opposed to the best interests of the Corporation, and, with respect to any criminal action or proceeding, had no reasonable cause to believe his conduct was unlawful. The termination of any action, suit or proceeding by judgment, order, settlement, conviction, or upon a plea of nolo contendere or its equivalent, shall not, of itself, create a presumption that the person did not act in good faith and in a manner which he reasonably believed to be in or not opposed to the best interests of the Corporation, and, with respect to any criminal action or proceeding, had reasonable cause to believe that his conduct was unlawful.

Section 2. Power to Indemnify in Actions, Suits or Proceedings by or in the Right of the Corporation.

Subject to Section 3 of this Article VII, the Corporation shall indemnify any person who was or is a party or is threatened to be made a party to any threatened, pending or completed action or suit by or in the right of the Corporation to procure a judgment in its favor by reason of the fact that he is or was a director, officer, employee or agent of the Corporation, or is or was serving at the request of the Corporation as a director, officer, employee or agent of another

19

---



corporation, partnership, joint venture, trust or other enterprise against expenses (including attorneys' fees) actually and reasonably incurred by him in connection with the defense or settlement of such action or suit if he acted in good faith and in a manner he reasonably believed to be in or not opposed to the best interests of the Corporation; except that no indemnification shall be made in respect of any claim, issue or matter as to which such person shall have been adjudged to be liable to the Corporation unless and only to the extent that the Court of Chancery or the court in which such action or suit was brought shall determine upon application that, despite the adjudication of liability but in view of all the circumstances of the case, such person is fairly and reasonably entitled to indemnity for such expenses which the Court of Chancery or such other court shall deem proper.

Section 3. Authorization of Indemnification.

Any indemnification under this Article VII (unless ordered by a court) shall be made by the Corporation only as authorized in the specific case upon a determination that indemnification of the director, officer, employee or agent is proper in the circumstances because he has met the applicable standard of conduct set forth in Section 1 or Section 2 of this Article VII, as the case may be. Such determination shall be made (i) by the Board of Directors by a majority vote of a quorum consisting of directors who were not parties to such action, suit or proceeding, or (ii) if such quorum is not obtainable, or, even if obtainable a quorum of disinterested directors so directs, by independent legal counsel in a written opinion, or (iii) by the stockholders. To the extent, however, that a director, officer, employee or agent of the Corporation has been successful on the merits or otherwise in defense of any action, suit or proceeding described above, or in defense of any claim, issue or matter therein, he shall be indemnified against expenses (including attorneys' fees) actually and reasonably incurred by him in connection therewith, without the necessity of authorization in the specific case.

Section 4. Good Faith Defined.

For purposes of any determination under Section 3 of this Article VII, a person shall be deemed to have acted in good faith and in a manner he reasonably believed to be in or not opposed to the best interests of the Corporation, or, with respect to any criminal action or proceeding, to have had no reasonable cause to believe his conduct was unlawful, if his action is based on the records or books of account of the Corporation or another enterprise, or on information supplied to him by the officers of the Corporation or another enterprise in the course of their duties, or on the advice of legal counsel for the Corporation or another enterprise or on information or records given or reports made to the Corporation or another enterprise by an independent certified public accountant or by an appraiser or other expert selected with reasonable care by the Corporation or another enterprise. The term "another enterprise" as used in this Section 4 shall mean any other corporation or any partnership, joint venture, trust or other enterprise of which such person is or was serving at the request of the Corporation as a director, officer, employee or agent. The provisions of this Section 4 shall not be deemed to be exclusive or to limit in any way the circumstances in which a person may be deemed to have met the applicable standard of conduct set forth in Sections 1 or 2 of this Article VII, as the case may be.

Section 5. Indemnification by a Court.

Notwithstanding any contrary determination in the specific case under Section 3 of this

20

---

Article VII, and notwithstanding the absence of any determination thereunder, any director, officer, employee or agent may apply to any court of competent jurisdiction in the State of Delaware for indemnification to the extent otherwise permissible under Sections 1 and 2 of this Article VII. The basis of such indemnification by a court shall be a determination by such court that indemnification of the director, officer, employee or agent is proper in the circumstances because he has met the applicable standards of conduct set forth in Sections 1 or 2 of this Article VII, as the case may be. Notice of any application for indemnification pursuant to this Section 5 shall be given to the Corporation promptly upon the filing of such application.

Section 6. Expenses Payable in Advance.

Expenses incurred in defending or investigating a threatened or pending action, suit or proceeding may be paid by the Corporation in advance of the final disposition of such action, suit or proceeding upon receipt of an undertaking by or on behalf of the director, officer, employee or agent to repay such amount if it shall ultimately be determined that he is not entitled to be indemnified by the Corporation as authorized in this Article VII.

Section 7. Non-exclusivity of Indemnification and Advancement of Expenses.

The indemnification and advancement of expenses provided by or granted pursuant to this Article VII shall not be deemed exclusive of any other rights to which those seeking indemnification or advancement of expenses may be entitled under any By-Law, agreement, contract, vote of stockholders or disinterested directors or pursuant to the direction (howsoever embodied) of any court of competent jurisdiction or otherwise, both as to action in his official capacity and as to action in another capacity while holding such office, it being the policy of the Corporation that indemnification of the persons specified in Sections 1 and 2 of this Article VII shall be made to the fullest extent permitted by law. The provisions of this Article VII shall not be deemed to preclude the indemnification of any person who is not specified in Sections 1 or 2 of this Article VII but whom the Corporation has the power or obligation to indemnify under the provisions of the General Corporation Law of the State of Delaware, or otherwise.

Section 8. Insurance.

The Corporation may purchase and maintain insurance on behalf of any person who is or was a director, officer, employee or agent of the Corporation, or is or was serving at the request of the Corporation as a director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise against any liability asserted against him and incurred by him in any such capacity, or arising out of his status as such, whether or not the Corporation would have the power or the obligation to indemnify him against such liability under the provisions of this Article VII.

Section 9. Meaning of "Corporation" for Purposes of Article VII.

For purposes of this Article VII, references to "the Corporation" shall include, in addition to the resulting corporation, any constituent corporation (including any constituent of a constituent) absorbed in a consolidation or merger which, if its separate existence had continued, would have had power and authority to indemnify its directors, officers, and employees or agents, so that any person who is or was a director, officer, employee or agent of such constituent

corporation, or is or was serving at the request of such constituent corporation as a director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise, shall stand in the same position under the provisions of this Article VII with respect to the resulting or surviving corporation as he would have with respect to such constituent corporation if its separate existence had continued.

Section 10. Survival of Indemnification and Advancement of Expenses.

The indemnification and advancement of expenses provided by, or granted pursuant to, this section shall, unless otherwise provided when authorized or ratified, continue as to a person who has ceased to be a director, officer, employee or agent and shall inure to the benefit of the heirs, executors and administrators of such a person.

ARTICLE VIII  
FORUM FOR ADJUDICATION OF DISPUTES

Unless the Corporation consents in writing to the selection of an alternative forum, the Court of Chancery (the “Chancery Court”) of the State of Delaware (or, in the event that the Chancery Court does not have jurisdiction, the federal district court for the District of Delaware or other state courts of the State of Delaware) shall, to the fullest extent permitted by law, be the sole and exclusive forum for (a) any derivative action or proceeding brought on behalf of the Corporation, (b) any action asserting a claim of breach of a fiduciary duty owed by any director, officer or stockholder of the Corporation to the Corporation or to the Corporation’s stockholders, (c) any action arising pursuant to any provision of the Delaware GCL or the certificate of incorporation or these bylaws (as each may be amended from time to time), (d) any action to interpret, apply, enforce or determine the validity of the Certificate of Incorporation or these Bylaws or (e) any action asserting a claim against the Corporation governed by the internal affairs doctrine. Any person or entity purchasing or otherwise acquiring any interest in shares of capital stock of the Corporation shall be deemed to have notice of, and to have consented to, the provisions of this Article VIII.

ARTICLE IX  
AMENDMENTS

Section 1. Amendments by Stockholders or Board.

These Bylaws may be altered, amended or repealed, in whole or in part, or new Bylaws may be adopted by the majority vote or written consent of the stockholders or the Board of Directors; provided however, that a change in the authorized number of directors must be accomplished as provided in Article III, Section 1 of these Bylaws. Notwithstanding the foregoing and anything contained in this Certificate of Incorporation to the contrary, unless otherwise required by applicable law, Sections 14 and 15 of Article II the Bylaws shall not be amended, modified or repealed by the stockholders, and no provision inconsistent therewith shall be adopted by the stockholders, without the affirmative vote of the holders of at least 66<sup>2/3</sup>% of the voting power of all of the outstanding shares of the Corporation’s capital stock, voting together as a single class.

CERTIFICATE OF SECRETARY

The undersigned does hereby certify:

- (1) That the undersigned is the duly elected and acting Secretary of ITERIS, INC., a Delaware corporation; and
- (2) That the foregoing Bylaws, comprising 22 pages, constitute the restated Bylaws of said Corporation as amended as of the date hereof.

IN WITNESS WHEREOF, the undersigned has duly signed his name as of the 5th day of June, 2018.

/s/ Andrew C. Schmidt  
Andrew C. Schmidt, Secretary

## ITERIS, INC. EMPLOYEE STOCK PURCHASE PLAN

1. **Purpose.** This Iteris, Inc. (“Company”) Employee Stock Purchase Plan (the “Plan”) is intended to provide employees of the Company and its Participating Subsidiaries with an opportunity to acquire a proprietary interest in the Company through the purchase of shares of Common Stock. The Company intends that the Plan qualify as an “employee stock purchase plan” under Section 423 of the Code and the Plan shall be interpreted in a manner that is consistent with that intent.

2. **Definitions.**

“**Board or Board of Directors**” means the Board of Directors of the Company, as constituted from time to time.

“**Code**” means the U.S. Internal Revenue Code of 1986, as it may be amended from time to time. Any reference to a section of the Code shall be deemed to include a reference to any regulations promulgated thereunder.

“**Committee**” means the Compensation Committee or other committee appointed by the Board to administer the Plan.

“**Common Stock**” means the common stock of the Company, par value \$0.10 per share.

“**Company**” means Iteris, Inc., a Delaware corporation, including any successor thereto.

“**Compensation**” means the fixed salary or base wage paid by the Company or a Participating Subsidiary to a Participant as reported by the Company or a Participating Subsidiary, as applicable, to the United States government for income tax purposes, including bonuses and commissions and an Employee’s portion of salary deferral contributions pursuant to Section 401(k) of the Code and any amount excludable pursuant to Section 125 of the Code, overtime, vacation pay, holiday pay, jury duty pay and funeral leave pay, but excluding education or tuition reimbursements, imputed income arising under any group insurance or benefit program, travel expenses, business and relocation expenses, and income received in connection with stock options or other equity-based awards.

“**Corporate Transaction**” means a merger, consolidation, acquisition of property or stock, separation, reorganization or other corporate event described in Section 424 of the Code.

“**Designated Broker**” means the financial services firm or other agent designated by the Company to maintain ESPP Share Accounts on behalf of Participants who have purchased shares of Common Stock under the Plan.

“**Effective Date**” means January 1, 2018, subject to the Plan obtaining stockholder approval in accordance with Section 19.11 hereof.

“**Employee**” means any person who renders services to the Company or a Participating Subsidiary as an employee pursuant to an employment relationship with such employer. For purposes of the Plan, the employment relationship shall be treated as continuing intact while the individual is on military leave, sick leave or other leave of absence approved by the Company or a Participating Subsidiary that meets the requirements of Treasury Regulation Section 1.421-1(h)(2). Where the period of leave exceeds three (3) months, or such other period of time specified in Treasury Regulation Section 1.421-1(h)(2), and the individual’s right to re-employment is not guaranteed by statute or contract, the employment relationship shall be deemed to have terminated on the first day immediately following such three-month period, or such other period specified in Treasury Regulation Section 1.421-1(h)(2).

“**Eligible Employee**” means an Employee who is customarily employed (and regularly scheduled) for at least twenty (20) hours per week and more than five (5) months in any calendar year. Notwithstanding the foregoing, the Committee may exclude from participation in the Plan or any Offering Employees who are “highly compensated employees” of the Company or a Participating Subsidiary (within the meaning of Section 414(q) of the Code) or a sub-set of such highly compensated employees.

“**Enrollment Form**” means an agreement pursuant to which an Eligible Employee may elect to enroll in the Plan, to authorize a new level of payroll deductions, or to stop payroll deductions and withdraw from an Offering Period.

“**ESPP Share Account**” means an account into which Common Stock purchased with accumulated payroll deductions at the end of an Offering Period are held on behalf of a Participant.

“**Exchange Act**” means the U.S. Securities Exchange Act of 1934, as amended.

“**Fair Market Value**” means, as of any date, the value of the shares of Common Stock as determined below. If the shares are listed on any established stock exchange or a national market system, including, without limitation, the NASDAQ Stock Market, the Fair Market Value shall be the closing selling price of a share (or if no sales were reported, the closing price on the date immediately preceding such date) at the close of regular hours trading (i.e., before after-hours trading begins) as quoted on such exchange or system on the day of determination, as reported by the National Association of Securities Dealers (if primarily traded on the Nasdaq Global or Global Select Market) or as officially quoted in the composite tape of transactions on any other Stock Exchange on which the Common Stock is then primarily traded. In the absence of an established market for the shares, the Fair Market Value shall be determined in good faith by the Committee and such determination shall be conclusive and binding on all persons.

“**Offering Date**” means the first Trading Day of each Offering Period as designated by the Committee.

“**Offering**” or “**Offering Period**” means a period of six months beginning each January 1<sup>st</sup> and July 1<sup>st</sup> of each year; provided, that, pursuant to Section 5, the Committee may change the duration of future Offering Periods (subject to a maximum Offering Period of twenty-seven (27) months) and/or the start and end dates of future Offering Periods.

“**Participant**” means an Eligible Employee who is actively participating in the Plan.

“**Participating Subsidiaries**” means the Subsidiaries that have been designated as eligible to participate in the Plan, and such other Subsidiaries that may be designated by the Committee from time to time in its sole discretion.

“**Plan**” means this Iteris, Inc. Employee Stock Purchase Plan, as set forth herein, and as amended from time to time.

“**Purchase Date**” means the last Trading Day of each Offering Period.

“**Purchase Price**” means an amount equal to the lesser of (1) eighty-five percent (85%) (or such greater percentage as determined by the Committee) of the Fair Market Value on the Offering Date or (2) eighty-five percent (85%) (or such greater percentage as determined by the Committee) of the Fair Market Value on the Purchase Date; provided, that, the Purchase Price per share of Common Stock will in no event be less than the par value of the Common Stock.

“**Securities Act**” means the Securities Act of 1933, as amended.

“**Subsidiary**” means any domestic corporation, of which not less than 50% of the combined voting power is held by the Company or a Subsidiary, whether or not such corporation exists now or is hereafter organized or acquired by the Company or a Subsidiary. In all cases, the determination of whether an entity is a Subsidiary shall be made in accordance with Section 424(f) of the Code.

“**Trading Day**” means any day on which the national stock exchange upon which the Common Stock is listed is open for trading or, if the Common Stock is not listed on an established stock exchange or national market system, a business day, as determined by the Committee in good faith.

3. Administration. The Plan shall be administered by the Committee, which shall have the authority to construe and interpret the Plan, prescribe, amend and rescind rules relating to the Plan’s administration and take any other actions necessary or desirable for the administration of the Plan. The Committee may correct any defect or supply any omission or reconcile any inconsistency or ambiguity in the Plan. The Committee shall have the authority and discretion to change the Purchase Price within the parameters set forth above, and if the Committee changes the Purchase Price from one Offering Period to another, the Company will notify Participants of any change in Purchase Price at least fifteen (15) days prior to the beginning of the next Offering Period to which the changed Purchase Price applies. The decisions of the Committee shall be final and binding on all persons. All expenses of administering the Plan shall be borne by the Company.

---

3

4. Eligibility. Unless otherwise determined by the Committee in a manner that is consistent with Section 423 of the Code, any individual who is an Eligible Employee as of the Offering Date for a particular Offering Period shall be eligible to participate in such Offering Period, subject to the requirements of Section 423 of the Code.

Notwithstanding any provision of the Plan to the contrary, no Eligible Employee shall be granted an option under the Plan if (i) immediately after the grant of the option, such Eligible Employee (or any other person whose stock would be attributed to such Eligible Employee pursuant to Section 424(d) of the Code) would own capital stock of the Company or hold outstanding options to purchase stock possessing 5% or more of the total combined voting power or value of all classes of stock of the Company or any Subsidiary or (ii) such option would permit his or her rights to purchase stock under all employee stock purchase plans (described in Section 423 of the Code) of the Company and its Subsidiaries to accrue at a rate that exceeds \$25,000 of the Fair Market Value of such stock (determined at the time the option is granted) for each calendar year in which such option is outstanding at any time.

5. Offering Periods. The Plan shall be implemented by a series of Offering Periods, each of which shall be six (6) months in duration, with new Offering Periods commencing on or about January 1 and July 1 of each year (or such other times as determined by the Committee). The Committee shall have the authority to change the duration, frequency, start and end dates of Offering Periods.

6. Participation.

6.1 Enrollment; Payroll Deductions. An Eligible Employee may elect to participate in the Plan by properly completing an Enrollment Form, which may be electronic, and submitting it to the Company, in accordance with the enrollment procedures established by the Committee. Participation in the Plan is entirely voluntary. By submitting an Enrollment Form, the Eligible Employee authorizes payroll deductions from his or her pay check in an amount equal to at least 1%, but not more than 15% of his or her Compensation on each pay day occurring during an Offering Period (or such other maximum percentage as the Committee may establish from time to time before an Offering Period begins). Payroll deductions shall commence on the first payroll date following the Offering Date and end on the last payroll date on or before the Purchase Date. The Company shall maintain records of all payroll deductions but shall have no obligation to pay interest on payroll deductions or to hold such amounts in a trust or in any segregated account.

6.2 Election Changes. During an Offering Period, a Participant may decrease or increase his or her rate of payroll deductions applicable to such Offering Period only once. To make such a change, the Participant must submit a new Enrollment Form authorizing the new rate of payroll deductions and any change shall become effective on the next payroll period that begins no earlier than five (5) business days after the Company’s receipt of a new Enrollment Form or such other notice period as may be established by the Compensation Committee from time to time in its sole discretion (to the extent practical).

under the Company's payroll practices) following delivery of a new Enrollment Form. A Participant may decrease or increase his or her rate of payroll deductions for future Offering Periods by submitting a new Enrollment Form authorizing the new rate of payroll deductions at least fifteen days before the start of the next Offering Period.

6.3 Automatic Re-enrollment. The deduction rate selected in the Enrollment Form shall remain in effect for subsequent Offering Periods unless the Participant (a) submits a new Enrollment Form authorizing a new level of payroll deductions in accordance with Section 6.2, (b) withdraws from the Plan in accordance with Section 10, or (c) terminates employment or otherwise becomes ineligible to participate in the Plan.

7. Grant of Option. On each Offering Date, each Participant in the applicable Offering Period shall be granted an option to purchase, on the Purchase Date, a number of shares of Common Stock determined by dividing the Participant's accumulated payroll deductions by the applicable Purchase Price; provided, however, that in no event shall any Participant purchase more than 5,000 shares of Common Stock during an Offering Period (subject to adjustment in accordance with Section 18 and the limitations set forth in Section 13 of the Plan).

8. Exercise of Option/Purchase of Shares. A Participant's option to purchase shares of Common Stock will be exercised automatically on the Purchase Date of each Offering Period. The Participant's accumulated payroll deductions will be used to purchase the maximum number of whole shares that can be purchased with the amounts in the Participant's notional account. No fractional shares may be purchased but any remaining funds that are not used to purchase Common Stock will carry forward to the next Offering Period, subject to earlier withdrawal by the Participant in accordance with Section 10 or termination of employment in accordance with Section 11.

9. Transfer of Shares. As soon as reasonably practicable after each Purchase Date, the Company will arrange for the delivery to each Participant of the shares of Common Stock purchased upon exercise of his or her option. The Committee may permit or require that the shares be deposited directly into an ESPP Share Account established in the name of the Participant with a Designated Broker and may require that the shares of Common Stock be retained with such Designated Broker for a specified period of time. Participants will not have any voting, dividend or other rights of a shareholder with respect to the shares of Common Stock subject to any option granted hereunder until such shares have been delivered pursuant to this Section 9.

10. Withdrawal.

10.1 Withdrawal Procedure. A Participant may withdraw from an Offering by submitting to the Company a revised Enrollment Form indicating his or her election to withdraw at any time before the Purchase Date, provided that such revised Enrollment Form is received at least ten (10) business days prior to the Purchase Date (or such other period as may be established by the Compensation Committee from time to time in its sole discretion). The accumulated payroll deductions held on behalf of a Participant in his or her notional account (that have not been used to purchase shares of Common Stock) shall be paid to the Participant promptly following receipt of the Participant's Enrollment Form indicating his or

5

---

her election to withdraw and the Participant's option shall be automatically terminated. If a Participant withdraws from an Offering Period, no payroll deductions will be made during any succeeding Offering Period, unless the Participant re-enrolls in accordance with Section 6.1 of the Plan.

10.2 Effect on Succeeding Offering Periods. A Participant's election to withdraw from an Offering Period will not have any effect upon his or her eligibility to participate in succeeding Offering Periods that commence following the completion of the Offering Period from which the Participant withdraws, provided the Participant submits a new Enrollment Form in accordance with this Plan.

11. Termination of Employment; Change in Employment Status. Upon termination of a Participant's employment for any reason, including death, disability or retirement, or a change in the Participant's employment status following which the Participant is no longer an Eligible Employee, which in either case occurs at least fifteen days (or such other period as may be established by the Compensation Committee from time to time in its sole discretion) before the Purchase Date, the Participant will be deemed to have withdrawn from the Plan and the payroll deductions in the Participant's notional account (that have not been used to purchase shares of Common Stock) shall be returned to the Participant, or in the case of the Participant's death, to the person(s) entitled to such amounts under Section 17, and the Participant's option shall be automatically terminated. If the Participant's termination of employment or change in status occurs within fifteen days (or such other period as may be established by the Compensation Committee from time to time in its sole discretion) before a Purchase Date, the accumulated payroll deductions shall be used to purchase shares on the Purchase Date.

12. Interest. No interest shall accrue on or be payable with respect to the payroll deductions of a Participant in the Plan.

13. Shares Reserved for Plan.

13.1 Number of Shares. A total of One Million (1,000,000) shares of Common Stock have been reserved as authorized for the grant of options under the Plan. The shares of Common Stock may be newly issued shares, treasury shares or shares acquired on the open market.

13.2 Over-subscribed Offerings. The number of shares of Common Stock which a Participant may purchase in an Offering under the Plan may be reduced if the Offering is over-subscribed. No option granted under the Plan shall permit a Participant to purchase shares of Common Stock which, if added together with the total number of shares of Common Stock purchased by all other Participants in such Offering would exceed the total number of shares of Common Stock remaining available under the Plan. If the Committee determines that, on a particular Purchase Date, the number of shares of Common Stock with respect to which options are to be exercised exceeds the number of shares of Common Stock then available under the Plan, the Company shall make a pro rata allocation of the shares of Common Stock remaining available for purchase in as uniform a manner as practicable and as the Committee determines to be equitable.

6

---

14. Transferability. No payroll deductions credited to a Participant, nor any rights with respect to the exercise of an option or any rights to receive Common Stock hereunder may be assigned, transferred, pledged or otherwise disposed of in any way (other than by will, the laws of descent and distribution, or as provided in Section 17 hereof) by the Participant. Any attempt to assign, transfer, pledge or otherwise dispose of such rights or amounts shall be without effect.

15. Application of Funds. All payroll deductions received or held by the Company under the Plan may be used by the Company for any corporate purpose to the extent permitted by applicable law, and the Company shall not be required to segregate such payroll deductions or contributions.

16. Statements. Participants will be provided with statements at least annually which shall set forth the contributions made by the Participant to the Plan, the Purchase Price of any shares of Common Stock purchased with accumulated funds, the number of shares of Common Stock purchased, and any payroll deduction amounts remaining in the Participant's notional account.

17. Designation of Beneficiary. A Participant may file, on forms supplied by the Company, a written designation of beneficiary who is to receive any shares of Common Stock and cash in respect of any fractional shares of Common Stock, if any, from the Participant's ESPP Share Account under the Plan in the event of such Participant's death. In addition, a Participant may file a written designation of beneficiary who is to receive any cash withheld through payroll deductions and credited to the Participant's notional account in the event of the Participant's death prior to the Purchase Date of an Offering Period.

18. Adjustments Upon Changes in Capitalization; Dissolution or Liquidation; Corporate Transactions.

18.1 Adjustments. In the event that any dividend or other distribution (whether in the form of cash, Common Stock, or other property), recapitalization, stock split, reverse stock split, reorganization, merger, consolidation, reincorporation, other reorganization, split-up, spin-off, combination, repurchase, or exchange of Common Stock or other securities of the Company, or other change in the Company's structure affecting the Common Stock occurs without the Company's receipt of consideration, or should the value of shares of Common Stock be substantially reduced as a result of a spin-off transaction or an extraordinary dividend or distribution, then in order to prevent dilution or enlargement of the benefits or potential benefits intended to be made available under the Plan, the Committee will, in such manner as it deems equitable, adjust the number of shares and class of Common Stock that may be delivered under the Plan, the Purchase Price per share and the number of shares of Common Stock covered by each outstanding option under the Plan, and the numerical limits of Section 7 and Section 13.

18.2 Dissolution or Liquidation. Unless otherwise determined by the Committee, in the event of a proposed dissolution or liquidation of the Company, any Offering Period then in progress will be shortened by setting a new Purchase Date and the Offering Period will end immediately prior to the proposed dissolution or liquidation. The new Purchase Date will be before the date of the Company's proposed dissolution or liquidation. Before the new Purchase Date, the Committee will provide each Participant with written notice, which may

7

---

be electronic, of the new Purchase Date and that the Participant's option will be exercised automatically on such date, unless before such time, the Participant has withdrawn from the Offering in accordance with Section 10.

18.3 Corporate Transaction. In the event of a Corporate Transaction, the Committee may cause each outstanding option to be assumed or an equivalent option substituted by the successor corporation or a parent or Subsidiary of such successor corporation. If the successor corporation does not assume or substitute the option, the Committee may either: (a) shorten the Offering Period with respect to which the option relates and set a new Purchase Date on which the Offering Period will end. The new Purchase Date will occur before the date of the Corporate Transaction. Prior to the new Purchase Date, the Committee will provide each Participant with written notice, which may be electronic, of the new Purchase Date and that the Participant's option will be exercised automatically on such date, unless before such time, the Participant has withdrawn from the Offering in accordance with Section 10; or (b) terminate the Offering Period and refund all accumulated payroll deductions to the Participants.

19. General Provisions.

19.1 Equal Rights and Privileges. Notwithstanding any provision of the Plan to the contrary and in accordance with Section 423 of the Code, all Eligible Employees who are granted options under the Plan shall have the same rights and privileges.

19.2 No Right to Continued Service. Neither the Plan nor any compensation paid hereunder will confer on any Participant the right to continue as an Employee or in any other capacity.

19.3 Rights as Stockholder. A Participant will become a stockholder with respect to the shares of Common Stock that are purchased pursuant to options granted under the Plan when the shares are transferred to the Participant's ESPP Share Account. A Participant will have no rights as a stockholder with respect to shares of Common Stock for which an election to participate in an Offering Period has been made until such Participant becomes a stockholder as provided above.

19.4 Successors and Assigns. The Plan shall be binding on the Company and its successors and assigns.

19.5 Entire Plan. This Plan constitutes the entire plan with respect to the subject matter hereof and supersedes all prior plans with respect to the subject matter hereof.

19.6 Compliance with Law. The obligations of the Company with respect to payments under the Plan are subject to compliance with all applicable laws and regulations. Common Stock shall not be issued with respect to an option granted under the Plan unless the exercise of such option and the issuance and delivery of the shares of Common Stock pursuant thereto shall comply with all applicable provisions of law, including, without limitation, the Securities Act, the Exchange Act, and the requirements of any stock exchange upon which the shares may then be listed.

8

---

19.7 Notice of Disqualifying Dispositions. Each Participant shall give the Company prompt written notice of any disposition or other transfer of shares of Common Stock acquired pursuant to the exercise of an option acquired under the Plan, if such disposition or transfer is made within two years after the Offering Date or within one year after the Purchase Date.

19.8 Term of Plan. The Plan shall become effective on the Effective Date and, unless terminated earlier pursuant to Section 19.9, shall have a term of ten years.

19.9 Amendment or Termination. The Committee may, in its sole discretion, amend, suspend or terminate the Plan at any time and for any reason, provided, however, that in no event may the Committee effect any of the following amendments or revisions to the Plan without the approval of the Company's shareholders: (i) increase the number of shares of Common Stock issuable under the Plan (other than adjustments pursuant to Section 19.1) or (ii) materially modify the requirements for eligibility to participate in the Plan. If the Plan is terminated, the Committee may elect to terminate all outstanding Offering Periods either immediately or once shares of Common Stock have been purchased on the next Purchase Date (which may, in the discretion of the Committee, be accelerated) or permit Offering Periods to expire in accordance with their terms (and subject to any adjustment in accordance with Section 18). If any Offering Period is terminated before its scheduled expiration, all amounts that have not been used to purchase shares of Common Stock will be returned to Participants (without interest, except as otherwise required by law) as soon as administratively practicable.

19.10 Applicable Law. The laws of the State of Delaware shall govern all questions concerning the construction, validity and interpretation of the Plan, without regard to such state's conflict of law rules.

19.11 Stockholder Approval. The Plan shall be subject to approval by the shareholders of the Company within twelve (12) months before or after the date the Plan is adopted by the Board.

19.12 Section 423. The Plan is intended to qualify as an "employee stock purchase plan" under Section 423 of the Code. Any provision of the Plan that is inconsistent with Section 423 of the Code shall be reformed to comply with Section 423 of the Code.

19.13 Withholding. To the extent required by applicable Federal, state or local law, a Participant must make arrangements satisfactory to the Company for the payment of any withholding or similar tax obligations that arise in connection with the Plan.

19.14 Severability. If any provision of the Plan shall for any reason be held to be invalid or unenforceable, such invalidity or unenforceability shall not affect any other provision hereof, and the Plan shall be construed as if such invalid or unenforceable provision were omitted.

19.15 Headings. The headings of sections herein are included solely for convenience and shall not affect the meaning of any of the provisions of the Plan.

## ITERIS, INC.

2016 OMNIBUS INCENTIVE PLAN

## ARTICLE 1

GENERAL PROVISIONS**1.1 PURPOSE OF THE PLAN**

This 2016 Omnibus Incentive Plan (the “Plan”) is intended to promote the interests of Iteris, Inc., a Delaware corporation, by providing eligible persons in the Corporation’s service with the opportunity to acquire a proprietary interest, or otherwise increase their proprietary interest, in the Corporation as an incentive for them to remain in such service.

The Plan serves as the successor to the Corporation’s 2007 Omnibus Incentive Plan (the “Predecessor Plan”), and no further awards shall be made under the Predecessor Plan on or after the Plan Effective Date. All awards outstanding under the Predecessor Plan on the Plan Effective Date shall remain outstanding under the Predecessor Plan and shall be governed solely by the terms of the documents evidencing such award, and no provision of the Plan shall be deemed to affect or otherwise modify the rights or obligations of the holders of such awards.

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

**1.2 TYPES OF AWARDS**

Awards may be made under the Plan in the form of (i) options, (ii) stock appreciation rights, (iii) stock awards, (iv) restricted stock units, (v) cash incentive awards and (vi) dividend equivalent rights.

**1.3 ADMINISTRATION OF THE PLAN**

(a) The Compensation Committee shall have sole and exclusive authority to administer the Plan with respect to Section 16 Insiders. Administration of the Plan with respect to all other persons eligible to participate in the Plan may, at the Board’s discretion, be vested in the Compensation Committee or a Secondary Board Committee, or the Board may retain the power to administer those programs with respect to such persons. To the extent permitted by law, the Board or the Compensation Committee may delegate any or all of its authority to administer the Plan with respect to one or more classes of eligible persons (other than Section 16 Insiders) to one or more officers of the Corporation.

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

---

(c) Each Plan Administrator shall, within the scope of its administrative functions under the Plan, have full authority to determine (i) which eligible persons are to receive Awards under the Plan, (ii) the type, size, terms and conditions of the Awards to be made to each Participant, (iii) the time or times when those Awards are to be made, (iv) the number of shares or amount of payment to be covered by each such Award, (v) the time or times when the Award is to become exercisable, (vi) the status of an option for federal tax purposes, (vii) the maximum term for which an Award is to remain outstanding, (viii) the vesting and issuance schedules applicable to the shares which are the subject of the Award, (ix) the cash consideration (if any) payable for those shares and the form (cash or shares of Common Stock) in which the Award is to be settled, (x) the vesting schedule for a cash incentive award, and (xi) with respect to performance—based Awards, the performance objectives for each such Award, the amounts payable at designated levels of attained performance, any applicable service vesting requirements, and the payout schedule for each such Award.

(d) Each Plan Administrator shall, within the scope of its administrative functions under the Plan, have full power and authority (subject to the provisions of the Plan) to establish such rules and regulations as it may deem appropriate for proper administration of the Plan and to make such determinations under, and issue such interpretations of, the provisions of the Plan and any outstanding Awards thereunder as it may deem necessary or advisable. Decisions of the Plan Administrator within the scope of its administrative functions under the Plan shall be final and binding on all parties who have an interest in the Plan under its jurisdiction or any Award thereunder.

(e) Service as a Plan Administrator by the members of the Compensation Committee or the Secondary Board Committee shall constitute service as Board members, and the members of each such committee shall accordingly be entitled to full indemnification and reimbursement as Board members for their service on such committee. No member of the Compensation Committee or the Secondary Board Committee shall be liable for any act or omission made in good faith with respect to the Plan or any Award thereunder.

**1.4 ELIGIBILITY**

(a) The persons eligible to participate in the Plan are as follows:

- (i) Employees,
- (ii) Non-Employee Directors and non-employee members of the board of any Parent or Subsidiary, and
- (iii) consultants and other independent advisors who provide services to the Corporation (or any Parent or Subsidiary).



## 1.5 STOCK SUBJECT TO THE PLAN

(a) The stock issuable under the Plan shall be shares of authorized but unissued or reacquired Common Stock, including shares repurchased by the Corporation on the open market. Subject to Section 1.5(h) and adjustment pursuant to Section 1.5(j), the number of shares reserved for issuance under the Plan shall be 3,404,771. However, such share reserve shall be reduced by one (1) share for every one (1) share that was subject to an option or stock appreciation right granted after July 22, 2016 and prior to the Plan Effective Date under the Predecessor Plan and 1.79 shares for every one (1) share that was subject to an award (other than an option or stock appreciation right) granted after July 22, 2016 and prior to the Plan Effective Date under the Predecessor Plan (such awards granted after July 22, 2016 and prior to the Plan Effective Date under the Predecessor Plan, the “Interim Period Awards”).

(b) Subject to adjustment pursuant to Section 1.5(j), the maximum number of shares of Common Stock that may be issued pursuant to Incentive Options granted under the Plan shall be 3,404,771.

(c) The maximum number of shares of Common Stock for which options and stock appreciation rights that are settled in shares may be granted to any person under the Plan in any fiscal year shall not exceed 2,000,000 shares of Common Stock in the aggregate.

(d) The maximum number of shares of Common Stock for which Awards (other than options and stock appreciation rights that are settled in shares) may be granted to any person under the Plan in any fiscal year shall not exceed 2,000,000 shares of Common Stock (which limit shall refer to the maximum amount that can be earned) in the aggregate.

(e) During any fiscal year no Participant may be granted cash incentive awards under which a total of more than \$3,000,000 may be earned for each twelve (12) months in the performance period.

(f) The maximum aggregate grant date fair value (computed as of the date of grant in accordance with applicable financial accounting rules) of all Awards made to any Non-Employee Director under the Plan in any fiscal year, taken together with any cash payments (including the annual retainer and any other compensation) paid to such Non-Employee Director in respect of such fiscal year, shall not exceed \$250,000 in total value.

(g) The number of shares of Common Stock reserved for award and issuance under this Plan pursuant to Section 1.5(a) shall be reduced on a one-for-one basis for each share of Common Stock subject to an option or stock appreciation right and by a fixed ratio of 1.79 shares of Common Stock for each share of Common Stock subject to a Full Value Award.

(h) Shares of Common Stock subject to outstanding Awards (including awards granted under the Predecessor Plan) shall be available for subsequent award and issuance under the Plan to the extent those Awards expire, are forfeited or cancelled or terminate for any reason prior to the issuance of the shares of Common Stock subject to those Awards. Any shares that again become available for Awards under the Plan pursuant to this Section shall be added as (i) one (1) share for every one (1) share subject to options or stock appreciation rights granted under the Plan and the Predecessor Plan, (ii) as 1.79 shares for every one (1) share subject to

3

---

Awards other than options or stock appreciation rights granted under the Plan and the Predecessor Plan, and (iii) for each unvested share issued under the Plan and the Predecessor Plan for cash consideration not less than the Fair Market Value per share of Common Stock on the date of grant and subsequently repurchased by the Corporation, at a price per share not greater than the original issue price paid per share, pursuant to the Corporation's repurchase rights under the Plan and Predecessor Plan, as applicable, one share shall become available for subsequent award and issuance under the Plan.

(i) Should the exercise price of an option or any withholding taxes incurred in connection with the exercise of an option under the Plan (or any options granted under the Predecessor Plan) be paid with shares of Common Stock (whether through the withholding of a portion of the otherwise issuable shares or through the tender of actual outstanding shares), then in each such case, the shares so tendered or withheld shall be added to the shares of Common Stock available for grant under the Plan on a one-for-one basis. Upon the exercise of any stock appreciation right under the Plan (and any Interim Period Awards), the share reserve shall be reduced only by the net number of shares issued upon such exercise and not by the gross number of shares as to which such right is exercised. If shares of Common Stock are withheld by the Corporation, or if shares of Common Stock are tendered by the Participant, in either case, in satisfaction of the withholding taxes incurred in connection with the vesting or settlement of a Full Value Award (or an award other than a stock option or stock appreciation right that was granted under the Predecessor Plan), then in each such case the shares of Common Stock so tendered or withheld shall be added to the shares of Common Stock available for issuance under the Plan in accordance with the ratio described in Sections 1.5(h) above.

(j) Should any change be made to the Common Stock by reason of any stock split, stock dividend, recapitalization, combination of shares, exchange of shares, spin-off transaction or other change affecting the outstanding Common Stock as a class without the Corporation's receipt of consideration, or should the value of outstanding shares of Common Stock be substantially reduced as a result of a spin-off transaction or an extraordinary dividend or distribution, or should there occur any merger, consolidation, reincorporation or other reorganization, then equitable adjustments shall be made by the Plan Administrator to (i) the maximum number and/or class of securities issuable under the Plan, (ii) the maximum number and/or class of securities for which any one person may be granted options and Stand-alone Rights that are settled in shares under the Plan in any fiscal year, (iii) the maximum number and/or class of securities for which any one person may be granted Awards (other than Stock options and Stand-alone Rights that are settled in shares) under the Plan in any fiscal year, (iv) the maximum number and/or class of securities that may be issued pursuant to Incentive Options, (v) the number and/or class of securities and the exercise or base price per share in effect under each outstanding Award under the Plan (including the Interim Period Awards) and the consideration (if any) payable per share, and (vi) the number and/or class of securities subject to the Corporation's outstanding repurchase rights under the Plan and the repurchase price payable per share. The adjustments shall be made in such manner as the Plan Administrator deems appropriate and such adjustments shall be final, binding and conclusive. In addition, in the event of a Change in Control, the provisions of Section 2.7 shall apply.

(k) Outstanding Awards granted pursuant to the Plan shall in no way affect the right of the Corporation to adjust, reclassify, reorganize or otherwise change its capital or business structure or to merge, consolidate, dissolve, liquidate or sell or transfer all or any part of its business or assets.

4

---

(l) Substitute Awards shall not reduce the shares authorized for issuance under the Plan or the limitations on grants to a Participant under Section 1.5(c) or 1.5(d), nor shall shares subject to a terminated, cancelled or forfeited Substitute Award be added to the shares available for issuance under the Plan as provided above. Additionally, in the event that a company acquired by the Company or any Subsidiary (or Parent) or with which the Company or any Subsidiary (or Parent) combines has shares available under a pre-existing plan approved by stockholders and not adopted in contemplation of such acquisition or combination, the shares available for grant pursuant to the terms of such pre-existing plan (as adjusted, to the extent appropriate, using the exchange ratio or other adjustment or valuation ratio or formula used in such acquisition or combination to determine the consideration payable to the holders of common stock of the entities party to such acquisition or combination) may be used for Awards under the Plan and shall not reduce the shares authorized for issuance under the Plan (and shares subject to such Awards shall not be added to the shares available for issuance under the Plan as provided above); provided that Awards using such available shares shall not be made after the date awards or grants could have been made under the terms of the pre-existing plan, absent the acquisition or combination, and shall only be made to individuals who were not Employees or Non-Employee Directors prior to such acquisition or combination. For purposes of this section, “*Substitute Awards*” shall mean Awards granted or shares issued by the Company in assumption of, or in substitution or exchange for, awards previously granted, or the right or obligation to make future awards, in each case by a company acquired by the Company or any Subsidiary (or Parent) or with which the Company or any Subsidiary (or Parent) combines.

## ARTICLE 2

### AWARDS

#### 2.1 OPTIONS

(a) **Authority.** The Plan Administrator shall have full power and authority, exercisable in its sole discretion, to grant Incentive Options and Non-Statutory Options evidenced by an Award Agreement in the form approved by the Plan Administrator; provided, however, that the terms of each such agreement shall not be inconsistent with the terms specified below. Each agreement evidencing an Incentive Option shall, in addition, be subject to the provisions of Section 2.1(f) below.

(b) **Exercise Price.**

(i) The exercise price per share shall be fixed by the Plan Administrator; provided, however, that such exercise price shall not be less than one hundred percent (100%) of the Fair Market Value per share of Common Stock on the grant date.

(ii) The exercise price shall be payable in one or more of the following forms as determined by the Plan Administrator and specified in the Award Agreement:

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

5

(B) shares of Common Stock (whether delivered in the form of actual stock certificates or through attestation of ownership) held for the requisite period (if any) necessary to avoid any resulting charge to the Corporation's earnings for financial reporting purposes and valued at Fair Market Value on the Exercise Date,

(C) shares of Common Stock otherwise issuable under the option but withheld by the Corporation in satisfaction of the exercise price, with such withheld shares to be valued at Fair Market Value on the exercise date, or

(D) to the extent the option is exercised for vested shares of Common Stock, through a special sale and remittance procedure pursuant to which the Participant shall concurrently provide instructions to (a) a brokerage firm (reasonably satisfactory to the Corporation for purposes of administering such procedure in compliance with the Corporation's pre-clearance/pre-notification policies) to effect the immediate sale of the purchased shares and remit to the Corporation, out of the sale proceeds available on the settlement date, sufficient funds to cover the aggregate exercise price payable for the purchased shares plus all applicable income and employment taxes required to be withheld by the Corporation by reason of such exercise and (b) the Corporation to deliver the certificates for the purchased shares directly to such brokerage firm on such settlement date in order to complete the sale.

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

(c) **Exercise and Term of Options.** Each option shall be exercisable at such time or times, during such period and for such number of shares as shall be determined by the Plan Administrator and set forth in the Award Agreement evidencing the option, subject to Section 2.9. However, no option shall have a term in excess of ten (10) years measured from the option grant date.

(d) **Effect of Termination of Service.**

(i) The following provisions shall govern the exercise of any options that are outstanding at the time of the Participant's cessation of Service or death:

(A) Any option outstanding at the time of the Participant's cessation of Service for any reason shall remain exercisable for such period of time thereafter as shall be determined by the Plan Administrator and set forth in the documents evidencing the option, but no such option shall be exercisable after the expiration of the option term.

(B) Any option held by the Participant at the time of the Participant's death and exercisable in whole or in part at that time may be subsequently exercised by the personal representative of the Participant's estate or by the person or persons to whom the option is transferred pursuant to the Participant's will or the laws of inheritance or by the Participant's designated beneficiary or beneficiaries of that option.

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

6

(D) During the applicable post-Service exercise period, the option may not be exercised for more than the number of vested shares for which the option is at the time exercisable. No additional shares shall vest under the option following the Participant's cessation of Service except to the extent (if any) specifically authorized by the Plan Administrator in its sole discretion pursuant to an express written agreement with the Participant. Upon the expiration of the applicable exercise period or (if earlier) upon the expiration of the option term, the option shall terminate and cease to be outstanding for any shares for which the option has not been exercised.

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

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

(B) include an automatic extension provision whereby the specified post-Service exercise period in effect for any option shall automatically be extended by an additional period of time equal in duration to any interval within the specified post-Service exercise period during which the exercise of that option or the immediate sale of the shares acquired under such option could not be effected in compliance with applicable federal and state securities laws, but in no event shall such an extension result in the continuation of such option beyond the expiration date of the term of that option; and/or

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

(e) **Repurchase Rights.** The Plan Administrator shall have the discretion to grant options which are exercisable for unvested shares of Common Stock. Should the Participant exercise an option for unvested shares and subsequently cease Service while such shares are unvested, the Corporation shall have the right to repurchase any or all of those unvested shares at a price per share equal to the **lower** of (i) the exercise price paid per share or (ii) the Fair Market Value per share of Common Stock at the time of repurchase. The terms upon which such repurchase right shall be exercisable (including the period and procedure for exercise and the appropriate vesting schedule for the purchased shares) shall be established by the Plan Administrator and set forth in the document evidencing such repurchase right.

(f) **Incentive Options.** The terms specified below shall be applicable to all Incentive Options. Except as modified by the provisions of this Section 2.1(f), all the provisions of the Plan shall be applicable to Incentive Options. Options which are specifically designated as Non-Statutory Options when issued under the Plan shall not be subject to the terms of this Section 2.1(f).

7

(i) **Eligibility.** Incentive Options may only be granted to Employees.

(ii) **Dollar Limitation.** The aggregate Fair Market Value of the shares of Common Stock (determined as of the respective date or dates of grant) for which one or more options granted to any Employee under the Plan (or any other option plan of the Corporation or any Parent or Subsidiary) may for the first time become exercisable as Incentive Options during any one calendar year shall not exceed the sum of One Hundred Thousand Dollars (\$100,000).

To the extent the Employee holds two (2) or more such options which become exercisable for the first time in the same calendar year, then for purposes of the foregoing limitations on the exercisability of those options as Incentive Options, such options shall be deemed to become first exercisable in that calendar year on the basis of the chronological order in which they were granted, except to the extent otherwise provided under applicable law or regulation.

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

## 2.2 STOCK APPRECIATION RIGHTS

(a) **Authority.** The Plan Administrator shall have full power and authority, exercisable in its sole discretion, to grant stock appreciation rights evidenced by an Award Agreement in the form approved by the Plan Administrator; provided, however, that the terms of each such agreement shall not be inconsistent with the terms specified below.

(b) **Types.** Two types of stock appreciation rights shall be authorized for issuance under this Section 2.2: (i) tandem stock appreciation rights ("Tandem Rights") and (ii) stand-alone stock appreciation rights ("Stand-alone Rights").

(c) **Tandem Rights.** The following terms and conditions shall govern the grant and exercise of Tandem Rights.

(i) One or more Participants may be granted a Tandem Right, exercisable upon such terms and conditions as the Plan Administrator may establish, subject to Section 2.9, to elect between the exercise of the underlying option for shares of Common Stock or the surrender of that option in exchange for a distribution from the Corporation in an amount equal to the excess of (i) the Fair Market Value (on the option surrender date) of

the number of shares in which the Participant is at the time vested under the surrendered option (or surrendered portion thereof) over (ii) the aggregate exercise price payable for such vested shares.

(ii) Any distribution to which the Participant becomes entitled upon the exercise of a Tandem Right may be made in (i) shares of Common Stock valued at Fair Market Value on the option surrender date, (ii) cash or (iii) a combination of cash and shares of Common Stock, as specified in the applicable Award Agreement.

(d) **Stand-Alone Rights.** The following terms and conditions shall govern the grant and exercise of Stand-alone Rights:

(i) One or more Participants may be granted a Stand-alone Right not tied to any underlying option. The Stand-alone Right shall relate to a specified number of shares of Common Stock and shall be exercisable upon such terms and conditions as the Plan Administrator may establish, subject to Section 2.9. In no event, however, may the Stand-alone Right have a maximum term in excess of ten (10) years measured from the grant date.

(ii) Upon exercise of the Stand-alone Right, the holder shall be entitled to receive a distribution from the Corporation in an amount equal to the excess of (i) the aggregate Fair Market Value (on the exercise date) of the shares of Common Stock underlying the exercised right over (ii) the aggregate base price in effect for those shares.

(iii) The number of shares of Common Stock underlying each Stand-alone Right and the base price in effect for those shares shall be determined by the Plan Administrator in its sole discretion at the time the Stand-alone Right is granted. In no event, however, may the base price per share be less than the Fair Market Value per underlying share of Common Stock on the grant date.

(iv) The distribution with respect to an exercised Stand-alone Right may be made in (i) shares of Common Stock valued at Fair Market Value on the exercise date, (ii) cash or (iii) a combination of cash and shares of Common Stock, as specified in the applicable Award agreement.

(v) The holder of a Stand-alone Right shall have no stockholder rights with respect to the shares subject to the Stand-alone Right unless and until such person shall have exercised the Stand-alone Right and become a holder of record of the shares of Common Stock issued upon the exercise of such Stand-alone Right.

(e) **Post-Service Exercise.** The provisions governing the exercise of Tandem and Stand-alone Rights following the cessation of the Participant's Service shall be substantially the same as those set forth in Section 2.1(d) for the options granted under the Plan, and the Plan Administrator's discretionary authority under Section 2.1(d)(ii) shall also extend to any outstanding Tandem or Stand-alone Appreciation Rights.

## 2.3 STOCK AWARDS

(a) **Authority.** The Plan Administrator shall have full power and authority, exercisable in its sole discretion, to grant stock awards either as vested or unvested shares of Common Stock, through direct and immediate issuances. Each stock award shall be evidenced by an Award Agreement in the form approved by the Plan Administrator; provided, however, that the terms of each such agreement shall not be inconsistent with the terms specified below.

(b) **Consideration.**

Shares of Common Stock may be issued under a stock award for any of the following items of consideration which the Plan Administrator may deem appropriate in each individual instance:

- (i) cash or check made payable to the Corporation,
- (ii) past services rendered to the Corporation (or any Parent or Subsidiary); or
- (iii) any other valid consideration under the State in which the Corporation is at the time incorporated.

(c) **Vesting Provisions.**

(i) Stock awards may, in the discretion of the Plan Administrator, be fully and immediately vested upon issuance as a bonus for Service rendered or may vest in one or more installments over the Participant's period of Service and/or upon the attainment of specified performance objectives. The elements of the vesting schedule applicable to any stock award shall be determined by the Plan Administrator and incorporated into the Award Agreement.

(ii) The Plan Administrator shall also have the discretionary authority, consistent with Code Section 162(m), to structure one or more stock awards so that the shares of Common Stock subject to those Awards shall vest upon the achievement of pre-established performance objectives based on one or more Performance Goals and measured over the performance period specified by the Plan Administrator at the time of the grant of the Award.

(iii) Should the Participant cease to remain in Service while holding one or more unvested shares of Common Stock issued under a stock award or should the performance objectives not be attained with respect to one or more such unvested shares of Common Stock, then those shares shall be immediately surrendered to the Corporation for cancellation, and the Participant shall have no further stockholder rights with respect to those shares. To the extent the surrendered shares were previously issued to the Participant for consideration paid in cash or cash equivalent, the Corporation shall

repay to the Participant the **lower** of (i) the cash consideration paid for the surrendered shares or (ii) the Fair Market Value of those shares at the time of cancellation.

(iv) The Plan Administrator may in its discretion waive the surrender and cancellation of one or more unvested shares of Common Stock which would otherwise occur upon the cessation of the Participant's Service or the non-attainment of the performance objectives applicable to those shares. Any such waiver shall result in the immediate vesting of the Participant's interest in the shares of Common Stock as to which the waiver applies. However, no vesting requirements tied to the attainment of performance objectives may be waived with respect to shares which were intended at the time of issuance to qualify as performance-based compensation under Code Section 162(m), except in the event of the Participant's death or Permanent Disability or a Change in Control.

10

---

(v) Any new, substituted or additional securities or other property (including money paid other than as a regular cash dividend) which the Participant may have the right to receive with respect to the Participant's unvested shares of Common Stock by reason of any stock dividend, stock split, recapitalization, combination of shares, exchange of shares, spin-off transaction, extraordinary dividend or distribution or other change affecting the outstanding Common Stock as a class without the Corporation's receipt of consideration shall be issued subject to (i) the same vesting requirements applicable to the Participant's unvested shares of Common Stock and (ii) such escrow arrangements as the Plan Administrator shall deem appropriate, unless and to the extent the Plan Administrator determines at the time to vest and distribute such securities or other property. Notwithstanding the provisions of this Section, cash dividends, stock and any other property (other than cash) distributed as a dividend or otherwise with respect to any stock Award that vests based on achievement of Performance Goals shall be accumulated, subject to restrictions and risk of forfeiture to the same extent as the underlying Award, and shall be paid at the time such restrictions and risk of forfeiture lapse. Equitable adjustments to reflect each such transaction shall also be made by the Plan Administrator to the repurchase price payable per share by the Corporation for any unvested securities subject to its existing repurchase rights under the Plan; provided the aggregate repurchase price shall in each instance remain the same.

## 2.4 RESTRICTED STOCK UNITS

(a) **Authority.** The Plan Administrator shall have the full power and authority, exercisable in its sole discretion, to grant restricted stock units evidenced by an Award Agreement in the form approved by the Plan Administrator; provided, however, that the terms of each such agreement shall not be inconsistent with the terms specified below.

(b) **Terms.** Each restricted stock unit award shall entitle the Participant to receive the shares underlying that Award (or an amount based on the value of the shares) upon vesting or upon the expiration of a designated time period following the vesting of those Awards. Payment of shares underlying a restricted stock unit Award may be deferred for a period specified by the Plan Administrator at the time the restricted stock unit is initially granted or (to the extent permitted by the Plan Administrator) designated by the Participant pursuant to a timely deferral election made in accordance with the requirements of Code Section 409A. Restricted stock units subject to performance vesting may also be structured so that the underlying shares are convertible into shares of Common Stock (or a payment based on the value of the shares), but the rate at which each share is to so convert shall be based on the attained level of performance for each applicable performance objective.

(c) **Vesting Provisions.**

(i) Restricted stock units may, in the discretion of the Plan Administrator, vest in one or more installments over the Participant's period of Service or upon the attainment of specified performance objectives.

(ii) The Plan Administrator shall also have the discretionary authority, consistent with Code Section 162(m), to structure one or more restricted stock unit awards so that the shares of Common Stock subject to those Awards shall vest (or vest and become

11

---

issuable) upon the achievement of pre-established performance objectives based on one or more Performance Goals and measured over the performance period specified by the Plan Administrator at the time of the grant of the Award.

(iii) Outstanding restricted stock units shall automatically terminate without any payment if the designated Performance Goals or Service requirements established for those Awards are not attained or satisfied. The Plan Administrator, however, shall have the discretionary authority to make a payment under one or more outstanding Awards of restricted stock units as to which the designated Performance Goals or Service requirements have not been attained or satisfied. However, no vesting requirements tied to the attainment of Performance Goals may be waived with respect to Awards which were intended, at the time those Awards were granted, to qualify as performance-based compensation under Code Section 162(m), except in the event of the Participant's death or Permanent Disability or a Change in Control.

(d) **Payment.** Restricted stock units that vest may be settled in (i) cash, (ii) shares of Common stock valued at Fair Market Value on the payment date or (iii) a combination of cash and shares of Common Stock, as determined by the Plan Administrator in its sole discretion.

## 2.5 CASH INCENTIVE AWARDS

(a) The Plan Administrator shall have full power and authority, exercisable in its sole discretion, to grant cash incentive awards. The Plan Administrator shall determine the terms and conditions applicable to cash incentive awards, including the criteria for the vesting and payment of cash incentive awards. Cash incentive awards shall be based on such measures as the Plan Administrator deems appropriate and need not relate to the value of shares of Common Stock. Cash incentive awards may, in the discretion of the Plan Administrator, vest in one or more installments over the Participant's period of Service or upon the attainment of specified performance objectives. Payment of cash incentive awards may be deferred for a period specified by the Plan Administrator at the time the Award is initially granted or (to the extent permitted by the Plan Administrator) designated by the Participant pursuant to a timely deferral election made in accordance with the requirements of Code Section 409A.

(b) The Plan Administrator shall also have the discretionary authority, consistent with Code Section 162(m), to structure one or more cash incentive awards so that the awards shall vest upon the achievement of pre-established performance objectives based on one or more Performance Goals

and measured over the performance period specified by the Plan Administrator at the time of the grant of the Award.

(c) Outstanding cash incentive awards units shall automatically terminate without any payment if the designated Performance Goals or Service requirements established for those Awards are not attained or satisfied. The Plan Administrator, however, shall have the discretionary authority to make a payment under one or more outstanding cash incentive awards as to which the designated Performance Goals or Service requirements have not been attained or satisfied. However, no vesting requirements tied to the attainment of Performance Goals may be waived with respect to cash incentive awards which were intended, at the time those Awards

were granted, to qualify as performance-based compensation under Code Section 162(m), except in the event of the Participant's death or Permanent Disability or a Change in Control.

## 2.6 DIVIDEND EQUIVALENT RIGHTS

(a) **Authority.** The Plan Administrator shall have full power and authority, exercisable in its sole discretion, to grant dividend equivalent rights evidenced by an Award Agreement in the form approved by the Plan Administrator; provided however, that the terms of each such agreement shall not be inconsistent with the terms specified below.

(b) **Terms.** The dividend equivalent rights may be granted as stand-alone awards or in tandem with other Awards made under the Plan, except dividend equivalent rights shall not be granted in connection with an option, stock appreciation right or cash incentive award. The term of each dividend equivalent right award shall be established by the Plan Administrator at the time of grant, but no such award shall have a term in excess of ten (10) years.

(c) **Entitlement.** Each dividend equivalent right shall represent the right to receive the economic equivalent of each dividend or distribution, whether in cash, securities or other property (other than shares of Common Stock), which is made per issued and outstanding share of Common Stock during the term the dividend equivalent right remains outstanding. A special account on the books of the Corporation shall be maintained for each Participant to whom a dividend equivalent right is granted, and that account shall be credited per dividend equivalent right with each such dividend or distribution made per issued and outstanding share of Common Stock during the term of that dividend equivalent right remains outstanding.

(d) **Timing of Payment.** Payment of the amounts credited to such book account may be made to the Participant either concurrently with the actual dividend or distribution made per issued and outstanding share of Common Stock or may be deferred for a period specified by the Plan Administrator at the time the dividend equivalent right is initially granted or (to the extent permitted by the Plan Administrator) designated by the Participant pursuant to a timely deferral election made in accordance with the requirements of Code Section 409A. In no event, however, shall any dividend equivalent right award made with respect to an Award subject to performance-vesting conditions vest or become payable prior to the vesting of that Award (or the portion thereof to which the dividend equivalent right award relates) upon the attainment of the applicable Performance Goals and shall accordingly be subject to cancellation and forfeiture to the same extent as the underlying Award.

(e) **Form of Payment.** Payment of the amounts due with respect to dividend equivalent rights may be made in (i) cash, (ii) shares of Common Stock or (iii) a combination of cash and shares of Common Stock, as determined by the Plan Administrator in its sole discretion and set forth in the Award Agreement. If payment is to be made in the form of Common Stock, the number of shares of Common Stock into which the cash dividend or distribution amounts are to be converted for purposes of the Participant's book account may be based on the Fair Market Value per share of Common Stock on the date of conversion, a prior date or an average of the Fair Market Value per share of Common Stock over a designated period, as determined by the Plan Administrator in its sole discretion.

## 2.7 EFFECT OF CHANGE IN CONTROL

Unless otherwise provided in an Award Agreement, the following provisions shall apply with respect to Awards in the event of a Change in Control:

(a) In the event of a Change in Control, each outstanding Award, as determined by the Plan Administrator in its sole discretion, may be (i) assumed by the successor corporation (or parent thereof), (ii) canceled and substituted with an Award granted by the successor corporation (or parent thereof), (iii) otherwise continued in full force and effect pursuant to the terms of the Change in Control transaction, or (iv) replaced with a cash retention program of the Corporation or any successor corporation (or parent thereof) which preserves the spread existing on the unvested Award shares subject to the Award at the time of the Change in Control (the excess of the Fair Market Value of those shares over the aggregate purchase price payable for such shares) and, subject to Section 2.7(c) below, provides for subsequent payout of that spread in accordance with the same exercise/vesting schedule applicable to those unvested Award shares, but only if such replacement cash program would not result in the treatment of the Award as an item of deferred compensation subject to Code Section 409A.

(b) To the extent an outstanding Award is not assumed, substituted, continued or replaced in accordance with Section 2.7(a), such Award shall automatically vest in full immediately prior to the effective date of the Change in Control, unless the acceleration of such Award is subject to other limitations imposed by the Plan Administrator at the time of the grant of the Award. The Plan Administrator in its sole discretion shall have the authority to provide that to the extent any such Award, as so accelerated, remains unexercised and outstanding on the effective date of the Change in Control, such Award shall terminate and cease to be outstanding. The holder of such Award shall become entitled to receive, upon consummation of the Change in Control and subject to Section 2.7(c), a lump sum cash payment in an amount equal to the product of (i) number of shares of Common Stock subject to such Award and (ii) the excess of (a) the Fair Market Value per share of Common Stock on the date of the Change in Control over (b) the per share exercise price or purchase price in effect for such Award. However, any such Award shall be subject to cancellation and termination, without cash payment or other consideration due the Award holder, if the Fair Market Value per share of Common Stock on the date of such Change in Control is less than the per share exercise price or purchase price in effect for such Award. Notwithstanding the foregoing, if any Award is subject to a performance-vesting condition tied to the attainment of one or more specified Performance Goals, and such Award is not to be so assumed, substituted, continued, or replaced, that Award shall vest immediately prior to the effective date of the actual Change in Control transaction, based on actual performance as of the Change in Control, and the shares of

Common Stock underlying the portion of the Award that vests on such accelerated basis (if any) shall be issued in accordance with the applicable Award Agreement, unless such accelerated vesting is precluded by other limitations imposed in the Award Agreement.

(c) The Plan Administrator shall have the authority to provide that any escrow, holdback, earn-out or similar provisions in the definitive agreement effecting the Change in Control shall apply to any cash payment made pursuant to Section 2.7(a) or Section 2.7(b) to the same extent and in the same manner as such provisions apply to a holder of a share of Common Stock.

14

---

(d) Immediately following the consummation of the Change in Control, all outstanding Awards shall terminate and cease to be outstanding, except to the extent assumed by the successor corporation (or parent thereof) or otherwise continued in full force and effect pursuant to the terms of the Change in Control transaction.

(e) In the event of any Change in Control, the Plan Administrator in its sole discretion may determine that all outstanding repurchase rights (i) are to be assigned to the successor corporation (or parent thereof) or otherwise continued in full force and effect pursuant to the terms of the Change in Control transaction or (ii) are to be terminated and the shares of Common Stock subject to those terminated rights are to immediately vest in full, unless such accelerated vesting is precluded by limitations imposed by the Plan Administrator at the time the repurchase right is issued.

(f) Each Award which is assumed in connection with a Change in Control or otherwise continued in effect shall be appropriately adjusted, immediately after such Change in Control, to apply to the number and class of securities into which the shares of Common Stock subject to that Award would have been converted in consummation of such Change in Control had those shares actually been outstanding at that time. Appropriate adjustments to reflect such Change in Control shall also be made to (i) the exercise or base price or cash consideration payable per share in effect under each outstanding Award, provided the aggregate exercise or base price or cash consideration in effect for such securities shall remain the same, (ii) the maximum number and/or class of securities available for issuance over the remaining term of the Plan, (iii) the maximum number and/or class of securities for which Incentive Options may be granted under the Plan, (iv) the maximum number and/or class of securities for which any one person may be granted Awards under the Plan per calendar year and (v) the number and/or class of securities subject to the Corporation's outstanding repurchase rights under the Plan and the repurchase price payable per share. To the extent the actual holders of the Corporation's outstanding Common Stock receive cash consideration for their Common Stock in consummation of the Change in Control, the successor corporation may, in connection with the assumption or continuation of the outstanding Awards under the Plan and subject to the Plan Administrator's approval, substitute, for the securities underlying those assumed Awards, 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 transaction, provided such common stock is readily traded on an established U.S. securities exchange or market.

(g) The Plan Administrator shall have the discretion, exercisable either at the time an Award is granted or at any time while an Award remains outstanding, to structure such Award so that (i) it shall automatically accelerate and vest in full (and any repurchase rights of the Corporation with respect to the unvested shares subject to that Award shall immediately terminate) upon the occurrence of a Change in Control, whether or not such Award is to be assumed in the Change in Control or otherwise continued in effect or (ii) the shares subject to such Award will automatically vest on an accelerated basis should the Participant's Service terminate by reason of an Involuntary Termination within a designated period following the effective date of any Change in Control in which the Award is assumed or otherwise continued in effect and the repurchase rights applicable to those shares do not otherwise terminate.

15

---

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

## **2.8 REPRICING PROGRAMS**

The Plan Administrator shall not have the discretionary authority, except pursuant to Section 1.5(j), to (i) implement cancellation/regrant programs pursuant to which outstanding options or stock appreciation rights under the Plan are cancelled and new options or stock appreciation rights are granted in replacement with a lower exercise or base price per share, (ii) cancel outstanding options or stock appreciation rights under the Plan with exercise or base prices per share in excess of the then current Fair Market Value per share of Common Stock for consideration payable in cash, other Awards, or in equity securities of the Corporation (except in the event of a Change in Control) or (iii) reduce the exercise or base price in effect for outstanding options or stock appreciation rights under the Plan, in any case without stockholder approval.

## **2.9 MINIMUM VESTING**

No option or stock appreciation right may vest over a period of less than one year from the date of grant of the award. Notwithstanding the foregoing, up to 5% of the available shares of Common Stock authorized for issuance under the Plan as of the Plan Effective Date may be issued pursuant to options or stock appreciation rights that vest (in full or in part) over a period of less than one year from the date of grant of the awards (the "5% Basket"). Any option or stock appreciation right granted under the Plan may vest in full or in part upon death or disability of the Participant, or upon a Change in Control, under Section 2.7 or the applicable Award Agreement, and such vesting shall not count against the 5% Basket.

# **ARTICLE 3**

## **MISCELLANEOUS**

### **3.1 DEFERRED COMPENSATION**

(a) The Plan Administrator may, in its sole discretion, structure one or more Awards (other than options and stock appreciation rights) so that the Participants may be provided with an election to defer the compensation associated with those Awards for federal income tax purposes. Any such deferral opportunity shall comply with all applicable requirements of Code Section 409A.

(b) The Plan Administrator may implement a non-employee Board member retainer fee deferral program under the Plan so as to allow the non-employee Board members the opportunity to elect, prior to the start of each calendar year, to convert the Board and Board committee retainer fees to be earned for such year into restricted stock units under the Plan that will defer the issuance of the shares of Common Stock that vest under those restricted stock units until a permissible date or event under Code Section 409A. If such program is implemented, the

Plan Administrator shall have the authority to establish such rules and procedures as it deems appropriate for the filing of such deferral elections and the designation of the permissible distribution events under Code Section 409A.

(c) To the extent the Corporation maintains one or more separate non-qualified deferred compensation arrangements which allow the Participants the opportunity to make notional investments of their deferred account balances in shares of Common Stock, the Plan Administrator may authorize the share reserve under the Plan to serve as the source of any shares of Common Stock that become payable under those deferred compensation arrangements. In such event, the share reserve under the Plan shall be reduced on a share-for-share basis for each share of Common Stock issued under the Plan in settlement of the deferred compensation owed under those separate arrangements.

### **3.2 TRANSFERABILITY OF AWARDS**

The transferability of Awards granted under the Plan shall be governed by the following provisions:

(a) Incentive Options. During the lifetime of the Participant, Incentive Options shall be exercisable only by the Participant and shall not be assignable or transferable other than by will or the laws of inheritance following the Participant's death.

(b) Other Awards. All other Awards shall be subject to the same limitation on transfer as Incentive Options, except that the Plan Administrator may structure one or more such Awards so that the Award may be assigned in whole or in part during the Participant's lifetime to one or more Family Members of the Participant or to a trust established exclusively for the Participant and/or such Family Members, to the extent such assignment is in connection with the Participant's estate plan or pursuant to a domestic relations order. The assigned portion of an Award may only be exercised (if applicable) by the person or persons who acquire a proprietary interest in the Award pursuant to the assignment. The terms applicable to the assigned portion of the Award shall be the same as those in effect for the Award immediately prior to such assignment and shall be set forth in such documents issued to the assignee as the Plan Administrator may deem appropriate.

(c) Beneficiary Designation. Notwithstanding the foregoing, a Participant may, to the extent permitted by the Plan Administrator, designate one or more persons as the beneficiary or beneficiaries of some or all of his or her outstanding Awards, and those Awards shall, in accordance with such designation, automatically be transferred to such beneficiary or beneficiaries upon the Participant's death while holding those Awards. Such beneficiary or beneficiaries shall take the transferred Awards subject to all the terms and conditions of the applicable agreement evidencing each such transferred Award, including (without limitation) the limited time period during which the Award may be exercised (if applicable) following the Participant's death.

### **3.3 STOCKHOLDER RIGHTS**

A Participant shall not have any of the rights of a stockholder with respect to shares of Common Stock covered by an Award until the Participant becomes the holder of record of such shares. However, a Participant may be granted the right to receive dividend equivalents under Section 2.6 with respect to one or more outstanding Awards.

### **3.4 TAX WITHHOLDING**

(a) The Corporation's obligation to deliver shares of Common Stock upon the exercise, issuance or vesting of an Award under the Plan shall be subject to the satisfaction of all applicable tax withholding requirements.

(b) The Plan Administrator may, in its discretion, provide Participants to whom Awards are made under the Plan with the right to use shares of Common Stock in satisfaction of all or part of the Withholding Taxes to which such holders may become subject in connection with the issuance, exercise, vesting or settlement of those Awards or the issuance of shares of Common Stock thereunder. Such right may be provided to any such holder in either or both of the following formats:

(i) Stock Withholding: The election to have the Corporation withhold, from the shares of Common Stock otherwise issuable upon the issuance, exercise, vesting or settlement of such Award or the issuance of shares of Common Stock thereunder, a portion of those shares with an aggregate Fair Market Value at the time of delivery equal to the percentage of the Withholding Taxes based on the minimum required tax withholding rate for the Participant, or such other rate as determined by the Plan Administrator.

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

### **3.5 SHARE ESCROW/LEGENDS**

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

### **3.6 EFFECTIVE DATE AND TERM OF THE PLAN**



(a) The Plan shall become effective on the Plan Effective Date.

(b) The Plan shall terminate upon the ***earliest*** to occur of (i) the date immediately preceding the tenth anniversary of the Plan Effective Date, (ii) the date on which all shares available for issuance under the Plan shall have been issued as fully vested shares, (iii) the termination of all outstanding Awards in connection with a Change in Control, or (iii) the termination of the Plan by the Board. Should the Plan terminate under subsection (i) above, then all Awards outstanding at that time shall continue to have force and effect in accordance with the provisions of the documents evidencing those Awards.

18

---

### 3.7 AMENDMENT OF THE PLAN

(a) The Board shall have complete and exclusive power and authority to amend or modify the Plan in any or all respects, subject to stockholder approval to the extent required under applicable law or regulation or pursuant to the listing standards of the Stock Exchange on which the Common Stock is at the time primarily traded. However, no such amendment or modification shall adversely affect the rights and obligations with respect to Awards at the time outstanding under the Plan unless the Participant consents to such amendment or modification.

(b) The Compensation Committee shall have the discretionary authority to adopt and implement from time to time such addenda or subplans to the Plan as it may deem necessary in order to bring the Plan into compliance with applicable laws and regulations of any foreign jurisdictions in which Awards are to be made under the Plan and/or to obtain favorable tax treatment in those foreign jurisdictions for the individuals to whom the Awards are made.

(c) Awards may be made under the Plan that involve shares of Common Stock in excess of the number of shares then available for issuance under the Plan, provided no shares shall actually be issued pursuant to those Awards until the number of shares of Common Stock available for issuance under the Plan is sufficiently increased by stockholder approval of an amendment of the Plan authorizing such increase. If such stockholder approval is not obtained within twelve (12) months after the date the first excess Award is made, then all Awards granted on the basis of such excess shares shall terminate and cease to be outstanding.

### 3.8 USE OF PROCEEDS

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

### 3.9 REGULATORY APPROVALS

(a) The implementation of the Plan, the granting of any Award under the Plan and the issuance of any shares of Common Stock in connection with the issuance, exercise, vesting or settlement of any Award under the Plan shall be subject to the Corporation's procurement of all approvals and permits required by regulatory authorities having jurisdiction over the Plan, the Awards made under the Plan and the shares of Common Stock issuable pursuant to those Awards.

(b) No shares of Common Stock or other assets shall be issued or delivered under the Plan unless and until there shall have been compliance with all applicable requirements of applicable securities laws, and all applicable listing requirements of any Stock Exchange on which Common Stock is then listed for trading.

### 3.10 NO EMPLOYMENT/SERVICE RIGHTS

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

19

---

### 3.11 RECOUPMENT

Participants shall be subject to any clawback, recoupment or other similar policy required by law or regulations or adopted by the Board as in effect from time to time and Awards and any cash, shares of Common Stock or other property or amounts due, paid or issued to a Participant shall be subject to the terms of such policy, as in effect from time to time.

20

---

## APPENDIX

The following definitions shall be in effect under the Plan:

(a) **Award** shall mean any of the following awards authorized for issuance or grant under the Plan: options, stock appreciation rights, stock awards, restricted stock units, cash incentive awards and dividend equivalents.

(b) **Award Agreement** shall mean the written agreement(s) (which may be in electronic form) between the Corporation and the Participant evidencing a particular Award made to that individual under the Plan, as such agreement(s) may be in effect from time to time.

(c) **Board** shall mean the Corporation's Board of Directors.

(d) **Change in Control** shall, with respect to each Award made under the Plan, be defined in accordance with the following provisions:

(i) Change in Control shall have the meaning assigned to such term in the Award Agreement for the particular Award or in any other agreement incorporated by reference into the Award Agreement for purposes of defining such term.

(ii) In the absence of any other Change in Control definition in the Award Agreement (or in any other agreement incorporated by reference into the Award Agreement), Change in Control shall mean a change in ownership or control of the Corporation effected through any of the following transactions:

(A) consummation of a merger, consolidation or other reorganization approved by the Corporation's stockholders, unless securities representing at least fifty percent (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 Corporation's outstanding voting securities immediately prior to such transaction,

(B) a sale, transfer or other disposition of all or substantially all of the Corporation's assets,

(C) the closing of any transaction or series of related transactions pursuant to which any person or any group of persons comprising a "group" within the meaning of Rule 13d-5(b)(1) of the 1934 Act (other than the Corporation or a person that, prior to such transaction or series of related transactions, directly or indirectly controls, is controlled by or is under common control with, the Corporation) becomes directly or indirectly (whether as a result of a single acquisition or by reason of one or more acquisitions within the twelve (12)-month period ending with the most recent acquisition) the beneficial owner (within the meaning of Rule 13d-3 of the 1934 Act) of securities possessing (or convertible into or exercisable for securities possessing) more than fifty percent (50%) of the total combined voting power of the Corporation's securities (as measured in terms of the power to vote with respect to the election of Board members) outstanding immediately after the consummation of such transaction or series of related transactions, whether such transaction involves a direct issuance from the Corporation or the acquisition of outstanding securities held by one or more of the Corporation's existing stockholders, or

A-1

---

(D) a change in the composition of the Board over a period of twenty-four (24) consecutive months or less such that a majority of the Board members ceases to be comprised of individuals who either (A) have been Board members continuously since the beginning of such period ("Incumbent Directors") or (B) have been elected or nominated for election as Board members during such period by at least a majority of the Incumbent Directors who were still in office at the time the Board approved such election or nomination; provided that any individual who becomes a Board member subsequent to the beginning of such period and whose election or nomination was approved by two-thirds of the Board members then comprising the Incumbent Directors will be considered an Incumbent Director.

(e) **Code** shall mean the Internal Revenue Code of 1986, as amended.

(f) **Common Stock** shall mean the Corporation's Common Stock.

(g) **Compensation Committee** shall mean the Compensation Committee of the Board comprised of two (2) or more non-employee Board members, each of whom is intended to qualify as a "non-employee director" (as defined in Rule 16b-3 under the Exchange Act), an "outside director" for purposes of Section 162(m) of the Code and an "independent director" under the rules of any securities exchange or automated quotation system on which the Common Stock is then listed, quoted or traded; provided that any action taken by the Compensation Committee shall be valid and effective, whether or not one or more members of the Compensation Committee at the time of such action are later determined not to have satisfied the requirements for membership set forth in this definition or otherwise provided in the charter of the Compensation Committee.

(h) **Corporation** shall mean Iteris, Inc., a Delaware corporation, and any corporate successor to all or substantially all of the assets or voting stock of Iteris, Inc.

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

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

(k) **Fair Market Value** per share of Common Stock on any relevant date shall be determined in accordance with the following

provisions:

(i) If the Common stock is at the time traded on a Stock Exchange, then the Fair Market Value shall be the closing selling price per share of Common Stock at the close of regular hours trading (i.e., before after-hours trading begins) on date in question on the Stock Exchange serving as the primary market for the Common Stock, as such price is reported by the National Association of Securities Dealers (if primarily traded on the Nasdaq Global or Global Select Market) or as officially quoted in the composite tape of transactions on any other

A-2

---

Stock Exchange on which the Common Stock is then primarily traded. If there is no closing selling price for the Common Stock on the date in question, then the Fair Market Value shall be the closing selling price on the last preceding date for which such quotation exists.

(ii) If the Common Stock is at the time quoted on a national or regional securities exchange or market system (including over-the-counter markets and the Nasdaq Capital Market) determined by the Plan Administrator to be the primary market for the Common Stock, then the

Fair Market Value shall be the closing selling price per share of Common Stock on the date in question, as such price is officially reported by such exchange or market system. If there is no closing selling price for the Common Stock on the date in question, then the Fair Market Value shall be the closing selling price of a share of Common Stock on the last preceding date for which such quotation exists.

(l) **Family Member** shall mean, with respect to a particular Participant, any child, stepchild, grandchild, parent, stepparent, grandparent, spouse, former spouse, sibling, niece, nephew, mother-in-law, father-in-law, son-in-law, daughter-in-law, brother-in-law or sister-in-law.

(m) **Full Value Award** means an Award other than an option or stock appreciation right.

(n) **Good Reason** shall, with respect to each Award made under the Plan, be defined in accordance with the following provisions:

(i) Good Reason shall have the meaning assigned to such term in the Award Agreement for the particular Award or in any other agreement incorporated by reference into the Award Agreement for purposes of defining such term.

(ii) In the absence of any other Good Reason definition in the Award Agreement (or in any other agreement incorporated by reference into the Award Agreement), Good Reason shall mean an individual's voluntary resignation following one or more of the following without the individual's consent; (A) a change in his or her position with the Corporation (or any Parent or Subsidiary) which materially reduces his or her duties, responsibilities or authority, (B) a material diminution in the duties, responsibilities or authority of the person to whom such individual reports, (C) a material reduction in such individual's level of base compensation, with a reduction of more than fifteen percent (15%) to be deemed material for such purpose, or (D) a material relocation of such individual's place of employment, with a relocation of more than fifty (50) miles to be deemed material for such purpose, ***provided, however,*** that a resignation for Good Reason may be effected only after (i) the individual provides written notice to the Corporation of the event or transaction constituting grounds for such resignation within sixty (60) days after the occurrence of that event or transaction, (ii) the Corporation fails to take the requisite remedial action with respect to such event or transaction within thirty (30) days after receipt of such notice, and (iii) the individual resigns within thirty (30) days after the expiration of the Corporation's cure period set forth in subsection (ii).

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

---

A-3

(p) **Involuntary Termination** shall, with respect to each Award made under the Plan, be defined in accordance with the following provisions:

(i) Involuntary Termination shall have the meaning assigned to such term in the Award Agreement for the particular Award or in any other agreement incorporated by reference into the Award Agreement for purposes of defining such term.

(ii) In the absence of any other Involuntary Termination definition in the Award Agreement (or in any other agreement incorporated by reference into the Award Agreement), Involuntary Termination shall mean such individual's involuntary dismissal or discharge by the Corporation (or any Parent or Subsidiary) for reasons other than Misconduct, or such individual's voluntary resignation for Good Reason.

(q) **Misconduct** shall, with respect to each Award made under the Plan, be defined in accordance with the following provisions:

(i) Misconduct shall have the meaning assigned to such term in the Award Agreement for the particular Award or in any other agreement incorporated by reference into the Award Agreement for purposes of defining such term.

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

(r) **1934 Act** shall mean the Securities Exchange Act of 1934, as amended.

(s) **Non-Employee Director** shall mean a non-employee member of the Board.

(t) **Non-Statutory Option** shall mean an option not an Incentive Option.

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

(v) **Participant** shall mean any eligible person who is granted an Award under the Plan.

---

A-4

(w) **Permanent Disability** shall mean the inability of the Participant to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment expected to result in death or to be of continuous duration of twelve (12) months or more.

(x) **Performance Goals** shall mean any of the following performance criteria upon which the vesting of one or more Awards under the Plan may be based: (i) cash flow; (ii) earnings (including earnings before interest and taxes, earnings before taxes, earnings before interest, taxes, depreciation, amortization and charges for stock-based compensation, earnings before interest, taxes, depreciation and amortization, and net earnings);

(iii) earnings per share; (iv) growth in earnings or earnings per share; (v) stock price; (vi) return on equity or average stockholder equity; (vii) total stockholder return or growth in total stockholder return either directly or in relation to a comparative group; (viii) return on capital; (ix) return on assets or net assets; (x) invested capital, required rate of return on capital or return on invested capital; (xi) revenue, growth in revenue or return on sales; (xii) income or net income; (xiii) operating income, net operating income or net operating income after tax; (xiv) operating profit or net operating profit; (xv) operating margin or gross margin; (xvi) return on operating revenue or return on operating profit; (xvii) market share, (xviii) market capitalization, (xix) application approvals, (xx) litigation and regulatory resolution goals, (xxi) implementation, completion or attainment of key projects, product sales or milestones, (xxii) budget comparisons, (xxiii) growth in stockholder value relative to the growth of a peer group or index; (xxiv) development and implementation of strategic plans and/or organizational restructuring goals; (xxv) development and implementation of risk and crisis management programs; (xxvi) improvement in workforce diversity; (xxvii) compliance requirements and compliance relief; (xxviii) productivity goals; (xxix) workforce management and succession planning goals; (xxx) economic value added (including typical adjustments consistently applied from generally accepted accounting principles required to determine economic value added performance measures); (xxxi) recruiting and maintaining personnel, employee retention, measures of customer satisfaction, employee satisfaction or staff development; (xxxii) development or marketing collaborations, formations of joint ventures or partnerships or the completion of other similar transactions intended to enhance the Corporation's revenue or profitability or enhance its customer base; and (xxxiii) merger and acquisitions. In addition, such performance criteria may be based upon the attainment of specified levels of the Corporation's performance under one or more of the measures described above relative to the performance of other entities and may also be based on the performance of any of the Corporation's business units or divisions or any Parent or Subsidiary. Any performance goals that are financial metrics, may be determined in accordance with U.S. Generally Accepted Accounting Principles ("GAAP"), in accordance with accounting principles established by the International Accounting Standards Board ("IASB Principles"), or may be adjusted when established to include or exclude any items otherwise includable or excludable under GAAP or under IASB Principles. Each applicable Performance Goal may include a minimum threshold level of performance below which no Award will be earned, levels of performance at which specified portions of an Award will be earned and a maximum level of performance at which an Award will be fully earned. Each applicable Performance Goal may be structured at the time of the Award to provide for appropriate adjustment for one or more of the following items: (A) asset impairments or write-downs; (B) litigation or claim judgments or settlements; (C) the effect of changes in tax law, accounting principles or other such laws or provisions affecting reported results; (D) accruals for reorganization and restructuring programs;

---

A-5

(E) the operations of any business acquired by the Corporation; (F) the divestiture of one or more business operations or the assets thereof; (G) the effects of any corporate transaction, such as a merger, consolidation, separation (including spin-off or other distributions of stock or property by the Corporation) or reorganization; (H) restructurings, discontinued operations, extraordinary items, and other unusual, infrequently occurring or non-recurring charges or events; (I) acquisitions or divestitures; (J) change in the corporate structure or capital structure of the Corporation; (K) an event either not directly related to the operations of the Corporation, Parent, Subsidiary, division, business segment or business unit or not within the reasonable control of management; (L) foreign exchange gains and losses; (M) a change in the fiscal year of the Corporation; (N) the refinancing or repurchase of bank loans or debt securities; (O) unbudgeted capital expenditures; (P) the issuance or repurchase of equity securities and other changes in the number of outstanding shares; (Q) conversion of some or all of convertible securities to common stock; (R) any business interruption event; (S) the cumulative effects of tax or accounting changes in accordance with GAAP; (T) the effect of changes in other laws or regulatory rules affecting reported results; and (U) any other adjustment consistent with the operation of the Plan.

(y) **Plan** shall mean the Corporation's 2016 Equity Omnibus Plan, as set forth in this document.

(z) **Plan Administrator** shall mean the particular entity, whether the Compensation Committee, the Board, the Secondary Board Committee or any delegate of the Board or the Compensation Committee authorized to administer the Plan with respect to one or more classes of eligible persons, to the extent such entity is carrying out its administrative functions under the Plan with respect to the persons under its jurisdiction.

(aa) **Plan Effective Date** shall mean the date upon which the Plan is approved by the stockholders.

(bb) **Predecessor Plan** shall mean the Corporation's 2007 Omnibus Incentive Plan.

(cc) **Secondary Board Committee** shall mean a committee of one or more Board members appointed by the Board to administer the Plan with respect to eligible persons other than Section 16 Insiders.

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

(ee) **Service** shall, with respect to each Award made under the Plan, be defined in accordance with the following provisions:

(i) Service shall have the meaning assigned to such term in the Award Agreement for the particular Award or in any other agreement incorporated by reference into the Award Agreement for purposes of defining such term.

(ii) In the absence of any other definition of Service in the Award Agreement for a particular Award (or in any other agreement incorporated by reference into the Award Agreement), Service shall mean the performance of services for the Corporation (or any

---

A-6

Parent or Subsidiary, whether now existing or subsequently established) by a person in the capacity of an Employee, a Non-Employee Director or a consultant or independent advisor, except to the extent otherwise specifically provided in the documents evidencing the Award. For purposes of this particular definition of Service, a Participant shall be deemed to cease Service immediately upon the occurrence of the either of the following events: (i) the Participant no longer performs services in any of the foregoing capacities for the Corporation or any Parent or Subsidiary or (ii) the entity for which the Participant is performing such services ceases to remain a Parent or Subsidiary of the Corporation, even though the Participant may subsequently continue to perform services for that entity.

(iii) Service shall not be deemed to cease during a period of military leave, sick leave or other personal leave approved by the Corporation; provided, however, that should such leave of absence exceed three (3) months, then for purposes of determining the period within which an Incentive Option may be exercised as such under the federal tax laws, the Participant's Service shall be deemed to cease on the first day immediately

following the expiration of such three (3)-month period, unless Participant is provided with the right to return to Service following such leave either by statute or by written contract. Except to the extent otherwise required by law or expressly authorized by the Plan Administrator or by the Corporation's written policy on leaves of absence, no Service credit shall be given for vesting purposes for any period the Participant is on a leave of absence.

(ff) **Stand-alone Rights** shall have the meaning set forth in Section 2.2.

(gg) **Stock Exchange** shall mean the American Stock Exchange, the Nasdaq Global or Global Select Market or the New York Stock Exchange.

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

(ii) **Tandem Rights** shall have the meaning set forth in Section 2.2.

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

(kk) **Withholding Taxes** shall mean the applicable federal, state and foreign income and employment withholding taxes and other payments to which the holder of an Award under the Plan may become subject in connection with the issuance, exercise, vesting or settlement of that Award.

**SECOND AMENDMENT TO LEASE**

This SECOND AMENDMENT TO LEASE ("Amendment") is made as of September 29, 2014, between RREF II FREEWAY ACQUISITIONS, LLC, a Delaware limited liability company ("Landlord"), and ITERIS, INC., a Delaware corporation ("Tenant"), with reference to the following:

**RECITALS**

- A. Tenant and Landlord's predecessor-in-interest, Crown Carnegie Associates, LLC, a Delaware limited liability company ("Crown") are parties to that certain Office Lease, dated as of May 24, 2007 ("Original Lease"), pursuant to which Tenant leased from Crown certain office space within the office building at 1700 E. Carnegie Avenue, Suites 100 & 200, Santa Ana, California, as more particularly described in the Lease ("Premises") within the complex known as Freeway Corporate Park ("Development");
- B. Landlord acquired the Development, including the Premises, from Crown on or about May 30, 2013;
- C. Landlord and Tenant amended the Original Lease pursuant to that certain First Amendment to Lease, dated February 21, 2014 ("First Amendment", and collectively with the Original Lease, the "Lease"); and
- D. Landlord and Tenant desire to further amend the Lease upon the terms and conditions set forth herein.

NOW, THEREFORE, for good, valuable and sufficient consideration received, Landlord and Tenant hereby agree as follows:

- Terms.** All capitalized terms used but not defined herein shall have the meaning given to them in the Lease.
- Parking Spaces; Fenced Area.** The Fenced Area, as defined in Section 8.3 of the Original Lease, shall be increased by four (4) parking spaces for use by another tenant within the Building, Bendix Commercial Vehicle Systems, LLC ("Bendix"). Bendix shall also be assigned two (2) of the eighteen (18) existing spaces within the fenced area. Except as may be otherwise agreed between Tenant and Bendix (and subject to Landlord approval), Tenant shall continue to have the right to use only sixteen (16) parking spaces within the Fenced Area. The expansion of the Fenced Area shall be made at Bendix's sole cost and expense. Tenant shall provide Bendix with access to the Fenced Area. Exhibit F to the Original Lease depicting the Fenced Area, Test Lane, Test Target Area and the Parking Lot is hereby deleted and replaced with attached Exhibit E. All other terms related to parking spaces and the Parking Lot remain unchanged.
- Lease Unchanged and Complete.** Except as changed by this Amendment, the Lease remains unchanged and contains the entire agreement of Landlord and Tenant with respect to the Premises. Landlord and Tenant each represent and warrant it does not believe or claim there are

1

---

any oral or written agreements between Landlord and Tenant relating to the Premises, and that it is not relying on any agreements relating to the Premises, other than those agreements contained in the Lease as amended by this Amendment.

- Authority.** Each person signing this Amendment on behalf of Landlord or Tenant represents and warrants that that party has duly authorized him or her to execute and deliver this Amendment and by so doing to bind that party.
- Counterparts.** This Amendment may be signed in any number of counterparts, each of which shall constitute one and the same instrument.

**[Signatures on following page]**

2

---

IN WITNESS WHEREOF, Landlord and Tenant have executed this Amendment as of the date first set forth above.

**"LANDLORD"**

RREF II FREEWAY ACQUISITIONS, LLC,  
a Delaware limited liability company

By: RREF II REI, LP,  
a Delaware limited partnership,  
its Sole Member

By: Rialto Partners GP II, LLC,  
a Delaware limited liability company,  
its General Partner

By: Rialto Capital Advisors, LLC,  
a Delaware limited liability company,  
its Attorney in fact

By: \_\_\_\_\_

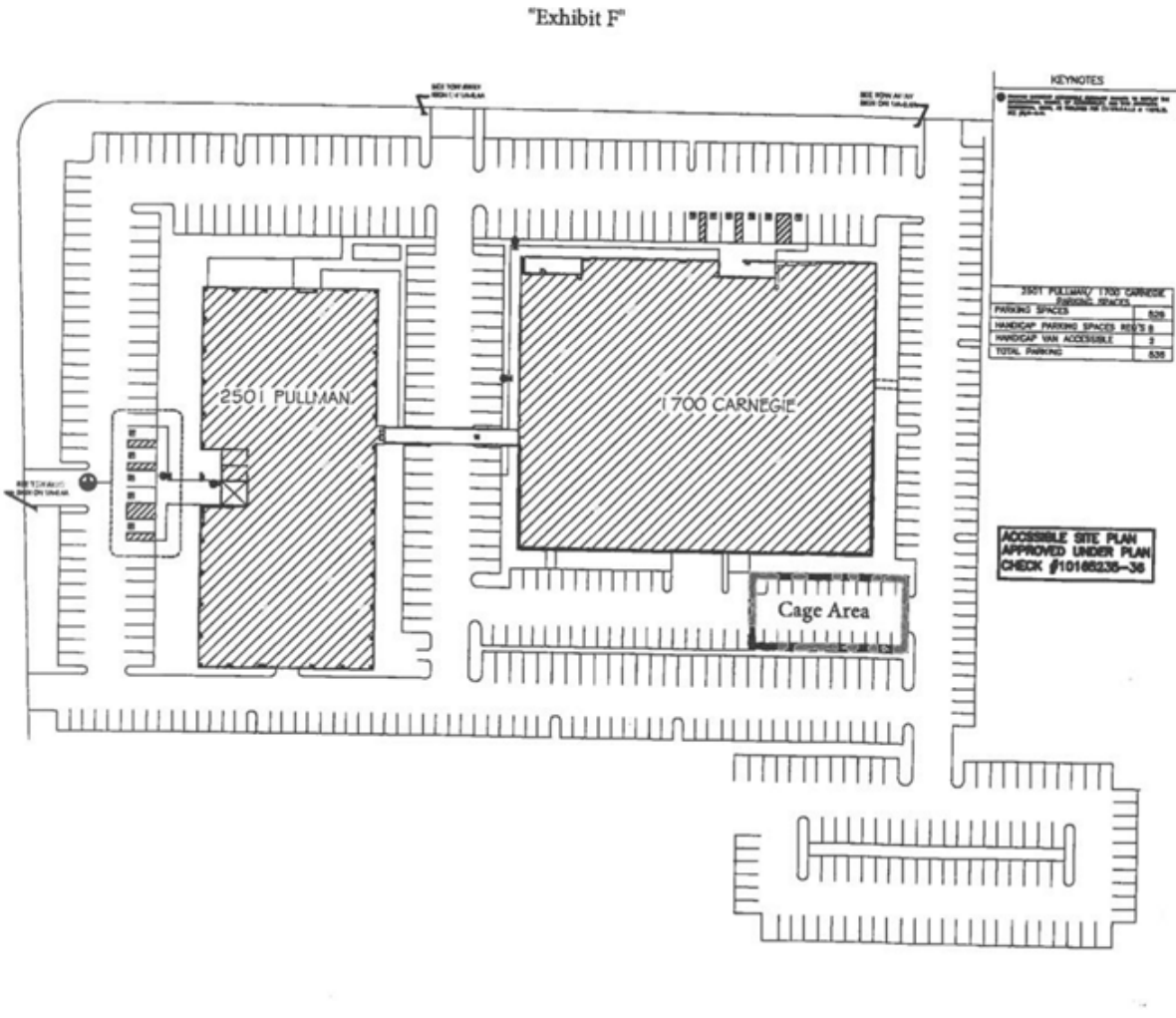
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

“TENANT”

ITERIS, INC.,  
a Delaware corporation

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_  
  
By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

EXHIBIT F  
PARKING LOT  
[See attached]



### THIRD AMENDMENT TO LEASE

This Third Amendment to Lease (the “**Third Amendment**”) is dated for reference purposes this 15<sup>th</sup> day of December, 2016 and is entered into by and between The Realty Associates Fund X, L.P., a Delaware limited partnership (“**Landlord**”), and Iteris, Inc., a Delaware corporation (“**Tenant**”), with reference to the following recitals.

#### RECITALS:

A. On or about May 24, 2007, Crown Carnegie Associates, LLC (“**Crown**”) and Tenant entered into an Office Lease (the “**Original Lease**”) for that certain premises commonly known as Suites 100 and 200 (the “**Original Premises**”), 1700 East Carnegie, Santa Ana, California (the “**Building**”). The Original Premises was comprised of approximately 52,116 rentable square feet of space. Crown subsequently assigned all of its rights and obligations under the Original Lease to RREF II Freeway Acquisitions, LLC (“**RREF**”) and RREF assumed all of Crown’s rights and obligations under the Original Lease. On or about February 21, 2014, RREF and Tenant entered into a First Amendment to Lease (the “**First Amendment**”). Pursuant to the First Amendment the size of the Original Premises was reduced by 11,059 rentable square feet, and Tenant now occupies 41,057 rentable square feet in the Building (the “**Existing Premises**”). On or about September 29, 2014, RREF and Tenant entered into a Second Amendment to Lease (the “**Second Amendment**”). The Original Lease as modified by the First Amendment and the Second Amendment is hereinafter referred to as the “**Lease**”.

B. Tenant now desires to lease from Landlord Suite 225 in the Building which contains approximately 5,980 rentable square feet and which is depicted on Exhibit A attached hereto (the “**Expansion Space**”).

C. Landlord and Tenant wish to amend the Lease on the terms and conditions set forth below.

NOW, THEREFORE, for good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, the parties hereto agree as follows:

1. Lease of Expansion Space. Subject to the terms and conditions set forth below, Landlord hereby agrees to lease to Tenant and Tenant hereby agrees to lease from Landlord the Expansion Space. The Expansion Space is currently occupied by Bendix Commercial Vehicle Systems LLC (the “**Existing Tenant**”) and the Existing Tenant’s lease is scheduled to expire on March 31, 2017. The date that Existing Tenant delivers possession of the Expansion Space to Landlord is hereinafter referred to as the “**Existing Tenant Delivery Date**”. On the later to occur of one (1) business day after the Existing Tenant Delivery Date and March 31, 2017, Landlord shall offer Tenant possession of the Expansion Space (the “**Landlord Delivery Date**”). Tenant shall accept possession of the Expansion Space from Landlord on the Landlord Delivery Date in its “as is” condition. As of the Landlord Delivery Date, the total rentable area of the Premises (the Existing Premises and the Expansion Space) shall be 47,037 square feet. From and after the Landlord Delivery Date, all references in the Lease to the “Premises” shall include the Expansion Space. For purposes of this Third Amendment, the “**Rent Commencement Date**” shall mean the date that is ninety (90) days after the Landlord Delivery Date. When the Landlord Delivery Date and Rent Commencement Date are established by Landlord, Tenant shall, within five (5) business days after Landlord’s request, complete and execute the memorandum attached hereto as Exhibit B and deliver it to Landlord. Tenant’s failure to execute the memorandum attached hereto as Exhibit B within said five (5) business day period shall constitute Tenant’s acknowledgment of the truth of the facts contained in the memorandum delivered by Landlord to Tenant.

2. Term. Tenant’s lease of the Expansion Space shall commence on the Landlord Delivery Date and shall end when the term of the Lease ends on March 31, 2022, subject to extension of the term of the Lease, as hereby amended, by Tenant pursuant to Section 4 of the First Amendment.

3. Base Rent. Prior to the Landlord Delivery Date, Tenant shall continue to pay the monthly Base Rent required by the Lease. Notwithstanding anything to the contrary contained in the Lease, from and after the Landlord Delivery Date, in addition to the Base Rent Tenant pays for the Existing Premises pursuant to the Lease, Tenant shall pay additional Base Rent for its use of the Expansion Space in the following amounts:

Period	Base Rent Due Each Month
Landlord Delivery Date — Rent Commencement Date:	\$ 0
Rent Commencement Date through 12 <sup>th</sup> full calendar month after Rent Commencement Date:	\$ 14,053.00
13 <sup>th</sup> through 24 <sup>th</sup> month after Rent Commencement Date:	\$ 14,474.59
25 <sup>th</sup> through 36 <sup>th</sup> month after Rent Commencement Date:	\$ 14,908.83
37 <sup>th</sup> through 48 <sup>th</sup> month after Rent Commencement Date:	\$ 15,356.09
49 <sup>th</sup> month after Rent Commencement Date through March 31, 2022:	\$ 15,816.78

4. Abatement of Expansion Space Base Rent. Landlord hereby agrees to waive the Base Rent due for the Expansion Space for the first, second and third full calendar months after the Rent Commencement Date. The Base Rent applicable to the Existing Premises shall not be waived. No amounts due to Landlord under the Lease other than the Base Rent referred to above shall be waived.

5. Tenant’s Share. Tenant’s Share (as defined in the Original Lease) with respect to the Existing Premises shall continue to be 52.291% with respect to the Project and 32.009% with respect to the Development. Tenant’s Share with respect to the Expansion Space shall be 7.815% with respect to the Project and 4.662% with respect to the Development.

6. Base Year. For purposes of calculating Tenant’s Share of Direct Expenses applicable to the Existing Premises, the Base Year for the Existing Premises shall continue to be the calendar year 2014. For purposes of calculating Tenant’s Share of Direct Expenses applicable to the Expansion Space, the Base Year for the Expansion Space shall be the calendar year 2017.

7. Direct Expenses. Notwithstanding anything to the contrary contained in the Lease, Tenant shall not be obligated to pay Tenant’s Share of Direct Expenses attributable to the Expansion Space during the period commencing on the Landlord Delivery Date and ending on the date that is twelve (12) full calendar months after the Rent Commencement Date.



8. Limitation on Operating Expense Increases. Section 6(b) of the First Amendment shall not apply to or otherwise limit the payment by Tenant of Tenant's Share of Direct Expenses attributable to the Expansion Space.

9. Parking. From and after the Landlord Delivery Date, the number of unreserved parking spaces allotted to Tenant is hereby increased from one hundred twenty-eight (128) parking spaces to one hundred fifty-two (152) parking spaces. All other terms related to parking spaces and the Parking Lot shall remain the same. Pursuant to Section 2 of the Second Amendment, the Existing Tenant has the right to use six (6) parking spaces in the Fenced Area (as defined in the Original Lease) (the "**Existing Tenant Fenced Area Spaces**"). The Existing Tenant Fenced Area Spaces shall constitute six (6) of the one hundred fifty-two (152) parking spaces referred to above.

10. Tenant Improvements.

(a) Improvements. Within thirty (30) days after the execution of this Third Amendment, Tenant shall submit to Landlord for approval a detailed space plan ("**Space Plan**") for the improvements to the Expansion Space which shall include without limitation, the location of doors, partitions, electrical and telephone outlets, plumbing fixtures, heavy floor loads and other special requirements. The Space Plan and

2

---

the Construction Drawings (as defined below) shall be prepared by H. Hendy Associates (the "**Architect**"). Landlord agrees to cooperate with Tenant and its design representatives in connection with the preparation of the Space Plan. Within five (5) business days after receipt by Landlord of the Space Plan, Landlord (i) shall give its written approval with respect thereto, or (ii) shall notify Tenant in writing of its disapproval and state with specificity the grounds for such disapproval and the revisions or modifications necessary in order for Landlord to give its approval. Within five (5) business days following Tenant's receipt of Landlord's disapproval, Tenant shall submit to Landlord for approval the requested revisions or modifications. Within five (5) business days following receipt by Landlord of such revisions or modifications, Landlord shall give its written approval with respect thereto or shall request other revisions or modifications therein (but relating only to the extent Tenant has failed to comply with Landlord's earlier requests). The preceding sentence shall be implemented repeatedly until Landlord gives its approval to Tenant's Space Plan. The improvements to be made to the Expansion Space that are described in the final Space Plan are hereinafter referred to as the "**Improvements**".

(b) Construction Drawings. If the preparation of the Construction Drawings requires the input of engineers (the "**Engineers**"), as reasonably determined by Landlord, Architect shall retain Engineers that are reasonably acceptable to Landlord to prepare all plans and engineering drawings relating to the structural, mechanical, electrical, plumbing, HVAC, life safety, and sprinkler work in the Expansion Space. The plans and specifications to be prepared by the Architect and the Engineers hereunder shall reflect only the improvements described on the Space Plan and shall be known collectively as the "**Construction Drawings**." Tenant and Architect shall verify, in the field, the dimensions of the Expansion Space and the conditions at the Expansion Space, and Tenant and Architect shall be solely responsible for the same, and Landlord shall have no responsibility in connection therewith. Landlord shall have the right to approve the Construction Drawings in Landlord's reasonable discretion, and the Construction Drawings shall not materially deviate from the Space Plan. Landlord's review of the Construction Drawings are for its sole benefit and Landlord shall have no liability to Tenant or Tenant's contractors arising out of or based on Landlord's review. Accordingly, notwithstanding that any Construction Drawings are reviewed by Landlord or its space planner, architect, engineers and consultants, and notwithstanding any advice or assistance which may be rendered to Tenant or Tenant's Architect, Engineers or contractors by Landlord or Landlord's space planner, architect, engineers and consultants, Landlord shall have no liability whatsoever in connection therewith and shall not be responsible for any omissions or errors arising therefrom.

(c) Permits and Changes. The Construction Drawings approved by Landlord (the "**Final Construction Drawings**") shall be submitted by Tenant to the appropriate governmental agencies in order to obtain all applicable building permits. Prior to commencing construction of the Improvements, Tenant shall provide Landlord with copies of the permits. Tenant hereby agrees that neither Landlord nor Landlord's consultants shall be responsible for obtaining any building permits or a certificate of occupancy for the Expansion Space and that obtaining the same shall be Tenant's sole responsibility; provided, however, that Landlord shall cooperate with Tenant in executing permit applications and performing other ministerial acts reasonably necessary to enable Tenant to obtain any such permits or certificate of occupancy. No changes, modifications or alterations in the Final Construction Drawings may be made without the prior written consent of Landlord, which consent shall not be unreasonably withheld or delayed.

(d) Compliance with Laws. Tenant shall be solely responsible for constructing the Improvements in compliance with all laws. Tenant acknowledges and agrees that it may be obligated to modify, alter or upgrade the Expansion Space and the systems therein in order to complete the construction of the Improvements, and Landlord shall have no liability or responsibility for modifying, altering or upgrading the Expansion Space or its existing systems. If, as a result of Improvements constructed in accordance with this Third Amendment, Landlord is obligated to comply with the Americans With Disabilities Act and such compliance requires Landlord to make any improvements or alterations to any portion of the Development in the common areas of the Development outside the Expansion Space and Existing Premises (an "**Exterior Alteration**"), Landlord shall pay the cost of making the Exterior Alteration at Landlord's sole cost and expense and the cost of the Exterior Alteration shall not be paid from the Improvement Allowance.

3

---

(e) Contractors. Landlord shall have the right to approve in advance the contractors (the "**Contractors**") used by Tenant to construct the Improvements, in Landlord's reasonable discretion, and Landlord may require Tenant to use union Contractors. Notwithstanding the forgoing, Landlord shall have the right to designate which subcontractors may perform work on the Building's systems, including, but not limited to, the Building's HVAC, electrical, plumbing, roof and life, fire and safety systems. Tenant's indemnification obligations in the Lease shall also apply with respect to any and all damages, cost, loss or expense (including attorney's fees) related to any act or omission of Tenant or its Contractors, or anyone directly or indirectly employed by any of them, or in connection with Tenant's non-payment of any amount arising out of the Improvements. The Contractors shall carry worker's compensation insurance covering all of their respective employees, public liability insurance, including property damage, and such other insurance as required by Landlord, in Landlord's sole discretion. Certificates for all insurance carried pursuant to this section shall be delivered to Landlord before the commencement of construction of the Improvements. All such policies of insurance shall name Landlord and its property manager as an additional insured.

(f) Construction Procedures. The Contractors shall comply with all of Landlord's rules, regulations and procedures concerning the construction of improvements at the Project (collectively, the "**Construction Procedures**"), and if any Contractor fails to comply with the Construction Procedures after Landlord has provided the Contractor with written notice of its non-compliance, Landlord shall have the right to prohibit such Contractor from performing any further work in the Building, and Landlord shall have no liability to Tenant due to such prohibition. Landlord's Construction Procedures

are available from the Building's property manager. To the extent not inconsistent with the provisions of this Section 10, Article 11 of the Original Lease shall apply to the construction of the Improvements. If there is a conflict between Article 11 of the Original Lease, and this Section 10, this Section 10 shall control. Tenant's Contractors shall not perform any construction work at the Building if such work might disturb other tenants of the Building, as determined by Landlord in Landlord's sole discretion, from 8:00 a.m. to 6:00 p.m., Monday through Friday. Tenant and the Contractors shall not have the right, at any time, to disrupt any Building service (e.g., electrical, plumbing etc.) to the Common Areas or to another tenant's premises. Tenant and the Contractors shall only store construction materials inside the Premises or the Expansion Space and the Contractors shall not dispose of their refuse or construction materials in the Project's or Developments trash receptacles. Tenant's Contractors shall only use Building entrances and Building freight elevators designated by Landlord to transport construction materials to the Expansion Space, and Tenant and Tenant's Contractors shall take whatever precautions Landlord may reasonably prescribe to protect the Project and the Development from damages due to such activities. Tenant shall reimburse Landlord for the cost of repairing any damage to the Project or Development caused by the construction of the Improvements. Landlord shall have the right to inspect the Improvements at all times upon reasonable notice to Tenant, provided however, that Landlord's inspection of the Improvements shall not constitute Landlord's approval of the Improvements. Should Landlord reasonably disapprove any portion of the Improvements, Landlord shall notify Tenant in writing of such disapproval and shall specify the items disapproved. Any defects in the Improvements shall be rectified by Tenant at no expense to Landlord. Landlord shall have the right to receive a fee to reimburse it for its costs in providing approvals hereunder and in monitoring the construction of the Improvements in an amount equal to one and one-half percent (1.5%) of the total cost of constructing the Improvements (the "**Landlord Fee**"). In addition, if Landlord incurs architectural, engineering or other consultants' fees in evaluating such Improvements ("**Third Party Fees**"), Tenant shall reimburse Landlord for these fees in addition to the Landlord Fee. Landlord shall have the right to deduct the Landlord Fee and the Third Party Fees from the Improvement Allowance (as defined below).

(g) Improvement Allowance. Landlord hereby grants to Tenant an "**Improvement Allowance**" of \$119,600.00, which Improvement Allowance shall be used only to reimburse Tenant for the actual out-of-pocket costs paid by Tenant to independent third parties for the construction of the Improvements. After the completion of the construction of the Improvements, Landlord shall make one (1) disbursement of the Improvement Allowance. Prior to Landlord making the disbursement, Tenant shall deliver to Landlord: (A) a request for payment, approved by Tenant, in a form which is reasonably acceptable to Landlord; (B) invoices from all contractors whose work is being paid with respect to such payment request; (C) copies of executed mechanic's lien releases from all of the contractors which shall comply with the

4

---

provisions of California Civil Code Section 8138; (D) proof that Tenant has previously paid to the contractors the monies described in the payment request; (E) "as built" plans for the Improvements and (F) all other information reasonably requested by Landlord. Within thirty (30) days after Landlord has received all of this information, Landlord shall deliver a check to Tenant in an amount equal to the lesser of (i) the actual monies paid by Tenant to Tenant's contractors with respect to such payment request or (ii) the Improvement Allowance.

(h) Unused Allowance. If the actual cost of the Improvements does not exceed the Improvement Allowance, Tenant may use up to \$59,800.00 of the unused portion of the Improvement Allowance (the "**Maximum Amount**") to reimburse Tenant for the actual out-of-pocket costs it pays to unrelated third parties in order to (a) move its existing furniture and equipment into the Expansion Space, (b) purchase new furniture and equipment for use in the Expansion Space and (c) install telephone and computer cabling in the Expansion Space (collectively, "**Expenses**"). If Tenant desires to use the unused portion of the Improvement Allowance (not to exceed the Maximum Amount) to reimburse itself for Expenses, Tenant shall provide to Landlord bills, invoices and other information reasonably acceptable to Landlord to document monies paid by Tenant for Expenses, and Landlord shall reimburse Tenant within thirty (30) days after receiving such information for the lesser of the Maximum Amount and amount of the unused Improvement Allowance. After the Improvements are completed, Tenant shall have the right to make one request for the reimbursement of Expenses (the "**Reimbursement Request**") and the Reimbursement Request shall include all Expenses for which Tenant requests reimbursement. Landlord shall have no obligation to reimburse Tenant for any Expense that is not included in the Reimbursement Request. Any portion of the Improvement Allowance that has not been expended on or before December 31, 2017 on the construction of the Improvements or on the reimbursement of Expenses shall be retained by Landlord, and Tenant shall have no further right to the use of such unused portion of the Improvement Allowance for any purpose.

(i) Commencement Date. Tenant shall construct the Improvements after the Landlord Delivery Date, and Tenant's obligation to pay Base Rent and other charges due under the Lease is not conditioned on the completion of the Improvements.

11. Conflict. If there is a conflict between the terms and conditions of this Third Amendment and the terms and conditions of the Lease, the terms and conditions of this Third Amendment shall control. Except as modified by this Third Amendment, the terms and conditions of the Lease shall remain in full force and effect. Capitalized terms included in this Third Amendment shall have the same meaning as capitalized terms in the Lease unless otherwise defined herein. Tenant hereby acknowledges and agrees that the Lease is in full force and effect, Landlord is not currently in default under the Lease, and, to the best of Tenant's knowledge, no event has occurred which, with the giving of notice or the passage of time, or both, would ripen into Landlord's default under the Lease. The Lease, as hereby amended, contains all agreements of the parties with respect to the lease of the Premises. No prior or contemporaneous agreement or understanding pertaining to the Lease, as hereby amended, shall be effective.

12. Brokers. Tenant and Landlord each represent and warrant to the other that neither has had any dealings or entered into any agreements with any person, entity, broker or finder in connection with the negotiation of this Third Amendment except CBRE, Inc., and no other broker, person, or entity is entitled to any commission or finder's fee in connection with the negotiation of this Third Amendment, and Tenant and Landlord each agree to indemnify, defend and hold the other harmless from and against any claims, damages, costs, expenses, attorneys' fees or liability for compensation or charges which may be claimed by any such unnamed broker, finder or other similar party by reason of any dealings, actions or agreements of the indemnifying party.

13. Authority. The persons executing this Third Amendment on behalf of the parties hereto represent and warrant that they have the authority to execute this Third Amendment on behalf of said parties and that said parties have authority to enter into this Third Amendment.

5

---

14. Confidentiality. Tenant acknowledges and agrees that the terms of this Third Amendment are confidential and constitute proprietary information of Landlord. Disclosure of the terms hereof could adversely affect the ability of Landlord to negotiate other leases with respect to the property and may impair Landlord's relationship with other tenants of the property. Tenant agrees that it and its partners, officers, directors, employees, brokers, and attorneys, if any, shall not disclose the terms and conditions of this Third Amendment to any other person or entity without the prior written consent of

Landlord which may be given or withheld by Landlord, in Landlord’s sole discretion. It is understood and agreed that damages alone would be an inadequate remedy for the breach of this provision by Tenant, and Landlord shall also have the right to seek specific performance of this provision and to seek injunctive relief to prevent its breach or continued breach.

15. **Execution.** This Third Amendment and any documents or addenda attached hereto (collectively, the “**Documents**”) may be executed in two or more counterpart copies, each of which shall be deemed to be an original and all of which together shall have the same force and effect as if the parties had executed a single copy of the Document. Landlord shall have the right, in Landlord’s sole discretion, to insert the name of the person executing a Document on behalf of Landlord in Landlord’s signature block using an electronic signature (an “**Electronic Signature**”), and in this event the Document delivered to Tenant will not include an original ink signature and Landlord shall have no obligation to provide a copy of such Document to Tenant with Landlord’s original ink signature. A Document delivered to Tenant by Landlord with an Electronic Signature shall be binding on Landlord as if the Document had been originally executed by Landlord with an ink signature. Without the prior written consent of Landlord, which may be withheld in Landlord’s sole discretion, Tenant shall not have the right to insert the name of the person executing the Document on behalf of Tenant using an Electronic Signature and all Documents shall be originally executed by Tenant using an ink signature. A Document executed by Landlord or Tenant and delivered to the other party in PDF, facsimile or similar electronic format (collectively, “**Electronic Format**”) shall be binding on the party delivering the executed Document with the same force and effect as the delivery of a printed copy of the Document with an original ink signature. At any time upon Landlord’s written request, Tenant shall provide Landlord with a printed copy of the Document with an original ink signature. This Section describes the only ways in which Documents may be executed and delivered by the parties. An email from Landlord, its agents, brokers, attorneys, employees or other representatives shall never constitute Landlord’s Electronic Signature or be otherwise binding on Landlord. Subject to the limitations set forth above, the parties agree that a Document executed using an Electronic Signature and/or delivered in Electronic Format may be introduced into evidence in a proceeding arising out of or related to the Document as if it was a printed copy of the Document executed by the parties with original ink signatures. Landlord shall have no obligation to retain copies of Documents with original ink signatures, and Landlord shall have the right, in its sole discretion, to elect to discard originals and to retain only copies of Documents in Electronic Format.

16. **Delivery of Amendment.** Preparation of this Third Amendment by Landlord or Landlord’s agent and submission of same to Tenant shall not be deemed an offer by Landlord to enter into this Third Amendment. This Third Amendment shall become binding upon Landlord only when fully executed by all parties. The delivery of this Third Amendment to Tenant shall not constitute an agreement by Landlord to negotiate in good faith, and Landlord expressly disclaims any legal obligation to negotiate in good faith. To Landlord’s actual knowledge, as of the date of this Third Amendment, the Premises has not undergone an inspection by a certified access specialist. Landlord’s actual knowledge shall mean and be limited to the actual knowledge of the person who is the Building owner’s asset manager (not the Building’s property manager) on the date this Third Amendment is executed by Landlord, without any duty of inquiry or investigation, and such asset manager shall have no personal liability if such representation is untrue.

17. **Energy Use.** Landlord shall have the right to require Tenant to provide Landlord with copies of bills from electricity, natural gas or similar energy providers (collectively, “**Energy Providers**”) Tenant receives from Energy Providers relating to Tenant’s energy use at the Premises (“**Energy Bills**”) within ten (10) days after Landlord’s written request. In addition, Tenant hereby authorizes Landlord to obtain copies of the Energy Bills directly from the Energy Provider(s), and Tenant hereby authorizes each Energy Provider to provide Energy Bills and related usage information directly to Landlord without Tenant’s consent. From time

to time within ten (10) days after Landlord’s request, Tenant shall execute and deliver to Landlord an agreement provided by Landlord authorizing the Energy Provider(s) to provide to Landlord Energy Bills and other information relating to Tenant’s energy usage at the Premises.

18. **Notices.** All notices provided by Tenant to Landlord pursuant to the Lease shall be sent to the following addresses:

The Realty Associates Fund X, L.P.  
c/o TA Realty  
1301 Dove Street, Suite 860  
Newport Beach, California 92660  
Attention: Asset Manager/Freeway Corporate Park

and

The Realty Associates Fund X, L.P.  
c/o TA Realty  
28 State Street, Tenth Floor  
Boston, Massachusetts 02109  
Attention: Asset Manager/Freeway Corporate Park

With a copy to:

Davis Partners LLC  
1420 Bristol Street North, Suite 100  
Newport Beach, CA 92660  
Attention: Property Manager/Freeway Corporate Park.

[Remainder of page left intentionally blank.]

IN WITNESS WHEREOF, the parties hereby execute this Third Amendment as of the date first written above.

LANDLORD:

The Realty Associates Fund X, L.P.,  
a Delaware limited partnership

By: Realty Associates Fund X LLC,  
its general partner

By: TA Realty, LLC, its manager

By: \_\_\_\_\_  
Officer

By: Realty Associates Fund X REIT GP, LLC,  
its general partner

By: Realty Associates Fund X REIT, LLC,  
its manager

By: Realty Associates Fund X UTP, L.P.  
its manager

By: Realty Associates Fund X, LLC  
its general partner

By: TA Realty, LLC, its manager

By: \_\_\_\_\_  
Officer

TENANT:

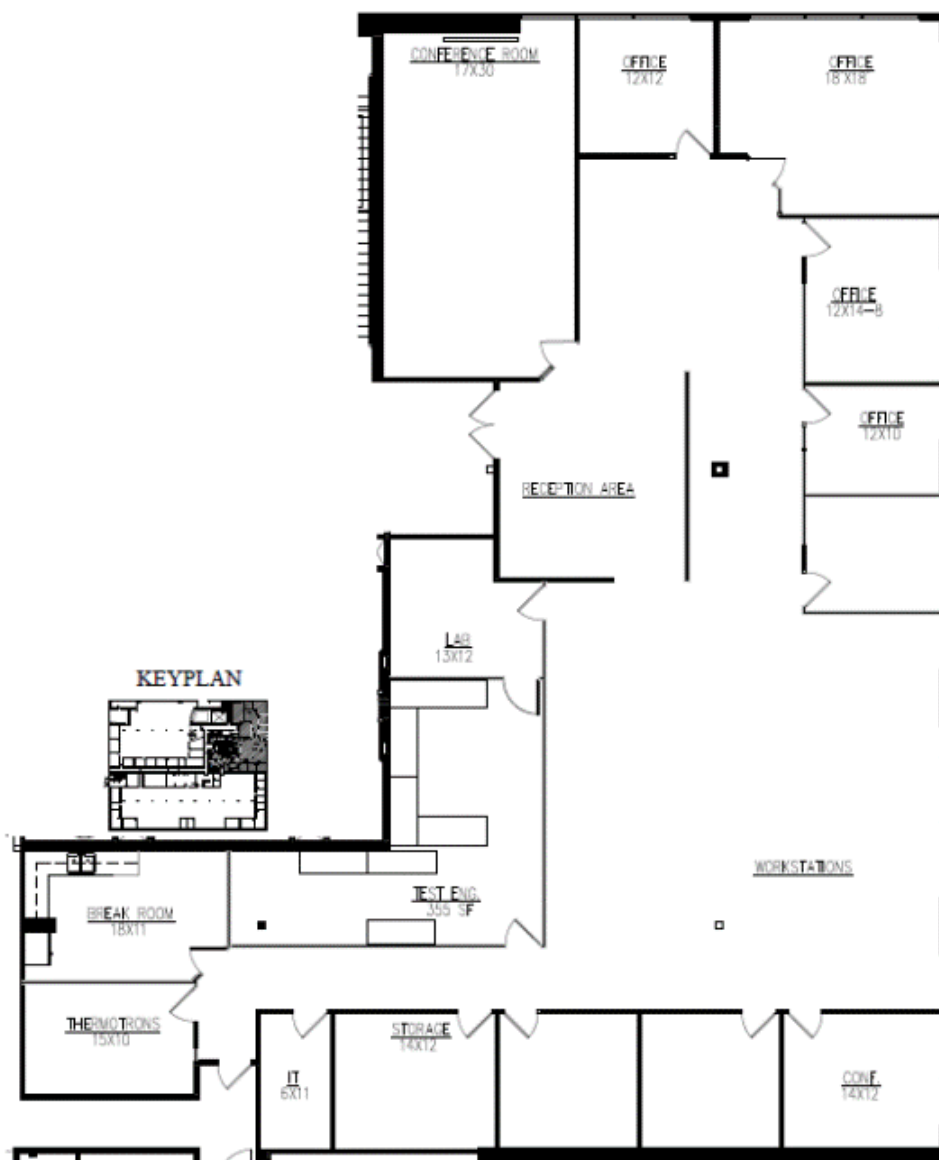
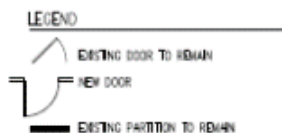
Iteris, Inc.,  
a Delaware corporation

By: \_\_\_\_\_  
\_\_\_\_\_  
(print name)

Its: \_\_\_\_\_  
(print title)

By: \_\_\_\_\_  
\_\_\_\_\_  
(print name)

Its: \_\_\_\_\_  
(print title)



10

## Exhibit B

### Memorandum

The Realty Associates Fund X, L.P., a Delaware limited partnership (“**Landlord**”), and Iteris, Inc., a Delaware corporation (“**Tenant**”), have entered into an Office Lease, as previously amended (the “**Lease**”), for certain space in the building located at 1700 East Carnegie, Santa Ana, California. Landlord and Tenant have entered into a Third Amendment to Lease (the “**Third Amendment**”) amending the Lease, and pursuant to the Third Amendment Tenant hereby acknowledges and agrees as follows:

1. The Landlord Delivery Date (as defined in the Third Amendment) is \_\_\_\_\_, 2017.
2. The Rent Commencement Date (as defined in the Third Amendment) is \_\_\_\_\_, 2017.

Iteris, Inc.,  
a Delaware corporation

By: \_\_\_\_\_

(print name)

Its: \_\_\_\_\_

(print title)

By: \_\_\_\_\_  
\_\_\_\_\_  
(print name)

Its: \_\_\_\_\_  
(print title)

List of Subsidiaries

<u>Subsidiary</u>	<u>Jurisdiction of Incorporation</u>
ClearAg, Inc.	Delaware



**CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

We consent to the incorporation by reference in Registration Statement Nos. 333-221790, 333-216407, 333-190309, 333-162807, 333-146459, and 333-75728 on Form S-8 and Registration Statement No. 333-220305 on Form S-3 of our report dated June 7, 2018, relating to the consolidated financial statements of Iteris, Inc. and subsidiary and the effectiveness of Iteris, Inc. and subsidiary's internal control over financial reporting appearing in this Annual Report on Form 10-K of Iteris, Inc. and subsidiary for the year ended March 31, 2018.

/s/ Deloitte & Touche LLP  
Costa Mesa, CA  
June 7, 2018

---



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

I, Joe Bergera, 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 subsidiary, 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 7, 2018

/s/ JOE BERGERA  
\_\_\_\_\_  
Joe Bergera  
Chief Executive Officer  
(Principal Executive Officer)

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

I, Andrew C. Schmidt, 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 subsidiary, 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 7, 2018

/s/ ANDREW C. SCHMIDT  
\_\_\_\_\_  
Andrew C. Schmidt  
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, 2018, as filed with the Securities and Exchange Commission (the “Report”), I, Joe Bergera, 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, as amended;  
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 7, 2018

/s/ JOE BERGERA

Joe Bergera

*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, 2018 as filed with the Securities and Exchange Commission (the “Report”), I, Andrew C. Schmidt, 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, as amended;  
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 7, 2018

/s/ ANDREW C. SCHMIDT

Andrew C. Schmidt

*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.