

DEI
Holdings,
Inc.

December 31

2008

Consolidated Financial Statements

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DEI Holdings, Inc.**

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Report of Independent Auditors

To The Board of Directors and Shareholders of DEI Holdings, Inc.

In our opinion, the accompanying consolidated balance sheets and the related consolidated statement of operations, of shareholder's deficit, and of cash flows present fairly, in all material respects, the financial position of DEI Holdings, Inc. and its subsidiaries at December 31, 2008 and 2007, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

/s/ PricewaterhouseCoopers LLP

San Diego, California

August 13, 2009

DEI HOLDINGS, INC.
CONSOLIDATED BALANCE SHEETS
(In thousands, except per share amounts)

	December 31,	
	2008	2007
ASSETS		
Current assets:		
Cash and cash equivalents.....	\$ 7,663	\$ 4,760
Accounts receivable.....	51,437	77,366
Inventories.....	69,835	64,219
Income taxes receivable.....	356	9,783
Prepaid expenses and other current assets.....	3,446	7,115
Deferred income taxes.....	1,200	6,038
Total current assets.....	133,937	169,281
Property and equipment, net.....	6,689	7,353
Intangible assets, net.....	94,472	157,265
Other assets.....	5,734	6,535
Total assets.....	\$ 240,832	\$ 340,434
LIABILITIES AND SHAREHOLDERS' DEFICIT		
Current liabilities:		
Accounts payable.....	\$ 55,768	\$ 44,814
Accrued liabilities.....	26,502	28,527
Current portion of senior notes payable.....	-	2,669
Total current liabilities.....	82,270	76,010
Revolving loan.....	-	4,000
Senior notes, less current portion.....	218,000	260,257
Deferred tax liabilities.....	13,369	8,864
Other liabilities.....	2,168	5,201
Total liabilities.....	315,807	354,332
Commitments and contingencies (Note 16)		
Shareholders' deficit:		
Common stock, \$0.01 par value:		
Authorized shares — 100,000; issued and outstanding shares — 25,645 and 25,420		
at December 31, 2008 and 2007, respectively.....	256	254
Paid-in capital.....	115,743	114,674
Accumulated other comprehensive income (loss).....	(5,938)	1,257
Accumulated deficit.....	(185,036)	(130,083)
Total shareholders' deficit.....	(74,975)	(13,898)
Total liabilities and shareholders' deficit.....	\$ 240,832	\$ 340,434

The accompanying notes are an integral part of the consolidated financial statements.

DEI HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share amounts)

	Years Ended December 31,	
	2008	2007
Sales:		
Security and entertainment product sales, net.....	\$ 243,360	\$ 280,509
Satellite radio product sales, net of \$66,716 of cost in 2008 (Note 3).....	13,424	115,982
Royalty and other revenue.....	6,133	4,649
Net sales.....	262,917	401,140
Cost of sales:		
Cost of security and entertainment sales.....	137,675	157,611
Cost of satellite radio sales (Note 3).....	-	101,832
Total cost of sales.....	137,675	259,443
Gross profit.....	125,242	141,697
Operating expenses:		
Selling, general and administrative.....	84,417	90,587
Amortization of intangibles.....	5,106	5,021
Goodwill and intangible asset impairment.....	54,215	194,832
Provision for litigation.....	-	5,074
Total operating expenses.....	143,738	295,514
Loss from operations.....	(18,496)	(153,817)
Other income (expense):		
Interest expense.....	(24,795)	(28,145)
Interest income.....	217	360
Loss before provision for (benefit from) income taxes.....	(43,074)	(181,602)
Provision for (benefit from) income taxes.....	11,879	(41,634)
Net Loss.....	\$ (54,953)	\$ (139,968)
Net loss per common share:		
Basic and diluted.....	\$ (2.13)	\$ (5.40)
Weighted average number of common shares:		
Basic and diluted.....	25,818	25,921

The accompanying notes are an integral part of the consolidated financial statements.

DEI HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' DEFICIT
(In thousands, except per share amounts)

	Common Stock		Paid-in Capital	Notes Receivable From Shareholders	Accumulated Other Comprehensive Income (Loss)	Accumulated Deficit	Total
	Shares	Amount					
Balances at January 1, 2007.....	25,164	\$ 251	\$ 114,571	\$ (10)	\$ 235	\$ 9,344	\$ 124,391
Decrease in reserves for uncertain tax positions for FIN 48 adoption.....	-	-	-	-	-	541	541
Delivery of common stock under RSU agreements, net of shares retained for withholding taxes.....	256	3	(789)	-	-	-	(786)
Stock-based compensation.....	-	-	892	-	-	-	892
Accrued interest on shareholder notes.....	-	-	-	(1)	-	-	(1)
Payments on note receivable.....	-	-	-	11	-	-	11
Comprehensive loss							
Foreign currency translation.....	-	-	-	-	3,553	-	3,553
Unrealized loss on derivative, net of tax.....	-	-	-	-	(2,531)	-	(2,531)
Net loss.....	-	-	-	-	-	(139,968)	(139,968)
Comprehensive loss.....							(138,946)
Balances at December 31, 2007.....	<u>25,420</u>	<u>254</u>	<u>114,674</u>	<u>-</u>	<u>1,257</u>	<u>(130,083)</u>	<u>(13,898)</u>
Delivery of common stock under RSU agreements, net of shares retained for withholding taxes.....	225	2	(171)	-	-	-	(169)
Stock-based compensation.....	-	-	1,240	-	-	-	1,240
Comprehensive loss							
Foreign currency translation, net of tax.....	-	-	-	-	(4,915)	-	(4,915)
Unrealized loss on derivative, net of tax.....	-	-	-	-	(2,280)	-	(2,280)
Net loss.....	-	-	-	-	-	(54,953)	(54,953)
Comprehensive loss.....							(62,148)
Balances at December 31, 2008.....	<u>25,645</u>	<u>256</u>	<u>115,743</u>	<u>-</u>	<u>(5,938)</u>	<u>(185,036)</u>	<u>(74,975)</u>

The accompanying notes are an integral part of the consolidated financial statements.

DEI HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Years Ended December 31,	
	2008	2007
Operating activities		
Net loss.....	\$ (54,953)	\$ (139,968)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation.....	3,875	2,613
Amortization.....	6,494	7,069
Goodwill and intangible asset impairment.....	54,215	194,832
Non-cash interest expense	2,552	2,062
Non-cash stock-based compensation	1,240	892
Deferred taxes	9,311	(39,308)
Changes in operating assets and liabilities, net of effects of acquisitions:		
Accounts receivable, net	24,424	81,260
Inventories.....	(7,212)	60,655
Prepaid expenses and other current assets	3,574	10,735
Accounts payable and accrued liabilities.....	10,428	(78,935)
Income taxes receivable	9,376	(16,889)
Other	(5,187)	1,944
Net cash provided by operating activities	58,137	86,962
Investing activities		
Purchases of property and equipment	(3,374)	(3,288)
Acquisitions of businesses, net of cash acquired.....	-	(12,603)
Net cash used in investing activities	(3,374)	(15,891)
Financing activities		
Proceeds from revolving loan.....	44,000	75,000
Payments on senior notes and revolving loan.....	(92,926)	(150,300)
Debt amendment fees.....	(1,823)	(1,011)
Payments received on shareholder loan	-	11
Net cash used in financing activities	(50,749)	(76,300)
Net effect of exchange rates on cash	(1,111)	128
Increase (decrease) in cash and cash equivalents	2,903	(5,101)
Cash and cash equivalents at beginning of period	4,760	9,861
Cash and cash equivalents at end of period.....	\$ 7,663	\$ 4,760
Supplemental disclosure of cash flow activities:		
Cash interest paid.....	\$ 21,249	\$ 23,004
Cash taxes paid (refunded).....	\$ (6,031)	\$ 12,912
Supplemental disclosure of non-cash financing activities:		
Accrued interest on shareholder notes receivable.....	\$ -	\$ 1

The accompanying notes are an integral part of the consolidated financial statements.

DEI HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2008 and 2007
(In thousands, except per share data)

1. The Company and Business Activities

At the Company's Annual Meeting of Shareholders held on June 19, 2008, the Company's shareholders approved the change of the Company's corporate name from Directed Electronics, Inc. to DEI Holdings, Inc. Headquartered in Southern California, DEI Holdings, Inc. (the "Company") is the parent company of some of the most respected brands in the consumer electronics industry. The Company is the largest designer and marketer in North America of premium home theater loudspeakers (sold under the Polk Audio® and Definitive Technology® brand names), and consumer-branded vehicle security and remote start systems (sold under the Viper®, Clifford®, Python®, Autostart®, and other brand names). The Company is also a supplier of mobile audio sold principally under both the Polk Audio® and Orion® brand names. The Company markets its broad portfolio of products through many channels including leading national retailers and specialty chains throughout North America and around the world and directly to end consumers. Founded in 1982, the Company has operations in California, Maryland, Canada, Europe, and Asia.

2. Liquidity and Financial Condition

Primarily due to non-cash goodwill and intangible asset impairment charges of \$54,215 and \$194,832 during the years ended December 31, 2008 and 2007, respectively, the Company incurred losses from operations of \$18,496 and \$153,817 for the years ended December 31, 2008 and 2007, respectively. These losses resulted in an accumulated deficit of \$185,036 and a shareholders' deficit of \$74,975 as of December 31, 2008. However, given that these impairment charges were non-cash, the Company generated \$58,137 and \$86,962 in cash from operating activities during 2008 and 2007, respectively.

During 2008, the financial crisis in the United States and related adverse changes in the economy have negatively impacted consumer spending, particularly discretionary spending for consumer products, which, in turn, have directly affected the Company's overall sales and profitability. In addition, the Company had \$218,000 outstanding under its senior credit facility as of December 31, 2008. The Company's senior credit facility requires the Company to comply with certain financial covenants at the end of each quarter, including maintaining a maximum debt to trailing twelve-month adjusted earnings before interest, income taxes, depreciation and amortization, including goodwill and intangible asset impairment ("Adjusted EBITDA"), as defined in the Company's lending agreement. The Company's maximum leverage ratio was 5.25x as of December 31, 2008 and was scheduled to decrease to 4.95x for the quarterly periods ending June 30, September 31, and December 31, 2009. In August 2009, the Company obtained an amendment to its senior credit facility with an effective date of July 31, 2009 that, among other things, made the Company's maximum leverage ratio less restrictive. See Note 8 for further information on the Company's amended credit facility. If the Company is unable to maintain compliance with the financial covenants going forward, the Company would be in default under its senior credit facility. If the lenders accelerate amounts owed under the senior secured credit facility because of a default and the Company is unable to pay such amounts, the lenders have the right to foreclose on substantially all of the Company's assets.

In order to respond to the current economic environment and remain in compliance with the covenants under the senior credit facility, management has or intends to implement certain cost cutting programs. These programs include reductions in workforce, decreases in discretionary spending and cost improvements relating to the termination of the Sirius business. Additionally, during 2008, the Company prepaid an aggregate of \$43,591 of its outstanding debt. As a result, the Company does not have any required principal payments due until September 2010. Based on forecasted results and amended covenant requirements, the Company expects to remain in compliance with its financial debt covenants and believes that its cash, operating cash flows and credit arrangements, taken together, provide adequate resources to fund ongoing working capital needs, capital expenditures, and interest and principal payments as they become due under the terms of its senior credit facility for the foreseeable future.

3. Summary of Significant Accounting Policies

The financial statements and accompanying notes are prepared in accordance with accounting principles generally accepted in the United States of America.

Principles of Consolidation

The consolidated financial statements include the accounts of DEI Holdings, Inc. and its wholly owned subsidiaries. All significant intercompany transactions and balances have been eliminated.

Use of Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period. On an ongoing basis, management evaluates these estimates and judgments, including those related to sales returns, bad debts, inventories, long-lived assets, goodwill and other intangible assets, warranties, income taxes, and stock-based compensation. The Company bases its estimates on historical experience and on various other assumptions that it believes are reasonable under the circumstances. The results form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Revenue Recognition

Revenue from sales of products to customers is recognized when title and risk of ownership are transferred to customers; when persuasive evidence of an arrangement exists; when the price to the buyer is fixed or determinable; and when collection is reasonably assured in accordance with SEC Staff Accounting Bulletin No. 104, "Revenue Recognition in Financial Statements."

Pursuant to the Company's agreement with SIRIUS, during 2008, the Company had exclusive rights to market and sell certain SIRIUS-branded satellite radio receivers and accessories to its existing U.S. retailer customer base. The Company recognizes these revenues in accordance with SEC Staff Accounting Bulletin No. 104, "Revenue Recognition in Financial Statements," and EITF Issue No. 99-19, "Reporting Revenue Gross as a Principal versus Net as an Agent". The agreement was amended in November 2007, which was effective as of January 1, 2008, to provide for or amend existing terms relating to product sourcing and pricing, product returns, and product warranties. Prior to the effective date of the November 2007 amendment, the Company accounted for the proceeds received for sales of SIRIUS-related hardware products as revenue on a gross basis as the Company determined that it was the principal in the transaction. The November 2007 amendment significantly reduced the Company's exposure to economic losses resulting from inventory obsolescence, sales returns, and the fulfillment of warranty obligations related to satellite radio products. In exchange for SIRIUS bearing these risks, the Company agreed to a reduced inventory margin, as defined in the agreement, on sales of satellite radio products. Accordingly, the Company determined that it was no longer the principal in the transaction and, starting on January 1, 2008, satellite radio revenues were reported on a net basis, based on the gross amounts billed to customers less (i) amounts paid to suppliers, (ii) rebates and discounts, and (iii) other direct costs. In accordance with SFAS No. 154, "Accounting Changes and Error Corrections," the Company has not recast prior period satellite radio sales to conform with the current period's presentation as the change in presentation is not the result of a change in accounting principle but the application of the same principle to new facts and circumstances that are different from those prior to January 1, 2008. For the year ended December 31, 2008, gross billings and direct costs for satellite radio products were \$80,140 and \$66,716, respectively. See Note 15 for further information on the Company's agreement with SIRIUS.

In accordance with SFAS No. 48, "Revenue Recognition When a Right of Return Exists," estimated product returns are deducted from revenue, based on historical return rates, the product stage relative to its expected life cycle, and assumptions regarding the rate of sell-through to end users from the Company's various channels.

The Company accounts for payments to customers for volume rebates and cooperative advertising as a reduction of revenue in accordance with EITF Issue No. 01-9, "Accounting for Consideration Given by a Vendor to a Customer or a Reseller of the Vendor's Products." Reductions to revenue for payments to resellers for volume rebates and cooperative advertising are based on customer purchases and fixed contractual terms. Certain of the Company's volume incentive rebates offered to customers include a sliding scale of the amount of the sales incentive with different required minimum quantities to be purchased. The Company makes an estimate of the ultimate amount of the rebate its customers will earn based upon past history with the customer and other facts and circumstances. The Company has the ability to estimate these volume incentive rebates as a relatively long period of time does not exist for a particular rebate to be claimed. The Company has historical experience with these sales incentive programs and a large volume of relatively homogenous transactions. Any changes in the estimated amount of volume incentive rebates are recognized immediately on a cumulative basis.

The Company's royalty revenue related to technology licensing agreements is recognized as earned in accordance with the specific terms of each agreement.

Fair Value Measurement

As of December 31, 2008, the Company's financial assets and liabilities requiring measurement at fair value on a recurring basis included a money market fund and two derivative financial instruments. The fair values are determined based on the application of valuation techniques contemplated within SFAS No. 157, which specifies a hierarchy of inputs to valuation techniques used to measure fair value. The levels of the hierarchy are broadly defined as follows: Level 1 – quoted prices for identical assets or liabilities, Level 2 – quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, and model-based valuations in which significant inputs are corroborated by observable market data, and Level 3 – valuation techniques in which significant inputs are unobservable.

The fair value of the Company's money market fund, which is included in cash and cash equivalents on the consolidated balance sheet, is derived from quoted prices available in an active market. The Company has determined such input to be a Level 1 measurement as defined previously. The fair values of the Company's derivative financial instruments discussed in Note 7 are derived from quotes from observable market data. The Company has determined such input to be a Level 2 measurement as defined above.

The Company's financial assets and liabilities measured at fair value on a recurring basis subject to the disclosure requirements of SFAS No. 157 at December 31, 2008 were as follows:

	Fair Value Measurements at December 31, 2008 Using			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets				
Money market fund.....	\$ 1,631	\$ -	\$ -	\$1,631
Derivative.....	-	167	-	167
	<u>\$ 1,631</u>	<u>\$ 167</u>	<u>\$ -</u>	<u>\$1,798</u>
Liabilities				
Derivative.....	\$ -	\$ 6,469	\$ -	\$6,469

Research and Development

Research and development costs are expensed as incurred. The amounts expensed in the years ended December 31, 2008 and 2007 were \$9,998 and \$10,462, respectively, which includes salaries of research and development personnel.

Shipping and Handling Fees and Costs

In accordance with EITF 00-10, "Accounting for Shipping and Handling Fees and Costs," the Company classifies shipping and handling costs billed to customers as revenue.

Shipping and handling costs incurred on outbound freight amounting to \$10,864 and \$13,233 in 2008 and 2007, respectively, are included in selling, general, and administrative expenses.

Advertising Costs

Advertising costs are expensed as incurred or when the advertising is first run and amounted to \$1,685 and \$2,218 during the years ended December 31, 2008 and 2007, respectively.

Cash and Cash Equivalents

Cash and cash equivalents consist of cash on hand and highly liquid investments with initial maturities of 90 days or less.

Concentration of Risk

Financial instruments, which potentially subject the Company to concentrations of credit risk, consist principally of cash, cash equivalents and accounts receivable. In 2008, one customer accounted for 24% of the Company's security and entertainment sales and satellite radio gross billings and 12% of the Company's accounts receivable. In 2007, two customers accounted for 21% and 10%, respectively, of the Company's sales and two customers accounted for 28% and 14%, respectively, of the Company's accounts receivable.

The Company currently purchases the majority of its components from a few suppliers. In 2008, the Company purchased 20%, 19%, 13%, and 10% of inventory from four suppliers. In 2007, the Company purchased 24%, 18%, 13%, and 11% of inventory from four suppliers. Although the Company believes that other suppliers could provide components on similar terms if needed, the loss of its relationship with these suppliers could adversely impact the Company's operating results.

Fair Value of Financial Instruments

The carrying amount of cash, accounts receivable, accounts payable, and accrued liabilities are considered to be representative of their respective fair values because of the short-term nature of those instruments. All of the Company's outstanding debt was subject to variable rates as of December 31, 2008. Based on quoted market prices for loans with similar terms, the fair value of the Company's long-term senior notes was approximately \$115,540 as of December 31, 2008.

Allowance for Doubtful Accounts

The Company establishes an allowance for doubtful accounts. Bad debt reserves are maintained based on a variety of factors, including length of time receivables are past due, macroeconomic events, significant one-time events, and the Company's historical experience. A specific reserve for individual accounts is recorded when the Company becomes aware of circumstances that may impact a specific customer's ability to meet its financial obligations subsequent to the original sale, such as in the case of bankruptcy filings or deterioration in the customer's operating results or financial position. If circumstances related to customers change, estimates of the recoverability of receivables are further adjusted.

The following is a summary of the changes to the balance of the Company's allowance for doubtful accounts:

	Years Ended December 31,	
	2008	2007
Beginning balance.....	\$1,521	\$1,464
Increases related to acquisitions.....	-	49
Increases in reserves, charged to operations.....	2,555	619
Charge-offs.....	(1,931)	(611)
Ending balance.....	<u>\$2,145</u>	<u>\$1,521</u>

Inventories

Inventories are valued at the lower of cost or market value. Cost is determined by the average cost method. The Company records adjustments to its inventory for estimated obsolescence or diminution in market value equal to the difference between the cost of the inventory and the estimated market value. At the point of a loss recognition, a new cost basis for that inventory is established, and subsequent changes in facts and circumstances do not result in the restoration or increase in that newly established cost basis.

Property and Equipment

Property and equipment is stated at cost less accumulated depreciation and amortization. Additions, improvements, and major renewals are capitalized. Maintenance, repairs, and minor renewals are expensed as incurred. Depreciation is provided using the straight-line method over the estimated useful lives of the assets. Estimated useful lives are three years for vehicles, three years for computers and purchased software, three to seven years for furniture and machinery, and three to ten years for molds and tooling.

Leasehold improvements are amortized over the life of the lease or the asset, whichever is shorter.

Goodwill and Indefinite-Lived Intangible Assets

During 2007, the Company determined that its goodwill was impaired. Accordingly, a non-cash impairment charge of \$168,362 was recorded in 2007, which reduced the value of goodwill to zero.

For indefinite-lived intangibles, the Company compares the fair value of its indefinite-lived intangible assets, which consist of trademarks, to their carrying value. The Company estimates the fair value of these intangible assets using the royalty savings approach. An asset's value is deemed impaired if the discounted cash flows or earnings projections generated do not substantiate the carrying value of the asset. As a result of the 2008 and 2007 annual impairment tests, the Company recorded non-cash impairment charges of \$49,391 and \$26,471, respectively, related to certain indefinite-lived trademarks.

See Note 6 for further information on goodwill and intangible assets.

Impairment of Long-Lived Assets

Long-lived assets with finite lives are amortized using the straight-line method over their estimated economic lives, currently ranging from two to twenty years. The Company estimates the useful lives of intangible assets by considering various pertinent factors including the expected use of the asset, legal or contractual provisions which may limit the life of the asset, and the effects of obsolescence and other economic factors. The Company evaluates the estimated useful lives of these intangible assets each reporting period to determine whether events or circumstances warrant revised estimates of useful lives. During the fourth quarter of 2008, the Company impaired two customer relationship intangible assets resulting in the write-off of the remaining net book value of these two intangible assets totaling \$4,824. This non-cash charge is included in intangible asset impairment on the consolidated statement of operations. Long-lived assets are evaluated for impairment whenever events or changes in circumstances indicate the carrying value of an asset may not be recoverable in accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." The Company assesses the recoverability of an asset based on the undiscounted future cash flow the asset is expected to generate. Impairment is identified if such cash flow plus net proceeds expected from disposition of the asset, if any, are less than the carrying value of the asset. When an impairment is identified, the Company reduces the carrying amount of the asset to its fair value based on a discounted cash flow approach or, when available and appropriate, to comparable market values. As a result of the impairment of certain of the Company's indefinite-lived intangible assets during 2008 and 2007, the Company assessed the recoverability of the related long-lived assets. The undiscounted future cash flows related to these assets exceed their carrying amounts. Accordingly, the Company concluded that its long-lived assets with finite lives were not impaired.

Deferred Financing Costs

Deferred financing costs related to direct costs incurred to obtain debt financing are included in other assets in the accompanying consolidated balance sheets. Deferred financing costs are amortized to interest expense using the effective interest rate method over the financing term of the related debt. See Note 8 for further information on deferred financing costs.

Warranties

The Company records a reserve for product warranties at the time revenue is recognized. The Company offers warranties of various lengths depending upon the specific product. Where applicable, the Company returns to the manufacturer or receives credit from the manufacturer for defective security and entertainment products to the extent that it cannot repair or resell the refurbished product. Pursuant to the Company's amended agreement with SIRIUS, the Company has the right to return defective satellite radio products to SIRIUS for which the Company is paid its original cost for such returns. The Company records an estimate for warranty related costs based upon historical product warranty return rates, materials usage, and service delivery costs incurred in correcting the product where applicable. During the year ended December 31, 2007, for both security and entertainment and satellite radio products, and during the year ended December 31, 2008 for security and entertainment products, the estimate for warranty related costs was recorded in cost of sales. Should actual product warranty return rates, materials usage, or service delivery costs differ from the historical rates, revisions to the estimated warranty reserve would be required. The warranty reserve is included in accrued liabilities on the consolidated balance sheet.

The following is a summary of the changes to the balance of the warranty reserve:

	<u>Years Ended December 31,</u>	
	<u>2008</u>	<u>2007</u>
Beginning balance.....	\$4,248	\$8,631
Increases in reserve.....	4,155	10,133
Costs charged against reserve.....	(3,547)	(14,516)
Ending balance.....	<u>\$4,856</u>	<u>\$4,248</u>

Foreign Currency Transactions

The functional currencies for the Company’s international operations are the respective local currencies. The Company translates foreign currency balance sheets at the end-of-period exchange rates and net sales and expenses at the average exchange rates in effect during each period. The resulting foreign currency translation adjustments are a component of accumulated other comprehensive income, which is included in shareholders’ equity (deficit) on the consolidated balance sheet. Gains resulting from foreign currency transactions are included in operating expenses and totaled \$145 and \$385 for the years ended December 31, 2008 and 2007, respectively.

Accounting for Derivative Instruments and Hedging Activities

All derivatives are recognized on the balance sheet at fair value. On the date the derivative contract is entered into, the Company designates the derivative as (1) a hedge of the fair value of a recognized asset or liability or of an unrecognized firm commitment (fair-value hedge), (2) a hedge of a forecasted transaction or of the variability of cash flows to be received or paid related to a recognized asset or liability (cash-flow hedge), (3) a foreign-currency fair-value or cash-flow hedge (foreign-currency hedge), or (4) a hedge of a net investment in a foreign operation. Some derivatives may also be considered natural hedging instruments (changes in fair value are recognized to act as economic offsets to changes in fair value of the underlying hedged item and do not qualify for hedge accounting under SFAS No. 133).

The Company is hedging the cash flows of a portion of its long-term debt using two interest rate swap agreements combined as one hedging instrument (the “interest rate swap”). The Company entered into this interest rate swap to manage its exposure to interest rate changes by achieving a desired proportion of fixed rate versus variable rate debt and to comply with covenant requirements of its senior credit facility. In the interest rate swap, the Company agreed to exchange the difference between a variable interest rate and a fixed interest rate, multiplied by a notional principal amount.

As the interest rate swap is designated as a cash flow hedge and the hedging relationship qualifies for cash flow hedge accounting, the effective portion of the change in fair value of the derivative is recorded in other comprehensive income (loss) and reclassified to interest expense when the hedged debt affects interest expense. The ineffective portion of the change in fair value of the derivative, if any, is recognized in interest expense in the period of the change.

At inception, the Company determined that the hedge was highly effective. In addition, on a quarterly basis, the Company performs an assessment to determine whether the change in the fair value of the derivative is deemed highly effective in offsetting the change in cash flows of the hedged item. If, at any time subsequent to the inception of the hedge, the assessment indicates that the derivative is no longer highly effective as a hedge, the Company will discontinue hedge accounting and recognize all subsequent derivative gains and losses in results of operations.

The Company uses forward contracts that are not designated as hedging instruments under SFAS No. 133 to hedge the impact of the variability in exchange rates on a portion of accounts receivable and collections denominated in Canadian Dollars. The derivative instrument is recorded at its fair value on its balance sheet with changes in the fair value recorded in earnings in the period of the change.

The Company does not use derivative instruments for trading or other speculative purposes. See Note 7 for additional information.

Product Lines and Geographic Disclosures

The Company's combined U.S. security and entertainment net sales and satellite radio gross billing in 2008 and 2007 were \$277,102 and \$345,045, respectively. The Company's foreign security and entertainment net sales and satellite radio gross billing, including sales to international distributors and through the Company's foreign subsidiaries, in 2008 and 2007 were \$52,531 and \$56,095. The Company's security and entertainment sales and satellite radio gross billing in Canada in 2008 and 2007 were \$34,826 and \$34,986, respectively. Other than Canada, no single foreign country accounted for more than 1% of the Company's net sales in 2008 or 2007. The Company's U.S. long-lived assets were \$5,485 and \$6,568 as of December 31, 2008 and 2007, respectively. The Company's foreign long-lived assets were approximately \$1,204 and \$785 as of December 31, 2008 and 2007, respectively.

Income Taxes

The Company provides for income taxes utilizing the liability method. Under the liability method, current income tax expense or benefit is the amount of income taxes expected to be payable or refundable for the current year. A deferred income tax asset or liability is computed for the expected future impact of differences between the financial reporting and tax bases of assets and liabilities and for the expected future tax benefit to be derived from tax credits. Tax rate changes are reflected in the computation of the income tax provision during the period such changes are enacted.

Deferred tax assets are reduced by a valuation allowance when, in management's opinion, it is more likely than not that some portion or all of the deferred tax assets will not be realized. The Company considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. The Company's valuation allowance is based on available evidence, including its current year operating loss, evaluation of positive and negative evidence with respect to certain specific deferred tax assets including evaluation sources of future taxable income to support the realization of the deferred tax assets.

The Company adopted the provisions of FIN 48, "Accounting for Uncertainty in Income Taxes," on January 1, 2007. Under FIN 48, the Company recognizes the tax benefit from an uncertain tax position only if it is more likely than not that such tax position will be sustained upon examination by taxing authorities, based on the technical merits of the position. See Note 13 for additional information regarding the adoption of FIN 48.

Comprehensive Income

Comprehensive income includes all changes in shareholders' equity (deficit) except those resulting from investments by, and distributions to, shareholders. Accordingly, the Company's comprehensive income includes net income and adjustments that arise from the translation of the financial statements of the Company's foreign operations into U.S. dollars and the changes in the fair value related to derivatives designated as cash flow hedges.

Stock-Based Compensation

Effective January 1, 2006, the Company adopted the fair value method of accounting for employee stock options pursuant to SFAS No. 123(R), "Share-Based Payment." See Note 10 for additional information on stock-based compensation.

Recent Accounting Pronouncements

In December 2007, the FASB issued SFAS No. 141(R), "Business Combinations." SFAS No. 141(R) establishes principles and requirements for how the acquirer of a business recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree. The statement also provides guidance for recognizing and measuring the goodwill acquired in the business combination and determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. SFAS No. 141(R) is effective for financial statements issued for fiscal years beginning after December 15, 2008. The Company does not expect that SFAS No. 141(R) will have a material impact on its previous acquisitions. The impact on the Company's consolidated financial statements will depend upon the nature, terms, and size of acquisitions consummated, if any, after the effective date.

In March 2008, the FASB issued SFAS No. 161, "Disclosures about Derivative Instruments and Hedging Activities," an amendment of SFAS No. 133. SFAS No. 161 requires disclosures of how and why an entity uses derivative instruments, how derivative instruments and related hedged items are accounted for, and how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. SFAS No. 161 is effective for fiscal years beginning after

November 15, 2008, with early adoption permitted. The Company adopted the accounting provisions of SFAS No. 161 on January 1, 2009 and does not expect it to have a material impact on its consolidated financial statements.

In April 2008, the FASB issued FSP No. FAS 142-3, "Determination of the Useful Life of Intangible Assets." FSP No. FAS 142-3 amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under SFAS No. 142, "Goodwill and Other Intangible Assets," in order to improve the consistency between the useful life of a recognized intangible asset under SFAS No. 142 and the period of expected cash flows used to measure the fair value of the asset under SFAS No. 141R and other GAAP. FSP No. FAS 142-3 applies to all intangible assets, whether acquired in a business combination or otherwise, and will be effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. The guidance for determining the useful life of intangible assets will be applied prospectively to intangible assets acquired after the effective date. The disclosure requirements apply prospectively to all intangible assets recognized as of, and subsequent to, the effective date. Early adoption is prohibited. The Company adopted the accounting provisions of FSP No. FAS 142-3 on January 1, 2009 and is currently evaluating this guidance but does not expect it to have a significant impact on the Company's consolidated financial statements.

In November 2008, the FASB ratified EITF Issue No. 08-7, "Accounting for Defensive Intangible Assets," or EITF 08-7, which clarifies the accounting for certain separately identifiable intangible assets which an acquirer does not intend to actively use but intends to hold to prevent its competitors from obtaining access to them. EITF 08-7 requires an acquirer in a business combination to account for a defensive intangible asset as a separate unit of accounting which should be amortized to expense over the period the asset diminishes in value. EITF 08-7 is effective for fiscal years beginning after December 15, 2008, with early adoption prohibited. It is effective prospectively for intangible assets acquired on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. The Company adopted the accounting provisions of EITF 08-7 on January 1, 2009. The impact on the Company's consolidated financial statements will depend upon the nature, terms, and size of acquisitions consummated, if any, after the effective date.

4. Balance Sheet Details

The following provides certain balance sheet details:

	December 31,	
	2008	2007
Inventories:		
Raw materials.....	\$ 3,189	\$ 2,346
Finished goods.....	66,646	61,873
	<u>\$ 69,835</u>	<u>\$ 64,219</u>
Property and equipment:		
Machinery and equipment.....	\$ 8,857	\$ 7,073
Molds and tooling.....	5,812	4,349
Furniture and fixtures.....	857	878
Leasehold improvements.....	1,532	1,138
Construction in process.....	314	779
	<u>17,372</u>	<u>14,217</u>
Accumulated depreciation and amortization.....	(10,683)	(6,864)
	<u>\$ 6,689</u>	<u>\$ 7,353</u>
Accrued liabilities:		
Accrued warranty costs.....	\$ 4,856	\$ 4,248
Accrued salaries, bonuses and employee benefits.....	2,987	2,702
Accrued sales incentives.....	6,099	6,945
Accrued interest.....	2,018	4,694
Current portion of fair value of interest rate swap.....	6,469	1,848
Other.....	4,073	8,090
	<u>\$ 26,502</u>	<u>\$ 28,527</u>

5. Acquisitions

On May 22, 2007, the Company acquired 100% of the outstanding capital stock of a security and remote start company. The acquired net assets consisted principally of trade receivables, inventory, property and equipment, trade payables, accrued liabilities, developed technology, customer relationships, covenants not to compete, and goodwill. The acquisition was accounted for under the purchase method of accounting whereby the net tangible and intangible assets acquired and liabilities assumed were recognized at their fair values at the date of acquisition. The company was acquired for \$11,367 in cash, including \$410 in acquisition-related costs, of which \$559 was allocated to tangible net assets, \$3,255 was allocated to separately identifiable intangible assets, and \$7,553 was allocated to goodwill. The acquisition agreement allows for potential contingent earnout consideration to be paid if certain financial targets are achieved in the first two years after the acquisition. These potential earnout payments were not included in the purchase price that was recorded at the acquisition date because they are contingent. Future payments made under these arrangements, if any, will be recorded as additional goodwill when the underlying contingency is resolved. The financial targets for the first year after acquisition were not met and, as such, there was no contingent earnout consideration paid during 2008. As a result of the acquisition, the acquired company became a wholly owned subsidiary of the Company and, therefore, is included in the results of operations for the period from the acquisition date to December 31, 2008 and 2007. The unaudited pro forma consolidated net earnings and EPS are not materially different from the amounts reflected in the accompanying financial statements.

6. Goodwill and Intangible Assets

The Company performed its 2008 and 2007 annual impairment review of indefinite-lived intangible assets, which consist of trademarks, during the fourth quarter. The estimated fair value of all indefinite-lived trademarks was determined using a royalty savings methodology similar to that employed when the associated businesses were acquired but using updated estimates of sales, cash flow, and profitability. The impairment assessment of these trademarks resulted in non-cash impairment charges of \$49,391 and \$26,471 during 2008 and 2007, respectively. Based upon slower than anticipated sales during 2008 and 2007 and an estimated slower economic outlook, the Company's projected discounted cash flows and earnings related to the impaired trademarks no longer substantiate the carrying value of the assets.

The Company's long-lived assets, including finite-lived intangible assets, are evaluated for impairment whenever events or changes in circumstances indicate the carrying value of the asset may not be recoverable. The Company evaluates the estimated useful lives of these intangible assets each reporting period to determine whether events or circumstances warrant revised estimates of useful lives. During the fourth quarter of 2008, the Company impaired two customer relationship intangible assets resulting in the write-off of the remaining net book value of these two intangible assets totaling \$4,824. This non-cash charge is included in intangible asset impairment on the consolidated statement of operations. As a result of the impairment of certain of the Company's indefinite-lived intangible assets during the fourth quarters of 2008 and 2007, the Company assessed the recoverability of the related finite-lived intangible assets. The undiscounted future cash flows that these assets are expected to generate indicated that the Company's finite-lived intangible assets were not impaired.

As a result of the completion of 2007 annual goodwill impairment test, a non-cash impairment charge of \$168,362 was recorded, which reduced the value of goodwill to zero.

The following tables present intangible assets as of December 31, 2008 and 2007.

December 31, 2008					
Useful Life (Years)	Gross Amount	Accumulated Amortization	Impairment	Net Book Value	
Intangibles subject to amortization:					
Patents and other developed technology.....	2-20 \$ 17,483	\$ (11,482)	\$ -	\$ 6,001	
Customer relationships.....	7-20 58,253	(23,445)	(4,824)	29,984	
Licensing agreements.....	5-12 2,250	(1,711)	-	539	
Non-compete agreements.....	2-5 2,982	(1,669)	-	1,313	
Trademarks.....	10-20 1,127	(231)	-	896	
	<u>82,095</u>	<u>(38,538)</u>	<u>(4,824)</u>	<u>38,733</u>	
Intangibles not subject to amortization, excluding goodwill:					
Trademarks.....	105,130	-	(49,391)	55,739	
Total intangibles.....	<u>\$187,225</u>	<u>\$ (38,538)</u>	<u>\$ (54,215)</u>	<u>\$ 94,472</u>	
December 31, 2007					
Useful Life (Years)	Gross Amount	Accumulated Amortization	Impairment	Net Book Value	
Intangibles subject to amortization:					
Patents and other developed technology.....	2-20 \$ 18,017	\$ (10,599)	\$ -	\$ 7,418	
Customer relationships.....	7-20 59,671	(19,448)	-	40,223	
Licensing agreements.....	5-12 2,250	(1,103)	-	1,147	
Non-compete agreements.....	2-5 3,081	(1,101)	-	1,980	
Trademarks.....	10-20 1,178	(132)	-	1,046	
	<u>84,197</u>	<u>(32,383)</u>	<u>-</u>	<u>51,814</u>	
Intangibles not subject to amortization, excluding goodwill:					
Trademarks.....	131,922	-	(26,471)	105,451	
Total intangibles.....	<u>\$216,119</u>	<u>\$ (32,383)</u>	<u>\$ (26,471)</u>	<u>\$157,265</u>	

Excluding the impact of foreign currency translation, amortization expense of intangible assets subject to amortization is estimated to be \$5,445 in 2009, \$5,314 in 2010, \$5,014 in 2011, \$4,361 in 2012, and \$4,128 in 2013.

There have been no changes in the carrying amount of goodwill during 2008. The changes in the carrying amount of goodwill for during 2007 are as follows:

Balance at January 1, 2007.....	\$ 156,617
Goodwill acquired during the year.....	7,553
Accrual of contingent consideration.....	1,750
Adjustment to previously acquired working capital.....	(212)
Adjustment to previously acquired deferred tax liabilities.....	1,645
Foreign exchange translation adjustment in 2007.....	1,009
Impairment.....	(168,362)
Balance at December 31, 2007.....	<u>\$ -</u>

7. Derivative Instruments and Hedging Activities

In 2007, the Company entered into two interest rate swap agreements with three-year terms, combined as one hedging instrument (the “derivative contract” or “interest rate swap”). Under the agreements, floating rate interest payments on \$153,000 of the Company’s senior credit facility were swapped for a fixed rate interest payment at a rate of 5.04%. The Company entered into this derivative contract to manage its exposure to interest rate changes by achieving a desired proportion of fixed rate versus variable rate debt and to comply with covenant requirements of the Company’s senior credit facility.

For the years ended December 31, 2008 and 2007, the interest rate swap was highly effective in offsetting cash flows of the hedged item and, thus, there is no impact on earnings due to hedge ineffectiveness. The fair value of the derivative contract at inception was zero. The Company records the derivative contract on its consolidated balance sheet at its fair value. The Company classifies the portion of the fair value that is related to cash flows that are expected to occur within the next 12 months as current with the remaining amount classified as non-current. The fair value of the derivative contract as of December 31, 2008 was a liability of \$6,469, all of which was recorded as a current liability. The fair value of the derivative contract as of December 31, 2007 was a liability of \$4,189, of which \$1,848 was recorded as a current liability.

The amount recorded in accumulated other comprehensive income (loss) related to cash flow hedging instruments was as follows:

	December 31,	
	2008	2007
Beginning balance.....	\$ (2,531)	\$ -
Changes in fair value of derivatives.....	(2,280)	(4,189)
Deferred income tax provision.....	-	1,658
Ending balance.....	<u>\$ (4,811)</u>	<u>\$ (2,531)</u>

In 2008 and 2007, the Company entered into forward contracts that are derivative instruments to mitigate the impact of the variability in exchange rates on a portion of accounts receivable and collections denominated in Canadian Dollars. These derivative instruments are not designated as hedging instruments under SFAS No. 133. The derivative instruments are recorded at their fair value on the Company’s balance sheet with changes in the fair value recorded in operating expense in the period of the change. The net gains (losses) recorded in earnings for contracts not designated as hedging instruments in 2008 and 2007 was \$89 and \$78, respectively. The fair value of the derivative contract as of December 31, 2008 and 2007 was \$167 and \$78, respectively, which was recorded in other current assets on the consolidated balance sheet.

8. Financing Arrangements

In April 2007, the Company was granted an amendment to its senior credit facility that allows a higher leverage ratio through 2009 (“Amendment No. 1”). In March 2008, the Company further amended certain terms, conditions, and covenants contained in its senior credit facility (“Amendment No. 2”). Amendment No. 2 increased the Company’s allowable leverage ratio to 5.25x through March 31, 2009, stepping down to 4.95x through December 31, 2009, with step-downs thereafter consistent with the previous terms of the agreement. Amendment No. 2 also increased the Company’s interest rate by 100 to 150 basis points, depending upon leverage ratios, from its previous rate of LIBOR plus 250 basis points. In addition, Amendment No. 2 permits additional add-backs to adjusted EBITDA in the calculation of its leverage ratio, modifies principal payment terms and revolving loan availability, and permits the

right to execute the sale of certain accounts receivable so long as the proceeds are used to reduce indebtedness.

Under the senior credit facility the Company is required to provide annual audited financial statements to the lenders. In May 2009, the Company obtained an amendment ("Amendment No. 3") which extended the deadline to provide the 2008 audited financial statements to the lenders through July 31, 2009. The lenders under the Company's credit agreement also temporarily waived their right to declare an event of default or exercise any remedies available to them pursuant to the credit agreement or any applicable law with respect to the Company's compliance with certain financial covenants in the first quarter of 2009. The waiver also increased the Company's interest rate 200 basis points from its previous rate of LIBOR plus 350 basis points. The waiver expired July 31, 2009.

In August 2009, the Company further amended certain terms, conditions, and covenants contained in its senior credit facility ("Amendment No. 4"). Amendment No. 4, which has an effective date of July 31, 2009, waived the Company's maximum consolidated leverage and minimum consolidated fixed charge ratios for the first and second quarters of 2009 and further extended the deadline to provide the 2008 audited financial statements. In addition, Amendment No. 4 increases the Company's allowable consolidated leverage ratio to 8.00x through September 30, 2009 and to 8.80x through December 31, 2009, with quarterly decreases thereafter through the maturity date. Amendment No. 4 also increases the Company's interest rate to LIBOR plus 550 basis points, reduces the Company's revolving loan availability, modifies the minimum consolidated fixed charge coverage ratio for certain periods, permits additional add-backs to adjusted EBITDA, introduces a LIBOR floor of 200 basis points and a minimum consolidated EBITDA covenant, and permits certain term loan repurchases by the Company. Effective with Amendment No.4, payment-in-kind ("PIK") interest will also accrue should the Company's consolidated total leverage ratio be greater than 6.00x.

The Company's credit agreement, as most recently amended in August 2009, provides for senior notes in an aggregate principal amount equal to \$306,800, of which \$218,000 was outstanding as of December 31, 2008, plus a revolving loan in a maximum principal amount of \$35,000 from October 1, 2009 through February 28, 2010, \$30,000 from October 1, 2010 through February 28, 2011, and \$25,000 at all other times. The revolving loan will mature on September 22, 2012 and the senior notes will mature on September 22, 2013. The revolving loan may be used for working capital requirements, general corporate purposes, and certain permitted acquisitions. The Company's senior credit facility contains certain affirmative and negative covenants related to indebtedness, leverage and fixed charges coverage, and restrictions against paying cash dividends without the lenders' consent. The Company was in compliance with all financial covenants at December 31, 2008. During 2008, the Company prepaid an aggregate of \$43,591 of its outstanding debt. As a result, the Company does not have required principal payments until September 2010, at which time principal is payable in quarterly installments of \$567, with balloon payments of \$9,477 on December 31, 2010, 2011, and 2012, with the final installment of the total remaining principal due on September 22, 2013. The Company expects to refinance or extend its senior credit facility prior to September 22, 2013, but may not be able to obtain such refinancing on acceptable terms or at all.

During the year ended December 31, 2008, the effective interest rate of all borrowings under the senior credit facility was 8.12%. During 2008 and 2007, the Company incurred \$1,823 and \$1,011, respectively, of debt fees and issuance costs related to Amendments No. 1 and 2 to the senior credit facility, which are included in other assets and are amortized to interest expense over the term of the debt using the effective interest method. In connection with Amendment No. 2 of the credit facility in 2008, the Company wrote off unamortized debt issuance costs of \$137. Upon prepayment of \$43,591 and \$39,233 of the outstanding principal of the senior notes in 2008 and 2007, respectively, the Company wrote off unamortized debt issuance costs of \$945 and \$830. These costs are recorded as interest expense in the accompanying consolidated statements of operations.

9. Shareholders' Equity (Deficit)

(a) Common Stock

The authorized number of common shares at December 31, 2008 and 2007 was 100,000 with a par value of \$0.01 per share. The holders of common stock are entitled to dividends if and when such dividends are declared by the Company's Board of Directors. However, the Company's senior credit facility covenants restrict the payment of cash dividends without the lenders' consent. Each holder of common stock is entitled to one vote for each share of common stock.

10. Accounting for Stock-Based Compensation Expense

The Company's 2005 Incentive Compensation Plan ("the 2005 Plan") provides for the issuance of incentive stock options, stock appreciation rights, restricted stock, stock units, stock granted as a bonus or in lieu of another award, dividend equivalents or other stock-based awards or performance awards to executives, employees, officers, directors, consultants, and other persons who provide services to the Company. At the Company's Annual Meeting of Shareholders held on June 19, 2008, the Company's shareholders

approved an increase in the maximum number of shares of common stock available for issuance in connection with awards by 2,000 shares from 2,750 to 4,750. As of December 31, 2008, 2,248 shares remained available for grant under the 2005 Plan.

The Company reported stock-based compensation expense of \$1,240 and \$892 as a component of selling, general and administrative expense in the consolidated statement of operations for the years ended December 31, 2008 and 2007, respectively.

As of December 31, 2008, there was approximately \$1,511 of total unrecognized compensation cost related to unvested share-based awards granted. The unrecognized compensation cost is expected to be recognized over a weighted-average period of approximately two years.

Restricted Stock Units (RSUs)

In December 2005, the Company granted RSU awards for an aggregate of 1,006 shares of common stock of which 984 were vested when granted. The December 2005 awards generally provide for delivery of one-third of the underlying common stock on each of the first three anniversaries of their grant date, with delivery of stock on a quarterly basis to four of the Company's executive officers. Delivery of the vested 984 underlying shares of common stock is not contingent on the Company's continued employment of the holders of the RSUs.

Since December 2005, the Company has granted RSU awards for an aggregate of 115 shares of common stock. Of the 115 RSU awards, 112 vest between three and four years after grant. Delivery is contingent upon the Company's continued employment of the holders of the RSUs. The remaining RSUs were vested when granted.

In addition, in September 2006, the Company entered into an agreement whereby a variable number of RSUs may be granted in three separate tranches during a three-year period based upon the awardees' achievement of certain performance criteria in each and every year. If granted, each tranche vests over a period not in excess of three years. The first and second tranches related to this agreement were based on 2008 and 2007 results and were not earned.

A summary of the status of the Company's RSUs at December 31, 2008 and 2007 are as follows:

	Fully Vested Shares	Vesting Shares	Total Shares	Weighted-Average Grant Price
RSUs outstanding at January 1, 2007.....	816	55	871	\$ 15.35
Granted.....	3	63	66	6.11
Vested.....	13	(13)	-	15.48
Forfeited.....	-	(11)	(11)	10.77
Delivered, including 112 shares withheld for payroll taxes...	(367)	-	(367)	15.92
RSUs outstanding at December 31, 2007.....	<u>465</u>	<u>94</u>	<u>559</u>	<u>14.90</u>
Granted.....	-	-	-	-
Vested.....	13	(13)	-	15.48
Forfeited.....	-	(4)	(4)	12.23
Delivered, including 134 shares withheld for payroll taxes...	(360)	-	(360)	15.98
RSUs outstanding at December 31, 2008.....	<u><u>118</u></u>	<u><u>77</u></u>	<u><u>195</u></u>	<u><u>\$ 12.96</u></u>

Stock Options

Stock options issued under the 2005 Plan are exercisable at various dates and will expire no more than ten years from their date of grant. As of December 31, 2008, there were options for an aggregate of 1,711 shares outstanding under the 2005 Plan. The fair value of stock options is determined on the date of grant using the Black-Scholes valuation model. Such value is recognized as expense over the requisite service period, net of estimated forfeitures, using the straight-line method. The determination of the fair value of stock options is affected by the Company's stock price, as well as assumptions regarding a number of complex and subjective variables. The volatility assumption is based on a combination of the historical volatility of the Company's common stock and the volatilities of similar companies over a period of time equal to the expected term of the stock options. The volatilities of similar companies are used in conjunction with the Company's historical volatility because of the lack of sufficient relevant history for the Company's common stock equal to the expected term. The expected term of employee stock options represents the weighted-average period the stock options are expected to remain outstanding. The expected term assumption is estimated based primarily on the options' vesting terms.

and remaining contractual life and employees' expected exercise and post-vesting employment termination behavior. The risk-free interest rate assumption is based upon observed interest rates on the grant date appropriate for the term of the employee stock options. The dividend yield assumption is based on the expectation of no future dividend payouts by the Company.

The assumptions used in the Black-Scholes pricing model were as follows:

	<u>2008</u>	<u>2007</u>
Expected dividend yield.....	0.00%	0.00%
Risk-free interest rate.....	2.84% - 3.48%	3.10% - 5.10%
Expected life (in years).....	4.35 - 8.00	4.58 - 8.00
Expected volatility.....	55.6% - 60.6%	39.6% - 53.2%
Weighted-average grant date fair value.....	\$ 0.73	\$ 3.21

A summary of stock option activity for 2008 and 2007 is as follows:

	<u>2008</u>		<u>2007</u>	
	<u>Shares</u>	<u>Weighted-Average Exercise Price</u>	<u>Shares</u>	<u>Weighted-Average Exercise Price</u>
Stock options outstanding at the beginning of the year.....	588	\$ 8.41	105	\$ 14.96
Stock options forfeited or expired.....	(162)	3.95	(35)	11.52
Stock options granted.....	1,285	1.44	518	7.29
Stock options exercised.....	-	-	-	-
Stock options outstanding at the end of the year.....	<u>1,711</u>	<u>\$ 3.60</u>	<u>588</u>	<u>\$ 8.41</u>

Options outstanding as of December 31, 2008 have a weighted-average remaining contractual term of 6 years, and had an aggregate intrinsic value of \$0 at December 31, 2007. An aggregate of 255 of the outstanding options were exercisable at December 31, 2008. The exercisable options have a weighted-average exercise price of \$9.91 and had an aggregate intrinsic value of \$0.

11. Net Income (Loss) per Common Share

Basic net income (loss) per common share ("EPS") is calculated by dividing net income (loss) available to common shareholders by the weighted-average number of common shares outstanding for the period, without consideration of potential common stock. Vested RSU grants have been treated as outstanding shares of common stock for purposes of basic and diluted earnings per share. Unvested RSUs that are not subject to performance conditions are included in diluted EPS using the treasury stock method. Unvested RSUs that are subject to performance conditions are included in diluted EPS using the treasury stock method when it is probable that the performance conditions will be achieved.

The Company has excluded options and restricted stock units for an aggregate of 1,841 and 460 shares from the calculation of diluted net income (loss) per common share for the years ended December 31, 2008 and 2007, respectively, because the effect of their inclusion would be antidilutive.

12. Benefit Plans

Employee Savings Plan

The Company sponsors a 401(k) savings plan (the "Plan"). The Plan allows for eligible employees to contribute up to 20% of their annual compensation up to the statutory limitations. During 2007, the Company provided a match totaling 50% of the employee's contribution up to a maximum of \$2. Under the Plan, contributions vest over four years. Polk, a wholly owned subsidiary of the Company, sponsors a separate 401(k) savings plan (the "Polk Plan"). The Polk Plan allows for eligible employees to contribute up to 15% of their annual compensation up to the statutory limitations. During 2007, the Company provided a match totaling 60% of the employee's contribution, up to 5% of pay, with no maximum other than the statutory maximum. Under the Polk Plan, contributions vest under a three year cliff vesting. The Company temporarily suspended contribution matching during 2008. Consolidated contributions under these plans were \$280 for the year ended December 31, 2007.

13. Income Taxes

The geographic sources of income (loss) from continuing operations before taxes are as follows:

	Years Ended December 31,	
	2008	2007
United States.....	\$ (41,429)	\$ (171,949)
Foreign.....	(1,645)	(9,653)
	<u>\$ (43,074)</u>	<u>\$ (181,602)</u>

The components of the provision for (benefit from) income taxes are as follows:

	Years Ended December 31,	
	2008	2007
Current:		
Federal.....	\$ 1,199	\$ (3,534)
State.....	871	(61)
Foreign.....	231	349
	<u>2,301</u>	<u>(3,246)</u>
Deferred:		
Federal.....	10,045	(32,919)
State.....	535	(4,626)
Foreign.....	(1,002)	(843)
	<u>9,578</u>	<u>(38,388)</u>
	<u>\$ 11,879</u>	<u>\$ (41,634)</u>

The provision for (benefit from) income taxes differs from the federal statutory rate as follows:

	Years Ended December 31,	
	2008	2007
Expected provision at federal statutory rate.....	\$ (15,076)	\$ (63,561)
State tax, net of federal tax benefit.....	(2,157)	(3,674)
Goodwill impairment.....	-	23,593
Tax credits.....	(600)	(132)
US taxes on accumulated foreign earnings.....	2,387	
Foreign tax.....	-	111
Other permanent items.....	195	301
Stock-based compensation.....	2,019	1,293
Change in deferred tax valuation allowance.....	24,857	498
Other, net.....	254	(63)
	<u>\$ 11,879</u>	<u>\$ (41,634)</u>

Significant components of the Company's deferred tax assets and liabilities were as follows:

	<u>Years Ended December 31,</u>	
	<u>2008</u>	<u>2007</u>
Deferred tax assets:		
Allowances and accruals.....	\$ 4,899	\$ 4,834
Revenue deferred for books.....	168	166
State taxes.....	56	197
Stock-based compensation.....	142	436
Net operating losses.....	55	144
Other comprehensive income.....	2,577	-
Other.....	644	459
Total current deferred tax assets.....	<u>8,541</u>	<u>6,236</u>
Goodwill.....	19,171	21,452
Stock-based compensation.....	1,526	2,987
Foreign tax credits.....	1,490	
Other comprehensive income.....	401	1,393
Net operating losses.....	710	570
Depreciation.....	292	142
Other.....	263	-
Non-current deferred tax asset.....	<u>23,853</u>	<u>26,544</u>
Total deferred tax assets.....	32,394	32,780
Valuation allowance.....	(27,891)	(498)
Total deferred tax assets.....	<u>\$ 4,503</u>	<u>\$ 32,282</u>
Deferred tax liabilities:		
Inventory step-up.....	\$ -	\$ (108)
Total current deferred tax liability.....	<u>-</u>	<u>(108)</u>
Intangible assets.....	(14,290)	(35,000)
US taxes on unremitted foreign accumulated earnings.....	(2,382)	-
Total long-term deferred tax liability.....	<u>(16,672)</u>	<u>(35,000)</u>
Total deferred tax liabilities.....	<u>(16,672)</u>	<u>(35,108)</u>
Net deferred income taxes.....	<u>\$ (12,169)</u>	<u>\$ (2,826)</u>

The Company had federal net operating loss and tax credit carryovers as of December 31, 2007 of \$9,723 and \$132, respectively. The Company utilized all of the 2007 net operating loss and tax credits in the federal carryback period.

The Company has total state net operating loss carryforwards of approximately \$20,927. The carryforwards begin to expire in 2009. Certain of the state loss carryforwards are likely to expire unused, for which the company has provided a valuation allowance.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. Management considers all available evidence including the scheduled reversal of deferred tax liabilities, projected future taxable income and tax planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable losses over the periods which the deferred taxes are deductible, management believes it is more likely than not that the Company will not realize the benefits of the remaining deductible differences. The Company has established a full valuation allowance against its U.S. deferred tax assets except for the net operating losses that can be carried back to recover taxes previously paid. The valuation allowance at December 31, 2008 and 2007 was \$27,891 and \$498, respectively. Management will reassess the realization of the deferred tax assets based on the criteria of SFAS No. 109 each reporting period. To the extent that the financial results of the U.S. operations improve and the deferred tax asset becomes realizable, the Company will be able to reduce the valuation allowance through earnings.

If the actual tax deduction realized when stock options are exercised or restricted stock units are delivered is less than recognized

compensation expense, the Company may have significant tax shortfalls in the future. The tax provision for 2008 and 2007 includes tax shortfalls of \$2,019 and \$1,293, respectively.

On January 1, 2007, the Company adopted FIN 48, "Accounting for Uncertainty in Income Taxes." As a result of the implementation of FIN 48, the Company recognized a \$541 decrease to reserves for uncertain tax positions. This decrease was accounted for as an adjustment to the beginning balance of retained earnings.

A reconciliation of the beginning and ending balance of unrecognized tax benefits is as follows:

Balance at January 1, 2007.....	\$	876
Additions based on tax positions related to the current year.....		907
Additions for tax positions of prior years.....		463
Reductions for tax positions of prior years.....		-
Settlements.....		(38)
Expiration of the statute of limitations for the assessment of taxes.....		(151)
Balance at December 31, 2007.....		<u>2,057</u>
Additions based on tax positions related to the current year.....		69
Additions for tax positions of prior years.....		8
Reductions for tax positions of prior years.....		(180)
Settlements.....		(421)
Expiration of the statute of limitations for the assessment of taxes.....		(173)
Balance at December 31, 2008.....	\$	<u><u>1,360</u></u>

The total amount of unrecognized tax benefits that, if recognized, would affect the Company's effective tax rate as of December 31, 2008 and 2007 was \$539 and \$1,558, respectively.

The Company's continuing practice is to recognize interest and penalties related to uncertain tax positions in income tax expense. Accrued interest and penalties related to uncertain tax position as of December 31, 2008 and 2007 was \$516 and \$718, respectively.

The Company expects the change in the FIN 48 liability for unrecognized tax benefits to be a decrease of approximately \$400 in the next 12 months and does not expect the changes to materially affect its operating results or financial position. The 2004 through 2007 tax years remain open to examination by major taxing jurisdictions to which the Company is subject.

Management regularly reviews that status of the accumulated earnings of each of our foreign subsidiaries and reassesses the determination to reinvest those earnings based on the Company's overall financing plans. Management has determined that the accumulated earnings of the foreign subsidiaries will not be reinvested indefinitely and has recognized US tax on those earnings, net of any foreign tax credits, in accordance with APB No. 23, "Accounting for Income Taxes, Special Area."

14. Related Party Transactions

Under an operating lease agreement for its primary distribution facility and corporate headquarters, the Company paid a company owned by a Board member \$2,067 and \$1,994 during the years ended December 31, 2008 and 2007, respectively.

Under a service agreement to develop software, the Company paid a vendor owned by a member of management \$172 during the year ended December 31, 2008.

15. SIRIUS Satellite Radio Agreement

Since 2005, the Company has had exclusive rights to market and sell certain SIRIUS-branded satellite radio receivers and accessories to its existing U.S. retailer customer base. In October 2008, the Company and SIRIUS XM Radio, Inc ("SIRIUS", f/k/a SIRUS Satellite Radio, Inc.) agreed to allow the distribution agreement to terminate on its own terms effective January 31, 2009. To facilitate the efficient transition and termination of the agreement, the Company and SIRIUS agreed to a process and timeline relating to the wind-down of the relationship. Through January 31, 2009, the Company continued to fulfill orders from its retailer customer base. In accordance with the timeline and process specified in the letter agreement, during the first quarter of 2009, on a prepayment basis,

SIRIUS purchased from the Company substantially all remaining SIRIUS-branded inventory and all such products returned to the Company by retailers at prices defined in the agreement. Effective February 1, 2009, SIRIUS, or its new distributor, assumed all cost and responsibility for any further product returns.

16. Commitments and Contingencies

Operating leases

The Company leases its facilities and some equipment under non-cancelable operating leases that expire on various dates through December 2016. Rent expense is recognized on a straight-line basis over the lease term, and for the years ended December 31, 2008 and 2007 was approximately \$4,996 and \$5,025, respectively. The Company subleases a portion of two of its facilities to others. For the years ended December 31, 2008 and 2007, sublease income of \$472 and \$437, respectively, is reflected as a reduction of operating expenses in the accompanying consolidated statement of operations.

Future minimum lease payments, net of sublease income, for all operating leases for the years ending December 31 are as follows:

2009.....	\$	4,273
2010.....		4,192
2011.....		4,155
2012.....		4,320
2013.....		4,487
Thereafter		12,262
Total	\$	<u>33,689</u>

Litigation

On March 31, 2004, Omega Patents, L.L.C. (“Omega”), filed a claim in the United States District Court for the Middle District of Florida, OMEGA PATENTS, L.L.C. vs. FORTIN AUTO RADIO, INC., alleging breach of a license agreement. On November 11, 2005, Omega amended its complaint to add the Company as a defendant in the suit, alleging patent infringement. Specifically, Omega alleged that certain of the Company’s products infringed certain Omega patents. Omega sought both an injunction and unspecified monetary damages, as well as exemplary damages, attorneys’ fees, and costs. On February 12, 2007, the jury returned a verdict in favor of Omega, awarding Omega \$615 in damages, which was accrued as of December 31, 2006. On April 4, 2007, the trial court enhanced the damages for a total award of \$1,800. The trial court also awarded attorney’s fees to Omega and granted a permanent injunction that prohibited the Company from making, using, or selling any products that infringe on the Omega patents, and required the Company to recall and destroy any of the infringing products that were in the inventory of retailer customers. On May 12, 2007, the Company entered into a Master and Cross-License Agreement with Omega settling all disputes between the parties. The agreement provided that the Company pay an upfront fee of \$5,000 and take a royalty bearing license from Omega on vehicle databus systems and vehicle tracking systems. The Company has also entered into a broad long-term cross-license for technology related to vehicle security and convenience systems. In May 2007, the court dismissed the case with prejudice. During the year ended December 31, 2007, the Company paid all \$5,000 owed pursuant to this settlement. As such, the Company had no accrual related to the settlement as of December 31, 2007. The Company incurred legal fees of approximately \$689 during 2007.

From time to time, the Company is involved in other litigation and proceedings in the ordinary course of its business. The Company is not currently involved in any legal proceedings that it believes would have a material adverse effect on its business or financial condition.

17. Subsequent Event

On January 11, 2009, the Company’s board of directors approved the filing of a Form 25 and a Form 15 to voluntarily delist the Company’s common stock from the NASDAQ Global Market, voluntarily deregister the Company’s common stock with the Securities and Exchange Commission, and suspend the Company’s reporting obligations under the Securities Exchange Act of 1934, as amended. The Company filed the Form 25 on January 26, 2009 and the Form 15 on February 6, 2009. The Company expects the deregistration to become effective within 90 days of the filing of the Form 15 with the Securities and Exchange Commission.