ITERIS, INC.
Form 10-K
June 07, 2018

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended March 31, 2018

OR

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 (State or Other Jurisdiction of Incorporation or Organization)	**95-2588496** (I.R.S. Employer Identification No.)
1700 Carnegie Ave., Santa Ana, California (Address of Principal Executive Offices)	**92705** (Zip Code)

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

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

Title of each class	**Name of each exchange on which registered**
Common Stock, $0.10 par value	The NASDAQ Stock Market LLC

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

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act of 1933, as amended (the "Securities Act"). Yes o No ý

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

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 ý No o

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

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

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

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

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

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

The aggregate market value of the registrant's common stock held by nonaffiliates of the registrant as of September 30, 2017 was approximately $147,100,000. For the purposes of this calculation, shares owned by officers, directors and 10% stockholders known to the registrant have been deemed to be owned by affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes. As of May 29, 2018, there were 33,203,740 shares of our common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

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

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ITERIS, INC.
ANNUAL REPORT ON FORM 10-K
FOR THE FISCAL YEAR ENDED MARCH 31, 2018
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Unless otherwise indicated in this report, the "Company," "we," "us" and "our" refer to Iteris, Inc. and its wholly-owned subsidiary, ClearAg, Inc. CheckPoint , ClearAg®, ClearPath Weather®, CVIEW-Plus , Edge®, EdgeConnect , EMPower®, EvapoSmart , IMFocus , inspect , iPeMS®, Iteris®, Next®, P10 , P100 , PedTrax®, Pegasus , SmartCycle®, SmartSpan®, TransitHelper®, UCRLink , Vantage®, VantageLive! , VantageNext®, VantagePegasus®, VantageRadius , Vantage Vector®, VantageView , Velocity®, VersiCam and WeatherPlot are among, but not all of, the trademarks of Iteris, Inc. Any other trademarks or trade names mentioned herein are the property of their respective owners.

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Cautionary Statement

This report, including the following discussion and analysis, contains forward-looking statements (within the meaning of the Private Securities Litigation Reform Act of 1995) that are based on our current expectations, estimates and projections about our business and our industry, and reflect management's beliefs and certain assumptions made by us based upon information available to us as of the date of this report. When used in this report and the information incorporated herein by reference, the words "expect(s)," "feel(s)," "believe(s)," "intend(s)," "plan(s)," "should," "will," "may," "anticipate(s)," "estimate(s)," "could," "should," and similar expressions or variations of these words are intended to identify forward-looking statements. These forward-looking statements include, but are not limited to, statements regarding our anticipated growth, sales, revenue, expenses, profitability, capital needs, backlog, manufacturing capabilities, the market acceptance of our products, competition, the impact of any current or future litigation, the impact of recent accounting pronouncements, the applications for and acceptance of our products and services, and the status of our facilities and product development. These statements are not guarantees of future performance and are subject to certain risks and uncertainties that could cause our actual results to differ materially from those projected. You should not place undue reliance on these forward-looking statements that speak only as of the date hereof. We encourage you to carefully review and consider the various disclosures made by us which describe certain factors which could affect our business, including in "Risk Factors" set forth in Part I, Item 1A of this report, before deciding to invest in our company or to maintain or increase your investment. We undertake no obligation to revise or update publicly any forward-looking statement for any reason, including to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

PART I

ITEM 1. BUSINESS

Overview

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

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

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

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

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

Iteris was incorporated in Delaware in 1987. Our principal executive offices are located at 1700 Carnegie Avenue, Santa Ana, California 92705, and our telephone number at that location is

(949) 270-9400. Our website address is www.iteris.com. The inclusion of our website address in this report does not include or incorporate by reference into this report any information on, or accessible through, our website. Our annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K, together with amendments to these reports, are available on the "Investor Relations" section of our website, free of charge, as soon as reasonably practicable after such material is electronically filed with, or furnished to, the U.S. Securities and Exchange Commission ("SEC").

Recent Developments

ClearAg, Inc.

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

Products and Services

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

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

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

Roadway Sensors

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

Our Vantage detection systems detect vehicle presence at intersections, as well as vehicle count, speed and other traffic data used in traffic management systems. Vantage detection systems typically include up to four of our advanced cameras or radar devices. Our Vantage systems give traffic managers the tools to mitigate roadway congestion by visualizing and analyzing traffic patterns allowing them to modify traffic signal timing to improve traffic flow. Our various software components complement our Vantage detection systems by providing integrated platforms to manage and view detection assets remotely over a network connection, as well as mobile application for viewing anywhere.

Our Vantage Vector video/radar hybrid product is an all-in-one detection sensor with a wide range of capabilities, including stop bar and advanced zone detection, which enable advanced safety and adaptive control applications. Vantage Vector includes all of the benefits of Iteris video detection, including high accuracy, high-availability remote viewing of video images, bicycle and pedestrian detection capability, and dilemma-zone detection.

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VantageLive! is a cloud-based platform that allows users to collect, process and analyze advanced intersection data, as well as to view and understand intersection activity.

All of our Vantage systems are available with SmartCycle capability, which can effectively differentiate between bicycles and other vehicles with a single video detection camera, enabling more efficient signalized intersections, improved traffic throughput and increased bicyclist safety. Agencies using bicycle timing can now benefit from bicycle-specific virtual detection zones that can be placed anywhere within the approaching traffic lanes, eliminating the need for separate bicycle-only detection systems.

The SmartCycle Bike Indicator, which leverages the SmartCycle bicycle detection algorithm, is a device that mounts onto traffic signals and illuminates when cyclists waiting at an intersection have been detected, allowing cyclists to avoid interacting with vehicle traffic to push pole-mounted buttons.

Our Vantage systems are also available with the PedTrax capability, which provides bi-directional counting and speed tracking of pedestrians within the crosswalk to help improve signal timing efficiency, as well as providing an additional data stream to existing vehicle and bicycle counts.

VersiCam, our integrated camera and processor video detection system, is a cost-efficient video detection system for smaller intersections that require only a few detection points.

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

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

Transportation Systems

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

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

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

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

Agriculture and Weather Analytics

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

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

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

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

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

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

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

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

Sales and Marketing

We currently sell our Roadway Sensors products through both direct and indirect sales channels. In the territories where we sell direct, we use a combination of our own sales personnel and outside sales organizations to sell, oversee installations and set-up issues, and support our products. Our indirect sales channel is comprised of a network of independent distributors in the U.S. and select international locations, which sell integrated systems and related products to the traffic management market. In the fourth quarter of our fiscal year ended March 31, 2018 ("Fiscal 2018"), we entered into a distribution agreement to expand our northern European sales coverage in the U.K. and Ireland. Our independent distributors are trained in, and primarily responsible for, sales, installation, set-up and support of our products, maintain an inventory of demonstration traffic products from various manufacturers, and sell directly to government agencies and installation contractors. These distributors often have long-term arrangements with local government agencies in their respective territories for the supply of various products for the construction and renovation of traffic intersections, and are generally well-known suppliers of various high-quality ITS products to the traffic management market. We periodically hold technical training classes for our distributors and end users, and maintain a full-time staff of customer support technicians throughout the U.S. to provide technical assistance when needed. When appropriate, we have the ability to modify or make changes to our distributor network to accommodate the needs of the market and our customer base.

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

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

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

Manufacturing and Materials

We use contract manufacturers to build subassemblies that are used in our Roadway Sensors products. Additionally, we procure certain components for our Roadway Sensors products from qualified suppliers, both in the U.S. and internationally, and generally use multi-sourcing strategies when technically and economically feasible to mitigate supply risk. These subassemblies and components are typically delivered to our Santa Ana, California facility, where they go through final assembly and testing prior to shipment to our customers. Our key suppliers include Veris Manufacturing, MoboTrex, Inc. and Sony Electronics, Inc. Our manufacturing activities are conducted in approximately 9,000 square feet of space at our Santa Ana, California facility. Production volume at

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our subcontractors is based upon quarterly forecasts that we generally adjust on a monthly basis to control inventory levels. We typically do not manufacture any of the hardware used in the transportation management and traveler information systems that we design and implement. Our production facility is currently ISO 9001 certified.

Customer Support and Services

We provide warranty service and support for our products, as well as follow-up service and support for which we charge separately. Such service revenue was not a material portion of our total revenues for Fiscal 2018, Fiscal 2017 and the fiscal year ended March 31, 2016 ("Fiscal 2016"). We believe customer support is a key competitive factor for our company.

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

Backlog

Our total backlog of unfulfilled firm orders was approximately $47.5 million as of March 31, 2018, which included $37.7 million related to Transportation Systems. We typically recognize approximately 70% of our Transportation Systems backlog as of the end of a fiscal year in the subsequent fiscal year, and currently expect that trend to continue for the near future for both Transportation Systems and Agriculture and Weather Analytics. Substantially the entire backlog for Roadway Sensors as of March 31, 2018 is expected to be recognized as revenue in the fiscal year ending March 31, 2019. At March 31, 2017, we had backlog of approximately $64.5 million, which included $54.4 million related to Transportation Systems. The decline in backlog in the current fiscal year was largely due to the completion of a large Transportation Systems contract in the current fiscal year.

The timing and realization of our backlog is subject to the inherent uncertainties of doing business with federal, state and local governments, particularly in view of budgetary constraints, cut-backs and other delays or reallocations of funding that these entities typically face. In addition, pursuant to the customary terms of our agreements with government contractors and other customers, our customers can generally cancel or reschedule orders with little or no penalties. Lead times for the release of purchase orders often depend upon the scheduling and forecasting practices of our individual customers, which also can affect the timing of the conversion of our backlog into revenues. For these reasons, among others, our backlog at a particular date may not be indicative of our future revenues, in particular for our Roadway Sensors segment.

Product Development

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

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

Competition

We generally face significant competition in each of our target markets. Increased competition may result in price reductions, reduced gross margins and loss of market share, any of which could have a material adverse effect on our business, financial condition and results of operations.

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

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

The markets in which our Transportation Systems segment operate are highly fragmented and subject to evolving national and regional quality, operations and safety standards. Our competitors vary in number, scope and breadth of the products and services they offer. Our competitors in advanced transportation systems include large, national corporations that generally offer expertise in traveler information, integration and transportation management. Our competitors in transportation engineering, planning and design include major regional ITS engineering firms, as well as many smaller local engineering firms.

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

Intellectual Property and Proprietary Rights

Our ability to compete effectively depends in part on our ability to develop and maintain the proprietary aspects of our technology. Our policy is to obtain appropriate proprietary rights protection for any potentially significant new technology acquired or developed by us. We currently have a total of

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

In addition to patent laws, we rely on copyright and trade secret laws to protect our proprietary rights. We attempt to protect our trade secrets and other proprietary information through agreements with customers and suppliers, proprietary information agreements with our employees and consultants, and other similar measures. We do not have any material licenses or trademarks other than those relating to product names. We cannot be certain that we will be successful in protecting our proprietary rights. While we believe our patents, patent applications, software and other proprietary know-how have value, rapidly evolving technology makes our future success dependent largely upon our ability to successfully achieve continuing innovation.

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

Employees

As of March 31, 2018, we employed 414 full-time employees and 33 part-time employees, for a total of 447 employees. None of our employees are represented by a labor union, and we have never experienced a work stoppage. We believe our relations with our employees are good.

Government Regulation

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

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ITEM 1A. RISK FACTORS

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

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

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

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

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

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

We may not be able to achieve profitability on a quarterly or annual basis in the future. For Fiscal 2018 and Fiscal 2017, we had net losses of $3.5 million and $4.8 million, respectively, and we cannot assure you that we will be profitable in the future. Our ability to become profitable in future periods could be impacted by governmental budgetary constraints, government and political agendas, economic instability and other items that are not in our control. Furthermore, we rely on operating profits from certain of our business segments to fund investments in sales and marketing and research and development initiatives. We cannot assure you that our financial performance will sustain a sufficient level to completely support those investments. Most of our expenses are fixed in advance. As such, we generally are unable to reduce our expenses significantly in the short-term to compensate for any unexpected delay or decrease in anticipated revenues or increases in planned investments. As a result, we may continue to experience operating losses and net losses in the future, which would make it difficult to fund our operations and achieve our business plan, and could cause the market price of our common stock to decline.

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

- our ability to transition employees from completed projects to new assignments and to hire and assimilate new employees;
- our ability to forecast demand for our services and thereby maintain an appropriate headcount in our various regions;
- the timing of new contract awards or the completion of large contract;
- availability of funding or other budget issues;

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

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

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

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

If we do not keep pace with rapid technological changes and evolving industry standards, we will not be able to remain competitive, and the demand for our products will likely decline. Our markets are in general characterized by the following factors:

- rapid technological advances;

- downward price pressures in the marketplace as technologies mature;

- changes in customer requirements;

- additional qualification requirements related to new products or components;

- frequent new product introductions and enhancements;

- inventory issues related to transition to new or enhanced models; and

- evolving industry standards and changes in the regulatory environment.

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

If we are unable to develop and introduce new products and product enhancements successfully and in a cost-effective and timely manner, or are unable to achieve market acceptance of our new products, our operating results would be adversely affected. We believe our revenue growth and future operating results will depend on our ability to complete development of new products and enhancements, introduce these products in a timely, cost-effective manner, achieve broad market acceptance of these products and enhancements, and reduce our production costs. During the past two fiscal years, we have introduced both new and enhanced products across all segments. We cannot guarantee the success of these products, and we may not be able to introduce any new products or any enhancements to our existing products on a timely basis, or at all. In addition, the introduction of any new products could adversely affect the sales of certain of our existing products.

We believe that we must continue to make substantial investments to support ongoing research and development in order to develop new or enhanced products and software to remain competitive. We need to continue to develop and introduce new products that incorporate the latest technological advancements in outdoor image processing hardware, camera technologies, software and analysis in response to evolving customer requirements. We cannot assure you that we will be able to adequately

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

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

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

We compete with existing, well-established companies and technologies in our Roadway Sensors segment, both domestically and abroad. Only a portion of the traffic intersection market has adopted advanced above-ground detection technologies, and our future success will depend in part upon gaining broader market acceptance for such technologies. Certain technological barriers to entry make it difficult for new competitors to enter the market with competing video or other technologies; however, we are aware of new market entrants from time to time. Increased competition could result in loss of market share, price reductions and reduced gross margins, any of which could seriously harm our business, financial condition and results of operations.

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

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

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

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We may not be able to adequately protect or enforce our intellectual property rights, which could harm our competitive position. If we are not able to adequately protect or enforce the proprietary aspects of our technology, competitors may be able to access our proprietary technology and our business, financial condition and results of operations will likely be seriously harmed. We currently attempt to protect our technology through a combination of patent, copyright, trademark and trade secret laws, employee and third party nondisclosure agreements and similar means. Despite our efforts, other parties may attempt to disclose, obtain or use our technologies or systems. Our competitors may also be able to independently develop products that are substantially equivalent or superior to our products or design around our patents. In addition, the laws of some foreign countries do not protect our proprietary rights as fully as do the laws of the U.S. As a result, we may not be able to protect our proprietary rights adequately in the U.S. or abroad.

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

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

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

We may be unable to attract and retain key personnel, including senior management, which could seriously harm our business. Due to the specialized nature of our business, we are highly dependent on the continued service of our executive officers and other key management, engineering and technical

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personnel. We believe that our success will depend on the continued employment of a highly qualified and experienced senior management team and our ability to retain existing business and generate new business. The loss of any of our officers, or any of our other executives or key members of management could adversely affect our business, financial condition, or results of operations (e.g., loss of customers or loss of new business opportunities). Our success will also depend in large part upon our ability to continue to attract, retain and motivate qualified engineering and other highly skilled technical personnel. Particularly in highly specialized areas, it has become more difficult to retain employees and meet all of our needs for employees in a timely manner, which may adversely affect our growth in the current fiscal year and in future years. Although we intend to continue to devote significant resources to recruit, train and retain qualified skilled personnel, we may not be able to attract and retain these employees and therefore could impair our ability to perform our contractual obligations efficiently and timely meet our customers' needs and win new business, which could adversely affect our future results. The future success of our Transportation Systems segment will depend on our ability to hire additional qualified engineers, planners and technical personnel. The future success of our Agriculture and Weather Analytics segment will depend on our ability to hire additional software developers, qualified engineers and technical personnel. Competition for qualified employees, particularly development engineers and software developers, is intense. We may not be able to continue to attract and retain sufficient numbers of such highly skilled employees. Our inability to attract and retain additional key employees or the loss of one or more of our current key employees could adversely affect our business, financial condition and results of operations.

Our management information systems and databases could be disrupted by system security failures, cyber threats or by the failure of, or lack of access to, our Enterprise Resource Planning system. These disruptions could negatively impact our sales, increase our expenses and/or harm our reputation. Internal users and computer programmers may be able to penetrate, aka "hack", our network security and create system disruptions, cause shutdowns and/or misappropriate our confidential information or that of our employees and third parties. Therefore, we could incur significant expenses addressing problems created by security breaches to our network. We must, and do, take precautions to secure customer information and prevent unauthorized access to our databases and systems containing confidential information. Any data loss or information security lapses resulting in the compromise of personal information or the improper use or disclosure of confidential, sensitive or classified information could result in claims, remediation costs, regulatory sanctions against us, loss of current and future contracts and serious harm to our reputation. We operate our Enterprise Resource Planning system on a software-as-a-service platform, and we use this system for reporting, planning, sales, audit, customer relationship management, inventory control, loss prevention, purchase order management and business intelligence. Accordingly, we depend on this system, and the third-party provide of this service, for a number of aspects of our operations. If this service provider or this system fails, or if we are unable to continue to have access to this system on commercially reasonable terms, or at all, operations would be severely disrupted until an equivalent system could be identified, licensed or developed, and integrated into our operations. This disruption would have a material adverse effect on our business.

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

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

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

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

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

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

If our internal controls over financial reporting do not comply with the requirements of the Sarbanes-Oxley Act, our business and stock price could be adversely affected. Section 404 of the Sarbanes-Oxley Act of 2002 currently requires us to evaluate the effectiveness of our internal controls over financial reporting at the end of each fiscal year and to include a management report assessing the effectiveness of our internal controls over financial reporting in all annual reports. We are required to obtain our auditors' attestation pursuant to Section 404(b) of the Sarbanes-Oxley Act. Going forward, we may not be able to complete the work required for such attestation on a timely basis and, even if we timely complete such requirements, our independent registered public accounting firm may still conclude that our internal controls over financial reporting are not effective.

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

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

- delays in government contracts and funding from time to time and budgetary constraints at the federal, state and local levels;
- our ability to access stimulus funding, funding from the federal highway bill or other government funding;
- declines in new home and commercial real estate construction and related road and other infrastructure construction;
- changes in our pricing policies and the pricing policies of our suppliers and competitors, pricing concessions on volume sales, as well as increased price competition in general;
- the long lead times associated with government contracts;
- the size, timing, rescheduling or cancellation of significant customer orders;
- our ability to control costs;
- our ability to raise additional capital;

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the mix of our products and services sold in a quarter, which has varied and is expected to continue to vary from time to time;

seasonality due to winter weather conditions;

seasonality with respect to revenues from our ClearPath Weather and related weather forecasting services due to the decrease in revenues generated for such services during the spring and summer time periods;

our ability to develop, introduce, patent, market and gain market acceptance of new products, applications and product enhancements in a timely manner, or at all;

market acceptance of the products incorporating our technologies and products;

the introduction of new products by competitors;

the availability and cost of components used in the manufacture of our products;

our success in expanding and implementing our sales and marketing programs;

the effects of technological changes in our target markets;

the amount of our backlog at any given time;

the nature of our government contracts;

decrease in revenues derived from key or significant customers;

deferrals of customer orders in anticipation of new products, applications or product enhancements;

risks and uncertainties associated with our international business;

market condition changes such as industry structure consolidations that could slow down our ability to procure new business;

general economic and political conditions;

international conflicts and acts of terrorism; and other factors beyond our control, including but not limited to, natural disasters.

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

We rely on outside suppliers that could experience supply shortages or may experience production gaps that could materially and adversely impact our sales and financial results. It is possible that we could experience unforeseen quality control issues or part shortages as we adjust production to meet current demand for our products. We have historically used single suppliers for certain significant components in our products, and have had to reengineer products from time to time to address obsolete components, especially in our Roadway Sensors products. Should any such delay or disruption occur, or should a key supplier discontinue operations, our future sales will likely be materially and adversely affected. Additionally, we rely heavily on select contract manufacturers to produce many of our products and do not have any long-term contracts to guarantee supply of such products. Although we believe our contract manufacturers have sufficient capacity to meet our production schedules for the foreseeable future and we believe we could find alternative contract manufacturing sources for many of our products, if necessary, we could experience a production gap if for any reason our contract

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manufacturers were unable to meet our production requirements and our cost of goods sold could increase, adversely affecting our margins.

We may engage in acquisitions of companies or technologies that may require us to undertake significant capital infusions and could result in disruptions of our business and diversion of resources and management attention. We have completed two acquisitions since November 2011 and, in the future, we may acquire additional complementary businesses, products, and technologies. Acquisitions may require significant capital infusions and, in general, acquisitions also involve a number of special risks, including:

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

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

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

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

- unexpected changes in regulatory requirements, tariffs and other trade barriers or restrictions;
- required compliance with existing and new foreign regulatory requirements and laws, more restrictive labor laws and obligations, including but not limited to the U.S. Foreign Corrupt Practices Act;
- difficulties in managing and staffing international operations;
- potentially adverse tax consequences; and
- reduced protection for intellectual property rights in some countries.

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

Any of the factors mentioned above may adversely affect our future international revenues and, consequently, affect our business, financial condition and operating results. Additionally, as we pursue the expansion of our international business, certain fixed and other overhead costs could outpace our revenues, thus adversely affecting our results of operations. We may likewise face local competitors in certain international markets who are more established, have greater economies of scale and stronger customer relationships. Furthermore, as we increase our international sales, our total revenues may also be affected to a greater extent by seasonal fluctuations resulting from lower sales that typically occur during the summer months in Europe and certain other parts of the world.

We may need to raise additional capital in the future, which may not be available on terms acceptable to us, or at all. We have historically experienced volatility in our earnings and cash flows from operations from year to. On September 1, 2017, we filed a registration statement on a Form S-3, utilizing a "shelf" registration process, and may consider a new equity financing in the future. Should the credit markets further tighten or our business declines, we may need or choose to raise additional capital to fund our operations, to repay indebtedness, pursue acquisitions or expand our operations. Such additional capital may be raised through bank borrowings, or other debt or equity financings. We cannot assure you that any additional capital will be available on a timely basis, on acceptable terms, or at all, and such additional financing may result in further dilution to our stockholders.

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

- market acceptance of our products and product enhancements, and the overall level of sales of our products;
- our ability to control costs;
- the supply of key components for our products;
- our ability to increase revenue and net income;
- increased research and development expenses and sales and marketing expenses;
- our need to respond to technological advancements and our competitors' introductions of new products or technologies;

capital improvements to new and existing facilities and enhancements to our infrastructure and systems;

potential acquisitions of businesses and product lines;

our relationships with customers and suppliers;

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- government budgets, political agendas and other funding issues, including potential delays in government contract awards;
- our ability to successfully negotiate credit arrangements with our bank and the state of the financial markets in general; and
- general economic conditions, including the effects of the economic slowdowns and international conflicts.

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

The trading price of our common stock is highly volatile. The trading price of our common stock has been subject to wide fluctuations in the past. From August 1, 2015 through May 31, 2018, our common stock has traded at prices as low as $1.77 per share and as high as $8.17 per share. The market price of our common stock could continue to fluctuate in the future in response to various factors, including, but not limited to:

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

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

- international conflicts, political unrest and acts of terrorism.

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

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

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

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

ITEM 3. LEGAL PROCEEDINGS

The information set forth under the heading "Litigation and Other Contingencies" under Note 8 of Notes to Consolidated Financial Statements, included in Part II, Item 8 of this report, is incorporated herein by reference.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

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

Market Information and Holders

Our common stock is traded on the NASDAQ Capital Market under the symbol "ITI" since February 8, 2016. Prior to that, our common stock traded on the NYSE MKT under the same symbol. The following table sets forth, for the periods indicated, the highest and lowest sales prices for our common stock:

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

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

Securities Authorized for Issuance under Equity Compensation Plans

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

Dividend Policy

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

Issuer Purchases of Equity Securities

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

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from time to time in open market and privately negotiated transactions and block trades, and may also repurchase shares pursuant to a 10b5-1 trading plan during our closed trading windows. There is no guarantee as to the exact number of shares that will be repurchased. We may modify or terminate the repurchase program at any time without prior notice. On November 6, 2014, our Board of Directors approved a $3.0 million increase to the Company's existing stock repurchase program, pursuant to which the Company may continue to acquire shares of its outstanding common stock from time to time for an unspecified length of time.

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

Performance Graph

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

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

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

ITEM 6. SELECTED FINANCIAL DATA

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

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

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

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

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

You should read the following discussion and analysis in conjunction with our Consolidated Financial Statements and related Notes thereto included in Part II, Item 8 of this report and the "Risk Factors" section in Item 1A, as well as the other cautionary statements and risks described elsewhere in this report before deciding to purchase, hold or sell our common stock.

Overview

General. We are a provider of essential applied informatics that enable smart transportation and digital agriculture. Municipalities, government agencies, crop science companies, farmers and agronomists use our solutions to make roads safer and travel more efficient, as well as farmlands more sustainable, healthy and productive.

Sale of Vehicle Sensors. On July 29, 2011, we completed the sale of substantially all of our assets used in connection with our former Vehicle Sensors segment to Bendix Commercial Vehicle Systems LLC ("Bendix"), a member of Knorr-Bremse Group, pursuant to an Asset Purchase Agreement signed on July 25, 2011 (the "Asset Sale"). In connection with the Asset Sale, we were entitled to additional consideration in the form of certain performance and royalty-related earn-outs through December 31, 2017. From the date of the Asset Sale through March 31, 2018, we received approximately $2.6 million in connection with such royalty-related earn-out provisions. We also had approximately $106,000 in royalty-related receivables included in the prepaid expenses and other current assets in the accompanying consolidated balance sheet as of March 31, 2018. We do not anticipate any further payments from Bendix.

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

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

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

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

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

Critical Accounting Policies and Estimates

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

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

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

Transportation Systems revenues are derived primarily from long-term contracts with governmental agencies. Certain Agriculture and Weather Analytics revenues are also derived from long-term contracts with governmental agencies, as well as contracts with commercial companies. ClearAg revenues that are derived from contracts with commercial companies are from subscription revenue that we typically invoice our customers at the beginning of the term, in multiyear, annual, semi-annual or quarterly installments, and revenue is recognized ratably over the period of the subscription beginning once all requirements for revenue recognition have been met, including provisioning the service so that it is available to our customers. When appropriate, revenues are recognized using the percentage of completion method of accounting, whereby revenue is recognized as contract performance progresses and is determined based on the relationship of costs incurred to total estimated costs. Any anticipated losses on contracts are charged to earnings when identified. Changes in job

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performance and estimated profitability, including those arising from contract penalty provisions and final contract settlements, may result in revisions to costs and revenues and are recognized in the period in which the revisions are determined. Profit incentives are included in revenues when their realization is reasonably assured. Certain of our revenues are recognized as services are performed and amounts are earned, which is measured by time incurred or other contractual milestones or output measures. Revenues accounted for in this manner generally relate to certain fixed fee professional services, cost-plus fixed fee or time-and-materials contracts. Revenues for ongoing operations and maintenance services contracts are generally accounted for ratably as the services are performed throughout the term of the contract. Payments received in advance of services performed are deferred and recognized when the related services are performed.

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

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

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

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

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

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

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

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

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

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

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

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Recent Accounting Pronouncements

Refer to Note 1 of Notes to Consolidated Financial Statements, included in Part II, Item 8 of this report for a discussion of recent accounting pronouncements.

Results of Operations

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

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

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

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

Year Ended March 31,			
2018	**2017**	**$ Increase**	**% Change**
(In thousands, except percentages)			

Product revenues	$	46,464	$	43,735	$	2,729	6.2%
Service revenues		57,265		52,247		5,018	9.6%
Total revenues	$	103,729	$	95,982	$	7,747	8.1%

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Selling, General and Administrative Expense

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

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

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

Research and Development Expense

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

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

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

Impairment of Goodwill

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

Amortization of Intangible Assets

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

Interest Income, Net

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

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Income Taxes

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

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

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

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

In assessing the realizability of our deferred tax assets, we review all available positive and negative evidence, including reversal of deferred tax liabilities, potential carrybacks, projected future taxable income, tax planning strategies and recent financial performance. As the Company has sustained a cumulative pre-tax loss over the trailing three years, we considered it appropriate to maintain valuation allowances of $9.8 million and $11.7 million against our deferred tax assets at March 31, 2018 and 2017, respectively. We will continue to reassess the appropriateness of maintaining a valuation allowance.

As we update our estimates in future periods, adjustments to our deferred tax asset and valuation allowance may be necessary. We anticipate this will cause our future overall effective tax rate in any given period to fluctuate from prior effective tax rates and statutory tax rates. We utilize the liability method of accounting for income taxes. We record net deferred tax assets to the extent that we believe these assets will more likely than not be realized.

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

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

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

Liquidity and Capital Resources

Cash Flows

We have historically financed our operations with a combination of cash flows from operations and the sale of equity securities. We have historically relied, and expect to continue to rely on cash flows from operations and our cash reserves to fund our operations, which we believe to be sufficient to fund our operations for at least the next twelve months. However, we may need or choose to raise additional capital to fund potential future acquisitions and our future growth. We may raise such funds by selling equity or debt securities to the public or to selected investors or by borrowing money from financial institutions. If we raise additional funds by issuing equity or convertible debt securities, our existing stockholders may experience significant dilution, and any equity securities that may be issued may have rights senior to our existing stockholders. There is no assurance that we will be able to secure additional funding on a timely basis, on terms acceptable to us, or at all.

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

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

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

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

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

Cash used in our operations during Fiscal 2016 was primarily the result of our net loss of approximately $12.3 million, adjusted by approximately $10.5 million in non-cash items, of which approximately $9.0 million related to the change in our deferred income taxes and related valuation allowance recorded against our federal net operating loss carryforwards. Such non-cash items also included higher stock-based compensation primarily due to the recent large equity grant to our new CEO, as well as depreciation, amortization, gain on the sale of discontinued operation and loss on disposal of equipment. Cash used in our operations was also driven by approximately $2.3 million used in working capital.

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

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

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

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

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

Borrowings

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

Off-Balance Sheet Arrangements

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

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Seasonality

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

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate Risk

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

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ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Iteris, Inc.
Index to Consolidated Financial Statement

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

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

Opinions on the Financial Statements and Internal Control over Financial Reporting

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

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

Basis for Opinions

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

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

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

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Definition and Limitations of Internal Control over Financial Reporting

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

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

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

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

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Iteris, Inc.

Consolidated Balance Sheets

(In thousands, except par value)

	March 31, 2018	March 31, 2017
Assets		
Current assets:		
Cash and cash equivalents	$ 10,152	$ 18,201
Short-term investments	5,319	
Trade accounts receivable, net of allowance for doubtful accounts of $333 and $389 at March 31, 2018 and March 31, 2017, respectively	12,866	14,299
Unbilled accounts receivable	7,473	6,456
Inventories	2,921	2,250
Prepaid expenses and other current assets	1,165	2,108
Total current assets	39,896	43,314
Property and equipment, net	2,333	2,064
Intangible assets, net	3,751	1,498
Goodwill	15,150	15,150
Other assets	1,756	319
Total assets	$ 62,886	$ 62,345
Liabilities and stockholders' equity		
Current liabilities:		
Trade accounts payable	$ 7,838	$ 7,886
Accrued payroll and related expenses	7,398	6,443
Accrued liabilities	2,358	2,201
Deferred revenue	4,900	4,049
Total current liabilities	22,494	20,579
Deferred rent	638	649
Deferred income taxes	65	707
Unrecognized tax benefits	168	186
Total liabilities	23,365	22,121
Commitments and contingencies (Note 9)		
Stockholders' equity:		
Preferred stock, $1.00 par value:		
Authorized shares 2,000		
Issued and outstanding shares none		
Common stock, $0.10 par value:		
Authorized shares 70,000 at March 31, 2018 and March 31, 2017		
Issued and outstanding shares 33,186 at March 31, 2018 and 32,488 at March 31, 2017	3,318	3,249
Additional paid-in capital	139,722	136,968
Accumulated deficit	(103,519)	(99,993)
Total stockholders' equity	39,521	40,224
Total liabilities and stockholders' equity	$ 62,886	$ 62,345

See accompanying notes.

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Iteris, Inc.

Consolidated Statements of Operations

(In thousands, except per share amounts)

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

Shares used in basic per share calculations	32,776	32,174	32,049
Shares used in diluted per share calculations	32,776	32,174	32,049

See accompanying notes.

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Iteris, Inc.

Consolidated Statements of Stockholders' Equity

(In thousands)

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

See accompanying notes.

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Iteris, Inc.

Consolidated Statements of Cash Flows

(In thousands)

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

	2018	2017	2016
Supplemental cash flow information:			
Cash paid during the year for:			
Interest	$	$ 14	$ 18
Income taxes	130	166	177

Supplemental schedule of non-cash investing and financing activities:

Capitalized software development costs included in accounts payable and accrued expenses	$ 102	$	$
Issuance of common stock for vested restricted stock units	10	5	5
Landlord contribution for tenant improvements	145		

See accompanying notes.

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Iteris, Inc.

Notes to Consolidated Financial Statements

March 31, 2018

1. Description of Business and Summary of Significant Accounting Policies

Description of Business

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

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

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

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

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

Iteris was incorporated in Delaware in 1987.

Recent Developments

ClearAg, Inc.

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

Basis of Presentation

Our consolidated financial statements include the accounts of Iteris, Inc. and its subsidiary and have been prepared in accordance with generally accepted accounting principles in the United States of America ("GAAP"). All intercompany accounts and transactions have been eliminated in consolidation.

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

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Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

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

Use of Estimates

The preparation of consolidated financial statements in conformity with GAAP requires our management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements, and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates made in the preparation of the consolidated financial statements include the collectability of accounts receivable and related allowance for doubtful accounts, projections of taxable income used to assess realizability of deferred tax assets, warranty reserves, costs to complete long-term contracts, indirect cost rates used in cost plus contracts, the valuation of purchased intangible assets and goodwill, the valuation of equity instruments, estimates of future cash flows used to assess the recoverability of long-lived assets and the impairment of goodwill, and fair value of our stock option awards used to calculate the stock-based compensation.

Revenue Recognition

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

Transportation Systems revenues are derived primarily from long-term contracts with governmental agencies. Certain Agriculture and Weather Analytics revenues are also derived from long-term contracts with governmental agencies, as well as contracts with commercial companies. Agriculture and Weather Analytics revenues that are derived from contracts with commercial companies are generally from subscription revenue that we typically invoice our customers at the beginning of the term, in multiyear, annual, semi-annual or quarterly installments, and revenue is recognized ratably over the period of the subscription beginning once all requirements for revenue recognition have been met, including provisioning the service so that it is available to our customers. When appropriate, revenues are recognized using the percentage of completion method of accounting, whereby revenue is recognized as contract performance progresses and is determined based on the relationship of costs incurred to total estimated costs. Changes in job performance and estimated profitability, including those arising from contract penalty provisions and final contract settlements, may result in revisions to costs and revenues, and are recognized in the period in which the revisions are determined. Profit incentives are included in revenues, when their realization is reasonably assured. Certain of our revenues are recognized as services are performed and amounts are earned, which is measured by time incurred or other contractual milestones or output measures. Revenues accounted for in this manner generally relate to certain fixed fee professional services, cost plus fixed fee, or time and materials contracts. Revenues for ongoing operations and maintenance services contracts are generally accounted for ratably as the services are performed throughout the term of the contract. Payments received in advance of services performed are deferred and recognized when the related services are performed.

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

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

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

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

Unbilled Accounts Receivable

Unbilled accounts receivable in the accompanying audited consolidated balance sheets represent unbilled amounts earned and reimbursable under services sales arrangements, including approximately $1.5 million of costs and estimated earnings in excess of billings on uncompleted contracts as of March 31, 2018, accounted for under Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 605-35, *Construction-Type and Production-Type Contracts* ("ASC 605-35"). At any given period-end, a large portion of the balance in this account represents the accumulation of labor, materials and other costs that have not been billed due to timing, whereby the accumulation of each month's costs and earnings are not administratively billed until the subsequent month. Also included in this account are amounts that will become billable according to contract terms, which usually require the consideration of the passage of time, achievement of milestones or completion of the project.

Deferred Revenue

Deferred revenue in the accompanying consolidated balance sheets is comprised of cash collected from customers and billings to customers on contracts in advance of work performed, advance payments negotiated as a contract condition, estimated losses on uncompleted contracts, project-related legal liabilities and other project-related reserves, including approximately $1.5 million of billings in excess of costs and estimated earnings on uncompleted contracts accounted for under FASB ASC 605-35. The unearned amounts are expected to be earned within the next twelve months.

Concentration of Credit Risk

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

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Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

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

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

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

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

Fair Values of Financial Instruments

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

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

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

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

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

Cash and Cash Equivalents

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

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Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

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

Investments

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

Prepaid Expenses and Other Current Assets

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

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

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

Allowance for Doubtful Accounts

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

Inventories

Inventories consist of finished goods, work-in-process and raw materials and are stated at the lower of cost or net realizable value. Cost is determined using the first-in, first-out method.

Property and Equipment

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

Goodwill and Long-Lived Assets

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

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

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

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

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

We test long-lived assets and purchased intangible assets (other than goodwill) for impairment if we believe indicators of impairment exist. We determine whether the carrying value of an asset or asset group is recoverable, based on comparisons to undiscounted expected future cash flows the asset or asset group is expected to generate. If an asset is not recoverable, we record an impairment loss equal to the amount by which the carrying value of the asset exceeds its fair value. We primarily use the income valuation approach to determine the fair value of our long lived assets and purchased intangible assets. As of March 31, 2018, there was no impairment to our long-lived and intangible assets.

Income Taxes

We utilize the asset and liability method of accounting for income taxes, under which deferred taxes are determined based on the temporary differences between the financial statement and tax basis of assets and liabilities using tax rates expected to be in effect during the years in which the basis differences reverse. A valuation allowance is recorded when it is more-likely-than-not that some or all of the deferred tax assets will not be realized, which increases our income tax expense in the period such determination is made. As such, we determined it was appropriate to record a valuation allowance of approximately $10.1 million in the third quarter of Fiscal 2016 against our deferred tax assets. We will continuously reassess the appropriateness of maintaining a valuation allowance.

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

Stock-Based Compensation

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

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Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

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

Research and Development Expenditures

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

Shipping and Handling Costs

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

Sales Taxes

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

Advertising Expenses

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

Warranty

We generally provide a one to three year warranty from the original invoice date on all products, materials and workmanship. Products sold to various original equipment manufacturer customers sometimes carry longer warranties. Defective products will be either repaired or replaced, usually at our option, upon meeting certain criteria. We accrue a provision for the estimated costs that may be incurred for product warranties relating to a product as a component of cost of sales at the time revenue for that product is recognized. The accrued warranty reserve is included within accrued liabilities in the accompanying consolidated balance sheets.

Repair and Maintenance Costs

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

Comprehensive Loss

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

Recent Accounting Pronouncements

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

Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

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

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

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

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

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

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

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Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

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

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

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

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

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

2. Supplementary Financial Information

Inventories

The following table presents details regarding our inventories:

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

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Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

2. Supplementary Financial Information (Continued)

Property and Equipment, net

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

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

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

Intangible Assets

The following table presents details regarding our intangible assets:

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

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

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

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Iteris, Inc.

Notes to Consolidated Financial Statements (Continued)

March 31, 2018

2. Supplementary Financial Information (Continued)

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

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

Goodwill

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

	Roadway Sensors	**Transportation Systems**	**Ag & Weather Analytics**	**Total**
		(In thousands)		
Balance March 31, 2016				
Goodwill	$ 8,214	$ 14,906	$ 2,168	$ 25,288
Accumulated impairment losses		(7,970)		(7,970