

ITERIS, INC.
Form 10-K
June 20, 2016

Use these links to rapidly review the document

[TABLE OF CONTENTS](#)

[PART IV](#)

[Iteris, Inc. Index to Consolidated Financial Statements](#)

[Table of Contents](#)

**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, 2016
OR
 TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _____ to _____
Commission file number 001-08762

ITERIS, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

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

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

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

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

| Title of each class | Name of each exchange on which registered |
|--------------------------------|--|
| Common Stock, \$0.10 par value | 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. 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

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

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

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

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

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company
(Do not check if a smaller reporting company)

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

The aggregate market value of the registrant's common stock held by nonaffiliates of the registrant as of September 30, 2015 was approximately \$63,350,000. For the purposes of this calculation, shares owned by officers, directors and 10% stockholders known to the registrant have been deemed to be owned by affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes. As of June 8, 2016, there were 32,057,503 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 2016 Annual Meeting of Stockholders, which will be filed with the Securities and Exchange Commission not later than 120 days after the end of the fiscal year ended March 31, 2016.

Table of Contents

ITERIS, INC.
ANNUAL REPORT ON FORM 10-K
FOR THE FISCAL YEAR ENDED MARCH 31, 2016
TABLE OF CONTENTS

| | | |
|------------------------|---|-----------|
| <u>PART I</u> | | |
| <u>ITEM 1.</u> | <u>BUSINESS</u> | <u>3</u> |
| <u>ITEM 1A.</u> | <u>RISK FACTORS</u> | <u>9</u> |
| <u>ITEM 1B.</u> | <u>UNRESOLVED STAFF COMMENTS</u> | <u>20</u> |
| <u>ITEM 2.</u> | <u>PROPERTIES</u> | <u>20</u> |
| <u>ITEM 3.</u> | <u>LEGAL PROCEEDINGS</u> | <u>20</u> |
| <u>ITEM 4.</u> | <u>MINE SAFETY DISCLOSURES</u> | <u>20</u> |
| <u>PART II</u> | | |
| <u>ITEM 5.</u> | <u>MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES</u> | <u>21</u> |
| <u>ITEM 6.</u> | <u>SELECTED FINANCIAL DATA</u> | <u>22</u> |
| <u>ITEM 7.</u> | <u>MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u> | <u>22</u> |
| <u>ITEM 7A.</u> | <u>QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u> | <u>35</u> |
| <u>ITEM 8.</u> | <u>FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA</u> | <u>35</u> |
| <u>ITEM 9.</u> | <u>CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE</u> | <u>35</u> |
| <u>ITEM 9A.</u> | <u>CONTROLS AND PROCEDURES</u> | <u>35</u> |
| <u>ITEM 9B.</u> | <u>OTHER INFORMATION</u> | <u>36</u> |
| <u>PART III</u> | | |
| <u>ITEM 10.</u> | <u>DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE</u> | <u>37</u> |
| <u>ITEM 11.</u> | <u>EXECUTIVE COMPENSATION</u> | <u>37</u> |
| <u>ITEM 12.</u> | <u>SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS</u> | <u>37</u> |
| <u>ITEM 13.</u> | <u>CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE</u> | <u>37</u> |
| <u>ITEM 14.</u> | <u>PRINCIPAL ACCOUNTING FEES AND SERVICES</u> | <u>37</u> |
| <u>PART IV</u> | | |
| <u>ITEM 15.</u> | <u>EXHIBITS, FINANCIAL STATEMENT SCHEDULES</u> | <u>38</u> |

Unless otherwise indicated in this report, the "Company," "we," "us" and "our" refer to Iteris, Inc. and its wholly-owned subsidiary. Abacus®, ClearAg®, ClearPath 511®, ClearPath Weather®, Edge®, EdgeConnect , iPerform®, iPeMS®, Iteris®, Next®, P10 , P100 , Pegasus , Radius , Reverse 511 , RZ-4 , SmartCycle®, SmartSpan®, TransitHelper®, Vantage®, VantageNext®, VantagePegasus®, VantageRadius , Vantage Vector®, VantageView , Velocity®, and VersiCam are among the trademarks of Iteris, Inc. Any other trademarks or trade names mentioned herein are the property of their respective owners.

Table of Contents

Cautionary Statement

This report, including the following discussion and analysis, contains forward-looking statements (within the meaning of the Private Securities Litigation Reform Act of 1995) that are based on our current expectations, estimates and projections about our business and our industry, and reflect management's beliefs and certain assumptions made by us based upon information available to us as of the date of this report. When used in this report and the information incorporated herein by reference, the words "expect(s)," "feel(s)," "believe(s)," "should," "will," "may," "anticipate(s)," "estimate(s)," "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 and manufacturing capabilities, 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.

Table of Contents

PART I

ITEM 1. BUSINESS

Overview

Iteris, Inc. (referred to collectively with its subsidiary in this report as "Iteris," the "Company," "we," "our" and "us") is a provider of intelligent information solutions for both the traffic management and global agribusiness markets. We are focused on the development and application of advanced technologies and software-based information systems that reduce traffic congestion, provide measurement, management and predictive traffic and weather analytics, and improve the safety of surface transportation systems infrastructure. By combining our unique intellectual property, products, decades of experience in traffic management, weather forecasting solutions and information technologies, we offer a broad range of Intelligent Transportation Systems ("ITS") solutions to customers throughout the U.S. and internationally. We believe our products, services and solutions, in conjunction with sound traffic management, minimize the environmental impact of traffic congestion.

In the agribusiness markets, we have combined our unique intellectual property with enhanced soil, land surface and agronomy modeling techniques to create a set of ClearAg solutions. These solutions provide analytical support to large enterprises in the agriculture market and field-specific advisories to individual producers. We continue to make significant investments to leverage our existing technologies and further expand our software-based information systems to offer solutions to the precision agriculture technology markets.

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 Internet website address is 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 "Investors" section of our website, free of charge, as soon as reasonably practicable after such material is electronically filed with, or furnished to, the Securities and Exchange Commission ("SEC").

Products and Services

We currently operate in three reportable segments: Roadway Sensors, Transportation Systems and Performance Analytics. The Roadway Sensors segment provides various vehicle detection and information systems and products for traffic intersection control, incident detection and roadway traffic data collection applications. The Transportation Systems segment includes transportation engineering and consulting services, and the development of transportation management and traveler information systems for the ITS industry. The Performance Analytics segment includes iPeMS, our specialized transportation performance measurement and traffic analytics solutions, as well as ClearPath Weather, our road-maintenance applications, and ClearAg, our precision agriculture solutions. See Note 13 of Notes to Consolidated Financial Statements, included in Part IV, Item 15 of this report, for further details on our reportable segments.

Roadway Sensors

Our Roadway Sensors segment product line uses advanced image processing technology and other techniques to capture and analyze sensor data through sophisticated algorithms, enabling vehicle detection and transmission of both video images and data using various communication technologies. Our Roadway Sensors products include, among other products, our Vantage, VantageNext, VersiCam, Vantage Vector, SmartCycle, SmartSpan, Pegasus, Velocity, P10, P100 and Abacus products.

Table of Contents

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 radars. Our Vantage systems give traffic managers the ability to mitigate roadway congestion by modifying traffic signal timing or detecting incidents quickly. Our various software complement our Vantage detection systems by providing integrated platforms to manage and view detection assets remotely over a network connection.

Our Vantage Vector video/radar hybrid product is an all-in-one vehicle detection sensor with a wide range of capabilities, including stop bar detection, advanced-zone detection and sensing, which enable advanced safety and adaptive control applications. It includes all the proven benefits of Iteris video detection, including high accuracy, high availability remote viewing of video images, bicycle detection capability and high precision for dilemma zone detection, by integrating the video field-of-view with radar sensing. Enhanced information, including vehicle counts, speed and distance in user configurable zones that is available for use in special applications.

Our Vantage systems equipped with SmartCycle capability can effectively differentiate between bicycles and other vehicles with a single video detection camera, enabling more efficient signalized intersections and improved traffic throughput. 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.

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, particularly in developing countries, will be dependent in part on the continued adoption of above-ground video detection technologies, instead of traditional in-pavement loop technology, to manage traffic.

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

Transportation Systems

Our Transportation Systems segment includes transportation engineering and consulting services focused on the planning, design, development and implementation of software-based systems that integrate sensors, video surveillance, computers and advanced communications equipment to enable public agencies to monitor, control and direct traffic flow, assist in the quick dispatch of emergency crews and distribute real-time information about traffic conditions. Our services include planning, design and implementation of surface transportation infrastructure systems. We perform analysis and study goods movement, commercial vehicle operations, provide travel demand forecasting and systems engineering, and identify mitigation measures to reduce traffic congestion.

Our Transportation Systems segment is largely dependent upon governmental funding and is affected by state and local budgetary issues. On December 4, 2015, the Fixing America's Surface Transportation ("FAST") Act was signed into law, providing approximately \$305 billion over five years for surface transportation projects and programs. In addition, various other funding mechanisms exist to support transportation infrastructure and related projects as regulatory deadlines approach, which require these technologies. These include 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 government's use of funds under the federal highway bill. Delays in the allocation of funds may prolong uncertainty regarding the

Table of Contents

allotment of transportation funds in federal, state and local budgets. We believe that prolonged uncertainty regarding such matters has adversely impacted in the past, and may continue to adversely impact in the future, our Transportation Systems revenues and our overall financial performance in future periods.

Performance Analytics

Our Performance Analytics segment, formed during the first quarter of our fiscal year ended March 31, 2013 ("Fiscal 2013"), includes our performance measurement and information management solutions, including all of the operations of our former subsidiary, Berkeley Transportation Systems, Inc. ("BTS"), which we acquired in November 2011. BTS specialized in transportation performance measurement systems that leverage its real-time data collection, diagnostic, fusion and warehousing platform to aggregate and compute performance measurements. iPeMS is a state-of-the-art information management software suite that provides big data and software analytics solutions that 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.

The Performance Analytics segment also includes the operations of our former subsidiary, Meridian Environmental Technology, Inc. ("MET"), which we acquired in January 2011. MET specializes in 511/Advanced Traveler Information Systems, and includes our ClearPath Weather management tools that allow users to create solutions to meet roadway maintenance decision needs. Our ClearPath Weather tools provide winter road maintenance recommendations for state agencies, municipalities and for commercial companies.

With the addition of MET, we have experienced seasonality particularly related to certain ClearPath Weather services in our first and second fiscal quarters, mainly because ClearPath Weather services are generally not required in the summer months when weather conditions are typically less severe. Our Performance Analytics 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.

Beginning in late 2013, we undertook a focused development activity to supplement our intellectual property, technology base and product suites to provide products and services for the emerging precision agriculture ("PA") market. This activity included market research into the needs of the PA market, scientific modeling and forecasting development, computing infrastructure development to support both the required big data acquisition and processing and the distributed delivery vehicles required to service the commercial PA market, as well as the development of several products specifically intended for the PA market. We refer to our products for the PA market generically as ClearAg solutions. Our ClearAg platform provides access to a comprehensive database of weather, soil and agronomic information essential to making informed agricultural decisions. Our ClearAg application programming interfaces ("APIs") include historical, real-time and forecast weather content, soil and plant health information, as well as real-time weather and other useful crop growing information, to provide solutions in the precision agriculture technology markets. We commenced commercial sales of our ClearAg platform and related APIs in the first quarter of our fiscal year ended March 31, 2015 ("Fiscal 2015") and introduced our first ClearAg Application ("App") in the first quarter of our fiscal year ended March 31, 2016 ("Fiscal 2016"). We expect positive market acceptance of our ClearAg solutions to continue in upcoming quarters. We plan to continue to fund the

Table of Contents

investments in our ClearAg solutions through internally generated cash flow from our Roadway Sensors and Transportation Systems operations, as well as revenues from our Performance Analytics segment and our available cash on hand, if necessary.

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

We currently market and sell our ClearAg products to commercial entities in the PA market. We currently have two primary product sets which we are marketing for our PA segment; our ClearAg API integration and modeling services and our ClearAg Apps. Our ClearAg APIs are intended for large enterprises in the agriculture market that can benefit from the value of a tight integration of their processes with the ClearAg modeling and forecasting engine; our ClearAg App was introduced in May 2015 and is intended for individual agriculture producers that can benefit from advisories based upon the ClearAg platform that are tailored for their specific locations of interest. We generally deal directly to customers interested in the ClearAg API products, whereas we typically sell through selling partners for our ClearAg App products.

Manufacturing and Materials

We use contract manufacturers to build subassemblies that are used in our Roadway Sensors products. Additionally, we procure certain components from qualified suppliers, both locally and globally, 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, Sony Electronics, Inc. and LG 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

Table of Contents

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 each Fiscal 2016, Fiscal 2015 and our fiscal year ended March 31, 2014 ("Fiscal 2014"). We believe customer support is a key competitive factor.

Our ClearAg products 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 our ClearAg products.

Backlog

Our total backlog of unfulfilled firm orders was approximately \$63.3 million as of March 31, 2016, which included \$53.3 million related to Transportation Systems. In the past three fiscal years, we have recognized 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 Performance Analytics. Substantially the entire backlog for Roadway Sensors as of March 31, 2016 is expected to be recognized as revenue in the fiscal year ending March 31, 2017. At March 31, 2015, we had backlog of approximately \$39.2 million, which included \$29.6 million related to Transportation Systems.

The timing and realization of our backlog is subject to the inherent uncertainties of doing business with federal, state and local governments, particularly in view of budgetary constraints, cut-backs and other delays or reallocations of funding that these entities typically face. 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 conducted at our Performance Analytics facilities in Grand Forks, North Dakota and Berkeley, California, as well as at our principal facility in Santa Ana, California. Our research and development costs and expenses were approximately \$6.9 million for Fiscal 2016, \$5.4 million for Fiscal 2015 and \$4.0 million for Fiscal 2014. We expect to continue to pursue various product development programs and incur research and development expenditures, primarily in our Performance Analytics and Roadway Sensors segments, in future periods.

We believe our engineering and product development capabilities are a competitive strength. We strive to continue to develop new products to meet the needs of our ever-changing markets, as well as to enhance and refine our existing product lines. We plan to focus our development efforts in the near future in our Performance Analytics segment on our ClearAg products for the PA market; however, since 2014, our Roadway Sensors segment has introduced our VantageNext, Vantage Vector, SmartCycle, SmartSpan, Pegasus, Velocity, P10 and P100 products. Additionally, during Fiscal 2015 and Fiscal 2016, we engaged in development activities of our ClearAg precision agriculture solutions. We believe that developing new offerings across our segments and enhancing, refining and marketing our existing products are key components for strong organic growth and profitability.

Table of Contents

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 Performance Analytics segment operates vary from the commercial sector customers for ClearAg solutions to public sector customers for iPeMS and ClearPath Weather products. 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 Climate Corp (now a division of Monsanto) and John Deere as well as new entrants such as Granular and Conservis.

In the market for our Roadway Sensors vehicle detection products, we compete with manufacturers and distributors of other above ground video camera detection systems and manufacturers and distributors and 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.

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 have (i) two U.S. non-provisional patent applications relating to our Roadway Sensors technologies, (ii) twelve issued U.S. patents, two U.S. non-provisional patent applications that were allowed and issued in 2007 and twelve U.S. non-provisional patents, relating to our Performance Analytics technologies, and (iii) four issued U.S. patents and one U.S. non-provisional patent relating specifically to our Transportation Systems technologies. The twelve issued patents relating to our Performance Analytics technologies expire between 2033 and 2035, and our four issued U.S. patents relating to our Transportation Systems technologies expire between 2033 and 2035.

Table of Contents

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

We refer to our employees as associates. As of March 31, 2016, we employed 366 full-time associates and 34 part-time associates, for a total of 400 associates. None of our associates are represented by a labor union, and we have never experienced a work stoppage. We believe our relations with our associates are good.

Government Regulation

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

Table of Contents

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;

performance bond requirements;

long purchase cycles or approval processes;

competitive bidding and qualification requirements;

changes in government policies and political agendas;

milestone requirements and liquidated damage provisions for failure to meet contract milestones; and

international conflicts or other military operations that could cause the temporary or permanent diversion of government funding from transportation or other infrastructure projects.

Governmental budgets and plans are subject to change without warning. Certain risks of selling to governmental entities include dependence on appropriations and administrative allocation of funds, changes in governmental procurement legislation and regulations and other policies that may reflect political developments or agendas, significant changes in contract scheduling, intense competition for government business and termination of purchase decisions for the convenience of the governmental entity. Substantial delays in purchase decisions by governmental entities, and the current constraints on government budgets at the federal, state and local level, 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 Performance Analytics capabilities to address a new market segment, the agricultural market, which may not broadly accept our technologies and new products. The application of precision 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 performance 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 performance analytics or that our new ClearAg products for this market, will achieve broad market acceptance in the near future or at

Table of Contents

all. If the agricultural market fails to understand the benefit of our performance analytics products or chooses not to adopt our technologies, our business, financial condition and results of operations will be adversely affected.

Uncertainty and delays in government funding for transportation infrastructure projects and initiatives have adversely impacted our revenues. There was uncertainty in the past few years regarding allocation of government funds for transportation projects due to delays in the passage of a federal highway bill. On December 4, 2015, the Fixing America's Surface Transportation ("FAST") Act was signed into law, providing \$305 billion over five years for surface transportation projects and programs. Despite the recently enacted federal highway bill, delays in the allocation of such funds, the priority of infrastructure projects and the availability of funds for ITS related projects could continue to adversely impact our revenues and overall financial performance.

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. Certain of our new products have contained undetected software errors or "bugs" when first released by us, despite our testing. We may not discover these faults or errors until after a product has been installed and used by our customers. Any faults or errors in our existing products or in any new products may cause delays in product introduction and shipments, require design modifications, or harm customer relationships 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. 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.

Table of Contents

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, software and camera technologies in response to evolving customer requirements. We cannot assure you that we will be able to adequately manage product transition issues. Our business and results of operations could be adversely affected if we do not anticipate or respond adequately to technological developments or changing customer requirements or if we cannot adequately manage inventory issues typically related to new product transitions and introductions. We cannot assure you that any such investments in research and development will lead to any corresponding increase in revenue.

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 small portion of the traffic intersection market has adopted advanced detection technologies, and our future success will depend in part upon gaining broad market acceptance for detection in this above-ground market. 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 Performance Analytics segment operates vary from public sector customers who focus on performance measurement systems to help measure and manage the effectiveness of their transportation systems to commercial sector customers who ingest and disseminate traffic, weather and agronomic related data, information and analytics through various consumer outlets. Our competitors include divisions of large, multi-national corporations as well as a variety of small providers. 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 traffic and/or weather related data to that market.

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,

Table of Contents

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.

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. The loss of any of our officers, or any of our other executives or key members of management could adversely affect our business, financial condition, or results of operations. Our success will also depend in large part upon our ability to continue to attract, retain and motivate qualified engineering and other highly skilled technical personnel. 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 Performance 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 profitability could be adversely affected if we are not able to maintain adequate utilization of our Transportation Systems and Performance Analytics workforce. The cost of providing our Transportation Systems and Performance Analytics engineering and consulting services, including the extent to which we utilize our workforce, affects our profitability. The rate at which we utilize our workforce is affected by a number of factors, including:

our ability to transition employees from completed projects to new assignments and to hire and assimilate new employees;

our ability to forecast demand for our services and thereby maintain an appropriate headcount in our various regions;

our need to devote time and resources to training, business development, professional development and other non-chargeable activities; and

our ability to match the skill sets of our employees to the needs of the marketplace.

Table of Contents

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

Our failure to successfully bid on new contracts and renew existing contracts could reduce our revenues and profits. Our business depends on our ability to successfully bid on new contracts and renew existing contracts with private and public sector customers. Contract proposals and negotiations are complex and frequently involve a lengthy bidding and selection process, which are affected by a number of factors, such as market conditions, financing arrangements and required governmental approvals. For example, a customer may require us to provide a surety bond or letter of credit to protect the client should we fail to perform under the terms of the contract. If negative market conditions continue, or if we fail to secure adequate financing arrangements or the required governmental approval or fail to meet other required conditions, we may not be able to pursue particular projects, which could reduce or eliminate our profitability.

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.

We are currently not profitable on a consolidated basis and we may be unable to become profitable on a quarterly or annual basis. For Fiscal 2016, we had a net loss, 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 the Company's 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 use of the percentage of completion method of accounting for our Transportation Systems and Performance Analytics revenues could result in a reduction or reversal of previously recorded revenues and profits. A portion of Transportation Systems and Performance Analytics 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.

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

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Table of Contents

of 2002 currently requires us to evaluate the effectiveness of our internal controls over financial reporting at the end of each fiscal year and to include a management report assessing the effectiveness of our internal controls over financial reporting in all annual reports.

As a smaller reporting company, for Fiscal 2016, we were exempt from the auditor attestation requirement over our internal control over financial reporting; however, to the extent we do not qualify as a non-accelerated filer or smaller reporting company in subsequent fiscal years, we will be subject to the auditor attestation requirement under Section 404(b) of the Sarbanes-Oxley Act. In such an event, we may not be able to complete the work required for such attestation on a timely basis and, even if we timely complete such requirements, our independent registered public accounting firm may still conclude that our internal controls over financial reporting are not effective.

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

Our quarterly operating results fluctuate as a result of many factors. Therefore, we may fail to meet or exceed the expectations of securities analysts and investors, which could cause our stock price to decline. Our quarterly revenues and operating results have fluctuated and are likely to continue to vary from quarter to quarter due to a number of factors, many of which are not within our control. Factors that could affect our revenues include, among others, the following:

delays in government contracts and funding from time to time and budgetary constraints at the federal, state and local levels;

our ability to access stimulus funding, funding from 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;

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Table of Contents

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;

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 may 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 have been, and could in the future continue to be, from time to time, 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 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

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Table of Contents

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 operations experience, we currently have three transportation systems contracts in the United Arab Emirates and have been expanding our distribution capabilities for our Roadway Systems segment internationally, particularly in Australia, New Zealand 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;

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Table of Contents

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. Although we have a revolving line of credit, it includes, among other things, certain financial covenants, and a failure to meet such covenants or a material adverse change in the business could result in the bank limiting or eliminating our ability to borrow these or any funds. Should this occur, or if the credit markets further tighten or our business declines, we may need or choose to raise additional capital to repay indebtedness, pursue acquisitions or expand our operations. Such additional capital may be raised through bank borrowings, or other debt or equity financings. We cannot assure you that any additional capital will be available on a timely basis, on acceptable terms, or at all, and such additional financing may result in further dilution to our stockholders.

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

market acceptance of our products and product enhancements, and the overall level of sales of our products;

our ability to control costs;

the supply of key components for our products;

our ability to increase revenue and net income;

increased research and development expenses and sales and marketing expenses;

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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;

Table of Contents

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 April 1, 2013 through June 8, 2016, our common stock has traded at prices as low as \$1.48 per share and as high as \$2.96 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;

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government funding, political agendas and other budgetary constraints;

changes in earnings estimates or investment recommendations by securities analysts; and

international conflicts, political unrest and acts of terrorism.

The stock market 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.

Table of Contents

Certain provisions of our charter documents may discourage a third party from acquiring us and may adversely affect the price of our common stock. Certain provisions of our certificate of incorporation could make it difficult for a third party to acquire us, even though an acquisition might be beneficial to our stockholders. Such provisions could limit the price that investors might be willing to pay in the future for shares of our common stock. Under the terms of our certificate of incorporation, our Board of Directors is authorized to issue, without stockholder approval, up to 2,000,000 shares of preferred stock with voting, conversion and other rights and preferences superior to those of our common stock. In August 2009, we adopted a new stockholder rights plan and declared a dividend of preferred stock purchase rights to our stockholders. Generally, the stockholder rights plan provides that if a person or group acquires 15% or more of our common stock, subject to certain exceptions and under certain circumstances, the rights may be exchanged by us for common stock or the holders of the rights, other than the acquiring person or group, could acquire additional shares of our capital stock at a discount off of the then current market price. Such exchanges or exercise of rights could cause substantial dilution to a particular acquirer and discourage the acquirer from pursuing our company. The mere existence of a stockholder rights plan often delays or makes a merger, tender offer or other acquisition 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 9 of Notes to Consolidated Financial Statements, included in Part IV, Item 15 of this report.

ITEM 3. LEGAL PROCEEDINGS

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

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

Table of Contents**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:

| | High | Low |
|----------------------------------|---------|---------|
| Fiscal 2016 | | |
| Quarter Ended June 30, 2015 | \$ 1.91 | \$ 1.64 |
| Quarter Ended September 30, 2015 | 2.96 | 1.62 |
| Quarter Ended December 31, 2015 | 2.65 | 2.00 |
| Quarter Ended March 31, 2016 | 2.65 | 1.89 |
| Fiscal 2015 | | |
| Quarter Ended June 30, 2014 | \$ 2.11 | \$ 1.66 |
| Quarter Ended September 30, 2014 | 2.23 | 1.48 |
| Quarter Ended December 31, 2014 | 2.00 | 1.58 |
| Quarter Ended March 31, 2015 | 1.94 | 1.60 |

On June 8, 2016, the last reported sales price of our common stock on the NASDAQ Capital Market was \$2.33. As of June 8, 2016, we had 349 holders of record of our common stock according to information furnished by our transfer agent.

Dividend Policy

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

Issuer Purchases of Equity Securities

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. On August 9, 2012, our Board of Directors approved a new stock repurchase program pursuant to which we may acquire up to \$3.0 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 an existing or future 10b5-1 trading plan to facilitate repurchases 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 our existing stock repurchase program, pursuant to which we may continue to acquire shares of its outstanding common stock from time to time for an unspecified length of time.

Table of Contents

From inception of the original stock repurchase program in August 2011 through March 31, 2016, we repurchased approximately 3,422,000 shares of our common stock for an aggregate repurchase price of approximately \$5.6 million at an average purchase price of \$1.63 per share. We did not repurchase any shares of our common stock during the three months ended March 31, 2016. All repurchased shares from prior periods have been retired and resumed their status as authorized and unissued shares of our common stock. As of March 31, 2016, there was approximately \$1.7 million of remaining funds available under the stock repurchase program.

ITEM 6. SELECTED FINANCIAL DATA

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

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

You should read the following discussion and analysis in conjunction with our Consolidated Financial Statements and related Notes thereto included in Part IV, Item 15 of this report and the "Risk Factors" section in Item 1A, as well as 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 information solutions for the intelligent traffic systems ("ITS") and the precision agriculture ("PA") markets. In the ITS market, we are focused on the development and application of advanced technologies and software-based information systems that reduce traffic congestion, provide measurement, management and analytics, and that improve the efficiency and safety of surface transportation systems infrastructure. We believe our products, services and solutions, in conjunction with sound traffic management, minimize the environmental impact of traffic congestion and enhance the adoption of advanced ITS solutions that are required for the deployment of connected and autonomous vehicles. In the PA market, we have combined our unique intellectual property with enhanced soil, land surface, and agronomy modeling techniques utilizing our extensible EMPower hybrid computing architecture to create a set of ClearAg solutions that provide analytical support to large enterprises in the agriculture market and field-specific advisories to individual producers.

Acquisitions. In November 2011, we acquired all of the outstanding capital stock of Berkeley Transportation Systems, Inc. ("BTS"), a privately-held company based in Berkeley, California which specialized in transportation performance measurement. During the third quarter of the Fiscal 2014, we paid the former BTS shareholders \$250,000 pursuant to certain holdback provisions in the original stock purchase agreement. Additionally, in the third quarter of Fiscal 2015, we paid the former BTS shareholders approximately \$336,000 pursuant to certain deferred payment provisions in the stock purchase agreement. This payment completed our obligations under the deferred payment provisions of the purchase agreement.

In January 2011, we acquired all of the outstanding capital stock of Meridian Environmental Technology, Inc. ("MET"), which specialized in 511/Advanced Traveler Information Systems.

In connection with this acquisition, we held back \$250,000 of the purchase price. After we determined that the contingencies related to the release of the \$250,000 holdback were not met, no portion of the \$250,000 holdback was released and the entire amount was reversed into operating income during the second quarter of Fiscal 2013. In addition, in the fourth quarter of Fiscal 2013, we paid to the former MET shareholders a deferred earn-out payment in the amount of \$409,000, which payment completed our obligations under the deferred payment provisions of the purchase agreement.

Table of Contents

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

Sale of Vehicle Sensors. On July 29, 2011, we completed the sale of substantially all of our assets used in connection with our 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 are entitled to additional consideration in the form of certain performance and royalty-related earn-outs through June 30, 2017. As of March 31, 2016, we received approximately \$1.6 million in connection with such royalty-related earn-out provisions. We also had approximately \$160,000 in royalty-related receivables included in the prepaid expenses and other current assets in the accompanying consolidated balance sheet as of March 31, 2016.

As a result of the Asset Sale, we no longer operate in the Vehicle Sensors segment, and we determined that the Vehicle Sensors segment, which previously constituted one of our operating segments, 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 IV, Item 15 of this report, for additional discussion regarding the Asset Sale.

Business Segments. Subsequent to the Asset Sale and our acquisition of BTS, we have operated in three reportable segments: Roadway Sensors, Transportation Systems and Performance Analytics.

The Roadway Sensors segment provides hardware and software products to multiple segments of the ITS market. These various vehicle detection and information systems are used for traffic intersection control, incident detection and roadway traffic data collection applications.

The Transportation Systems segment includes transportation engineering and consulting services focused on the planning, design, development and implementation of software-based systems that integrate sensors, video surveillance, computers and advanced communications equipment to enable public agencies to monitor, control and direct traffic flow, assist in the quick dispatch of emergency crews and distribute real-time information about traffic conditions.

The Performance Analytics segment includes our performance measurement and information management solution iPeMS, a specialized transportation performance measurement and traffic analytics solution, as well as ClearPath Weather, our road-maintenance application, and ClearAg, our precision agriculture solution.

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. 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

Table of Contents

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 Performance Analytics revenues are also derived from long-term contracts with governmental agencies, as well as contracts with commercial companies. 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.

Accounts Receivable. The collectability of our accounts receivable is evaluated through review of outstanding invoices and ongoing credit evaluations of our customers' financial condition. We record an allowance for doubtful accounts for specific receivables deemed to be at risk for collection, as well as a general allowance based on our historical collections experience. Considerable judgment is required in assessing and estimating the ultimate realization of trade receivables, including the current credit-worthiness of each customer. If the financial condition of our customers deteriorates, resulting in an

Table of Contents

impairment of their ability to make required payments, additional allowances may be required that could adversely affect our operating results.

Inventories. Inventories consist of finished goods, work-in- process and raw materials and are stated at the lower of cost or market. We write down the carrying value of our inventories to net realizable value for estimated excess and obsolete inventories in an amount equal to the difference between the cost of the inventories and their estimated realizable value. These estimates are based on management's judgments and assumptions as to future demand requirements and our evaluation of market conditions. Demand for our products may fluctuate significantly over time, and actual demand and market conditions may be more or less favorable than those projected by management. In the event that actual demand is lower than originally projected, additional inventory write-downs may be required. Estimated inventory write-downs, once established, are not reversed until the related inventory has been sold or scrapped, so if actual market conditions are more favorable in the fiscal periods subsequent to those in which we record significant write-downs, we may have higher gross margins when products are sold.

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

We evaluate goodwill on an annual basis in our fourth fiscal quarter or more frequently if we believe indicators of impairment exist. We have determined that our reporting units for purposes of testing for goodwill impairment are identical to our reportable segments for financial reporting purposes. In the fiscal year ended March 31, 2012 ("Fiscal 2012"), we early adopted the provisions issued by the Financial Accounting Standards Board ("FASB") that were intended to simplify goodwill impairment testing. This guidance permits us to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If we conclude that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, we conduct a two-step goodwill impairment test. The first step of the impairment test involves comparing the fair values of the applicable reporting units with their carrying values. We determine the fair values of our reporting units using the income valuation approach, as well as other generally accepted valuation methodologies. If the carrying amount of a reporting unit exceeds the reporting unit's fair value, we perform the second step of the goodwill impairment test. The second step of the goodwill impairment test involves comparing the implied fair value of the affected reporting unit's goodwill with the carrying value of that goodwill. The amount by which the carrying value of the goodwill exceeds its implied fair value, if any, is recognized as an impairment loss. We monitor the indicators for goodwill impairment testing between annual tests. Certain adverse business conditions impacting one or more reporting units would cause us to test goodwill for impairment on an interim basis. As part of our annual assessment, management determines the most appropriate and efficient method to assess goodwill for impairment, which could include either the simplified testing approach or the two-step goodwill test described above.

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

Table of Contents

Warranty. We generally provide a one to three year warranty from the original invoice date on our 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. Should our actual experience of warranty returns be higher than anticipated, additional warranty reserves may be required, which would adversely affect our product gross margins and our operating results.

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

On an interim basis, we estimate what our anticipated annual effective tax rate will be, while also separately considering applicable discrete and other non-recurring items, and record a quarterly income tax provision in accordance with this anticipated rate. As the fiscal year progresses, we refine our estimates based upon actual events and financial results during the year. This estimation process can result in significant changes to our expected effective tax rate. When this occurs, we adjust our income tax provision during the quarter in which our estimates are refined so that the year-to-date provision reflects the expected annual effective tax rate. These changes, along with adjustments to our deferred taxes, among others, may create fluctuations in our overall effective tax rate from quarter to quarter.

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

Stock-Based Compensation. We record stock-based compensation in the statements of operations as an expense, based on the estimated grant date fair value of our stock-based awards, whereby such fair values are amortized over the requisite service period. Our stock-based awards are currently comprised of common stock options and restricted stock units. The fair value of our 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 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.

Table of Contents**Recent Accounting Pronouncements**

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

Results of Operations

The following table sets forth certain statement of operations data as a percentage of revenues for the periods indicated.

| | Year Ended March 31, | | |
|--|----------------------|--------|--------|
| | 2016 | 2015 | 2014 |
| Total revenues | 100.0% | 100.0% | 100.0% |
| Cost of revenues | 60.6 | 61.0 | 61.9 |
| Gross profit | 39.4% | 39.0% | 38.1% |
| Operating expenses: | | | |
| Selling, general and administrative | 34.4 | 33.8 | 28.3 |
| Research and development | 8.9 | 7.5 | 5.9 |
| Amortization of intangible assets | 0.5 | 0.6 | 0.9 |
| Change in fair value of contingent consideration | | 0.0 | 0.0 |
| Total operating expenses | 43.8 | 41.9 | 35.1 |
| Operating (loss) income | (4.4) | (2.9) | 3.0 |
| Non-operating income (expense): | | | |
| Other income (expense), net | 0.0 | (0.0) | |
| Interest income, net | 0.0 | 0.0 | |
| (Loss) income from continuing operations before income taxes | (4.4) | (2.9) | 3.0 |
| (Provision) benefit for income taxes | (11.7) | 1.1 | (1.0) |
| (Loss) income from continuing operations | (16.1) | (1.8) | 2.0 |
| Gain on sale of discontinued operation, net of tax | 0.3 | 0.3 | 0.1 |
| Net (loss) income | (15.8)% | (1.5)% | 2.1% |

Analysis of Fiscal 2016, Fiscal 2015 and Fiscal 2014 Results of Operations

Total Revenues. Total revenues are comprised of sales from our Roadway Sensors, Transportation Systems and Performance Analytics segments. The following tables present details of total revenues for Fiscal 2016 compared to Fiscal 2015, and Fiscal 2015 compared to Fiscal 2014:

| | Year Ended March 31, | | \$ Increase | % Change |
|------------------------------------|-------------------------|-----------|----------------|-------------|
| | 2016 | 2015 | | |
| (In thousands, except percentages) | | | | |
| Total revenues | \$ 77,748 | \$ 72,251 | \$ 5,497 | 7.6% |

| | Year Ended March 31, | | \$ Increase | % Change |
|------------------------------------|-------------------------|-----------|----------------|-------------|
| | 2015 | 2014 | | |
| (in thousands, except percentages) | | | | |
| Total revenues | \$ 72,251 | \$ 68,228 | \$ 4,023 | 5.9% |

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Table of Contents

Total revenues for Fiscal 2016 increased approximately 7.6% to \$77.7 million, compared to \$72.3 million in Fiscal 2015, due primarily to an increase of approximately 11% in Roadway Sensors revenues and approximately 7% in Transportation Systems revenues. The increases in revenues were partially offset by a decrease of approximately 8% in Performance Analytics revenues in Fiscal 2016.

Total revenues for Fiscal 2015 increased approximately 5.9% to \$72.3 million, compared to \$68.2 million in Fiscal 2014, due primarily to an increase of approximately 15% in Roadway Sensors revenues. The increase in revenues was partially offset by decreases of approximately 1% in Transportation Systems revenues and approximately 6% in Performance Analytics revenues in Fiscal 2015.

Roadway Sensors revenues in Fiscal 2016 increased approximately 11% compared to Fiscal 2015, primarily due to higher unit sales of our legacy Roadway Sensors products, and to a lesser extent, due to increases in our distribution of certain original equipment manufacturer ("OEM") products for the traffic intersection market. Revenue generated through the distribution of certain third party products was approximately \$5.3 million and approximately \$5.0 million for Fiscal 2016 and Fiscal 2015, respectively. Roadway Sensors revenues in Fiscal 2015 increased approximately 15% compared to Fiscal 2014, primarily due to increases in our distribution of certain third party products and increases in unit sales of our existing products. While OEM products generally have lower gross margins than our core video detection products, we believe the offering of OEM products will benefit sales of our core products by providing a more comprehensive suite of traffic solutions for our customers. Going forward, we plan to continue growing revenues by focusing on our core domestic intersection market, and refine and deliver products that address the needs of this market, primarily our VantageNext processors and camera systems and our Vantage Vector video/radar hybrid sensor, as well as our SmartCycle and SmartSpan products. Additionally, we plan to grow revenues by focusing on international distribution channel expansion and expect to continue to refine products that address these markets, namely our Abacus, P10 and P100 products.

Transportation Systems revenues in Fiscal 2016 increased approximately 7% compared to Fiscal 2015, primarily as a result of two large contract wins during the third quarter of Fiscal 2016, which positively impacted revenue growth in our fourth quarter of Fiscal 2016, as well as timing of backlog fulfillment on certain other projects. The Transportation Systems segment backlog experienced significant growth in Fiscal 2016 and reached approximately \$53.3 million as of March 31, 2016, compared to approximately \$29.6 million as of March 31, 2015. Transportation Systems revenues in Fiscal 2015 decreased approximately 1% compared to Fiscal 2014, primarily as a result of timing delays in starting certain new projects in our backlog, as well as a reduction in sub-consultant revenues. Going forward, we plan to continue to pursue larger contracts that may contain significant sub-consulting content. While larger contracts will likely contribute to overall revenue growth, the mix of sub-consulting content will likely reduce the related gross profit from period to period, as revenues derived from sub-consultants generally have lower gross margins than our professional services.

Performance Analytics revenues in Fiscal 2016 decreased approximately 8% compared to Fiscal 2015, which was primarily due to reductions in our iPeMS revenues as a result of deferred revenue on certain iPeMS implementation projects, delays in contract awards with certain public agencies, and the timing of backlog fulfillment on certain other projects, which were partially offset by increased revenues from our ClearAg solutions under newly signed contracts during Fiscal 2016. Performance Analytics revenues in Fiscal 2015 decreased approximately 6% compared to Fiscal 2014, which was primarily due to delays in contract awards with certain public agencies and the timing of backlog fulfillment. Going forward, we plan to continue investing in this segment, particularly in the research and development and sales and marketing of the ClearAg, ClearPath Weather and iPeMS performance measurement 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

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Table of Contents

decision support services that leverage our precision weather, soil and agronomic content and application intellectual property.

Gross Profit. The following tables present details of our gross profit for Fiscal 2016 compared to Fiscal 2015, and Fiscal 2015 compared to Fiscal 2014:

| | Year Ended March 31, | | \$ Increase | % Change |
|---------------------------------------|-------------------------|-----------|----------------|-------------|
| | 2016 | 2015 | | |
| (In thousands, except percentages) | | | | |
| Gross profit | \$ 30,669 | \$ 28,182 | \$ 2,487 | 8.8% |
| Gross profit as a % of total revenues | 39.4% | 39.0% | | |

| | Year Ended March 31, | | \$ Increase | % Change |
|---------------------------------------|-------------------------|-----------|----------------|-------------|
| | 2015 | 2014 | | |
| (in thousands, except percentages) | | | | |
| Gross profit | \$ 28,182 | \$ 25,974 | \$ 2,208 | 8.5% |
| Gross profit as a % of total revenues | 39.0% | 38.1% | | |

Our total gross profit as a percentage of total revenues for Fiscal 2016 increased approximately 40 basis points compared to Fiscal 2015 primarily due to higher revenues derived from our Roadway Sensors segment, which has generally experienced higher gross profits than our other segments and which increased to approximately 51.8% of our total revenues for Fiscal 2016, as compared to 50.3% for Fiscal 2015. Roadway Sensors revenues generally carry higher gross margins than Transportation Systems and Performance Analytics revenues. Therefore, the increase in Roadway Sensors revenues had a positive impact on our overall margin. The increase in gross profit as a percentage of total revenues was also attributable to an increase in Transportation Systems gross profit percentage, primarily due to timing of revenue recognition on certain projects and an increase in the percentage of revenue generated by internal labor compared to revenue generated by our sub-consultants, which typically generates lower profit margins.

Our total gross profit as a percentage of total revenues for Fiscal 2015 increased approximately 90 basis points compared to Fiscal 2014 also due to our product and service mix. Revenues derived from our Roadway Sensors segment increased to approximately 50.3% of our total revenues in Fiscal 2015, compared to 46.6% in Fiscal 2014.

Roadway Sensors gross profit can fluctuate in any specific quarter or year based on, among other factors, customer and product mix, competitive pricing requirements, product warranty costs and provisions for excess and obsolete inventories, as well as shifts of engineering resources from development activities to sustaining activities, which we record as cost of goods sold.

We recognize a portion of our Transportation Systems and Performance Analytics 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.

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Table of Contents

Selling, General and Administrative Expense

The following table presents selling, general and administrative expense for Fiscal 2016 and Fiscal 2015:

| | Year Ended March 31, | | Year Ended March 31, | | \$ | % Change |
|---|----------------------|---------------|----------------------|---------------|---------------------|----------|
| | 2016 | | 2015 | | | |
| | Amount | % of Revenues | Amount | % of Revenues | Increase (Decrease) | |
| (In thousands, except percentages) | | | | | | |
| Salary and personnel-related | \$ 18,546 | 23.9% | \$ 15,896 | 22.0% | \$ 2,650 | 16.7% |
| Facilities, insurance and supplies | 2,727 | 3.5 | 2,522 | 3.5 | 205 | 8.1 |
| Travel and conferences | 2,136 | 2.7 | 1,681 | 2.3 | 455 | 27.1 |
| Professional and outside services | 2,658 | 3.4 | 3,982 | 5.5 | (1,324) | (33.2) |
| Other | 779 | 1.0 | 344 | 0.5 | 435 | 126.5 |
| Selling, general and administrative | \$ 26,846 | 34.5% | \$ 24,425 | 33.8% | \$ 2,421 | 9.9 |

The overall increase in selling, general and administrative expense for Fiscal 2016, as compared to Fiscal 2015, was primarily due to planned investments in Performance Analytics sales and marketing, including an increase in the salesforce headcount, as well as increased headcount in general and administrative positions, which resulted in higher salary and personnel-related costs. The overall increase for Fiscal 2016 was also attributable to certain transition costs relating to the Company's previous CEO and interim CEO. These increases in sales, marketing, general and administrative expenses were offset by decreases in professional and outside services for audit fees incurred during Fiscal 2015 in connection with the audit of our financial statements for Fiscal 2014. As previously disclosed, the Company delayed its Fiscal 2014 earnings release and the filing of its Annual Report on Form 10-K for Fiscal 2014 until September 3, 2014, due to additional procedures performed by its auditors related to contract revenue testing. As a result of these additional procedures and related delays, we incurred an increase of approximately \$940,000 in audit fees during the first and second quarters of Fiscal 2015. We also incurred an increase of approximately \$175,000 in service fees for the review of our Fiscal 2015 quarters. In addition, in Fiscal 2015, we incurred approximately \$770,000 of outside professional consulting costs to assist with the completion of the Fiscal 2014 annual audit and the Fiscal 2015 quarterly reviews.

The following table presents selling, general and administrative expense for Fiscal 2015 and 2014:

| | Year Ended March 31, | | Year Ended March 31, | | \$ | % Change |
|---|----------------------|---------------|----------------------|---------------|---------------------|----------|
| | 2015 | | 2014 | | | |
| | Amount | % of Revenues | Amount | % of Revenues | Increase (Decrease) | |
| (In thousands, except percentages) | | | | | | |
| Salary and personnel-related | \$ 15,896 | 22.0% | \$ 12,955 | 19.0% | \$ 2,941 | 22.7% |
| Facilities, insurance and supplies | 2,522 | 3.5 | 2,603 | 3.8 | (81) | (3.1) |
| Travel and conferences | 1,681 | 2.3 | 1,502 | 2.2 | 179 | 11.9 |
| Professional and outside services | 3,982 | 5.5 | 1,593 | 2.3 | 2,389 | 150.0 |
| Other | 344 | 0.5 | 616 | 0.9 | (272) | (44.2) |
| Selling, general and administrative | \$ 24,425 | 33.8% | \$ 19,269 | 28.2% | \$ 5,156 | 26.8 |

The overall increase in selling, general and administrative expense for Fiscal 2015, as compared to Fiscal 2014, was primarily due to an increase in salary and personnel related expenses and audit and consulting fees incurred in connection with the audit of our Fiscal 2014 financial statements. The overall increase was also increased due to planned investments in Performance Analytics sales and

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Table of Contents

marketing costs, consisting primarily of increased headcount which resulted in higher salary and personnel related costs, recruiting and travel.

Research and Development Expense

The following table presents research and development expense for Fiscal 2016 and Fiscal 2015:

| | Year Ended March 31, | | Year Ended March 31, | | \$ | % |
|--------------------------------------|----------------------|---------------|----------------------|---------------|---------------------|--------|
| | 2016 | | 2015 | | | |
| | Amount | % of Revenues | Amount | % of Revenues | Increase (Decrease) | Change |
| (In thousands, except percentages) | | | | | | |
| Salary and personnel-related | \$ 3,325 | 4.3% | \$ 2,674 | 3.7% | \$ 651 | 24.3% |
| Facilities, development and supplies | 2,404 | 3.1 | 1,543 | 2.1 | 861 | 55.8 |
| Other | 1,204 | 1.5 | 1,179 | 1.6 | 25 | 2.1 |
| Research and development | \$ 6,933 | 8.9% | \$ 5,396 | 7.5% | \$ 1,537 | 28.5 |

The overall increase in research and development expense for Fiscal 2016 compared to Fiscal 2015, was primarily due to an increase in headcount, which resulted in higher salary and personnel-related costs. The increases were also attributable to research costs for certain software and application developments in the Performance Analytics segment and investments in securing intellectual property rights.

The Performance Analytics segment continued to invest in the development of ClearAg and ClearPath Weather solutions. ClearAg products include historical, real-time and forecast weather content, soil and crop growth information, and other useful crop health information to provide solutions in the precision agriculture technology markets. We successfully released generally available versions of a set of ClearAg products during the first half of Fiscal 2016 and the ClearAg iOS Mobile App in March 2016. Going forward, we expect to continue investing in our Performance Analytics segment to enhance the ClearAg, ClearPath Weather and iPeMS solutions. This continued investment may result in increases in research and development costs.

The following table presents research and development expense for Fiscal 2015 and Fiscal 2014:

| | Year Ended March 31, | | Year Ended March 31, | | \$ | % |
|--------------------------------------|----------------------|---------------|----------------------|---------------|---------------------|--------|
| | 2015 | | 2014 | | | |
| | Amount | % of Revenues | Amount | % of Revenues | Increase (Decrease) | Change |
| (In thousands, except percentages) | | | | | | |
| Salary and personnel-related | \$ 2,674 | 3.7% | \$ 2,314 | 3.4% | \$ 360 | 15.6% |
| Facilities, development and supplies | 1,543 | 2.1 | 1,232 | 1.8 | 311 | 25.2 |
| Other | 1,179 | 1.6 | 483 | 0.7 | 696 | 144.1 |
| Research and development | \$ 5,396 | 7.5% | \$ 4,029 | 5.9% | \$ 1,367 | 33.9 |

Research and development expense for Fiscal 2015 increased approximately 33.9% compared to Fiscal 2014, primarily due to the planned expenditures for product research, discovery and developments in the Performance Analytics segment. The increase in research and development was also attributable to additional salary and personnel costs related in the Performance Analytics segment.

Impairment of Goodwill

In Fiscal 2012, we adopted the provisions issued by the FASB that are intended to simplify goodwill impairment testing. The updated guidance permits us to first assess qualitative factors to

Table of Contents

determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If we conclude that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, we conduct a two-step goodwill impairment test. We performed annual impairment assessments of the carrying value of goodwill in the fourth quarter of each of Fiscal 2016, Fiscal 2015 and Fiscal 2014. We determined it was more appropriate to perform quantitative first-step assessments in Fiscal 2016, Fiscal 2015 and Fiscal 2014 to estimate the fair value of our reporting units using both the income approach and market approach. Based on our assessments, we determined that no impairment was indicated as the estimated fair value of each reporting unit exceeded its respective carrying value.

Based on our goodwill impairment testing for Fiscal 2016, Fiscal 2015 and Fiscal 2014, we believe the carrying value of our goodwill was not impaired as of March 31, 2016, 2015 and 2014, as the estimated fair values of our reporting units exceeded their carrying values at the end of such fiscal years. 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.

Interest Income (Expense), Net

Net interest income was approximately \$12,000 in Fiscal 2016. Net interest expense was approximately \$6,000 and \$0 in Fiscal 2015 and Fiscal 2014, respectively.

Income Taxes

The following table presents our provision for income taxes for Fiscal 2016, Fiscal 2015 and Fiscal 2014:

| | Year Ended March 31, | | |
|--------------------------------------|---|-------------|-------------|
| | 2016 | 2015 | 2014 |
| | (In thousands, except percentages) | | |
| Provision (benefit) for income taxes | \$ 9,079 | \$ (816) | \$ 704 |
| Effective tax rate | (262.6)% | 39.0% | 34.8% |

The difference between the statutory and the effective tax rate is primarily attributable to the recording of a valuation allowance against our deferred tax assets during Fiscal 2016.

The difference between the statutory and the effective tax rate is primarily attributable to state income taxes. Additionally, our effective tax rate for Fiscal 2015 was favorably impacted by the recognition of approximately \$233,000 of tax credits, partially offset by permanent non-deductible tax items, including share-based payments and other permanent differences amounting to approximately \$156,000.

Our effective tax rate for Fiscal 2014 was favorably impacted by the recognition of approximately \$359,000 of tax credits, partially offset by permanent non-deductible tax items, including share-based payments and other permanent differences amounting to approximately \$103,000, and by the recording a valuation allowance against certain of our state net operating losses in the amount of \$185,000, net of federal benefit.

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 of December 31, 2015, the Company had generated a cumulative pre-tax loss over the trailing three years. As such, we considered it appropriate to record a valuation allowance of approximately \$10.1 million in our third quarter of

Table of Contents

Fiscal 2016 against our deferred tax assets. We will continuously 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, 2016, we had \$9.7 million of federal net operating loss carryforwards and \$794,000 of state net operating loss carryforwards that begin to expire in 2022 and 2031, respectively. Although the impact cannot be precisely determined at this time, we believe that our net operating loss carryforwards will cause us to have future income tax payments that are substantially lower than the income tax liability calculated using statutory tax rates.

Liquidity and Capital Resources*Cash Flows*

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

At March 31, 2016, we had \$24.3 million in working capital, which included \$16.0 million in cash and cash equivalents and reflected no borrowings on our \$12.0 million line of credit. This compares to working capital of \$30.9 million at March 31, 2015, which included no borrowings on our line of credit and \$22.0 million in cash and cash equivalents.

The following table summarizes our cash flows for Fiscal 2016, Fiscal 2015 and Fiscal 2014:

| | Year Ended March 31, | | |
|--|-----------------------------|-------------|-------------|
| | 2016 | 2015 | 2014 |
| | (In thousands) | | |
| Net cash provided by (used in): | | | |
| Operating activities | \$ (4,110) | \$ 3,577 | \$ 3,274 |
| Investing activities | (978) | (844) | (779) |
| Financing activities | (844) | (1,186) | (759) |

Operating Activities. 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 property and equipment. Cash used in our operations was also driven by approximately \$2.3 million used in working capital.

Table of Contents

Cash provided by our operations in Fiscal 2015 was primarily the result of approximately \$4.6 million provided by improvements in our accounts receivables, net costs and estimated earnings in excess of billings, and accounts payable and accrued expenses. Cash provided by operations was also attributable to approximately \$1.5 million of non-cash items for depreciation, amortization and stock-based compensation expense. This was offset by a decrease of approximately \$0.5 million used in working capital for inventories.

Cash provided by our operations in Fiscal 2014 was primarily the result of our net income of approximately \$1.4 million and approximately \$2.6 million non-cash items for depreciation, amortization, stock-based compensation expense and adjustments to deferred tax assets. This was offset by approximately \$0.7 million used in working capital, consisting of approximately \$1.5 million from accounts receivable, inventories, and net costs and estimated earnings in excess of billings, net of approximately \$0.8 million for prepaid expenses and other assets and accounts payable and accrued activities.

Investing Activities. 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 Performance Analytics business segment related to ClearAg assets, which were offset by approximately \$368,000 in proceeds from the sale of the Vehicle Sensors segment.

Cash used in our investing activities during Fiscal 2015 consisted of approximately \$986,000 for purchases of property and equipment, primarily related to leasehold improvements on our headquarters facility, which was offset by approximately \$142,000 in proceeds from the sale of the Vehicle Sensors segment.

Cash used in our investing activities during Fiscal 2014 consisted of approximately \$452,000 for purchases of property and equipment and approximately \$301,000 used for the development of software and data acquisitions in the Performance Analytics segment.

Financing Activities. 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 by approximately \$383,000 of cash proceeds received from the exercises of stock options.

Net cash used in financing activities during Fiscal 2015 was primarily the result of approximately \$863,000 in cash used to repurchase shares of our common stock under our stock repurchase program and approximately \$336,000 in cash used for the final deferred payment for the prior acquisition of BTS.

Net cash used in financing activities during Fiscal 2014 was primarily the result of approximately \$409,000 in cash used for a deferred payment for the prior acquisition of MET, approximately \$250,000 in cash used for an earn-out payment for the prior acquisition of BTS, and approximately \$339,000 in cash used to repurchase shares of our common stock under our stock repurchase program. This was partially offset by our receipt of proceeds of \$270,000 from stock option and warrant exercises.

Borrowings

We currently have a \$12.0 million revolving line of credit with California Bank & Trust ("CB&T"), which expires on October 1, 2016. Interest on borrowed amounts under the revolving line of credit is payable monthly at a rate equal to the current stated prime rate (3.50% at March 31, 2016). We are obligated to pay an unused line fee of 0.15% per annum applied to the average unused portion of the revolving line of credit during the preceding month. The revolving line of credit does not contain any early termination fees and is secured by substantially all of our assets. As of March 31, 2016 and 2015, no amounts were outstanding under the line of credit with CB&T. Availability under this line of credit

Table of Contents

may be reduced or otherwise limited in accordance with (or pursuant to) certain financial and other covenants. As of March 31, 2016 and 2015, we were in compliance with all such financial covenants. If we were to be in violation of certain covenants under this agreement, our lender could decline to extend further credit to us, or choose to accelerate payment on all outstanding loan balances, if any, and pursue its security interest in our assets. In this event, we cannot assure you that we would be able to quickly obtain equivalent or suitable replacement financing on acceptable terms, on a timely basis, or at all. If we were not able to secure alternative sources of financing, such acceleration could have a material adverse impact on our business and financial condition.

Off-Balance Sheet Arrangements

Other than our operating leases, which are further described at Note 9 of Notes to Consolidated Financial Statements, included in Part IV, Item 15 of this report, we do not have any other material off-balance sheet arrangements at March 31, 2016.

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 interest rate risk is limited to our line of credit, which bears interest equal to the prevailing prime rate plus 0.25%. We do not believe that a 10% increase in the interest rate on our line of credit would have a material impact on our financial position, operating results or cash flows.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

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

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

None.

ITEM 9A. CONTROLS AND PROCEDURES

(a) *Evaluation of disclosure controls and procedures.* In accordance with Rule 13a-15(b) of the Securities Exchange Act of 1934, as amended (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

Table of Contents

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 Fiscal 2016 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

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

We have assessed the effectiveness of our internal controls over financial reporting as of March 31, 2016. In making this assessment, we used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in *Internal Control Integrated Framework (2013)*. Based on our assessment, we believe that, as of March 31, 2016, our internal control over financial reporting was effective. This annual report does not include an attestation report of our independent registered public accounting firm regarding internal control over financial reporting. Such a report is not required pursuant to the rules of the SEC applicable to smaller reporting companies.

ITEM 9B. OTHER INFORMATION

None.

Table of Contents

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

(a) *Identification of Directors.* The information under the caption "Election of Directors," appearing in our proxy statement for the 2016 Annual Meeting of Stockholders, is incorporated herein by reference.

(b) *Identification of Executive Officers.* The information under the caption "Executive Compensation and Other Information Executive Officers," appearing in our proxy statement for the 2016 Annual Meeting of Stockholders, is incorporated herein by reference.

(c) *Compliance with Section 16(a) of the Exchange Act.* The information under the caption "Section 16(a) Beneficial Ownership Reporting Compliance," appearing in our proxy statement for the 2016 Annual Meeting of Stockholders, is incorporated herein by reference.

(d) *Corporate Governance.* The information under the caption "Corporate Governance," appearing in our proxy statement for the 2016 Annual Meeting of Stockholders, is incorporated herein by reference.

(e) *Audit Committee.* The information under the caption "Board Meetings and Committees Audit Committee," appearing in our proxy statement for the 2016 Annual Meeting of Stockholders, is incorporated herein by reference.

ITEM 11. EXECUTIVE COMPENSATION

The information under the caption "Executive Compensation and Other Information," appearing in our proxy statement for the 2016 Annual Meeting of Stockholders, is incorporated herein by reference.

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

The information under the captions "Equity Compensation Plans" and "Principal Stockholders and Common Stock Ownership of Certain Beneficial Owners and Management," appearing in our proxy statement for the 2016 Annual Meeting of Stockholders, is incorporated herein by reference.

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

The information under the captions "Corporate Governance Director Independence" and "Certain Transactions," appearing in our proxy statement for the 2016 Annual Meeting of Stockholders, is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

The information under the caption "Fees Paid to Independent Registered Public Accounting Firm," appearing in our proxy statement for the 2016 Annual Meeting of Stockholders, is incorporated herein by reference.

Table of Contents

PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

(a)

Documents filed as part of this report:

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

| | |
|---|-----------|
| <u>Report of Independent Registered Public Accounting Firm</u> | <u>42</u> |
| <u>Consolidated Balance Sheets as of March 31, 2016 and 2015</u> | <u>44</u> |
| <u>Consolidated Statements of Operations for the fiscal years ended March 31, 2016, 2015 and 2014</u> | <u>45</u> |
| <u>Consolidated Statements of Stockholders' Equity for the fiscal years ended March 31, 2016, 2015 and 2014</u> | <u>46</u> |
| <u>Consolidated Statements of Cash Flows for the fiscal years ended March 31, 2016, 2015 and 2014</u> | <u>47</u> |
| <u>Notes to Consolidated Financial Statements</u> | <u>48</u> |

2.

Exhibits.

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

Table of Contents

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 17, 2016

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:

| Signature | Title | Date |
|---|---|---------------|
| <u>/s/ JOE BERGERA</u> Joe Bergera | Director, President and Chief Executive Officer (principal executive officer) | June 17, 2016 |
| <u>/s/ ANDREW C. SCHMIDT</u> Andrew C. Schmidt | Chief Financial Officer (principal financial and accounting officer) | June 17, 2016 |
| <u>/s/ GREGORY A. MINER</u> Gregory A. Miner | Chairman of the Board | June 17, 2016 |
| <u>/s/ RICHARD CHAR</u> Richard Char | Director | June 17, 2016 |

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Table of Contents

| Signature | Title | Date |
|---|--------------|---------------|
| <u>/s/ KEVIN C. DALY</u> Kevin C. Daly, Ph.D | Director | June 17, 2016 |
| <u>/s/ GERARD M. MOONEY</u> Gerard M. Mooney | Director | June 17, 2016 |
| <u>/s/ THOMAS L. THOMAS</u> Thomas L. Thomas | Director | June 17, 2016 |
| <u>/s/ MIKEL WILLIAMS</u> Mikel Williams | Director | June 17, 2016 |

Table of Contents

Iteris, Inc.
Index to Consolidated Financial Statements

| | |
|---|-----------|
| <u>Report of Independent Registered Public Accounting Firm</u> | <u>42</u> |
| <u>Consolidated Balance Sheets as of March 31, 2016 and 2015</u> | <u>44</u> |
| <u>Consolidated Statements of Operations for the fiscal years ended March 31, 2016, 2015 and 2014</u> | <u>45</u> |
| <u>Consolidated Statements of Stockholders' Equity for the fiscal years ended March 31, 2016, 2015 and 2014</u> | <u>46</u> |
| <u>Consolidated Statements of Cash Flows for the fiscal years ended March 31, 2016, 2015 and 2014</u> | <u>47</u> |
| <u>Notes to Consolidated Financial Statements</u> | <u>48</u> |

Table of Contents

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders
Iteris, Inc.

We have audited the accompanying consolidated balance sheet of Iteris, Inc. and subsidiary as of March 31, 2016, and the related consolidated statements of operations, stockholders' equity, and cash flows for the year ended March 31, 2016. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Iteris, Inc. and subsidiary as of March 31, 2016, and the consolidated results of their operations and their cash flows for the year ended March 31, 2016, in conformity with accounting principles generally accepted in the United States of America.

/s/ Deloitte & Touche LLP
Costa Mesa, California
June 17, 2016

Table of Contents

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders
Iteris, Inc.

We have audited the accompanying consolidated balance sheet of Iteris, Inc. and subsidiaries (the Company) as of March 31, 2015, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the two years in the period ended March 31, 2015. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Iteris, Inc. and subsidiaries as of March 31, 2015, and the results of their operations and their cash flows for each of the two years in the period ended March 31, 2015, in conformity with U.S. generally accepted accounting principles.

/s/ RSM US LLP
Irvine, California
June 17, 2015

Table of Contents

Iteris, Inc.

Consolidated Balance Sheets

(In thousands, except par value)

| | March 31, | |
|---|------------------|------------------|
| | 2016 | 2015 |
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 16,029 | \$ 21,961 |
| Trade accounts receivable, net of allowance for doubtful accounts of \$714 and \$314 at March 31, 2016 and March 31, 2015, respectively | 13,241 | 11,206 |
| Costs and estimated earnings in excess of billings on uncompleted contracts | 5,250 | 4,266 |
| Inventories | 3,153 | 3,062 |
| Deferred income taxes | | 2,680 |
| Prepaid expenses and other current assets | 1,505 | 1,338 |
| Total current assets | 39,178 | 44,513 |
| Property and equipment, net | 2,139 | 1,990 |
| Deferred income taxes | | 5,610 |
| Intangible assets, net | 951 | 987 |
| Goodwill | 17,318 | 17,318 |
| Other assets | 434 | 214 |
| Total assets | \$ 60,020 | \$ 70,632 |
| Liabilities and stockholders' equity | | |
| Current liabilities: | | |
| Trade accounts payable | \$ 5,469 | \$ 5,915 |
| Accrued payroll and related expenses | 5,719 | 4,871 |
| Accrued liabilities | 1,445 | 1,320 |
| Billings in excess of costs and estimated earnings on uncompleted contracts | 2,294 | 1,549 |
| Total current liabilities | 14,927 | 13,655 |
| Deferred rent | 750 | 826 |
| Deferred income taxes | 685 | |
| Unrecognized tax benefits | 196 | 183 |
| Total liabilities | 16,558 | 14,664 |
| 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, 2016 and March 31, 2015 Issued and outstanding shares 32,048 at March 31, 2016 and 32,411 at March 31, 2015 | 3,205 | 3,242 |
| Additional paid-in capital | 135,424 | 135,572 |
| Accumulated deficit | (95,167) | (82,846) |
| Total stockholders' equity | 43,462 | 55,968 |

| | | | | |
|--|----|--------|----|--------|
| Total liabilities and stockholders' equity | \$ | 60,020 | \$ | 70,632 |
|--|----|--------|----|--------|

See accompanying notes.

Table of Contents

Iteris, Inc.

Consolidated Statements of Operations

(In thousands, except per share amounts)

| | Year Ended March 31, | | |
|--|----------------------|------------|-----------|
| | 2016 | 2015 | 2014 |
| Total revenues | \$ 77,748 | \$ 72,251 | \$ 68,228 |
| Cost of revenues | 47,079 | 44,069 | 42,254 |
| Gross profit | 30,669 | 28,182 | 25,974 |
| Operating expenses: | | | |
| Selling, general and administrative | 26,846 | 24,425 | 19,269 |
| Research and development | 6,933 | 5,396 | 4,029 |
| Amortization of intangible assets | 360 | 431 | 627 |
| Change in fair value of contingent consideration | | 9 | 25 |
| Total operating expenses | 34,139 | 30,261 | 23,950 |
| Operating (loss) income | (3,470) | (2,079) | 2,024 |
| Non-operating income (expense): | | | |
| Other income (expense), net | 2 | (20) | |
| Interest income, net | 12 | 6 | |
| (Loss) income from continuing operations before income taxes | (3,456) | (2,093) | 2,024 |
| (Provision) benefit for income taxes | (9,079) | 816 | (704) |
| (Loss) income from continuing operations | (12,535) | (1,277) | 1,320 |
| Gain on sale of discontinued operation, net of tax | 214 | 207 | 89 |
| Net (loss) income | \$ (12,321) | \$ (1,070) | \$ 1,409 |
| (Loss) income per share from continuing operations basic and diluted | \$ (0.39) | \$ (0.04) | \$ 0.04 |
| Gain per share from sale of discontinued operation basic and diluted | \$ 0.01 | \$ 0.01 | \$ 0.00 |
| Net (loss) income per share basic and diluted | \$ (0.38) | \$ (0.03) | \$ 0.04 |
| Shares used in basic per share calculations | 32,049 | 32,595 | 32,665 |

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| | | | |
|---|--------|--------|--------|
| Shares used in diluted per share calculations | 32,049 | 32,595 | 32,847 |
|---|--------|--------|--------|

See accompanying notes.

45

Table of Contents

Iteris, Inc.

Consolidated Statements of Stockholders' Equity

(In thousands)

| | Common Stock | | Additional Paid-In Capital | Accumulated Deficit | Total Stockholders' Equity |
|---|--------------|----------|----------------------------------|------------------------|----------------------------------|
| | Shares | Amount | | | |
| Balance at April 1, 2013 | 32,626 | \$ 3,264 | \$ 135,802 | \$ (83,185) | \$ 55,881 |
| Stock option exercises | 299 | 29 | 241 | | 270 |
| Stock-based compensation | | | 300 | | 300 |
| Issuance of shares pursuant to vesting of restricted stock units | 59 | 6 | (37) | | (31) |
| Repurchases of common stock | (196) | (19) | (320) | | (339) |
| Net income | | | | 1,409 | 1,409 |
| Balance at March 31, 2014 | 32,788 | 3,280 | 135,986 | (81,776) | 57,490 |
| Stock option exercises | 24 | 2 | 31 | | 33 |
| Stock-based compensation | | | 398 | | 398 |
| Issuance of shares pursuant to vesting of restricted stock units | 72 | 7 | (27) | | (20) |
| Repurchases of common stock | (473) | (47) | (816) | | (863) |
| Net loss | | | | (1,070) | (1,070) |
| 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 |

See accompanying notes.

Table of Contents

Iteris, Inc.

Consolidated Statements of Cash Flows

(In thousands)

| | Year Ended March 31, | | |
|--|----------------------|------------|-----------|
| | 2016 | 2015 | 2014 |
| Cash flows from operating activities | | | |
| Net (loss) income | \$ (12,321) | \$ (1,070) | \$ 1,409 |
| Adjustments to reconcile net (loss) income to net cash (used in) provided by operating activities: | | | |
| Deferred income taxes | 8,859 | (749) | 710 |
| Depreciation of property and equipment | 649 | 525 | 768 |
| Stock-based compensation | 659 | 398 | 300 |
| Amortization of intangible assets | 526 | 597 | 733 |
| Change in fair value of contingent consideration | | 9 | 25 |
| Gain on sale of discontinued operation, net of tax | (214) | (207) | (89) |
| Loss on disposal of equipment | 58 | 17 | |
| Loss on impairment of intangible asset | | | 108 |
| Changes in operating assets and liabilities, net of effects of discontinued operation: | | | |
| Accounts receivable | (2,035) | 1,143 | (1,403) |
| Net costs and estimated earnings in excess of billings | (239) | 1,705 | (34) |
| Inventories | (91) | (516) | (81) |
| Prepaid expenses and other assets | (407) | 9 | 140 |
| Accounts payable and accrued expenses | 446 | 1,716 | 688 |
| Net cash (used in) provided by operating activities | (4,110) | 3,577 | 3,274 |
| Cash flows from investing activities | | | |
| Purchases of property and equipment | (856) | (986) | (452) |
| Capitalized software development costs | (490) | | (301) |
| Net proceeds from sale of business segment | 368 | 142 | (26) |
| Net cash used in investing activities | (978) | (844) | (779) |
| Cash flows from financing activities | | | |
| Deferred payment for prior business combination | | (336) | (659) |
| Repurchases of common stock | (1,195) | (863) | (339) |
| Proceeds from stock option exercises | 383 | 33 | 270 |
| Tax withholding payments for net share settlements of restricted stock units | (32) | (20) | (31) |
| Net cash used in financing activities | (844) | (1,186) | (759) |
| (Decrease) increase in cash and cash equivalents | (5,932) | 1,547 | 1,736 |
| Cash and cash equivalents at beginning of period | 21,961 | 20,414 | 18,678 |
| Cash and cash equivalents at end of period | \$ 16,029 | \$ 21,961 | \$ 20,414 |
| Supplemental cash flow information: | | | |
| Cash paid during the year for: | | | |
| Interest | \$ 18 | \$ 30 | \$ 33 |
| Income taxes | 177 | 141 | 128 |

Supplemental schedule of non-cash investing and financing activities:

| | | | |
|--|---|-----|---|
| Issuance of common stock for vested restricted stock units | 5 | 7 | 6 |
| Landlord contribution for tenant improvements | | 328 | |

See accompanying notes.

Table of Contents

Iteris, Inc.

Notes to Consolidated Financial Statements

March 31, 2016

1. Description of Business and Summary of Significant Accounting Policies

Description of Business

Iteris, Inc. (referred to collectively with its subsidiary in these consolidated financial statements as "Iteris," the "Company," "we," "our" and "us") is a provider of intelligent information solutions for both the traffic management and global agribusiness markets. We are focused on the development and application of advanced technologies and software-based information systems that reduce traffic congestion, provide measurement, management and predictive traffic and weather analytics, and improve the safety of surface transportation systems infrastructure. We believe our products, services and solutions, in conjunction with sound traffic management, minimize the environmental impact of traffic congestion. By combining our unique intellectual property, products, decades of experience in traffic management, weather forecasting solutions and information technologies, we offer a broad range of Intelligent Transportation Systems ("ITS") solutions to customers throughout the U.S. and internationally. In the agribusiness markets, we have combined our unique intellectual property with enhanced soil, land surface and agronomy modeling techniques to create a set of ClearAg solutions. These solutions provide analytical support to large enterprises in the agriculture market and field-specific advisories to individual producers. We continue to make significant investments to leverage our existing technologies and further expand our software-based information systems to offer solutions to the precision agriculture technology markets. Iteris was incorporated in Delaware in 1987.

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.

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, contract reserves, the valuation of purchased intangible assets and goodwill, the valuation of equity instruments and 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.

Table of Contents

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2016

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

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 Performance Analytics revenues are also derived from long-term contracts with governmental agencies, as well as contracts with commercial companies. 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.

Costs and Estimated Earnings in Excess of Billings on Uncompleted Contracts

Costs and estimated earnings in excess of billings on uncompleted contracts in the accompanying consolidated balance sheets represent unbilled amounts earned and reimbursable under services sales arrangements. At any given period-end, a large portion of the balance in this account represents the accumulation of labor, materials and other costs that have not been billed due to timing, whereby the accumulation of each month's costs and earnings are not administratively billed until the subsequent

Table of Contents

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2016

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

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.

Billings in Excess of Costs and Estimated Earnings on Uncompleted Contracts

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

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

Concentration of Credit Risk

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

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

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.

Cash and Cash Equivalents

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

Table of Contents

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2016

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

Prepaid Expenses and Other Current Assets

Prepaid expenses and other current assets were \$1.5 million as of March 31, 2016 and \$1.3 million as of March 31, 2015 and included approximately \$520,000 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 remain in place through 2016.

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 market. Cost is determined using the first-in, first-out method.

Property and Equipment

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

Goodwill and Long-Lived Assets

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

Table of Contents

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2016

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

of a reporting unit exceeds the reporting unit's fair value, we perform the second step of the goodwill impairment test. The second step of the goodwill impairment test involves comparing the implied fair value of the affected reporting unit's goodwill with the carrying value of that goodwill. The amount by which the carrying value of the goodwill exceeds its implied fair value, if any, is recognized as an impairment loss. We monitor the indicators for goodwill impairment testing between annual tests. As of March 31, 2016, following a quantitative first-step assessment of the Company's reporting units, management determined that no adjustments to the carrying value of its goodwill and intangible assets were required.

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, 2016, 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 our fiscal year ended March 31, 2016 ("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

Table of Contents

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2016

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

the closing market price of our common stock on the grant date. If there are any modifications or cancellations of the underlying unvested stock-based awards, we may be required to accelerate, increase or cancel any remaining unearned stock-based compensation expense.

Research and Development Expenditures

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

Shipping and Handling Costs

Shipping and handling costs are included as cost of 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 \$164,000, \$134,000 and \$168,000 in Fiscal 2016, the fiscal year ended March 31, 2015 ("Fiscal 2015") and fiscal year ended March 31, 2014 ("Fiscal 2014"), 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 Income

Comprehensive income equals net income for all periods presented.

Table of Contents

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2016

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

Recent Accounting Pronouncements

In May 2014, the FASB issued Accounting Standards Update ("ASU") No. 2014-09, *Revenue from Contracts with Customers* ("ASU 2014-09"), which establishes principles for reporting revenue and cash flows arising from an entity's contracts with customers. This new revenue recognition standard will replace most of the recognition guidance within GAAP. This guidance was deferred by ASU No. 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*, issued by the FASB in August 2015, and is now effective for fiscal years beginning on or after December 15, 2017 with early adoption permitted as of the original effective date. In March 2016, the FASB issued ASU No. 2016-08, *Revenue from Contracts with Customers: Principal versus Agent Considerations*, which further clarifies the implementation guidance in ASU 2014-09. In April 2016, the FASB issued ASU No. 2016-10, *Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing*, to expand the guidance on identifying performance obligations and licensing within ASU 2014-09. These standards are effective for fiscal years beginning after December 15, 2017, including interim periods within that reporting period. We are currently evaluating the impact that these standards will have on our consolidated financial statements.

In July 2015, the FASB issued ASU No. 2015-11, *Simplifying the Measurement of Inventory* ("ASU 2015-11") to simplify the guidance on the measurement of inventory. Under the new standard, an entity should measure inventory at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. The standard is effective for interim and annual periods beginning after December 15, 2016. We do not anticipate a significant impact on our consolidated financial statements upon adoption of ASU 2015-11.

In November 2015, the FASB issued ASU No. 2015-17, *Balance Sheet Classification of Deferred Taxes* ("ASU 2015-17") to simplify the presentation of deferred taxes by requiring deferred tax assets and liabilities be classified as noncurrent on the balance sheet. ASU 2015-17 is effective for public companies for annual reporting periods beginning after December 15, 2016, and interim periods within those fiscal years. The standard may be adopted prospectively or retrospectively and early adoption is permitted. The Company early adopted ASU 2015-17, prospectively, in our fourth quarter of Fiscal 2016, which did not have a material impact on our consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-09, *Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting* ("ASU 2016-09"), which is intended to simplify several aspects of accounting for share-based compensation arrangements, including the income tax impact, classification on the statement of cash flows and forfeitures. The guidance will be effective for the fiscal year beginning after December 15, 2016, including interim periods within that year. We are currently evaluating the impact of ASU 2016-09 on our consolidated financial statements.

Table of Contents**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2016****2. Supplementary Financial Information****Inventories**

The following table presents details regarding our inventories:

| | March 31, | |
|------------------------|-----------------------|-------------|
| | 2016 | 2015 |
| | (In thousands) | |
| Materials and supplies | \$ 1,754 | \$ 1,566 |
| Work in process | 217 | 216 |
| Finished goods | 1,182 | 1,280 |
| | \$ 3,153 | \$ 3,062 |

Property and Equipment, net

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

| | March 31, | |
|--------------------------|-----------------------|-------------|
| | 2016 | 2015 |
| | (In thousands) | |
| Equipment | \$ 6,530 | \$ 6,473 |
| Leasehold improvements | 2,463 | 2,463 |
| Accumulated depreciation | (6,854) | (6,946) |
| | \$ 2,139 | \$ 1,990 |

Depreciation expense was approximately \$649,000, \$525,000 and \$768,000 in Fiscal 2016, Fiscal 2015 and Fiscal 2014, respectively.

Intangible Assets

The following table presents details regarding our intangible assets:

| | March 31, | | | |
|--|-----------------------|---------------------|-----------------|---------------------|
| | 2016 | | 2015 | |
| | Gross | Accumulated | Gross | Accumulated |
| | Carrying | Amortization | Carrying | Amortization |
| | Amount | Amount | Amount | Amount |
| | (In thousands) | | | |
| Technology | \$ 1,856 | \$ (1,708) | \$ 1,856 | \$ (1,565) |
| Customer contracts / relationships | 750 | (622) | 750 | (497) |
| Trade names and non-compete agreements | 1,110 | (1,008) | 1,110 | (916) |

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| | | | | |
|--|----------|------------|----------|------------|
| Capitalized software development costs | 988 | (415) | 498 | (249) |
| Total | \$ 4,704 | \$ (3,753) | \$ 4,214 | \$ (3,227) |

Amortization expense for intangible assets subject to amortization was approximately \$526,000, \$597,000 and \$733,000 for Fiscal 2016, Fiscal 2015 and Fiscal 2014, respectively. Approximately

Table of Contents**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2016****2. Supplementary Financial Information (Continued)**

\$166,000, \$166,000 and \$106,000 of the intangible asset amortization was recorded to cost of revenues, and approximately \$360,000, \$431,000 and \$627,000 was recorded to amortization expense for Fiscal 2016, Fiscal 2015 and Fiscal 2014, respectively, in the consolidated statement of operations.

Capitalized software development costs for the iPeMS platform began to be amortized in October 2013, resulting in approximately \$166,000 recorded to cost of revenues in the accompanying consolidated statements of operations for the fiscal years ended March 31, 2016 and 2015. We do not have any intangible assets with indefinite useful lives. As of March 31, 2016, the future estimated amortization expense of approximately \$951,000 is entirely associated with our Performance Analytics business segment, as follows:

Year Ending March 31,**(In thousands)**

| | | |
|------|----|-----|
| 2017 | \$ | 528 |
| 2018 | | 251 |
| 2019 | | 172 |
| | \$ | 951 |

Refer to Note 4 for additional information regarding intangible assets acquired during the last three fiscal years.

Goodwill

The following table presents the activity related to the carrying value of our goodwill by reportable segment for Fiscal 2014, Fiscal 2015 and Fiscal 2016:

| | Roadway Sensors | Transportation Systems | Performance Analytics | Total |
|-------------------------------|--------------------|---------------------------|--------------------------|-----------|
| | (In thousands) | | | |
| Balance March 31, 2014 | | | | |
| Goodwill | \$ 8,214 | \$ 14,906 | \$ 2,168 | \$ 25,288 |
| Accumulated impairment losses | | (7,970) | | (7,970) |
| | \$ 8,214 | \$ 6,936 | \$ 2,168 | \$ 17,318 |
| Balance March 31, 2015 | | | | |
| Goodwill | \$ 8,214 | \$ 14,906 | \$ 2,168 | \$ 25,288 |
| Accumulated impairment losses | | (7,970) | | (7,970) |
| | 8,214 | 6,936 | 2,168 | 17,318 |
| Balance March 31, 2016 | | | | |
| Goodwill | \$ 8,214 | \$ 14,906 | \$ 2,168 | \$ 25,288 |
| Accumulated impairment losses | | (7,970) | | (7,970) |
| | \$ 8,214 | \$ 6,936 | \$ 2,168 | \$ 17,318 |

Table of Contents**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2016****2. Supplementary Financial Information (Continued)****Warranty Reserve Activity**

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

| | Year Ended March 31, | | |
|-------------------------------------|----------------------|--------|--------|
| | 2016 | 2015 | 2014 |
| | (In thousands) | | |
| Balance at beginning of fiscal year | \$ 181 | \$ 184 | \$ 169 |
| Additions charged to cost of sales | 236 | 134 | 179 |
| Warranty claims | (224) | (137) | (164) |
| Balance at end of fiscal year | \$ 193 | \$ 181 | \$ 184 |

Earnings Per Share

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

| | Year Ended March 31, | | |
|--|--|------------|----------|
| | 2016 | 2015 | 2014 |
| | (In thousands, except per share amounts) | | |
| Numerator: | | | |
| (Loss) Income from continuing operations | \$ (12,535) | \$ (1,277) | \$ 1,320 |
| Denominator: | | | |
| Weighted average common shares used in basic computation | 32,049 | 32,595 | 32,665 |
| Dilutive stock options | | | 111 |
| Dilutive restricted stock units | | | 70 |
| Dilutive warrants | | | 1 |
| Weighted average common shares used in diluted computation | 32,049 | 32,595 | 32,847 |
| (Loss) income from continuing operations per share: | | | |
| Basic | \$ (0.39) | \$ (0.04) | \$ 0.04 |
| Diluted | \$ (0.39) | \$ (0.04) | \$ 0.04 |

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

| | Year Ended March 31, | | |
|------------------------|-----------------------------|-------------|-------------|
| | 2016 | 2015 | 2014 |
| | (In thousands) | | |
| Stock options | 3,220 | 2,252 | 854 |
| Restricted stock units | 186 | 198 | |

57

Table of Contents

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2016

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, 2016, we received approximately \$1.6 million in connection with royalty-related earn-outs provisions for a total of \$15.3 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, 2016, 2015 and 2014, we recorded a gain on sale of discontinued operation of approximately \$214,000, \$207,000 and \$89,000, respectively, net of tax, related to the earn-out provisions of the asset purchase agreement.

4. Acquisitions

Berkeley Transportation Systems, Inc.

In the fiscal year ended March 31, 2012 ("Fiscal 2012"), we acquired all of the outstanding capital stock of Berkeley Transportation Systems, Inc. ("BTS"). BTS was a privately-held company based in Berkeley, California, which specialized in transportation performance measurement. BTS' Performance Measurement System leverages its real-time data collection, diagnostic, fusion and warehousing platform to aggregate and compute performance measures. This information is used to analyze how a transportation system is performing based on pre-determined measures of effectiveness such as stops, delays and travel time. Our primary reasons for the acquisition were to add key technologies to complement our Performance Analytics solutions and strengthen our performance measurement and management initiative as a whole.

Our consolidated financial statements for Fiscal 2016, Fiscal 2015 and Fiscal 2014 include the results of operations of BTS. On or shortly after the acquisition date, we paid a total of approximately \$840,000 in cash to the shareholders of BTS. On December 17, 2012, the Company entered into an amendment to the BTS stock purchase agreement, which modified certain earn out provisions, and as a result, the Company paid \$700,000 in cash to the former BTS shareholders for achievement of those modified earn-out provisions in our fourth quarter of the fiscal year ended March 31, 2013 ("Fiscal 2013"). The amendment did not have a material impact on previous estimated amounts accrued in connection with the earn-out provisions. This payment completed the Company's obligation under the earn-out provisions of the agreement. During the third quarter of Fiscal 2014, the Company paid \$250,000 pursuant to certain holdback provisions. Additionally, the Company paid the BTS shareholders approximately \$336,000 in November 2014 pursuant to certain deferred payment provisions. These payments completed all of the Company's obligations under the purchase agreement.

Table of Contents

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2016

4. Acquisitions (Continued)

Meridian Environmental Technology, Inc.

In Fiscal 2012, we acquired all of the capital stock of Meridian Environmental Technology, Inc. ("MET"), a privately-held company based in Grand Forks, North Dakota. MET specialized in 511/Advanced Traveler Information Systems, as well as the ClearPath Weather management tools that allow users to create solutions to meet roadway maintenance decision needs.

On or shortly after the acquisition date, we paid approximately \$1.6 million in cash, exclusive of \$369,000 of cash acquired. We also agreed to pay up to \$1.0 million on each of the first two anniversaries of the closing of the acquisition upon the satisfaction of certain conditions, as well as up to an additional \$2.0 million under a 24-month earn-out provision.

In January 2012, we made a cash payment of approximately \$668,000 of the first deferred payment to the shareholders of MET and held back \$250,000 in accordance with certain provisions of the purchase agreement. In June 2012, we determined the contingencies related to the release of the \$250,000 holdback were not met. As a result, no portion of the \$250,000 holdback was reversed into operating income during the second quarter of Fiscal 2013. Additionally, no amounts were earned by the former MET shareholders related to the first and second year earn-out provisions which ended on December 31, 2011 and 2012, respectively. The second deferred payment of \$1.0 million was due in the fourth quarter of Fiscal 2013. As a result of certain holdback provisions and other deductions, the Company paid approximately \$409,000 to the former MET shareholders in the second quarter of Fiscal 2014. This payment completed the Company's obligations under the deferred payment provisions of the purchase agreement. The total purchase price paid for this business acquisition was approximately \$2.7 million.

5. Impairment of Goodwill

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

In Fiscal 2012, we early adopted the provisions issued by the FASB that are intended to simplify goodwill impairment testing. The updated guidance permits us to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If we conclude that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, we conduct a two-step goodwill impairment test. We determined it was appropriate to perform a quantitative first-step assessment in Fiscal 2014, Fiscal 2015 and Fiscal 2016 to estimate the fair value of our reporting units using both the income approach and the market approach. Based on our assessments, we determined that no impairment was indicated as of March 31, 2016 as the estimated fair value of each reporting unit exceeded its respective carrying value.

6. Fair Value Measurements

We measure fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Fair value measurements are based on a three-tier hierarchy that prioritizes the inputs used to measure fair value. These tiers include: Level 1, defined as observable inputs such as quoted prices in active markets for

Table of Contents

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2016

6. Fair Value Measurements (Continued)

identical assets and liabilities; Level 2, defined as observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities or prices quoted in inactive markets; and Level 3, defined as unobservable inputs that are significant to the fair value of the asset or liability, and for which little or no market data exists, therefore requiring management to utilize its own assumptions to provide its best estimate of what market participants would use in valuing the asset or liability.

The liability for the estimated fair value of the contingent consideration in connection with our acquisitions of MET and BTS was initially determined using Level 3 inputs based on a probabilistic calculation whereby we assigned estimated probabilities to achieving the earn-out targets and then discounted the total contingent consideration to net present value. The MET and BTS earn-out targets were completed during Fiscal 2013 and the deferred acquisition payments were completed during Fiscal 2015.

Other than the above, we did not have any material financial assets or liabilities measured at fair value on a recurring basis using Level 3 inputs as of March 31, 2016, 2015 or 2014. 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. No non-financial assets were measured at fair value during the fiscal years ended March 31, 2016 and 2015.

7. Credit Facility

We currently have a \$12.0 million revolving line of credit with California Bank & Trust ("CB&T"), which expires on October 1, 2016. Interest on borrowed amounts under the revolving line of credit is payable monthly at a rate equal to the current stated prime rate (3.50% at March 31, 2016). We are obligated to pay an unused line fee of 0.15% per annum applied to the average unused portion of the revolving line of credit during the preceding month. The revolving line of credit does not contain any early termination fees and is secured by substantially all of our assets. As of March 31, 2016 and 2015, no amounts were outstanding under the credit facility with CB&T. Availability under this line of credit may be reduced or otherwise limited as a result of our obligations to comply with certain financial and other covenants. As of March 31, 2016 and 2015, we were in compliance with all such financial and other covenants.

Table of Contents

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2016

8. Income Taxes

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

| | Year Ended March 31, | | |
|--|----------------------|----------|--------|
| | 2016 | 2015 | 2014 |
| | (In thousands) | | |
| Current income tax provision: | | | |
| Federal | \$ 170 | \$ 3 | \$ 21 |
| State | 50 | 49 | 20 |
| Deferred income tax provision (benefit): | | | |
| Federal | 8,289 | (655) | 330 |
| State | 570 | (213) | 333 |
| Net income tax provision (benefit) | \$ 9,079 | \$ (816) | \$ 704 |

The components of income tax expense (benefit) consist of the following:

| | Year Ended March 31, | | |
|---|----------------------|----------|--------|
| | 2016 | 2015 | 2014 |
| | (In thousands) | | |
| Current income tax expense | \$ 220 | \$ 52 | \$ 41 |
| Deferred income tax expense (benefit) | 1,232 | (781) | 663 |
| Benefit of operating loss carryforwards | (1,316) | (87) | |
| Recording of valuation allowance | 8,943 | | |
| Net income tax provision (benefit) | \$ 9,079 | \$ (816) | \$ 704 |

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

| | Year Ended March 31, | | |
|--|----------------------|----------|--------|
| | 2016 | 2015 | 2014 |
| | (In thousands) | | |
| (Benefit) provision for income taxes at statutory rates | \$ (1,175) | \$ (712) | \$ 688 |
| State income taxes net of federal benefit | (184) | (108) | 48 |
| Tax credits | (258) | (148) | (290) |
| Change in fair value of contingent acquisition consideration | | 3 | 8 |
| Compensation charges | 91 | 88 | 22 |
| Change in valuation allowance | 10,557 | | 185 |
| Other | 48 | 61 | 43 |
| Provision (benefit) for income taxes | \$ 9,079 | \$ (816) | \$ 704 |

Table of Contents**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2016****8. Income Taxes (Continued)**

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

| | March 31, | |
|--|-----------------------|-----------------|
| | 2016 | 2015 |
| | (In thousands) | |
| Deferred tax assets: | | |
| Net operating losses | \$ 2,468 | \$ 5,420 |
| Capitalized R&D | 3,557 | |
| Credit carry forwards | 2,130 | 1,610 |
| Deferred compensation and payroll | 1,306 | 1,163 |
| Bad debt allowance and other reserves | 665 | 504 |
| Deferred rent | 335 | 364 |
| Other, net | 242 | 271 |
| Total deferred tax assets | 10,703 | 9,332 |
| Valuation allowance | (10,561) | |
| Total deferred tax assets, net of valuation allowance | 142 | 9,332 |
| Deferred tax liabilities: | | |
| Property and equipment | (71) | (137) |
| Acquired intangibles | (71) | (252) |
| Goodwill | (685) | (653) |
| Total deferred tax liabilities | (827) | (1,042) |
| Net deferred tax (liabilities) assets | \$ (685) | \$ 8,290 |

At March 31, 2016, we had \$1.0 million in federal alternative minimum tax credit carryforwards that can be carried forward indefinitely, and \$797,000 in federal research credits that begin to expire in 2031. We also had \$480,000 in state tax credits that begin to expire in 2023. We had \$9.7 million of federal net operating loss carryforwards at March 31, 2016 that begin to expire in 2022. We also had \$794,000 of state net operating loss carryforwards at March 31, 2016 that begin to expire in 2031.

Our deferred tax assets at March 31, 2016 do not include approximately \$874,000 of excess tax benefits from employee stock option exercises that are a component of our net operating loss carryforwards. If and when such excess tax benefits are realized, stockholders' equity will be increased.

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. 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 of December 31, 2015, the Company had generated a cumulative pre-tax loss over the trailing three years. As such, we considered it appropriate to record a valuation allowance of approximately \$10.1 million in our third quarter of Fiscal 2016 against our deferred tax assets. We will continuously reassess the appropriateness of maintaining a valuation allowance.

Table of Contents**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2016****8. Income Taxes (Continued)****Unrecognized Tax Benefits**

As of March 31, 2016 and 2015, our gross unrecognized tax benefits were \$394,000 and \$319,000, respectively, of which \$251,000 and \$184,000, respectively, are netted against certain noncurrent deferred tax assets. The amounts that would affect our effective tax rate if recognized are \$328,000 and \$257,000, respectively.

We recognize interest income and/or interest expense, net, and penalties related to income tax matters in income tax expense. As of March 31, 2016 and 2015, we had accrued cumulatively \$52,000 and \$47,000, respectively, for the payment of potential interest and penalties. The total amount of interest expense and interest income, net, and penalties recognized in the consolidated statements of operations for the fiscal years ended March 31, 2016 and 2015 was \$5,000 and \$(6,000), respectively.

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

| | Year Ended March 31, | | |
|---|-----------------------------|-------------|-------------|
| | 2016 | 2015 | 2014 |
| | (In thousands) | | |
| Gross unrecognized tax benefits at beginning of year | \$ 319 | \$ 281 | \$ 218 |
| Increases for tax positions taken in prior years | 22 | 14 | 106 |
| Decreases for tax positions taken in prior years | | (3) | (53) |
| Increases for tax positions taken in the current year | 68 | 46 | 41 |
| Lapse in statute of limitations | (15) | (19) | (31) |
| Gross unrecognized tax benefits at March 31 | \$ 394 | \$ 319 | \$ 281 |

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, 2013 or later, and state and local income tax examination for fiscal tax years ended March 31, 2012 or later. However, if net operating loss ("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. Our Fiscal 2015 federal tax return is currently under examination by the U.S. Internal Revenue Service.

9. 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 has in the past been, and may in the future be from time to time, 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.

Table of Contents**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2016****9. Commitments and Contingencies (Continued)**

In November 2015, the City of Detroit, Michigan (the "City") filed a lawsuit against the Company in the United States Bankruptcy Court for the Eastern District of Michigan alleging that the Company received a payment in the amount of approximately \$124,000 from the City during the 90-day period prior to the City's bankruptcy filing in 2013. In March 2016, the Company entered into such agreement with the City for an immaterial amount to fully resolve the matter.

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.

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, 2016 were as follows:

Year Ending March 31,**(In thousands)**

| | |
|------------|-----------------|
| 2017 | \$ 1,861 |
| 2018 | 1,708 |
| 2019 | 1,454 |
| 2020 | 1,213 |
| 2021 | 1,161 |
| Thereafter | 1,153 |
| | \$ 8,550 |

Rent expense totaled approximately \$1.7 million, \$1.7 million and \$1.9 million for Fiscal 2016, Fiscal 2015 and Fiscal 2014, respectively.

Related Party Transaction

We previously subleased office space to Maxxess Systems, Inc. ("Maxxess"), one of our former subsidiaries that we sold in September 2003. Maxxess is currently owned by an investor group that includes one current Iteris director and one former Iteris director. The sublease terminated in

Table of Contents

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2016

9. Commitments and Contingencies (Continued)

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.

The amended and restated note bears interest at a rate of 6% per annum, compounded annually, with accrued interest to be paid quarterly on the first business day of each calendar quarter. Payments under the amended and restated note may only be paid in cash and all amounts outstanding will become due and payable on the earliest of (i) August 10, 2016, (ii) a change of control in Maxxess, or (iii) a financing by Maxxess resulting in gross proceeds of at least \$10 million. As of March 31, 2016, approximately \$219,000 of the original principal balance was outstanding and payable to Iteris. We have previously fully reserved for amounts owed to us by Maxxess and the outstanding principal balance remains fully reserved.

On June 30, 2015, the Company entered into an agreement with Maxxess to provide professional services for the Company's Performance Analytics segment, in support of its ClearAg software development initiative. The professional services commenced in July 2015 and continued through December 31, 2015. On February 19, 2016, the Company entered into an amendment of the agreement to extend the duration for an additional six months, to continue through August 2016. The total effort under this agreement is limited to 300 hours, billed on a time and materials basis, not to exceed \$102,600. During the fiscal year ended March 31, 2016, approximately \$54,000 of professional services were rendered to the Company.

Inventory Purchase Commitments

At March 31, 2016, we had firm commitments to purchase approximately \$4.4 million of inventory, operating assets and other supplies, which are expected to occur primarily during the first and second quarters of the fiscal year ended March 31, 2017.

10. Stockholders' Equity

Preferred Stock

Our certificate of incorporation provides for the issuance of up to 2,000,000 shares of preferred stock. Our Board of Directors is authorized to issue from time to time such authorized but unissued shares of preferred stock in one or more series and to fix or alter the designations, preferences, rights and any qualifications, limitations or restrictions of the shares of each such series, including the dividend, conversion, voting, redemption and liquidation rights. As of March 31, 2016 and 2015, 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

Table of Contents**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2016****10. Stockholders' Equity (Continued)**

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, 2016:

| | Number of Shares (In thousands) |
|--|--|
| Stock options outstanding | 3,309 |
| Restricted stock units outstanding | 173 |
| Authorized for future issuance under stock incentive plans | 902 |
| | 4,384 |

11. Employee Benefit Plans**Stock Incentive Plans**

In September 2007, our stockholders approved the 2007 Omnibus Incentive Plan (the "2007 Plan"), which provides that options to purchase shares of our unissued common stock may be granted to our employees, officers, consultants and directors at exercise prices which are equal to or greater than the market value of our common stock on the date of grant. Options expire no more than ten years after the date of grant and generally vest at the rate of 25% on each of the first four anniversaries of the grant date. The 2007 Plan also allows for the issuance of stock appreciation rights, restricted stock, restricted stock units ("RSUs") and other stock-based awards based on the value of our common stock. New shares are issued to satisfy stock option exercises and share issuances 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 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. At March 31, 2016, there were approximately 902,000 shares of common stock available for grant under this plan. As of March 31, 2016, options to purchase approximately 3,287,000 shares of common stock, as well as 173,000 RSUs, were outstanding under the 2007 Plan.

Our 1997 Stock Incentive Plan (the "1997 Plan") terminated in September 2007; however, all stock options outstanding under the 1997 Plan remain outstanding pursuant to the terms of such stock options. As of March 31, 2016, options to purchase approximately 23,000 shares of our common stock were outstanding under the 1997 Plan. No further options or other stock-based awards may be granted under the 1997 Plan.

Table of Contents**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2016****11. Employee Benefit Plans (Continued)**

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

Stock Options

A summary of activity in the Plans with respect to our stock options for Fiscal 2016 is as follows:

| | Options (In thousands) | Weighted Average Exercise Price Per Share | Weighted Average Remaining Contractual Life (Years) | Aggregate Intrinsic Value (In thousands) |
|---|---------------------------|---|--|---|
| Options outstanding at March 31, 2015 | 2,199 | \$ 1.83 | | |
| Granted | 1,808 | 2.35 | | |
| Exercised | (243) | 1.58 | | |
| Forfeited | (79) | 1.82 | | |
| Expired | (376) | 2.36 | | |
| Options outstanding at March 31, 2016 | 3,309 | \$ 2.07 | 8.1 | \$ 1,222 |
| Options exercisable at March 31, 2016 | 1,057 | \$ 1.70 | 5.9 | \$ 788 |
| Vested and expected to vest at March 31, 2016 | 2,948 | \$ 2.05 | 8 | \$ 1,167 |
| Options exercisable at March 31, 2016 pursuant to a change-in-control | 3,309 | \$ 2.07 | 8.1 | \$ 1,222 |

Restricted Stock Units

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

Table of Contents

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2016

11. Employee Benefit Plans (Continued)

A summary of activity with respect to our RSUs for Fiscal 2016 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, 2015 | 194 | \$ 1.74 | | |
| Granted | 63 | 2.37 | | |
| Vested | (66) | 1.61 | | |
| Forfeited | (18) | 1.84 | | |
| RSUs outstanding at March 31, 2016 | 173 | \$ 2.00 | 2.5 | \$ 273 |
| Expected to vest at March 31, 2016 | 150 | \$ 1.99 | 2.4 | \$ 245 |
| Common stock issuable (for RSUs) at March 31, 2016 upon a change-in-control | 173 | \$ 2.00 | 2.5 | \$ 273 |

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, | | |
|---|----------------------|--------|--------|
| | 2016 | 2015 | 2014 |
| | (In thousands) | | |
| Cost of revenues | \$ 42 | \$ 21 | \$ 30 |
| Selling, general and administrative expense | 567 | 315 | 246 |
| Research and development expense | 50 | 62 | 24 |
| Total stock-based compensation | \$ 659 | \$ 398 | \$ 300 |

At March 31, 2016, there was approximately \$2.1 million and \$265,000 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 3.1 years for stock options and 2.5 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.

Table of Contents**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2016****11. 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, | | |
|-------------------------------------|-------------------------|------|------|
| | 2016 | 2015 | 2014 |
| Expected life years | 7.2 | 7.7 | 7.0 |
| Risk-free interest rate | 1.9% | 2.0% | 2.0% |
| Expected volatility of common stock | 47% | 50% | 51% |
| Dividend yield | % | % | % |

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

| | Year Ended March 31, | | |
|---|---|---------|---------|
| | 2016 | 2015 | 2014 |
| | (In thousands, except per share amounts) | | |
| Weighted average grant date fair value per share of options granted | \$ 1.19 | \$ 1.01 | \$ 0.99 |
| Intrinsic value of options exercised | \$ 135 | \$ 9 | \$ 281 |

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, 2016, 2015 and 2014.

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 \$716,000, \$495,000 and \$504,000 for the fiscal years ended March 31, 2016, 2015 and 2014, respectively.

12. 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 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

Table of Contents

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2016

12. Stock Repurchase Program (Continued)

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 year ended March 31, 2016, 2015 and 2014, we repurchased approximately 656,000, 473,000 and 196,000 shares of our common stock, respectively. From inception of the program in August 2011 through March 31, 2016, 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, 2016, all repurchased shares have been retired and resumed their status as authorized and unissued shares of our common stock. As of March 31, 2016, approximately \$1.7 million remains available for the repurchase of our common stock under our current program.

13. Business Segments, Significant Customer and Geographic Information

Business Segments

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

The Roadway Sensors segment provides hardware and software products to multiple segments of the ITS market. These various vehicle detection and information systems are used for traffic intersection control, incident detection and roadway traffic data collection applications. These include, among other products, our Vantage, VantageNext, VersiCam, Vantage Vector, SmartCycle, SmartSpan, Pegasus, Velocity, P10, P100 and Abacus products.

The Transportation Systems segment includes transportation engineering and consulting services, and the development of transportation management and traveler information systems for the ITS industry.

The Performance Analytics segment includes our performance measurement and information management solution iPeMS, a specialized transportation performance measurement and traffic analytics solutions, as well as ClearPath Weather, our road-maintenance applications, and ClearAg, our precision agriculture solutions. iPeMS provides big data and software analytics solutions that help determine current and future traffic patterns, permitting the effective performance analysis and management of traffic infrastructure resources. ClearPath Weather provides winter road maintenance recommendations for state agencies, municipalities and for commercial companies. Our ClearAg platform provides access to a comprehensive database of weather, soil and agronomic information essential to making informed agricultural decisions.

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. The

Table of Contents

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2016

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

Company's Chief Executive Officer, who is the chief operating decision maker, or CODM, reviews financial information at the operating segment level. The Company's CODM does not review assets by segment in his resource allocation and therefore assets by segment are not disclosed below.

Selected financial information for our reportable segments for the fiscal years ended March 31, 2016, 2015 and 2014 is as follows:

| | Roadway Sensors | Transportation Systems | Performance Analytics | Total |
|----------------------------------|--------------------|---------------------------|--------------------------|-----------|
| (In thousands) | | | | |
| Year Ended March 31, 2016 | | | | |
| Revenues | \$ 40,259 | \$ 32,330 | \$ 5,159 | \$ 77,748 |
| Depreciation | 152 | 136 | 161 | 449 |
| Segment income (loss) | 7,718 | 4,031 | (7,380) | 4,369 |
| Year Ended March 31, 2015 | | | | |
| Revenues | \$ 36,370 | \$ 30,294 | \$ 5,587 | \$ 72,251 |
| Depreciation | 119 | 115 | 142 | 376 |
| Segment income (loss) | 6,302 | 4,239 | (4,449) | 6,092 |
| Year Ended March 31, 2014 | | | | |
| Revenues | \$ 31,769 | \$ 30,524 | \$ 5,935 | \$ 68,228 |
| Depreciation | 208 | 161 | 118 | 487 |
| Segment income (loss) | 5,791 | 3,363 | (1,575) | 7,579 |

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

| | Year Ended March 31, | | |
|---|----------------------|-------------------|-----------------|
| | 2016 | 2015 | 2014 |
| (In thousands) | | | |
| Segment income: | | | |
| Total income from reportable segments | \$ 4,369 | \$ 6,092 | \$ 7,579 |
| Unallocated amounts: | | | |
| Corporate and other expenses | (7,479) | (7,731) | (4,903) |
| Amortization of intangible assets | (360) | (431) | (627) |
| Change in fair value of contingent acquisition consideration | | (9) | (25) |
| Other (expense) income, net | 2 | (20) | |
| Interest income, net | 12 | 6 | |
| (Loss) income from continuing operations before income taxes | \$ (3,456) | \$ (2,093) | \$ 2,024 |

Significant Customer and Geographic Information

We currently have, and historically have had, a diverse customer base. For Fiscal 2016, no individual customer represented approximately 10% of our total revenues. For Fiscal 2015, one individual customer represented approximately 10% of our total revenues and no other individual

Table of Contents**Iteris, Inc.****Notes to Consolidated Financial Statements (Continued)****March 31, 2016****13. Business Segments, Significant Customer and Geographic Information (Continued)**

customer represented greater than 10% of our total revenues. For Fiscal 2014, one individual customer represented approximately 11% of our total revenues and no other individual customer represented greater than 10% of our total revenues.

No individual customer or government agency had a receivable balance at March 31, 2016 or 2015 greater than 10% of our total trade accounts receivable balances as of March 31, 2016 and 2015, 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, | | |
|-------------|-------------------------|------|------|
| | 2016 | 2015 | 2014 |
| Middle East | 1% | 3% | 4% |
| Other | | | 1 |
| | 1% | 3% | 5% |

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 | Basic Net Loss per Share | Diluted Net Loss per Share |
|--|-----------|--------------|-------------|--------------------------------|----------------------------------|
| (In thousands, except per share amounts) | | | | | |
| June 30, 2015 | \$ 18,365 | \$ 7,637 | \$ (192) | \$ (0.01) | \$ (0.01) |
| September 30, 2015 | 20,573 | 7,883 | (395) | (0.01) | (0.01) |
| December 31, 2015 | 19,014 | 7,211 | (10,442) | (0.33) | (0.33) |
| March 31, 2016 | 19,796 | 7,938 | (1,292) | (0.04) | (0.04) |
| | \$ 77,748 | \$ 30,669 | \$ (12,321) | \$ (0.39)* | \$ (0.39)* |
| June 30, 2014 | \$ 18,116 | \$ 6,807 | \$ (19) | \$ | \$ |
| September 30, 2014 | 18,550 | 7,299 | (187) | (0.01) | (0.01) |
| December 31, 2014 | 17,540 | 6,862 | (98) | | |
| March 31, 2015 | 18,045 | 7,214 | (766) | (0.02) | (0.02) |
| | \$ 72,251 | \$ 28,182 | \$ (1,070) | \$ (0.03)* | \$ (0.03)* |

*

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

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Table of Contents

Exhibit Index

| Exhibit Number | Description | Reference |
|-------------------|---|--|
| 2.2+ | Asset Purchase Agreement by and between Iteris, Inc. and Bendix Commercial Vehicle Systems LLC, dated as of July 25, 2011 | <i>Exhibit 2.1 to the registrant's Current Report on Form 8-K/A as filed with the SEC on November 1, 2011</i> |
| 3.1 | Restated Certificate of Incorporation of the registrant | <i>Exhibit 3.1 to the registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2009 as filed with the SEC on October 30, 2009</i> |
| 3.2 | Certificate of Designations of Series A Junior Participating Preferred Stock | <i>Exhibit 3.2 to the registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2009 as filed with the SEC on October 30, 2009</i> |
| 3.3 | Bylaws of the registrant, as amended | <i>Exhibit 4.2 to the registrant's Registration Statement on Form S-1 (Reg. No. 033-67932) as filed with the SEC on July 6, 1993</i> |
| 3.4 | Certificates of Amendment to Bylaws of the registrant dated April 24, 1998 and August 10, 2001 | <i>Exhibit 3.4 to the registrant's Annual Report on Form 10-K/A for the year ended March 31, 2003 as filed with the SEC on July 29, 2003</i> |
| 3.5 | Certificate of Amendment to Bylaws of registrant dated September 9, 2004 | <i>Exhibit 3.1 to the registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 2004 as filed with the SEC on November 15, 2004</i> |
| 3.6 | Certificate of Amendment to Bylaws of registrant effective September 16, 2005 | <i>Exhibit 3.5 to the registrant's Annual Report on Form 10-K for the year ended March 31, 2007</i> |
| 3.7 | Certificate of Amendment to Bylaws of registrant effective December 7, 2007 | <i>Exhibit 3.1 to the registrant's Current Report on Form 8-K as filed with the SEC on December 13, 2007</i> |
| 3.8 | Certificate of Amendment to Bylaws of registrant, effective August 20, 2009 | <i>Exhibit 3.3 to the registrant's Current Report on Form 8-K as filed with the SEC on August 21, 2009</i> |
| 4.1 | Specimen of common stock certificate | <i>Exhibit 4.1 to registrant's Registration Statement on Form 8-A as filed with the SEC on December 8, 2004</i> |
| 4.2 | Rights Agreement dated August 20, 2009 between the registrant and Computershare Trust Company, N.A., which includes the form of Certificate of Designations for the Series A Junior Participating Preferred Stock, the form of Right Certificate, and Summary of Rights to Purchase Preferred Stock as exhibits thereto | <i>Exhibit 4.1 to the registrant's Current Report on Form 8-K as filed with the SEC on August 21, 2009</i> |

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Table of Contents

| Exhibit Number | Description | Reference |
|-------------------|--|--|
| 4.3 | Amendment No. 1 to Rights Agreement, entered into as of August 8, 2012 by and between Iteris, Inc. and Computershare Trust Company, N.A. | <i>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</i> |
| 10.1 | Form of Indemnity Agreement entered into by the registrant and certain of its officers and directors | <i>Exhibit 19.4 to the registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 1988</i> |
| 10.2 | Form of Indemnification Agreement entered into by the registrant and certain of its officers and directors | <i>Exhibit 10.5 to the registrant's Annual Report on Form 10-K for the year ended March 31, 2004 as filed with the SEC on June 29, 2004</i> |
| 10.3* | 1997 Stock Incentive Plan (the "1997 Plan") as amended on May 3, 2003, as further amended on December 15, 2004 | <i>Exhibit 10.32 to the registrant's Annual Report on Form 10-K for the year ended March 31, 2005 as filed with the SEC on July 14, 2005</i> |
| 10.4* | Form of Notice of Grant of Stock Option for 1997 Plan | <i>Exhibit 99.2 to the registrant's Registration Statement on Form S-8 (File No. 333-30396) as filed with the SEC on February 14, 2000</i> |
| 10.5* | Form of Stock Option Agreement for the 1997 Plan | <i>Exhibit 99.3 to the registrant's Registration Statement on Form S-8 (File No. 333-30396) as filed with the SEC on February 14, 2000</i> |
| 10.6* | Form of Addendum to Stock Option Agreement for 1997 Plan Involuntary Termination Following Corporate Transaction or Change in Control | <i>Exhibit 99.4 to the registrant's Registration Statement on Form S-8 (File No. 333-30396) as filed with the SEC on February 14, 2000</i> |
| 10.7* | Form of Stock Issuance Agreement for 1997 Plan | <i>Exhibit 99.6 to the registrant's Registration Statement on Form S-8 (File No. 333-30396) as filed with the SEC on February 14, 2000</i> |
| 10.8* | Form of Addendum to Stock Issuance Agreement for 1997 Plan Involuntary Termination Following Corporate Transaction/Change in Control | <i>Exhibit 99.7 to the registrant's Registration Statement on Form S-8 (File No. 333-30396) as filed with the SEC on February 14, 2000</i> |
| 10.8* | Form of Notice of Grant of Automatic Stock Option for 1997 Plan Initial Grant | <i>Exhibit 99.8 to Exhibit 99.8 to registrant's Registration Statement on Form S-8 (File No. 333-30396) as filed with the SEC on February 14, 2000</i> |
| 10.10* | Form of Notice of Grant of Automatic Stock Option for 1997 Plan Annual Grant | <i>Exhibit 99.9 to the registrant's Registration Statement on Form S-8 (File No. 333-30396) as filed with the SEC on February 14, 2000</i> |
| 10.11* | Form of Automatic Stock Option Agreement for 1997 Plan | <i>Exhibit 99.10 to the registrant's Registration Statement on Form S-8 (File No. 333-30396) as filed with the SEC on February 19, 2000</i> |

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Table of Contents

| Exhibit Number | Description | Reference |
|----------------|---|--|
| 10.15* | Form of 1997 Stock Option Agreements | <i>Exhibit 99.4 to the registrant's Registration Statement on Form S-8 (File No. 333-126834) as filed with the SEC on July 22, 2005</i> |
| 10.17 | Office Lease, dated May 24, 2007, by and between Crown Carnegie Associates, LLC and Iteris, Inc. | <i>Exhibit 10.2 to the registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2007 as filed with the SEC on August 14, 2007</i> |
| 10.18* | 2007 Omnibus Incentive Plan | <i>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</i> |
| 10.19* | Forms of Stock Option Agreements under the 2007 Omnibus Incentive Plan | <i>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</i> |
| 10.20 | Amended and Restated Loan and Security Agreement dated February 4, 2009 by and between California Bank & Trust and the registrant | <i>Exhibit 10.1 to the registrant's Quarterly Report on Form 10-Q for the quarter ended December 31, 2008 as filed with the SEC on February 13, 2009</i> |
| 10.21* | Form of Restricted Stock Unit Award Agreement under the 2007 Omnibus Incentive Plan | <i>Exhibit 10.3 to the registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2010 as filed with the SEC on July 28, 2010</i> |
| 10.22 | Modification Agreement dated September 30, 2010 by and between Iteris, Inc. and California Bank & Trust | <i>Exhibit 10.1 to the registrant's Current Report on Form 8-K as filed with the SEC on October 6, 2010</i> |
| 10.23 | Modification Agreement dated September 28, 2012 by and between Iteris, Inc. and California Bank & Trust | <i>Exhibit 10.1 to the registrant's Current Report on Form 8-K as filed with the SEC on October 3, 2012</i> |
| 10.24 | Amended and Restated Promissory Note, effective July 23, 2013, by and between Maxxess Systems, Inc. in favor of Iteris, Inc. | <i>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</i> |
| 10.25* | Employment Agreement, dated July 29, 2013, by and between Iteris, Inc. and Abbas Mohaddes | <i>Exhibit 10.2 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</i> |
| 10.26 | First Amendment to Lease, dated February 21, 2014, by and between RREF II Freeway Acquisitions, LLC and Iteris, Inc. | <i>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.</i> |

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Table of Contents

| Exhibit Number | Description | Reference |
|---------------------------|---|--|
| 10.27 | Modification Agreement dated September 23, 2014 by and between Iteris, Inc. and California Bank & Trust | <i>Exhibit 10.1 to the registrant's Quarterly Report on Form 10-Q as filed with the SEC on November 12, 2014</i> |
| 10.28 | Modification Agreement dated November 18, 2014 by and between Iteris, Inc. and California Bank & Trust | <i>Exhibit 10.1 to the registrant's Current Report on Form 8-K as filed with the SEC on November 24, 2014</i> |
| 10.29 | Separation Agreement and Release of Claims dated February 25, 2015 between Iteris, Inc. and Abbas Mohaddes | <i>Exhibit 10.1 to the registrant's Current Report on Form 8-K as filed with the SEC on February 27, 2015</i> |
| 10.30 | Modification Agreement dated February 24, 2015 between the Iteris, Inc. and California Bank & Trust | <i>Exhibit 10.2 to the registrant's Current Report on Form 8-K as filed with the SEC on February 27, 2015</i> |
| 10.31 | Employment Agreement dated March 9, 2015 between Iteris, Inc. and Andrew Schmidt | <i>Exhibit 10.1 to the registrant's Current Report on Form 8-K as filed with the SEC on March 15, 2015</i> |
| 10.32 | Employment Agreement dated September 8, 2015 between Iteris, Inc. and Joe Bergera | <i>Exhibit 10.1 to the registrant's Current Report on Form 8-K as filed with the SEC on September 22, 2015</i> |
| 16.1 | Letter from McGladrey LLP dated October 16, 2015 regarding change in certifying accountant | <i>Exhibit 16.1 to the registrant's Current Report on Form 8-K as filed with the SEC on October 14, 2015</i> |
| 21 | Subsidiaries of the registrant | <i>Filed herewith</i> |
| 23.1 | Consent of Independent Registered Public Accounting Firm, dated June 17, 2016 | <i>Filed herewith</i> |
| 23.2 | Consent of Independent Registered Public Accounting Firm, dated June 17, 2016 | <i>Filed herewith</i> |
| 24 | Power of Attorney | <i>Filed herewith (included on the Signature page)</i> |
| 31.1 | Certification of the Chief Executive Officer, as required pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 | <i>Filed herewith</i> |
| 31.2 | Certification of the Chief Financial Officer, as required pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 | <i>Filed herewith</i> |
| 32.1 | Certification of the Chief Executive Officer, as required pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 | <i>Filed herewith</i> |
| 32.2 | Certification of the Chief Financial Officer, as required pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 | <i>Filed herewith</i> |
| 101.INS | XBRL Instance Document | <i>Filed herewith</i> |

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Table of Contents

| Exhibit Number | Description | Reference |
|-----------------------|---|-----------------------|
| 101.SCH | XBRL Taxonomy Extension Schema Document | <i>Filed herewith</i> |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document | <i>Filed herewith</i> |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document | <i>Filed herewith</i> |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document | <i>Filed herewith</i> |
| 101.DEF | XBRL Taxonomy Definition Presentation Linkbase Document | <i>Filed herewith</i> |

*

Indicates a 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.