ITERIS, INC.
Form 10-Q
August 14, 2007

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2007

OR

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

For the transition period from to

Commission file number: 001-08762

ITERIS, INC.

(Exact name of registrant as specified in its charter)

Delaware	**95-2588496**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1515 South Manchester Avenue Anaheim, California	**92802**
(Address of principal executive office)	(Zip Code)

(714) 774-5000

(Registrant s telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended (the Exchange Act) during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No o

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

Large accelerated filer o Accelerated filer o Non-accelerated filer x

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

As of August 13, 2007, the registrant had 32,858,572 shares of common stock outstanding

ITERIS, INC.

Quarterly Report on Form 10-Q
For the Three Months Ended June 30, 2007

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Unless otherwise indicated in this report, the Company, we, us and our collectively refer to Iteris, Inc. and its former subsidiary, Meyer, Mohaddes Associates, Inc., which was dissolved effective April 2006.

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

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

ITERIS, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except per share amounts)

	June 30, 2007 (unaudited)	March 31, 2007
ASSETS		
Current assets:		
Cash and cash equivalents	**$ 2,214**	$ 35
Trade accounts receivable, net of allowance for doubtful accounts of $721 and $664 at June 30, 2007 and March 31, 2007, respectively	**9,671**	11,493
Costs and estimated earnings in excess of billings on uncompleted contracts	**5,364**	3,689
Inventories, net of reserve for inventory obsolescence of $855 and $844 at June 30, 2007 and March 31, 2007, respectively	**5,921**	6,379
Deferred income taxes	**535**	494
Prepaid expenses and other current assets	**771**	385
Total current assets	**24,476**	22,475
Property and equipment, net	**1,700**	1,712
Deferred income taxes	**2,388**	2,533
Intangible assets, net of accumulated amortization of $445 and $408 at June 30, 2007 and March 31, 2007, respectively	**367**	404
Goodwill	**27,774**	27,774
Other assets	**442**	352
Total assets	**$ 57,147**	$ 55,250
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Trade accounts payable	**$ 3,459**	$ 3,542
Accrued payroll and related expenses	**3,469**	3,527
Accrued liabilities	**2,172**	1,618
Billings in excess of costs and estimated earnings on uncompleted contracts	**840**	847
Revolving line of credit	**4,437**	4,015
Current portion of long-term debt	**1,624**	1,947
Total current liabilities	**16,001**	15,496
Non-current accrued liabilities	**140**	163
Deferred compensation plan liability	**401**	730
Long-term debt	**9,487**	9,760
Total liabilities	**26,029**	26,149
Commitments and contingencies		
Redeemable common stock, 1,219 shares issued and outstanding at June 30, 2007 and March 31, 2007	**3,414**	3,414
Stockholders equity:		
Preferred stock, $1.00 par value, 2,000 shares authorized, none issued and outstanding at June 30, 2007 and March 31, 2007		
Common stock, $0.10 par value, 50,000 shares authorized, 31,513 and 30,601 shares issued or issuable and outstanding at June 30, 2007 and March 31, 2007, respectively	**3,151**	3,060
Additional paid-in capital	**131,302**	130,425
Common stock held in trust, 167 and 311 shares at June 30, 2007 and March 31, 2007, respectively	**(202)**	(374)
Notes receivable from employees		(5)
Accumulated deficit	**(106,566)**	(107,438)
Accumulated other comprehensive income	**19**	19
Total stockholders equity	**27,704**	25,687
Total liabilities and stockholders equity	**$ 57,147**	$ 55,250

See accompanying notes to unaudited condensed consolidated financial statements.

ITERIS, INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share amounts)

	Three Months ended June 30, 2007	2006
Net sales and contract revenues:		
Net sales	**$ 10,244**	$ 8,600
Contract revenues	**5,513**	5,216
Total net sales and contract revenues	**15,757**	13,816
Costs of net sales and contract revenues:		
Cost of net sales (a)	**5,175**	4,758
Cost of contract revenues (a)	**3,488**	3,339
Gross profit	**7,094**	5,719
Operating expenses:		
Selling, general and administrative (a)	**4,458**	4,001
Research and development (a)	**994**	1,003
Deferred compensation plan	**31**	(66)
Amortization of intangible assets	**37**	36
Total operating expenses	**5,520**	4,974
Operating income	**1,574**	745
Non-operating income (expense):		
Other income (expense), net	**19**	(690)
Interest expense, net	**(363)**	(386)
Income (loss) before income taxes	**1,230**	(331)
Income tax (provision) benefit	**(134)**	610
Net income	**$ 1,096**	$ 279
Earnings per share:		
Basic	**$ 0.03**	$ 0.01
Diluted	**$ 0.03**	$ 0.01
Weighted average shares outstanding:		
Basic	**32,089**	28,393
Diluted	**34,317**	32,368

(a) Includes stock-based compensation expense as follows:

Cost of net sales	$ 1	$ 5
Cost of contract revenues	3	29
Selling, general and administrative expense	59	54
Research and development expense	3	12
Total	$ 66	$ 100

See accompanying notes to unaudited condensed consolidated financial statements.

ITERIS, INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Three Months Ended June 30,	
	2007	**2006**
Cash flows from operating activities		
Net income	**$ 1,096**	$ 279
Adjustments to reconcile net income to net cash provided (used in) by operating activities:		
Change in deferred tax assets	**104**	(456)
Depreciation and amortization of property and equipment	**149**	130
Stock-based compensation expense	**66**	100
Amortization of deferred gain on sale leaseback transaction	**(71)**	(71)
Amortization of debt discount	**52**	52
Amortization of intangible assets	**37**	36
Amortization of deferred financing costs	**35**	34
Issuance of warrants for services		
Changes in operating assets and liabilities:		
Accounts receivable	**1,822**	914
Net costs and estimated earnings in excess of billings	**(1,682)**	(1,130)
Inventories	**458**	(175)
Prepaid expenses and other assets	**(511)**	(551)
Accounts payable and accrued liabilities	**308**	239
Net cash provided by (used in) operating activities	**1,863**	(599)
Cash flows from investing activities		
Purchases of property and equipment	**(137)**	(142)
Cash flows from financing activities		
Net borrowings on line of credit	**422**	847
Payments on long-term debt	**(648)**	(333)
Change in checks drawn in excess of available bank balances	**(47)**	153
Proceeds from stock option exercises	**726**	168
Net cash provided by financing activities	**453**	835
Increase in cash	**2,179**	94
Cash at beginning of period	**35**	131
Cash at end of period	**$ 2,214**	$ 225
Supplemental cash flow information:		
Cash paid during the period:		
Interest	**$ 301**	$ 301
Income taxes	**48**	40
Supplemental schedule of non-cash investing and financing activities:		
Fair value of common stock issued in settlement of liabilities	**$ 350**	$
Write-off of notes receivable from employees	**(5)**	

See accompanying notes to unaudited condensed consolidated financial statements.

ITERIS, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2007

1. Description of Business and Summary of Significant Accounting Policies

Description of Business

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

Basis of Presentation

The unaudited condensed consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Securities and Exchange Commission (SEC) Form 10-Q and Article 10 of SEC Regulation S-X. In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all adjustments, consisting of normal recurring adjustments, necessary to present fairly the consolidated financial position of the Company as of June 30, 2007, the consolidated results of operations for the three months ended June 30, 2007 and 2006, and the consolidated cash flows for the three months ended June 30, 2007 and 2006. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States (U.S. GAAP) have been condensed or omitted pursuant to the rules and regulations of the SEC. The results of operations for the three months ended June 30, 2007, are not necessarily indicative of those to be expected for the entire year. The accompanying unaudited condensed consolidated financial statements should be read in conjunction with the Company s Annual Report on Form 10-K for the year ended March 31, 2007, which was filed with the SEC on June 21, 2007.

Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities, 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. Actual results could differ from those estimates. Significant estimates made in the preparation of the consolidated financial statements include the allowance for doubtful accounts, deferred tax assets, inventory and warranty reserves, costs to complete long-term contracts, overhead rates used in cost-plus contracts, contract reserves and estimates of future cash flows used to assess the recoverability of long-lived assets, the valuation of debt and equity instruments and the realization of goodwill.

Reclassifications

Certain amounts in the prior period financial statements have been reclassified to conform with current year presentation.

Revenue Recognition

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

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

In addition to product and contract revenue, the Company derives revenue from technology access fees, the provision of specific non-recurring contract engineering services and royalties. Technology access fee revenues are recognized evenly over the period in which they are earned. Non-recurring contract engineering revenues are recognized in the period in which the related services are performed. Royalty revenues are recorded in the period in which the royalty is earned, based on unit sales of the Company s products. Technology access fee revenues, contract engineering revenues and royalty revenues are included in net sales in the accompanying condensed consolidated statements of operations.

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

Concentration of Credit Risk

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

Fair Values of Financial Instruments

The fair values of cash and cash equivalents, receivables, inventories, accounts payable and accrued expenses approximate carrying value because of the short period of time to maturity. The fair values of line of credit agreements and long-term debt approximate carrying value because the related rates of interest approximate current market rates. The fair value of convertible debentures approximates carrying value because the effective interest rate, taking into account recorded debt discounts, approximates current market rates. The estimated fair value of redeemable common stock was $2.9 million and $2.8 million at June 30, 2007 and March 31, 2007, respectively, based on the closing price of the Company s common stock on those dates.

Inventories

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

Property and Equipment

Property and equipment are recorded at cost and are generally 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

In accordance with Statement of Financial Accounting Standards (SFAS) No. 142, *Goodwill and Intangible Assets*, goodwill is tested for impairment on an annual basis in the Company s fourth fiscal quarter or more frequently if indicators of impairment exist, of which none have been identified. The performance of the test involves a two-step process. The first step of the impairment test involves comparing the fair value of the Company s reporting units with each respective reporting unit s carrying amount, including goodwill. The Company determines the fair value of reporting units using the income approach. If the carrying amount of a reporting unit exceeds the reporting unit s fair value, the second step of the goodwill impairment test is performed to determine the amount of any impairment loss. The second step of the goodwill impairment test involves comparing the implied fair value of the reporting unit s goodwill with the carrying amount of that goodwill.

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

Income Taxes

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

Stock-Based Compensation

Effective April 1, 2006, the Company adopted SFAS No. 123 (revised 2004), *Share-Based Payment* (SFAS 123R), which requires all stock-based payments, including grants of employee stock options, to be recognized in the statement of operations as an expense, based on their grant date fair values with such fair values amortized over the requisite service period. The Company elected to use the modified prospective transition method for transition to SFAS 123R. Under the modified prospective method, SFAS 123R applies to all awards granted or modified after the date of adoption. In addition, under the modified prospective method, compensation expense is recognized for all stock-based compensation awards granted prior to but not yet vested as of April 1, 2006, based on grant-date fair values estimated in accordance with the original provisions of SFAS No. 123, *Accounting for Stock-Based Compensation*.

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 in cost of sales in the period during which products ship.

Sales Taxes

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

Warranty

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

Repair and Maintenance Costs

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

Other Comprehensive Income

The only component of accumulated other comprehensive income is foreign currency translation adjustments.

Recent Accounting Pronouncements

In July 2006, the Financial Accounting Standards Board (the FASB) issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48). FIN 48 applies to all tax positions accounted for under SFAS 109, and defines the confidence level that a tax position must meet in order to be recognized in the financial statements. The interpretation requires that the tax effects of a position be recognized only if it is more-likely-than-not to be sustained by the taxing authority as of the reporting date. If a tax position is not considered more-likely-than-not to be sustained then no benefits of the position are to be recognized. FIN 48 requires additional disclosures and is effective as of the beginning of the first fiscal year beginning after December 15, 2006. As further discussed in Note 4, the Company adopted FIN 48 effective April 1, 2007.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* (SFAS 157), which defines fair value, establishes a framework for measuring fair value, and expands disclosure about fair value measurements. SFAS 157 does not require any new fair value measurements; rather it specifies valuation methods to be applied when fair value measurements are required under existing or future accounting pronouncements. SFAS 157 is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Early application of the statement is encouraged. Generally, this statement will be applied prospectively. The Company is currently evaluating the impact of SFAS 157 and expects to adopt SFAS 157 in the first quarter of its fiscal year ending March 31, 2009.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115* (SFAS 159). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. Unrealized gains and losses on items for which the fair value option has been elected will be recognized in earnings at each subsequent reporting date. SFAS 159 is effective for financial statements issued for fiscal years beginning after November 15, 2007. The Company is evaluating the impact that the adoption of SFAS 159 will have on its results of operations and financial condition and expects to adopt SFAS 159 in its fiscal year ending March 31, 2009.

2. Supplemental Financial Information

Inventories

The following table presents details of the Company s inventories:

	June 30, 2007	**March 31, 2007**
	(In thousands)	
Materials and supplies	**$ 4,478**	$ 4,705
Work in process	**334**	366
Finished goods	**1,109**	1,308
	$ 5,921	$ 6,379

Intangible Assets

	June 30, 2007		**March 31, 2007**	
	Gross Carrying Amount	**Accumulated Amortization**	**Gross Carrying Amount**	**Accumulated Amortization**
	(In thousands)			
Developed technology	**$ 495**	**$ (306)**	$ 495	$ (280)
Patents	**317**	**(139)**	317	(128)
Total	**$ 812**	**$ (445)**	$ 812	$ (408)

Amortization expense for intangible assets subject to amortization was $37,000 and $36,000 for the three months ended June 30, 2007 and 2006, respectively. Future estimated amortization expense for the remainder of the current fiscal year and the next four fiscal years is as follows:

Fiscal Year Ending March 31: **(In thousands)**	
2008	$ 110
2009	147
2010	58
2011	46
2012	6
	$ 367

Warranty Reserve Activity

The following table presents activity in accrued warranty obligations:

	Three Months Ended June 30,	
	2007	**2006**
	(In thousands)	
Balance at beginning of period	**$ 520**	$ 519
Additions charged to cost of sales	**99**	135
Warranty claims	**(50)**	(64)
Balance at end of period	**$ 569**	$ 590

Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per share:

	Three Months Ended June 30,	
	2007	**2006**
	(In thousands, except per share amounts)	
Numerator:		
Net income	**$ 1,096**	$ 279
Denominator:		
Weighted average common shares used in basic computation	**32,089**	28,393
Dilutive stock options	**2,197**	3,417
Dilutive warrants	**31**	558
Weighted average common shares used in dilutive computation	**34,317**	32,368
Earnings (loss) per share:		
Basic	**$ 0.03**	$ 0.01
Diluted	**$ 0.03**	$ 0.01

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

	Three Months Ended June 30,	
	2007	**2006**
	(In thousands)	
Stock options	**668**	525

Stock-Based Compensation

Warrants	**1,190**	1,380
Convertible debentures	**2,729**	2,729

3. Revolving Line of Credit and Long-Term Debt

Revolving Line of Credit

In October 2006, the Company replaced its former credit facility and entered into a new two-year credit facility with a different bank. The new facility provides for combined line of credit and bank term note borrowings of up to $8.0 million. Under the new credit facility, the Company may borrow against its eligible accounts receivable and eligible inventory, as defined in the credit agreement. Line of credit interest on borrowed amounts is payable monthly at the current stated prime rate plus 1.25% (9.50% at June 30, 2007). Additionally, the Company is obligated to pay an unused line fee of 0.25% per annum applied to the amount by which the maximum credit amount exceeds the average daily principal balance during the preceding month. The new credit facility requires $2,000 in monthly collateral management fees and includes an early termination fee equal to 2% of the total facility during the first year of the agreement and 1% of the total facility in the second year of the agreement. Additionally, the Company paid a commitment fee of $40,000 in October 2006 and is obligated to pay an additional $40,000 on the one-year anniversary of the facility. The new credit facility is secured by substantially all of the assets of the Company.

On June 30, 2007, the available credit under the credit facility was $8.0 million, of which $2.3 million was unused.

Long-Term Debt

The Company s long-term debt consists of the following:

	June 30, 2007 (In thousands)	**March 31, 2007**
Convertible debentures, net	**$ 9,462**	$ 9,410
Bank term note	**1,258**	1,573
Promissory note to landlord	**323**	646
Other	**68**	78
	11,111	11,707
Less current portion	**(1,624)**	(1,947)
	$ 9,487	$ 9,760

Convertible Debentures, Net. In May 2004, the Company sold and issued subordinated convertible debentures in the aggregate original principal amount of $10.1 million. In connection with the issuance of the debentures, the Company issued warrants to purchase an aggregate of 639,847 shares of its common stock, the value of which was recorded as a debt discount against the face amount of the debentures on the date of issuance and is being amortized to interest expense over the term of the convertible debentures.

The debentures are due in full on May 19, 2009, provide for 6.0% annual interest, payable quarterly, and are convertible into the Company s common stock at an initial conversion price of $3.61 per share, subject to certain adjustments, including adjustments for dilutive issuances. From May 19, 2008, until the maturity date, the Company may redeem the debentures at 110% of the principal amount. As of June 30, 2007, $250,000 of convertible debentures had been converted into 69,252 shares of common stock leaving $9.9 million of the originally issued convertible debentures outstanding at June 30, 2007.

Bank Term Note. In October 2004, the Company entered into a $5.0 million term note payable with a bank. The note was due on May 27, 2008, and provided for monthly principal payments of approximately $104,000. Interest accrued at the current stated prime rate plus 0.25%. In October 2006, the term note was assumed by the Company s new bank as part of the Company s new $8.0 million credit facility. The new term note is also due on May 27, 2008 and provides for monthly principal payments of approximately $104,000. Interest accrues under the new term note at the current stated prime rate plus 1.25% (9.50% at June 30, 2007). Amounts due under the term note reduce the Company s ability to borrow against its eligible assets on its line of credit.

Both the new bank term note and the new line of credit are held by one bank under the same credit agreement and are secured by substantially all of the assets of the Company.

Promissory Note to Landlord. The Company had an unsecured promissory note payable to the landlord of its Anaheim headquarters. Under the terms of the note agreement, interest is payable quarterly and accrues at a rate of prime plus 2.0% (10.25% at June 30, 2007). In October 2006, January 2007, April 2007 and July 2007, the Company made four required equal quarterly principal payments of $323,000. As of July 1, 2007, all interest and principal under this note was paid in full.

Scheduled aggregate maturities of long-term debt principal as of June 30, 2007 were as follows:

Fiscal Year Ending March 31, **(In thousands)**	
2008	**$ 1,299**
2009	**350**
2010	**9,850**
	11,499
Less: unamortized debt discount	**(388)**
	$ 11,111

4. Income Taxes

On April 1, 2007, the Company adopted FIN 48. In connection with the adoption of FIN 48, the Company recognized an adjustment of approximately $224,000 to the beginning balance of retained earnings on its consolidated balance sheet. The Company s continuing practice is to recognize interest and/or penalties related to income tax matters in income tax expense. As of June 30, 2007, the Company had recorded approximately $39,000 of accrued interest and penalties related to uncertain tax positions.

At April 1, 2007, the Company s fiscal 2004 through fiscal 2007 tax years remain open to examination by the Federal taxing authorities. The Company s fiscal 2003 through fiscal 2007 tax years remain open to examination by the state taxing authorities. However, the Company has consolidated and acquired NOLs beginning in fiscal 1995 which would cause the statute of limitations to remain open for the year in which the NOL was incurred.

5. Commitments and Contingencies

Litigation and Other Contingencies

On June 29, 2004, a supplier to Mariner Networks, Inc., a former subsidiary of the Company that was discontinued in the fiscal year ended March 31, 2002, filed a complaint in Orange County Superior Court against the Company alleging various breaches of written contract claims arising out of alleged purchase orders. The plaintiff in this lawsuit sought monetary damages aggregating approximately $850,000 plus attorney fees and related costs. On July 20, 2006, the Company entered into a settlement agreement in connection with this matter. The dispute was settled in full for $688,000 payable as follows: (i) the Company issued 88,912 shares of the Company s common stock on August 18, 2006 valued at $213,000 based on the closing sales price of the Company s common stock on the date of issuance; (ii) the Company made a cash payment of $125,000 on October 20, 2006; and (iii) the Company is obligated to pay $350,000 in cash in equal monthly installments of $9,700 over three years beginning in November 2006. In connection with this settlement, the Company recorded a charge of $688,000, representing the fair value of the settlement, to other expense in the accompanying condensed consolidated statement of operations for the three months ended June 30, 2006.

In August 2007, the Company received a complaint filed by American Signal Company against the Company and six other defendants, in the United States District Court, Middle District of Louisiana and which alleges negligence and other charges in connection with a contract to which the Company was a third party engineering service provider. The Company is reviewing the complaint, however, does not believe that this matter will ultimately have a material adverse effect on its consolidated results of operations, financial position or cash flows.

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

Furthermore, from time to time, the Company has experienced unforeseen developments in contingencies related to its former subsidiaries. For example, the Company has been the subject of a number of routine tax audits for time periods and jurisdictions related to the businesses of its former subsidiaries, some of which are still in process. Although the development and ultimate outcome of these and other unforeseen matters cannot be predicted with any certainty, management does not believe that the Company is presently involved in any matters related to its former subsidiaries that would have a material adverse effect on the Company s consolidated results of operations, financial position or cash flows.

Operating Lease Commitments

The Company has lease commitments for facilities in various locations throughout the United States. Future commitments under these non-cancelable operating leases at June 30, 2007 were as follows:

Fiscal Year Ending March 31, **(In thousands)**	
Remainder of 2008	**$ 883**
2009	**1,398**
2010	**1,391**
2011	**1,348**
2012	**1,332**
Thereafter	**3,823**
Total	**$ 10,175**

The Company subleases 10,000 square feet of space in its 94,000 square foot Anaheim, California facility at a monthly rate of $10,000 to MAXxess Systems, Inc. (MAXxess), a former subsidiary of the Company that was sold in September 2003 and is currently owned by an investor group that includes one of the Company s directors. Another member of the Company s board of directors is the Chief Executive Officer of MAXxess. At June 30, 2007, MAXxess owed the Company an aggregate of $229,000 related to this sublease and certain ancillary services provided by the Company to MAXxess. The Company previously had written off amounts aggregating $183,000 of this balance due to MAXxess inability to pay these obligations. During the three months ended June 30, 2007, the Company wrote off all incremental amounts charged to MAXxess, which aggregated $46,000. The Company intends to pursue full payment of any and all amounts due from MAXxess under this sublease, which terminates in September 2007.

Inventory Purchase Commitments

At June 30, 2007, the Company had firm commitments to purchase inventory in the amount of $3.2 million during the next two fiscal quarters.

6. Stock-Based Compensation

The Company s 1997 Stock Incentive Plan (the Plan) provides that options to purchase shares of the Company s unissued common stock may be granted to directors, associates and consultants to the Company at exercise prices which are equal to or greater than the fair market value of the Company s common stock on the date of grant. Options expire ten years after the date of grant or 90 days after termination of employment and generally vest ratably at the rate of 25% on each of the first four anniversaries of the grant date. New shares are issued to satisfy stock option exercises under the Plan. As of June 30, 2007, options to purchase 1.5 million shares of the Company s common stock were outstanding under the Plan.

In connection with the merger of the Company and the Iteris Subsidiary (Note 1), the Company assumed the 1998 Stock Incentive Plan of the Iteris Subsidiary (the 1998 Plan) and all outstanding options granted thereunder. As of June 30, 2007, options to purchase 3.2 million shares of the Company s common stock were outstanding under the 1998 Plan. No further options may be granted under the 1998 Plan.

Certain options granted under the Plan and the 1998 Plan (collectively, the Plans) provide for accelerated vesting of unvested options in the event of a change in control under certain circumstances. These change-in-control provisions meet the criteria of a performance condition under SFAS 123R.

As of June 30, 2007, the Company had 112,000 outstanding stock options that were originally granted outside of the Plans and that were assumed by the Plan in connection with the merger of the Company and the Iteris Subsidiary (Note 1).

A summary of activity in the Plans for the three months ended June 30, 2007 is as follows:

	Options	Weighted Average Exercise Price	Weighted Average Remaining Life (In Years)	Aggregate Intrinsic Value
	(In thousands, except per share amounts)			
Options outstanding at March 31, 2007	5,818	$ 1.60	3.4	$ 6,115
Granted		N/A	N/A	
Exercised	(913)	$ 0.79	N/A	
Forfeited	(17)	$ 3.16	N/A	
Expired	(19)	$ 4.29	N/A	
Options outstanding at June 30, 2007	4,869	$ 1.74	3.7	$ 4,396
Vested and expected to vest at June 30, 2007	4,794	$ 1.72	3.6	$ 4,389
Options exercisable at June 30, 2007	4,418	$ 1.66	3.2	$ 4,296
Options exercisable at June 30, 2007 pursuant to a change-in-control	4,869	$ 1.74	3.7	$ 4,396

At June 30, 2007, there were 35,000 shares of common stock available for grant under the Plan.

For the three month periods ended June 30, 2007 and 2006, the Company received $726,000 and $168,000, respectively, in cash from the exercise of stock options. Total stock-based compensation expense for the three months ended June 30, 2007 and 2006, was $66,000 and $100,000, respectively. No income tax benefit was realized from activity in the Plans during the three months ended June 30, 2007 and 2006.

At June 30, 2007, there was $778,000 of total unrecognized compensation expense related to unvested stock options. This expense is expected to be recognized over a weighted-average period of approximately 3.0 years.

The fair value of each stock-based award is estimated on the grant date using the Black-Scholes-Merton (BSM) option-pricing formula. Expected volatility is based on the historical volatility of the Company s stock price. The expected life of options granted subsequent to the adoption of SFAS 123R is derived based on the historical life of the Company s options. The risk-free interest rate for periods within the expected life of the option is based on the U.S. Treasury interest rates in effect at the time of grant. The grant date fair value of options granted was estimated using the following weighted-average assumptions:

	Three Months Ended June 30, 2007	2006	
Dividend yield	**N/A**	0.0	%
Expected life years	**N/A**	7.0	
Risk-free interest rate	**N/A**	5.0	%
Expected volatility of common stock	**N/A**	0.89	

A summary of the grant date fair value and intrinsic value information is as follows:

	Three Months Ended June 30, 2007	2006
	(In thousands, except per share amounts)	
Weighted average grant date fair value per share	**N/A**	$ 1.77
Intrinsic value of options exercised	**$ 1,417**	$ 163
Total fair value of options vested during the period	**$ 47**	$ 384

7. Business Segment Information

The Company currently operates in three reportable segments: Roadway Sensors, Automotive Sensors and Transportation Systems. The Roadway Sensors segment includes the Company s Vantage vehicle detection systems for traffic intersection control, incident detection and certain highway traffic data collection applications. The Automotive Sensors segment includes AutoVue and is comprised of all activities related to lane departure warning systems for vehicle

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safety. 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 accounting policies of the reportable segments are the same as those described in the summary of significant accounting policies. Prior to April 1, 2007, certain expenses, such as interest, amortization of certain intangibles and certain corporate expenses were not allocated to the segments. Beginning on April 1, 2007, the Company increased the portion of its corporate expenses that it allocates to its segments such that substantially all corporate expenses are allocated. Interest, amortization of certain intangibles and certain corporate expenses are still not allocated to the segments. In addition, certain assets, including cash and cash equivalents, deferred income taxes and certain long-lived and intangible assets, are not allocated to the segments. The reportable segments are each managed separately because they manufacture and distribute distinct products or provide services with different processes. All segment revenues are derived from external customers.

The following table sets forth selected unaudited financial information for the Company s reportable segments for the three months ended June 30, 2007 and 2006:

	Roadway Sensors	**Automotive Sensors**	**Transportation Systems**	**Total**
	(In thousands)			
Three Months Ended June 30, 2007				
Product revenue	$ 7,224	$ 2,584	$	$ 9,808
Service and other revenue		436	5,513	5,949
Stock-based compensation	6	13	7	26
Depreciation and amortization	26	36	31	93
Segment income (loss)	1,105	50	544	1,699
Three Months Ended June 30, 2006				
Product revenue	$ 6,516	$ 1,339	**$**	$ 7,855
Service and other revenue		745	5,216	5,961
Stock-based compensation	19	13	36	68
Depreciation and amortization	19	34	28	81
Segment income (loss)	1,482	(653)	622	1,451

The following table reconciles segment income to consolidated income (loss) before income taxes:

	Three Months Ended June 30,	
	2007	**2006**
	(In thousands)	
Total income for reportable segments	**$ 1,699**	$ 1,451
Unallocated amounts:		
Corporate expenses	**(125)**	(706)
Other income (expense), net	**19**	(690)
Interest expense, net	**(363)**	(386)
Income (loss) before income taxes	**$ 1,230**	$ (331)

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

This report, including the following discussion and analysis, contains forward-looking statements (within the meaning of the Private Securities Litigation Reform Act of 1995) that are based on our current expectations, estimates and projections about our business and our industry, and reflect management s beliefs and certain assumptions made by us based upon information available to us as of the date of this report. When used in this report and the information incorporated herein by reference, the words expect(s), feel(s), believe(s), should, will, may, anticipate(s), estimate(s) and similar expressions or variations of these words are intended to identify forward-looking statements. These forward-looking statements include but are not limited to statements regarding our anticipated sales, revenue, expenses, profits, capital needs, competition, development plans, backlog and manufacturing capabilities, 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 undertake no obligation to republish revised forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events. We encourage you to carefully review and consider the various disclosures made by us which describe certain factors which could affect our business, including in Risk Factors set forth in Part II, 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.

Overview

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

Our Vantage product is a video vehicle detection system that detects the presence of vehicles on roadways. Vantage systems are used at signalized intersections to enable a traffic controller to more efficiently allocate green signal time and are also used for incident detection and highway traffic data collection applications. We sell and distribute our Vantage products primarily to commercial customers and municipal agencies.

Our AutoVue Lane Departure Warning (LDW) systems consist of a small windshield mounted sensor that uses proprietary software to detect and warn drivers of unintended lane departures. Approximately 90,000 production AutoVue units have been sold for car and truck platforms in the North American and European markets. Our AutoVue LDW systems are currently qualified as an option on certain heavy trucks, including Mercedes-Benz, MAN, Iveco, DAF, Scania, Freightliner, International and FUSO, as well as Neoplan and MAN luxury bus and coach lines. In North America our LDW systems are sold primarily to truck fleets, and to date, 45 U.S. heavy truck fleets have selected our LDW systems, representing an estimated 25,000 vehicles. In September 2003, we entered into an agreement with Valeo Schalter and Sensuren GmbH (Valeo), pursuant to which we granted Valeo the exclusive right to sell and manufacture our AutoVue LDW systems to the worldwide passenger car market in exchange for royalty payments for each AutoVue LDW unit sold. To date, royalty payments from Valeo have not been significant. Pursuant to this agreement, we also provide specific contract engineering services, technical marketing and sales support to Valeo to enable the incorporation of our LDW technology on three Infiniti platforms, the FX, M and Q, where the device is offered as part of Infiniti s technology option package. Valeo is currently in discussions to provide our LDW system to other passenger car OEMs; however, we cannot assure you that such discussions will be successful. We plan to continue to provide technical marketing and sales support to Valeo in our efforts to win new OEM customers for the passenger car market as well as contract engineering services related to the possible launch of new Infiniti platforms that include our LDW system. We believe that AutoVue is a broad sensor platform that, through additional software development, may be expanded to incorporate additional safety and convenience features.

Our transportation management systems business includes 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, travel demand forecasting and systems engineering, and identify mitigation measures to reduce traffic congestion. These services and systems are primarily sold to local, state and national transportation agencies in the United States. Our transportation management systems business is largely dependent upon governmental funding and budgetary issues. The Federal Highway Bill that was passed in August 2005 provided for a significant increase in transportation funding over the following six years. We believe the recent expansion of our transportation management systems business was due in part to the passage of the Federal Highway Bill, combined with increased transportation funds available at state and local agencies throughout the country.

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

Critical Accounting Policies and Estimates

Management s Discussion and Analysis of Financial Condition and Results of Operations is based on our unaudited condensed consolidated financial statements included herein, which have been prepared in accordance with U.S generally accepted accounting principles. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and related disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. On an ongoing basis, we evaluate these estimates and assumptions, including those related to the collectibility of accounts receivable, the valuation of inventories, the recoverability of long-lived assets and goodwill, 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 our historical experience and on various other factors that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. These estimates and assumptions by their nature involve risks and uncertainties, and may prove to be inaccurate. In the event that any of our estimates or assumptions are inaccurate in any material respect, it could have a material adverse effect on our reported assets and liabilities at the date of the financial statements and our reported 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 unaudited condensed consolidated financial statements.

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

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

In addition to product and contract revenues, we derive revenue from technology access fees, the provision of specific non-recurring contract engineering services to our strategic partner, Valeo, related to our AutoVue LDW systems, and royalties earned on unit sales of our AutoVue LDW systems by Valeo to the passenger car market. Technology access fee revenues are recognized evenly over the period in which they are earned. Non-recurring contract engineering revenues are recognized in the period in which the related services are performed. Royalty revenues are recorded based on unit sales of our products by Valeo and are recognized in the period in which such sales occur. Technology access fee revenues, contract engineering revenues and royalty revenues are included in net sales.

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

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

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

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

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

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

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

Stock-Based Compensation

Effective April 1, 2007, we adopted Financial Accounting Standards Board Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48). FIN 48 applies to all tax positions accounted for under SFAS No. 109, *Accounting for Income Taxes*, and defines the confidence level that a tax position must meet in order to be recognized in the financial statements. FIN 48 requires that the tax effects of a position be recognized only if it is more-likely-than-not to be sustained by the taxing authority as of the reporting date. If a tax position is not considered more-likely-than-not to be sustained, then no benefits of the position are to be recognized.

Stock-Based Compensation. Effective April 1, 2006, we adopted SFAS No. 123 (revised 2004), *Share-Based Payment* (SFAS 123R), which requires all stock-based payments, including grants of employee stock options, to be recognized in the statement of operations as an expense, based on their grant date fair values with such fair values amortized over the requisite service period. We elected to utilize the modified prospective method for the transition to SFAS 123R. Under the modified prospective method, SFAS 123R applies to all awards granted or modified after the date of adoption. In addition, under the modified prospective method, compensation expense is recognized for all stock-based compensation awards granted prior to but not yet vested as of April 1, 2006, based on grant-date fair values estimated in accordance with the original provisions of SFAS No. 123, *Accounting for Stock-Based Compensation*.

We use the BSM option-pricing formula to estimate the fair value of stock-based awards granted subsequent to April 1, 2006. Our assumptions under the BSM formula include the following: expected volatilities are based on the historical volatility of our stock price, the expected life of options is derived based on the historical life of our options, and the risk-free interest rate for periods within the expected life of the option is based on the U.S. Treasury interest rates in effect at the time of grant. Additionally, our calculation of stock compensation expense under SFAS 123R includes an estimate of forfeitures based on our historical forfeiture rate. Future stock-based compensation expense in any particular quarter or year could be affected by changes in our assumptions or changes in market conditions.

Results of Operations

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

	Three Months Ended June 30,	
	2007	**2006**
Net sales and contract revenues:		
Net sales	**65.0 %**	62.2 %
Contract revenues	**35.0**	37.8
Total net sales and contract revenues	**100.0 %**	100.0 %
Costs of net sales and contract revenues:		
Cost of net sales	**32.9**	34.4
Cost of contract revenues	**22.1**	24.2
Gross profit	**45.0**	41.4
Operating expenses:		
Selling, general and administrative	**28.3**	29.0
Research and development	**6.3**	7.3
Deferred compensation plan	**0.2**	(0.5)
Amortization of intangible assets	**0.2**	0.2
Total operating expenses	**35.0**	36.0
Operating income	**10.0**	5.4
Non-operating income (expense):		
Other income (expense), net	**0.1**	(5.0)
Interest expense, net	**(2.3)**	(2.8)
Income (loss) before income taxes	**7.8**	(2.4)
Income tax benefit (provision)	**(0.8)**	4.4
Net income	**7.0 %**	2.0 %

Analysis of Quarterly Results of Operations

Net Sales and Contract Revenues. Net sales are comprised of Roadway Sensors sales, which are derived from sales of our Vantage video detection systems; and Automotive Sensor sales, which are derived from sales of AutoVue LDW systems, technology access fees, contract engineering revenue and royalty revenue generated from AutoVue related activities. Contract revenues consist entirely of Transportation Systems revenues, which are generated from systems integration and ITS consulting services with federal, state, county and municipal agencies. We currently have a

relatively diverse customer base with our largest customer constituting 7.3% of total net sales and contract revenues in the three months ended June 30, 2007.

Total net sales and contract revenues increased 14.0% to $15.8 million for the three months ended June 30, 2007, compared to $13.8 million in the corresponding period of the prior fiscal year. This increase was primarily driven by increased net sales in both the Roadway Sensors and Automotive Sensors segments, as well as increased contract revenues in the Transportation Systems segment, as discussed below.

Net sales increased 19.1% to $10.2 million for the three months ended June 30, 2007, compared to $8.6 million in the corresponding period of the prior fiscal year.

Roadway Sensors net sales increased 10.9% to $7.2 million for the three months ended June 30, 2007, versus $6.5 million in the corresponding period of the prior fiscal year. This increase primarily reflects the continued adoption, primarily in North America, of video vehicle detection technology such as the technology offered by our Vantage line of products. Additionally, we believe that the current increased rate of adoption has to some extent been due to increased government spending on traffic initiatives, which we believe has been at least partially made possible by the passage of the Federal Highway Bill in August 2005, as well as expanded sales and marketing efforts in North America.

Automotive Sensors net sales increased 44.9% to $3.0 million for the three months ended June 30, 2007, versus $2.1 million in the corresponding period of the prior fiscal year. This increase was primarily a result of increased unit sales of our LDW systems to European and Asian OEMs and North American heavy truck fleet customers. Sales of LDW systems to the heavy truck market increased by $1.2 million, or 93.0%, over the prior year period. Also included in Automotive Sensors net sales are revenues from contract engineering services, technology access fees and royalty revenues in the passenger car market that are derived from our partnership with Valeo, which aggregated $436,000 and $745,000 for the three months ended June 30, 2007 and 2006, respectively.

We expect sales of LDW units to the heavy truck market to continue to increase, when compared to the prior year period, for at least the remainder of Fiscal 2008; and we expect revenues from our strategic partnership with Valeo to decrease slightly as compared to the prior year largely because we will not receive any technology access fee revenues in Fiscal 2008. Technology access fee revenues totaled $125,000 for the three months ended June 30, 2006 and $500,000 in Fiscal 2007. Royalty revenues from Valeo for sales of our LDW systems for the passenger car market remained relatively insignificant in the current quarter. Our LDW systems are now offered as an option on three Infiniti models. While Valeo is currently in discussions to offer our LDW systems on other passenger car platforms, we cannot assure you that Valeo will be successful in these efforts.

Contract revenues increased 5.7% to $5.5 million for the three months ended June 30, 2007, compared to $5.2 million in the corresponding period of the prior fiscal year. This increase was largely due to increased funding at the federal, state and local levels throughout the country, as well as new contract awards. In response to this growth in funding, we have increased our Transportation Systems staff by 4% in the three months ended June 30, 2007, and we expect to continue to increase our Transportation Systems staff over the remainder of Fiscal 2008. We believe the ability of our Transportation Systems business to grow and successfully win and service new contracts will be highly dependent upon our continued success in recruiting and retaining qualified personnel. All of our contract revenues are derived from work performed in North America under a broad range of fixed price and cost plus fixed fee contracts.

Gross Profit. Total gross profit increased 24.0% to $7.1 million for the three months ended June 30, 2007, as compared to $5.7 million in the corresponding period of the prior fiscal year. Total gross profit as a percent of net sales and contract revenues increased to 45.0% for the three months ended June 30, 2007, as compared to 41.4% in the corresponding period of the prior fiscal year.

Gross profit as a percent of net sales was 49.5% for the three months ended June 30, 2007, compared to 44.7% in the corresponding period of the prior fiscal year. This increase in gross profit was primarily a result of increased gross profits in both the Roadway Sensors and Automotive Sensors segments. In Roadway Sensors, the increase was largely due to production efficiencies and a shift of engineering resources from manufacturing and support projects to research and development activities. Additionally, Roadway Sensors margins were positively impacted by our sales mix in terms of both geography and product mix. The increase in Automotive Sensor margins was primarily a result of higher sales volumes that created better coverage of our fixed manufacturing overhead costs. Furthermore, our Automotive Sensros customer base has expanded, which has mitigated the gross margin impact of contractual pricing to our largest European customer. Gross profit as a percent of net sales generally fluctuates in any specific quarter based on customer mix. Gross profit as a percent of net sales has fluctuated over the last nine quarters from a high of 50.2% in the first quarter of Fiscal 2006 to a low of 43.2% reported in the second quarter of Fiscal 2007, mainly as a result of customer mix.

Gross profit as a percent of contract revenues was 36.7% for the three months ended June 30, 2007, compared to 36.0% in the corresponding period of the prior fiscal year. We recognize contract revenues and related gross profit using percentage of completion contract accounting, and the underlying mix of contract activity affects the related gross profit recognized in any given period. The increase in gross profit as a percent of contract revenues in the most recent quarter reflects a contract mix weighted more toward higher margin contracts in the period.

Selling, General and Administrative Expense. Selling, general and administrative expense increased 11.4% to $4.5 million (or 28.3% of total net sales and contract revenues) in the three months ended June 30, 2007, compared to $4.0 million (or 29.0% of total net sales and contract revenues) in the corresponding period of the prior fiscal year. This increase was largely attributable to higher commissions and selling expenses driven by sales growth in our Roadway Sensors segment. In the coming quarters, we anticipate increased selling, general and administrative expenses related to our efforts to comply with the internal control attestation requirements of the Sarbanes-Oxley Act, with which we must begin to comply in Fiscal 2008.

Research and Development Expense. Research and development expense was flat year-over year at $1.0 million (or 6.3% and 7.3% of total net sales and contract revenues for the three months ended June 30, 2007 and 2006, respectively). We believe research and development activities are crucial to our ability to continue to be a leader in our markets and expect this level of research and development expenditure to continue for the remainder of Fiscal 2008.

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

Deferred Compensation Plan Expense. During the three months ended June 30, 2007, we incurred a non-cash charge of $31,000 related to the change in value of 310,510 shares of our common stock held in trust by our deferred compensation savings plan. This compares to a non-cash benefit of $66,000 recorded in the three month period ended June 30, 2006. In May 2007, our former Chief Executive Officer, who departed in March 2007, elected to receive a distribution of approximately fifty percent of his deferred compensation plan balance, representing 143,333 shares of our common stock and $10,000 in cash, all of which was paid out prior to June 30, 2007, and his remaining deferred compensation plan balance of 143,333 shares of our common stock and $5,000 in cash on the one year anniversary of this election. As a result of this election, at June 30, 2007, the trust held 167,177 shares of our common stock and $5,000 of cash. We expect to continue to experience non-cash expense or benefit in future periods as the value of the assets held in our deferred compensation savings plan fluctuates.

Other Income (Expense), Net. Other income (expense), net includes the following:

	Three Months Ended June 30, 2007 (In thousands)	2006
Settlement of lawsuit	**$**	$ (688)
Other	**19**	(2)
Other income (expense), net	**$ 19**	$ (690)

Other income (expense), net for the three months ended June 30, 2006 primarily reflects $688,000 of expense recorded in connection with the settlement of litigation in July 2006 related to one of our former subsidiaries. See Note 5 to the accompanying condensed consolidated financial statements for a description of the terms of the settlement and the additional amounts still payable in connection with the settlement.

Interest Expense, Net. Interest expense, net includes the following:

	Three Months Ended June 30, 2007 (In thousands)	2006
Interest expense	**$ (276)**	$ (300)

Amortization of debt discount	**(52)**	(52)
Amortization of deferred finance costs	**(35)**	(34)
Interest expense, net	**$ (363)**	$ (386)

Interest expense decreased for the three months ended June 30, 2007, compared to the corresponding period in the prior fiscal year primarily as a result of a lower level of borrowings on our line of credit in the current year.

Income Taxes. During the three months ended June 30, 2007, we recognized income tax expense of $134,000 as compared to an income tax benefit of $610,000 in the three months ended June 30, 2006. The tax expense recorded in the three months ended June 30, 2007 was primarily based on anticipated taxes to be paid in the current year, as well as a slight increase in the valuation allowance recorded against our deferred tax assets as a result of changes in estimates of the future realizability of these assets. Total deferred tax assets on our consolidated balance sheet decreased from $3.0 million at March 31, 2007 to $2.9 million at June 30, 2007. In the future, we may continue to record similar adjustments to our deferred tax asset valuation allowance as our estimates are updated. We anticipate this will cause our future overall effective tax rate in any given period to fluctuate from prior effective tax rates, estimated annual effective tax rates and statutory tax rates.

As discussed in Notes 1 and 4 of the accompanying condensed consolidated financial statements, we adopted FIN 48 on April 1, 2007. In connection with our adoption of FIN 48, we recognized an adjustment of approximately $224,000 to the beginning balance of retained earnings on our consolidated balance sheet. Additionally, there was no significant change in our income tax expense for the three months ended June 30, 2007 as a result of our implementation of FIN 48.

Liquidity and Capital Resources

Cash Flows

We have historically financed our operations with a combination of cash flows from operations, borrowings under credit facilities and the sale of equity securities. We currently rely on cash flows from operations and borrowings on a line of credit facility to fund our operations. At June 30, 2007, we had $8.5 million in working capital, which included borrowings of $4.4 million on our revolving line of credit and $2.2 million in cash and cash equivalents. This compares to working capital of $7.0 million at March 31, 2007, which included borrowings of $4.0 million on our revolving line of credit and $35,000 in cash and cash equivalents.

Our operating activities provided $1.9 million in cash during the three months ended June 30, 2007, primarily as a result of net income generated during the period as well as, to a lesser extent, the timing of cash flows from operating assets and liabilities. During the three months ended June 30, 2006, our operations used $599,000 of cash, primarily as a result of increases in prepayments, accounts payable and accrued expenses due to the timing of payments.

Our investing activities for the three months ended June 30, 2007 and 2006, consisted entirely of purchases of property and equipment, which aggregated $137,000 and $142,000, respectively.

Cash provided by financing activities was $453,000 in the three months ended June 30, 2007, which was largely the result of $726,000 in proceeds from the exercise of outstanding stock options to purchase our common stock, partially offset by net payments on borrowings of $273,000. During the three months ended June 30, 2006, financing activities provided $835,000 of cash, which was comprised of net borrowings of $667,000 and cash inflows of $168,000 from the exercise of outstanding stock options to purchase our common stock.

Borrowings

The following table summarizes our borrowings and long-term debt:

	At June 30, 2007 (In thousands)
Convertible debentures, net	$ 9,462
Line of credit	4,437
Bank term note	1,258
Promissory note to landlord	323
Other	68
	$ 15,548

In October 2006, we replaced our former credit facility and entered into a new two-year credit facility with a different bank. The facility provides for combined line of credit and bank term note borrowings of up to $8.0 million. Under the new credit facility, we may borrow against our eligible accounts receivable and eligible inventory, as defined in the credit agreement. Interest on borrowed amounts is payable monthly at the current stated prime rate plus 1.25%. Additionally, we are obligated to pay an unused line fee of 0.25% per annum applied to the amount by which the maximum credit amount exceeds the average daily principal balance during the preceding month. The new credit facility requires $2,000 in monthly collateral management fees and includes an early termination fee equal to 2% of the total facility during the first year of the agreement and 1% of the total facility in the second year of the agreement. Additionally, we paid a commitment fee of $40,000 in October 2006 and are obligated to pay an additional $40,000 on the one year anniversary of the facility. The new credit facility is secured by substantially all of the assets of the Company. At June 30, 2007, we had $8.0 million available under our credit facility, of which $2.3 million was unused.

We believe that the cash generated from our operations, together with funds available under our credit agreement, will be sufficient to fund our operations for at least the next twelve months. However, should a shortfall occur, we may need to raise additional funds through other debt financings or the sale of equity securities.

Contractual Obligations

Our contractual obligations are as follows at June 30, 2007:

	Payments Due by Period						
	2008	2009	2010	2011	2012	Thereafter	Total
	(In thousands)						
Lines of credit	$ 4,437	$	$	$	$	$	$ 4,437
Notes payable	1,299	350					1,649
Convertible debentures			9,850				9,850
Operating leases	883	1,398	1,391	1,348	1,332	3,823	10,175
Total	$ 6,619	$ 1,748	$ 11,241	$ 1,348	$ 1,332	$ 3,823	$ 26,111

At June 30, 2007, we had firm commitments to purchase inventory in the amount of $3.2 million during our next two fiscal quarters.

Off Balance Sheet Arrangements

In May 2004, we issued subordinated convertible debentures in an aggregate original principal amount of $10.1 million. These debentures are due in full on May 19, 2009 and are convertible into shares of our common stock at an initial conversion price of $3.61 per share. At June 30, 2007, $9.9 million of these convertible debentures remained outstanding. Because these debentures are conventionally convertible, we have not separately accounted for the conversion feature and, accordingly, no separate amounts are presented in our condensed consolidated financial statements in connection with this conversion feature.

At June 30, 2007, outstanding warrants to purchase an aggregate of 62,500 shares of our common stock at an exercise price of $1.95 per share and outstanding warrants to purchase an aggregate of 246,250 shares of our common stock at an exercise price of $3.25 were callable by us if the closing sales price of our common stock for 20 consecutive days is equal to or greater than two times the exercise price of the warrants. Outstanding warrants to purchase an aggregate of 75,000 shares of our common stock at an exercise price of $5.00 per share were callable by us if the price of our common stock for 20 consecutive days is equal to or greater than one and a half times the exercise price of the warrants.

In connection with warrants to purchase 246,250 shares of our common stock at $3.25 per share, we are a party to certain registration rights agreements that contain provisions under which we could be subjected to liquidated damages should we fail to maintain effective registration statements for the underlying shares of common stock. These warrants have been accounted for within equity in our condensed consolidated balance sheets in accordance with EITF 00-19, *Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company s Own Stock*, and, accordingly, no liabilities have been recorded in connection therewith. As of the date of this filing, no liquidated damages are payable under the provisions of the registration rights agreements associated with these warrants.

Recent Accounting Pronouncements

In September 2006, the FASB issued SFAS 157, which defines fair value, establishes a framework for measuring fair value, and expands disclosure about fair value measurements. SFAS 157

does not require any new fair value measurements; rather it specifies valuation methods to be applied when fair value measurements are required under existing or future accounting pronouncements. SFAS 157 is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Early application of the statement is encouraged. Generally, this statement will be applied prospectively. We are currently evaluating the impact of SFAS 157 and expect to adopt SFAS 157 in the first quarter of our fiscal year ending March 31, 2009.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115* (SFAS 159). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. Unrealized gains and losses on items for which the fair value option has been elected will be recognized in earnings at each subsequent reporting date. SFAS 159 is effective for financial statements issued for fiscal years beginning after November 15, 2007. We are evaluating the impact that the adoption of SFAS 159 will have on our results of operations and financial condition and expect to adopt SFAS 159 in our fiscal year ending March 31, 2009.

Seasonality

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

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our exposure to interest rate risk is limited to our line of credit, bank term note and a promissory note to our landlord. Our line of credit, bank term note and promissory note to our landlord bear interest based on the prevailing prime rate (8.25% at June 30, 2007). We do not believe that a 10% increase in the interest rate on our line of credit, bank term note and promissory note to our landlord (from 9.50% to 10.45% on the line of credit, from 9.50% to 10.45% on the bank term note and from 10.25% to 11.28% on the promissory note to our landlord) would have a material impact on our financial position, operating results or cash flows. In addition, we believe that the carrying value of our outstanding debt approximates fair value.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this report, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and our Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures, as such term is defined in Exchange Act Rules 13a-15(e) and 15d-15(e). Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission s rules and forms and are effective in ensuring that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, our management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. Our management necessarily applied its judgment in evaluating the cost-benefit relationship of such controls and procedures.

Changes in Internal Controls

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

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The information set forth under Note 5 of Notes to Unaudited Condensed Consolidated Financial Statements, included in Part I, Item I of this report, is incorporated herein by reference.

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.

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 generated significant net losses and operating losses in recent periods, and have experienced volatility in our cash flows from operations ranging from positive cash flows from operations of $590,000 in the year ended March 31, 2005 to negative cash flows from operations of $2.0 million in the year ended March 31, 2007. Additionally, we failed to meet certain debt covenants under our prior credit agreement in two of our last seven fiscal quarters, but replaced that credit facility in October 2006. Furthermore, we have $9.9 million in subordinated convertible debentures that are due in full in May 2009. Should the holders of the convertible debentures not elect to convert the principal into shares of our common stock, we may need to raise additional capital to refinance this debt.

At June 30, 2007, we had $2.2 million of cash and cash equivalents and relied on our line of credit to fund our operations. We may need to raise additional capital in the near future to fund our operations or to repay indebtedness. Such additional capital may be raised through bank borrowings, or other debt or equity financings. We cannot assure you that any additional capital will be available on a timely basis, on acceptable terms, or at all, 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 generate net income;
- increased research and development expenses;
- increased sales and marketing expenses;
- technological advancements and our competitors response to our products;
- capital improvements to new and existing facilities and enhancements to our infrastructure and systems;
- potential acquisitions of businesses and product lines;

- our relationships with customers and suppliers;

- government budgets, political agendas and other funding issues, including potential delays in government contract awards;

- our ability to successfully negotiate credit arrangements with our bank; and

- general economic conditions, including the effects of the current economic slowdown and international conflicts.

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

We Have Historically Experienced Substantial Losses And May Experience Losses In The Future. Although we have achieved net income in recent periods, we experienced a net loss of $11.3 million in the year ended March 31, 2005. We cannot assure you that we will be able to sustain or improve our financial performance, or that we will be able to continue to achieve profitability on a quarterly or annual basis in the future. Most of our expenses are fixed in advance. As such, we generally are unable to reduce our expenses significantly in the short-term to compensate for any unexpected delay or decrease in anticipated revenues. As a result, we may continue to experience operating losses and net losses, which would make it difficult to fund our operations and achieve our business plan, and could cause the market price of our common stock to decline.

We Plan to Relocate Our Corporate Headquarters in September 2007, Which Could Result in Significant Business Disruptions. The lease for our current headquarters in Anaheim, California terminates in September 2007. In May 2007, we entered into an agreement to lease space in Santa Ana, California beginning in September 2007. We expect to relocate our headquarters to this location by the end of September 2007. Should any portion of this relocation effort not proceed as expected and in the timeframe planned, we could experience a disruption in our operations, which could ultimately adversely affect our financial results.

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. Along with our independent registered public accounting firm, we will be evaluating the effectiveness of our internal controls over financial reporting to comply with Section 404 of the Sarbanes-Oxley Act of 2002. Section 404 currently requires us to evaluate the effectiveness of our internal controls over financial reporting at the end of each fiscal year beginning in our fiscal year ending March 31, 2008 and to include a management report assessing the effectiveness of our internal controls over financial reporting in all annual reports beginning with our Annual Report on Form 10-K for the fiscal year ending March 31, 2008. Section 404 also requires our independent accountant to attest to, and report on, management s assessment of our internal controls over financial reporting beginning in our fiscal year ending March 31, 2009. We may not be able to complete our Section 404 compliance on a timely basis, and even if we timely complete our compliance requirements, our independent auditors may still conclude that our internal controls over financial reporting are not effective.

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

As of March 31, 2005, we became aware of a material weakness in our internal controls related to the accounting for the consolidation of our deferred compensation savings plan and certain contract administration. We cannot assure you that we or our independent registered public accounting firm will not identify additional material weaknesses in our internal controls. A material weakness is a control deficiency, or combination of control deficiencies, that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected. Based on our evaluation, our management concluded that, as of March 31, 2004, our internal control over financial reporting

was not effective due to the existence of one material weakness. We may experience additional material weaknesses in the future. If our internal controls over financial reporting are not considered adequate, we may experience a loss of public confidence, which could have an adverse effect on our business and our stock price.

New Environmental Regulations May Result In A Decline In Our AutoVue Sales and Royalties. Recent environmental regulations in Europe became effective in 2006, which required more stringent emissions compliance in new trucks manufactured in Europe after 2006. These regulations caused the cost of certain trucks to increase significantly and could cause a decline in new truck sales in Europe in the near future. Similar regulations have been announced in North America that will impact diesel engines built after January 2007. North America heavy truck sales through the first half of 2007 have declined significantly versus the prior year, which we believe was primarily a result of large 2006 prebuys of heavy trucks made in anticipation of the new North America emission standards. We may experience a decline in our LDW sales to truck OEMs related to these stricter regulations.

We May Experience Production Gaps Which Could Materially And Adversely Impact Our Sales And Financial Results And The Ultimate Acceptance Of Our Products. It is possible that we could experience unforeseen quality control issues or part shortages as we increase production to meet current demand for our products. We have historically used single suppliers for certain of our components in our AutoVue and Vantage products. Should any such delay or disruption occur, our future sales will likely be materially and adversely affected. Additionally, we rely heavily on select contract manufacturers to produce many of our products. Although we believe our contract manufacturers have sufficient capacity to meet our production schedules for the foreseeable future and we believe we could find alternative contract manufacturing sources if necessary, we could experience a production gap if for any reason our contract manufacturers were unable to meet our production requirements.

We Depend Upon Valeo To Market Our AutoVue Technologies For The OEM Passenger Car Market. We have granted Valeo the exclusive right to sell and manufacture our AutoVue LDW system to the worldwide passenger car market in exchange for royalty payments for each AutoVue unit sold. As such, the future success and broad market acceptance of our AutoVue technologies in the passenger car market will depend upon Valeo s ability to manufacture, market and sell our technologies, and to convince more OEM passenger car manufacturers to adopt our technologies. If Valeo does not devote considerable resources and aggressively pursue opportunities, our expansion into the passenger car market could be adversely affected.

We May Be Unable To Attract And Retain Key Personnel, Which Could Seriously Harm Our Business. Due to the specialized nature of our business, we are highly dependent on the continued service of our executive officers and other key management, engineering and technical personnel. The loss of Abbas Mohaddes, our Chief Executive Officer, or any of the other executive officers or key members of management could adversely affect our business, financial condition or results of operations. Our success will also depend in large part upon our ability to continue to attract, retain and motivate qualified engineering and other highly skilled technical personnel. In particular, the future success of our Transportation Systems segment will depend on our ability to hire additional qualified engineers and planners. Competition for qualified employees, particularly development engineers, is intense. We may not be able to continue to attract and retain sufficient numbers of such highly skilled employees. Our inability to attract and retain additional key employees or the loss of one or more of our current key employees could adversely affect our business, financial condition and results of operations.

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

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

Market acceptance of our new products depends upon many factors, including our ability to accurately predict market requirements and evolving industry standards, our ability to resolve technical challenges in a timely and cost-effective manner, qualify any new products with OEMs and achieve manufacturing efficiencies, the perceived advantages of our new products over traditional products and the marketing capabilities of our independent distributors and strategic partners, including Valeo s ability to expand sales of AutoVue in the passenger car market. The success of our AutoVue system will

also depend in part on the success of the automotive vehicles that incorporate our technology, as well as the success of optional equipment that OEMs bundle with our technologies.

Certain of the components used in our Vantage and AutoVue products may need to be re-engineered in the next 12 to 36 months as the industry is moving towards a standard of using lead-free components. We cannot assure you as to the timing of the adoption of this new standard or our ability to successfully redesign our products to incorporate compliant components and gain market acceptance of such redesigned products. In addition, if the standard is adopted earlier than anticipated we may experience a shortage of Vantage and AutoVue products as a result of potential scarcity of lead-free components.

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

The Markets In Which We Operate Are Highly Competitive And Have Many More Established Competitors, Which Could Adversely Affect Our Sales Or The Market Acceptance Of Our Products. We compete with numerous other companies in our target markets including, but not limited to, large, multinational corporations, which include tier one automotive suppliers, and many smaller regional engineering firms. We expect such competition to increase due to technological advancements, industry consolidations and reduced barriers to entry. Increased competition is likely to result in price reductions, reduced gross margins and loss of market share, any of which could seriously harm our business, financial condition and results of operations. In Fiscal 2007, we began to experience more competition in our Roadway Sensors segment as the Department of Transportation in one of our largest sales territories moved to a multi-source contracting environment from one in which Iteris was the sole supplier. In addition, one of the other developers of LDW systems was acquired by a larger company during Fiscal 2007. While this developer has not been a material competitor to date, we may experience more competition from this provider as a result of its greater access to resources from its acquirer, and additional competitors may enter this market in the future. Furthermore, awareness of LDW technology is increasing and other market players are attempting to develop competing technologies, which may contain improvements or added features beyond those offered by our LDW systems. Should such efforts be successful, this could erode our ability to successfully market and sell our LDW systems.

Many of our competitors have far greater name recognition and greater financial, technological, marketing and customer service resources than we do. This may allow them to respond more quickly to new or emerging technologies and changes in customer requirements. It may also allow them to devote greater resources to the development, promotion, sale and support of their products than we can. Recent consolidations of end users, distributors and manufacturers in our target markets have exacerbated this problem. As a result of the foregoing factors, we may not be able to compete effectively in our target markets and competitive pressures could adversely affect our business, financial condition and results of operations.

An Economic Slowdown Or The Significant Military Operations In The Middle East Or Elsewhere May Impact Government Funding Or Consumer Spending, Causing A Decline In Our Revenues. In the near term, the funding of U.S. military operations in the Middle East or elsewhere may cause disruptions in funding of government contracts. Since military operations of such magnitude are not routinely included in U.S. defense budgets, supplemental legislative funding actions are often required to finance such operations. Even when such legislation is enacted, it may not be adequate for ongoing operations, causing other government resources to be temporarily or permanently diverted. Since a significant portion of our sales are derived from contracts with government agencies, such diversion of funds could produce interruptions in funding or delays in receipt of our contracts, causing disruptions and adversely effecting our revenue and operations.

Concerns about the recent international conflicts and terrorist and military actions, as well as concerns about inflation, decreased consumer confidence, and reduced corporate profits and capital spending have also resulted in a downturn in worldwide economic conditions, particularly in the United States. These unfavorable economic conditions may have a negative impact on customer orders (and also may result in decreased sales of automobiles and trucks that incorporate our LDW systems). Such concerns may result in cancellations and rescheduling of backlog. In addition, the recent decline in the U.S. real estate market, particularly in new home construction, could adversely impact new road construction

resulting in a decline in Roadway Sensor and Automotive Sensor net sales and Transportation Systems contract revenues. Any of the

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foregoing political, social and economic conditions make it extremely difficult for our customers, our suppliers and us to accurately forecast and plan future business activities and could result in a decline in our net sales and contract revenues. If such conditions continue or worsen, our business, financial condition and results of operations could be materially and adversely affected.

We Depend On Government Contracts And Subcontracts, And Because Many Of Our Government Contracts Are Fixed Price Contracts, Higher Than Anticipated Costs Will Reduce Our Profit And Could Adversely Impact Our Operating Results. A significant portion of our sales are derived from contracts with governmental agencies, either as a general contractor, subcontractor or supplier. Government contracts represented approximately 37.8%, 38.3% and 37.4% of our total net sales and contract revenues for the years ended March 31, 2007, 2006 and 2005, respectively. We anticipate that revenue from government contracts will continue to increase in the near future. Government business is, in general, subject to special risks and challenges, including:

- long purchase cycles or approval processes;
- competitive bidding and qualification requirements;
- the impact of international conflicts;
- performance bond requirements;
- changes in government policies and political agendas;
- delays in funding, including the delays in the allocation of funds to state and local agencies from the U.S. Federal Highway Bill;
- other government budgetary constraints and cut-backs; and
- milestone requirements and liquidated damage provisions for failure to meet contract milestones.

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

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:

- changes in our pricing policies and the pricing policies of our suppliers and competitors, pricing concessions on volume sales, as well as increased price competition in general;
- the long lead times associated with government contracts or required by vehicle manufacturers;
- delays in government contracts from time to time, including from delays in the allocation of funds to state and local agencies from the U.S. Federal Highway Bill;
- our ability to raise additional capital;
- our ability to control costs;
- the mix of our products and services sold in a quarter, which mix has varied and is expected to continue to vary from time to time;
- seasonality due to winter weather conditions;
- international conflicts and acts of terrorism;
- declines in new home construction and related road construction;
- 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 size, timing, rescheduling or cancellation of significant customer orders;
- the introduction of new products by competitors;
- the availability and cost of components used in the manufacture of our products;
- our success in expanding and implementing our sales and marketing programs;
- the effects of technological changes in our target markets;
- the amount of our backlog at any given time;
- the nature of our government contracts;
- deferrals of customer orders in anticipation of new products, applications or product enhancements;
- risks and uncertainties associated with our international business;
- currency fluctuations and our ability to get currency out of certain foreign countries; and
- general economic and political conditions.

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

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

- potential disruption of our ongoing business and the diversion of our resources and management s attention;
- the failure to retain or integrate key acquired personnel;
- the challenge of assimilating diverse business cultures, and the difficulties in integrating the operations, technologies and information system of the acquired companies;
- increased costs to improve managerial, operational, financial and administrative systems and to eliminate duplicative services;
- the incurrence of unforeseen obligations or liabilities;
- potential impairment of relationships with employees or customers as a result of changes in management; and
- increased interest expense and amortization of acquired intangible assets.

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

We Have Experienced Growth In Recent Periods. If We Fail To Manage Our Growth Effectively, We May Be Unable To Execute Our Business Plan And May Experience Future Weaknesses In Our Internal Controls. We have expanded our overall business. In order to achieve our business objectives, we will need to continue to expand our business and add additional qualified personnel. Such expansion has placed and is expected to continue to place, a significant strain on our managerial, administrative, operational, financial and other resources. If we are unable to successfully manage our growth, our business, financial condition and results of operations will be adversely affected.

To accommodate this growth, we launched a new ERP system in April 2006. Accordingly, we may experience problems commonly experienced by other companies in connection with such implementations, including but not limited to, potential bugs in the system, component or supply delays, training requirements and other integration challenges and delays. Any difficulties we might experience in connection with our new ERP system could have a material adverse effect on our financial reporting system and internal controls.

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

- rapid technological advances;
- downward price pressure in the marketplace as technologies mature;
- changes in customer requirements;

- frequent new product introductions and enhancements; and
- evolving industry standards and changes in the regulatory environment.

Our future success will depend upon our ability to anticipate and adapt to changes in technology and industry standards, and to effectively develop, introduce, market and gain broad acceptance of new products and product enhancements incorporating the latest technological advancements. In particular, our LDW system is incorporated into automobiles and trucks that face significant technological changes in each model year and among different vehicle models. Accordingly, we must adapt our technology from time to time to function with such changes.

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

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

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

- quarterly variations in operating results;
- our ability to control costs, improve cash flow and sustain profitability;
- our ability to raise additional capital;
- shortages announced by suppliers;
- announcements of technological innovations or new products or applications by our competitors, customers or us;
- transitions to new products or product enhancements;
- acquisitions of businesses, products or technologies;
- the impact of any litigation;
- changes in investor perceptions;
- government funding, political agendas and other budgetary issues;

- changes in earnings estimates or investment recommendations by securities analysts; and
- international conflicts, political unrest and acts of terrorism.

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

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

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

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

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

We Could Experience Negative Financial Impacts Arising From Developments In Contingencies Created Under Our Previous Structure Or By Former Subsidiaries. Although we divested ourselves of all business units prior to October 2004, with the exception of our Iteris business, from time to time we could experience unforeseen developments in contingencies related to our former subsidiaries. For example, in July 2006 we entered into a settlement agreement in connection with a lawsuit brought against Mariner Networks, Inc., one of our former subsidiaries, by one of Mariner s suppliers, pursuant to which we issued 88,912 shares of our common stock to this supplier (valued at $213,000 as of the date of issuance), paid this supplier $125,000 on October 20, 2006 and are required to pay an additional $350,000 in 36 equal monthly installments of $9,700 beginning in November 2006. Although we are not aware of any other material contingencies, it is possible that other matters could be brought against us in connection with activities related to former subsidiaries and that such matters could materially and adversely affect our financial results and cash flows.

Some Of Our Directors, Officers And Their Affiliates Can Control The Outcome Of Matters That Require The Approval Of Our Stockholders, And Accordingly We Will Not Be Able To Engage In Certain Transactions Without Their Approval. As of June 30, 2007, our officers and directors beneficially owned approximately 11% of the outstanding shares of our common stock (and approximately 17% of our common stock when including options, warrants and

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other convertible securities held by them which are currently exercisable or convertible or will become exercisable or convertible within 60 days after June 30, 2007). As a result of their stock ownership, our management will be able to influence the election of our directors and the outcome of corporate actions requiring stockholder approval, such as mergers and acquisitions, regardless of how our other stockholders may vote. This concentration of voting control may have a significant effect in delaying, deferring or preventing a change in our management or change in control and may adversely affect the voting or other rights of other holders of common stock.

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

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

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

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

None.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

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

Exhibit Number	Description	Where Located
3.1	Amended and Restated Certificate of Incorporation of the registrant	*Exhibit 3.1 to the registrant s current report on Form 8-K as filed with the SEC on October 28, 2004*
3.2	Bylaws of registrant, as amended	*Exhibit 4.2 to the registrant s Registration Statement on Form S-1 (Reg. No. 033-67932) as filed with the SEC on July 6, 1993*
3.3	Certificates of Amendment to Bylaws of the registrant dated April 24, 1998 and August 10, 2001	*Exhibit 3.4 to the registrant s Annual Report on Form 10-K/A for the year ended March 31, 2003 as filed with the SEC on July 29, 2003*
3.4	Certificate of Amendment to Bylaws of registrant dated September 9, 2004	*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

4.1	Specimen of Common Stock Certificate	*Exhibit 4.1 to the registrant s Amendment No. 1 to the Registration Statement on Form 8-A as filed with the SEC on December 8, 2004*
4.2	Amended and Restated Rights Agreement, dated as of May 10, 2004, by and between the registrant and U.S. Stock Transfer Corporation, including exhibits thereto	*Exhibit 99.1 to the registrant s Registration Statement on Form 8-A/A as filed with the SEC on June 18, 2004*
10.1	Sublease Agreement, dated September 30, 2003, by and between Odetics, Inc. and Maij, Inc.	*Filed herewith*
10.2	Office Lease Agreement, dated May 24, 2007, by and between Crown Carnegie Associates, LLC and Iteris, Inc.	*Filed herewith*
10.3	Termination Agreement, dated May 30, 2007, by and among Transportation Planning Group, Inc., Abbas Mohaddes and Iteris, Inc.	*Filed herewith*
31.1	Certification of the Principal Executive Officer, as required pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	*Filed herewith*
31.2	Certification of the Principal Financial and Accounting Officer, as required pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	*Filed herewith*
32.1	Certification of the Chief Financial Officer, as required pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	*Filed herewith*
32.2	Certification of the Chief Financial Officer, as required pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	*Filed herewith*

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Dated: August 13, 2007

ITERIS, INC.
(Registrant)

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

By /s/ JAMES S. MIELE
James S. Miele
Chief Financial Officer
(Principal Financial and Accounting Officer)