

ROCKFORD CORP

FORM 10-K (Annual Report)

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Industry	Audio & Video Equipment
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SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-K

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

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2007

Commission File Number 000-30138

ROCKFORD CORPORATION

(Exact name of Registrant as Specified in Its Charter)

Arizona
*(State or Other Jurisdiction of
Incorporation or Organization)*

86-0394353
*(IRS Employer
Identification No.)*

600 South Rockford Drive
Tempe, Arizona 85281
(480) 967-3565

(Address and Telephone Number of Principal Executive Offices)

Securities Registered Pursuant to Section 12(b) of the Act:

None

Securities Registered Pursuant to Section 12(g) of the Act:

Common Stock (\$.01 Par Value)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

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

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

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

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

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting Company

(Do not check if a smaller reporting company)

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

The aggregate market value of the voting stock held by non-affiliates of the registrant was \$12,249,008 computed by reference to the price at which registrant's common stock last sold as of June 30, 2007.

There were 8,781,208 shares of registrant's Common Stock issued and outstanding as of March 12, 2008.

Documents Incorporated by Reference: Portions of the registrant's definitive Proxy Statement relating to the 2008 Annual Meeting of Stockholders to be held on May 8, 2008, are incorporated by reference into Part III of this Form 10-K.

ROCKFORD CORPORATION
FORM 10-K
DECEMBER 31, 2007
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The market value of Rockford's voting stock held by non-affiliates shown on the cover page is based on:

- Rockford's estimate that the number of shares held by non-affiliates as of June 30, 2007, was approximately 5,212,344; and
- \$2.35 per share, the price at which Rockford's shares were last sold as of June 30, 2007, as reported by The NASDAQ Stock Market. June 30, 2007, is the last business day of Rockford's most recently completed second fiscal quarter.

Rockford's calculation of the number of shares held by affiliates is a good faith estimate for this Annual Report. Shares held by affiliates include all shares beneficially owned by Rockford's executive officers and directors. They also include shares held by any shareholder known to Rockford who beneficially owned more than 10% of Rockford's shares as of June 30, 2007.

Forward-Looking Statements And Risk Factors

We make forward-looking statements in this report including, without limitation, statements concerning the future of our industry, product development, business strategy, continued acceptance and growth of our products, dependence on significant customers and suppliers, and the adequacy of our available cash resources. Our statements may contain projections of results of operations or of financial condition. These statements may be identified by the use of forward-looking terminology such as “may,” “will,” “believe,” “expect,” “anticipate,” “estimate,” “continue” or other similar words.

Forward-looking statements are subject to many risks and uncertainties. We caution you not to place undue reliance on these forward-looking statements, which speak only as at the date on which they are made. Actual results may differ materially from those described in these forward-looking statements. We disclaim any obligation or undertaking to update these forward-looking statements to reflect changes in our expectations or changes in events, conditions, or circumstances on which our expectations are based.

When considering our forward-looking statements, you should keep in mind the risk factors and other cautionary statements identified in this report. The risk factors noted throughout this report, particularly in the discussion in Item 1A, and other risk factors that we have not anticipated or discussed, could cause our actual results to differ significantly from those anticipated in our forward-looking statements.

PART I

Item 1. *Business*

Rockford Business

Rockford designs, assembles, and distributes high performance mobile audio products. Rockford's mobile audio products are sold to consumers who want to listen to powerful, high quality sound in their cars, trucks and boats. Rockford's products include digital and analog amplifiers, subwoofers and speakers, accessories, signal processors, and speaker enclosures.

Rockford markets its products:

- Primarily in the mobile audio aftermarket, where Rockford's products replace or supplement a vehicle's original audio system. In this market Rockford sells its products under the Rockford Fosgate and Lightning Audio brands; and
- Secondly as OEM mobile audio products, installed as original equipment in select vehicles. Rockford's OEM products are offered primarily in various Nissan and Mitsubishi automobiles. Rockford's OEM products are sold primarily under the Rockford Fosgate and Rockford Acoustic Design brands.

Rockford's Brands

Rockford markets its products under the following primary brands:

- *Rockford Fosgate*. Rockford offers distinctive product lines that produce powerful, high quality sound under the Rockford Fosgate brand. Rockford Fosgate mobile audio products are marketed under two primary product lines:
 - Punch Series — the line for the majority of Rockford's amplifiers, subwoofers, speakers and enclosures; and
 - Power Series — the line for Rockford's higher performing amplifiers, subwoofers, and speakers.

Rockford sells a full line of Rockford Fosgate mobile audio accessories under the Connecting Punch brand. Rockford also sells Rockford Fosgate products, or licenses its brand and technology, to Nissan and Mitsubishi for installation as part of OEM audio systems;

- *Rockford Acoustic Design*. Rockford Acoustic Design is a premium brand, primarily for OEM products. Systems using this brand are currently offered in select Mitsubishi automobiles; and
- *Lightning Audio*. Rockford sells amplifiers, subwoofers, speakers, and accessories under the Lightning Audio brand. Lightning Audio products are generally more moderately priced than Rockford Fosgate products.

In addition to these primary brands Rockford markets complementary products under a secondary brand, *InstallEdge.com*. Rockford uses the InstallEdge.com business-to business brand to offer installation-shop supplies to installation shops and audio product installers.

Rockford Strategy

Rockford's goal is to sell some of the most recognized and respected high performance mobile audio products in the world. Key elements of Rockford's strategy are to:

- Continue to introduce new and technologically innovative mobile audio products that embody distinctive Rockford sound qualities;
- Expand Rockford's mobile audio OEM business; and
- Broaden Rockford's distribution by entering new distribution channels and increasing penetration of Rockford's existing distribution channels, both in the U.S. and internationally.

Rockford believes it can grow its business and become a more significant participant in the worldwide mobile audio market.

Rockford Products

Percent of Sales by Product Class

Rockford’s sales since 2005 were divided among Rockford’s principal product classes as shown in the following table:

Product Class:	Year Ended December 31,		
	2005	2006	2007
Amplifiers	43.8%	45.8%	42.2%
Speakers	35.4	34.9	36.2
Accessories	10.7	12.8	14.1
Others(1)	10.1	6.5	7.5
Total	100.0%	100.0%	100.0%

(1) Includes source units, enclosures, signal processors, digital media products, and other products. No single product class in this group accounted for more than 10% of Rockford’s sales in any of these years.

Financial information about geographic segments may be found in the Notes to Consolidated Financial Statements of this Form 10-K.

Aftermarket Mobile Audio Products

Rockford offers high performance aftermarket mobile audio products consisting of the following primary types of products:

- *Amplifiers.* Amplifiers increase the voltage and current coming from the source unit, providing more power than possible from a source unit alone. Amplifiers are essential for a high performance mobile audio system, particularly for consumers who desire strong bass (low frequency) performance;
- *Subwoofers and Speakers.* Subwoofers and speakers accept a signal from a source unit or amplifier and translate it into sound. Subwoofers are speakers that are eight inches or greater in diameter and are designed to play bass frequencies. Speakers less than eight inches in diameter are not subwoofers and are designed to play higher frequencies. Aftermarket subwoofers and speakers provide dramatically improved sound quality compared to most OEM mobile audio systems and are often the single most important improvement consumers can make to their mobile audio systems;
- *Accessories.* Accessories are the additional items required to install and use mobile audio products. Accessories include amplifier wiring kits, fuses, circuit breakers, interconnect cables, speaker cables, stiffening capacitors, battery clamps, connectors, adaptors, and carpet/fabric/surface applications. Accessories make Rockford’s products compatible with OEM components and improve the performance of a mobile audio system;
- *Signal Processors.* Signal processors provide the ability to “tune” the sound of the audio system for better performance and also simplify the installation of aftermarket amplifiers and speakers in OEM systems; and
- *Enclosures.* Enclosures are used to enhance the bass performance of subwoofers and to position speakers in locations that produce better sound.

Under the Rockford Fosgate brand Rockford currently offers the following products:

- Amplifiers:
 - Amplifiers under the Punch Series and Power Series lines, with rated power from 200 to 4,000 watts, and minimum advertised prices from \$200 to \$2,500. Rockford's amplifiers include 1, 2 and 4 channel alternatives, giving consumers the ability to select an optimum configuration for their system;
 - In the amplifier category Rockford has also introduced a Hybrid Technology 15,000-watt amplifier, the limited edition HT15kW, at a minimum advertised price of \$25,000;
- Subwoofers and Speakers:
 - Subwoofers and speakers under Rockford's Punch Series and Power Series lines, with minimum advertised prices from \$60 to \$1,800;
- Accessories:
 - Accessories under Rockford's Connecting Punch brand, including amplifier installation kits, interconnect and speaker cables, carpet/fabric/surface applications and stiffening capacitors;
- Signal Processors
 - In the signal processor category Rockford offers its 3Sixty Interactive Signal Processors in two models at minimum advertised prices of \$399 and \$699; and
- Enclosures:
 - Subwoofer enclosures, including "loaded enclosures" that include a subwoofer and, in some cases, an amplifier, at minimum advertised prices from \$149 to \$399.

Under the Lightning Audio brand Rockford currently offers the following products:

- Amplifiers:
 - Amplifier models with rated power from 60 to 2,000 watts and minimum advertised prices from \$100 to \$1,000;
- Subwoofers and Speakers:
 - Subwoofers and speakers with minimum advertised prices from \$30 to \$600; and
- Accessories:
 - Accessories, including interconnect and speaker cables, stiffening capacitors, battery clamps and installation kits.

Under Rockford's InstallEdge.com brand Rockford sells various back shop supplies, including vehicle harnesses, power distribution adapters, batteries, RCA connectors, wire, wiring accessories and fuses.

OEM Products

Nissan North America offers Rockford Fosgate branded OEM systems in several Nissan vehicles and Mitsubishi Motors offers Rockford Fosgate and Rockford Acoustic Design branded OEM systems in several vehicles. Rockford may provide amplifiers, enclosures or speakers for certain of these vehicles as well as branding the source unit (radio/CD player) or the entire audio system under the Rockford Fosgate and Rockford Acoustic Design brand.

New Products

Rockford introduces new products and enhances its existing products on a regular basis. In 2007 Rockford introduced new lines of Rockford Fosgate amplifiers, updating both the Punch and Power series of product lines, and also introduced new subwoofers and speakers under the Rockford Fosgate Punch series.

Engineering And Product Development

Engineering and product development is a primary focus of Rockford's business because of the demand by Rockford's core consumers for high quality and powerful sounding products. Rockford focuses its engineering and development efforts primarily on enhancing current products and developing new products. Rockford's engineering

and development staff consists of engineers in research, development and sustaining groups, as well as other support staff, dedicated to the development of Rockford's current products and of Rockford's technology for future products.

Sales and Marketing

Rockford endeavors to have its brands project an image that appeals to consumers who appreciate high quality and value. Rockford's primary sales and marketing activities are listed below:

- Making regular calls to dealers and providing them with demonstration products, point-of-purchase displays and other marketing materials;
- Training dealer sales and installation personnel. For 2007 and 2008 Rockford is re-emphasizing its "Rockford Technical Training Institute" training programs that are designed to enhance the ability of dealer personnel to design, sell and install superior audio systems using Rockford's products;
- Regular interaction with industry press editors who are often the opinion makers for salespeople at the retail level as well as end users;
- Support for competitors in regional and national car audio shows and competitions;
- Participation in professional and consumer trade shows;
- Maintaining product and brand information for consumers and retailers on Rockford's web sites; and
- Initiating targeted advertising in periodicals read by potential consumers.

Rockford's corporate web site, located at www.rockfordcorp.com, and its brand sites such as www.rockfordfosgate.com, www.lightningaudio.com, www.rockfordacousticdesign.com, and www.installedge.com offer consumers and retailers reliable and comprehensive information about product offerings and consumer services.

Distribution

North American Distribution. Rockford currently sells its mobile audio products in the U.S. and Canada directly to retailers who operate approximately 6,000 retail stores. These include stores operated by independent specialty dealers, audio/video retailers, consumer electronic chains, mass merchandisers, internet retailers and catalog merchants. Rockford may appoint a retailer to sell some or all of its brands.

Rockford sells directly to most of its authorized retailers using independent sales representative firms who identify, recruit, sell to, and provide support to retailers in their regions. Rockford has entered into agreements with each of these sales representative firms under which Rockford appoints them its sales representative for a specific territory and specific products under varying terms. Rockford pays its independent sales representatives commissions based on sales of Rockford's products in their territory. Commission amounts range from 1% to 10% of sales depending upon (1) product category, (2) customer category and (3) achievement of sales targets.

Some Rockford Fosgate sales representatives stock a small quantity of Rockford Fosgate products for resale to smaller dealers. These smaller dealers are generally located in rural areas, or otherwise have very small volume potential, so that it is not economical for Rockford to appoint them as direct retailers. They nevertheless provide a useful extension of Rockford's distribution system into more remote regions. Rockford's stocking representative program allows it to serve these smaller dealers efficiently. In addition, in a few instances where stocking representatives are not available, Rockford has also appointed independent distributors to sell Rockford Fosgate products to smaller dealers in a particular territory.

Rockford has converted the majority of the specialty retailer sales of Lightning Audio products in North America to an independent distribution model, appointing distributors who purchase Lightning Audio products and re-sell them to independent dealers in their territory. Rockford also continues to sell Lightning Audio products directly to larger national and regional dealers.

Rockford supports its North American independent sales representative firms, retailers and distributors using an internal staff of regional managers and sales support staff.

International Distribution. Rockford currently sells its mobile audio products in over 50 countries outside the U.S. and Canada. In all countries outside of the U.S. and Canada Rockford uses independent distributors who purchase products from Rockford and resell them to retailers in their designated territories. The distributors assume inventory risk and take responsibility for warranty service in their territory. Rockford supports its international distributors using an in-house staff of international sales managers.

Competition

Rockford competes in the mobile audio market on the basis of sound quality, brand recognition, innovation and technology, reliability, breadth of product line, distribution capabilities and price. Some of Rockford's competitors have greater financial, technical and other resources than Rockford. Some seek to offer higher perceived performance and others seek to offer lower prices on competing products. To remain competitive, Rockford believes it must regularly introduce new products, add performance features to existing products and limit increases in prices or even reduce prices.

Rockford competes in a crowded market with only limited barriers to entry. Its competitors include companies that span the gamut from integrated "full line" consumer electronics manufacturers to niche specialty companies focused solely on narrow segments of the mobile audio market. Rockford's principal competitors are listed below:

- *Mobile Audio Amplifiers:* Alpine, JL Audio, Kenwood, Kicker, MTX, Pioneer and Sony;
- *Mobile Audio Subwoofers and Speakers:* Alpine, Boston Acoustics, Infinity, JL Audio, Kenwood, Kicker, MTX, Pioneer and Sony;
- *Mobile Audio Accessories:* Monster Cable, AAMP of America and Scoshe;

Rockford's OEM products compete directly with each auto manufacturer's in-house manufacturing capability as well as such outside suppliers as Delphi, Visteon, Matsushita, Bose and Harman International.

The OEM products offered by automobile manufacturers also impact Rockford's aftermarket mobile audio products. In recent years, many automobile manufacturers have:

- integrated additional functions such as navigation into vehicle electronic systems;
- changed the designs of their cars in ways that make (or are perceived to make) installation of aftermarket audio products more difficult or expensive; and
- somewhat improved the quality of their mobile audio offerings.

These efforts have resulted in an increased market share for OEM mobile audio systems. Rockford believes that this increased market share for OEM products has reduced the overall market for aftermarket mobile audio products and is one of the causes of reduced sales in the aftermarket, both industry wide and for Rockford.

Sourcing and Manufacturing

Rockford has concluded that manufacturing is no longer a core part of its operations, that third party manufacturers are a more efficient source of manufacturing capacity, and that Rockford should focus its resources more directly on design, technology, and marketing. Rockford phased out internal manufacturing of subwoofers during 2007 and substantially reduced internal manufacturing of amplifiers. Rockford currently assembles amplifiers at Rockford's facilities in Tempe, Arizona, but plans to complete the outsourcing of amplifier assembly during 2008.

Rockford believes that outsourcing production of its products to third party manufacturers will reduce overall product costs. The transition involves significant operational risks as Rockford ramps down internal production and ramps up external manufacturing. In 2007, Rockford purchased approximately \$10.4 million and \$5.7 million, respectively, of finished product from its two largest suppliers, Edge Global Holdings Limited and Sound Factor. These Asian-based companies manufactured some of Rockford's speakers, subwoofers, amplifiers, and accessories.

When it outsources manufacturing to a third party manufacturer, Rockford provides specifications and cosmetic renderings for outsourced products and works with the manufacturer to develop products that meet Rockford's requirements. Rockford generally owns all of the tooling and the manufacturer is obligated not to sell identical products to anyone other than Rockford.

Most of Rockford's products use standard parts and components that can be purchased from multiple sources. In many instances, however, Rockford sources components or finished products from one or a small number of suppliers to leverage dollars and volumes. Rockford relied on two component suppliers, Kontion Manufacturing Services and Avnet, Inc., for purchases of approximately \$8.3 million and \$2.0 million, respectively, during 2007.

Rockford believes alternative sources are available for substantially all of Rockford's inventory requirements, although changes in suppliers would take time and would involve significant transitional costs. Rockford believes that its sources and supplies of finished goods and components are adequate for its needs.

Intellectual Property

Rockford relies upon a combination of trade secret and trademark laws, non-disclosure agreements and patents to protect its proprietary rights. Rockford has registered its trademarks and trade names both in the U.S. and, where appropriate, internationally and is committed to maintaining and protecting them. Rockford believes its trademarks and trade names are material to its business and are well known among consumers in its principal markets. Rockford's principal trademarks and trade names are:

- **Rockford Fosgate**®
 - Rockford's "Diamond R" logo®
 - The Punch®
 - Rockford Acoustic Design™
 - 3Sixty™
- **Lightning Audio**®
 - Strike®
 - Storm®
 - Bolt®

Significant Customers and Seasonality

Best Buy is a significant customer and accounted for 23.4%, 22.6% and 19.2% of Rockford's sales for 2005, 2006 and 2007, respectively. Rockford products are currently sold in each of its more than 900 Best Buy and Future Shop stores in North America. Best Buy is one of the largest volume specialty retailers of consumer electronics and entertainment software in the U.S. Rockford anticipates that Best Buy will continue to account for a significant portion of its sales for the foreseeable future.

Nissan is also a significant customer, representing 13.7%, 14.9% and 7.5% of sales during 2005, 2006, and 2007 respectively. Rockford anticipates that Nissan will continue to be significant customer for the foreseeable future. Sales to Nissan declined in 2007 because 2005 and 2006 sales were higher than normal levels because Nissan included Rockford Fosgate systems in a higher than normal proportion of Sentra cars during the last year of the prior model generation's life. Many of the Nissan vehicles in which Rockford Fosgate Systems are offered are truck based, so that the reductions in demand for trucks has also reduced sales to Nissan.

Neither Best Buy nor Nissan is obligated to long-term purchases of Rockford's products and each has considerable discretion to reduce, change or terminate purchases of Rockford's products. The loss of Best Buy or Nissan as a customer or significant reductions in their purchases of Rockford's products would materially reduce Rockford's sales.

Rockford's significant customers generally help to smooth out Rockford's sales seasonality. For Rockford's specialty and audio-video dealers, the peak-selling season is in the spring and summer and the slowest season is typically in the fourth quarter. Rockford believes that it experiences this seasonality because its core 16-24 year old consumers tend to buy mobile audio products during the spring and summer when they are on semester breaks and when generally more favorable weather makes it easier to install mobile audio products. Best Buy sales, while strong in May and June, are not as dependent upon Rockford's core consumers and are also strong in the fourth quarter due to seasonal retail sales.

Product Support

To maintain and enhance its relationships with retailers, Rockford provides numerous support services, including product and installation training, sales training and technical and customer service support. Rockford's "Rockford Technical Training Institute" training programs are designed to provide improved skills to dealer personnel and enhance their ability to design, sell and install superior audio systems using Rockford's products. In addition, Rockford's web site provides comprehensive information for dealers and distributors, including product schematics, ad layouts and logos.

Rockford products carry standard warranties to purchasers who buy Rockford products from authorized dealers. The warranties cover defects in material and workmanship under which Rockford will either repair or replace a product that fails during the warranty period. Rockford also offers repair services for products that are no longer covered under the original warranty. For U.S. and Canadian customers, Rockford has in-house customer service, repair and technical support personnel who provide general company information, installation support, troubleshooting and system design assistance. Rockford also provides a direct repair program that repairs and ships repaired product rapidly, reducing retailer and consumer inconvenience if products fail to perform properly.

For Rockford's international customers, Rockford requires its distributors to provide warranty and customer service to consumers in the countries where the distributors are authorized to sell Rockford products.

Employees

At December 31, 2007, Rockford had approximately 162 full-time employees in various functions. This was a reduction of 94 full-time employees compared to December 31, 2006. In addition, Rockford uses temporary personnel as needed. Rockford has never had a work stoppage and none of its employees are unionized. Rockford believes its employee relations are good.

Environmental Compliance

Whenever possible, Rockford avoids using hazardous materials in its production processes. Two chemicals used in the basic electronic manufacturing processes, lacquer and flux, are listed as hazardous substances by the U.S. Environmental Protection Agency. Rockford uses them in limited quantities in its production facility, taking care to see that they are stored, used and disposed of in the proper manner. Rockford's direct use of these materials was significantly lower in 2007 because of the planned outsourcing of manufacturing to third parties.

Rockford believes that its compliance with federal, state, local and foreign laws and regulations governing the discharge of materials into the environment, or otherwise relating to the protection of the environment, will not have a material effect upon its capital expenditures, earnings or competitive position. Rockford does not anticipate material capital expenditures for environmental control facilities for the remainder of the current fiscal year or the succeeding fiscal year.

All of Rockford's 2008 product offerings are compliant with the European Union's directive on the restriction of hazardous substances ("RoHS").

Item 1A. Risk Factors

RISK FACTORS THAT MAY AFFECT ROCKFORD'S OPERATING RESULTS, BUSINESS PROSPECTS AND STOCK PRICE

Before you buy or sell Rockford stock, you should be aware that there are risks, including those described below and others Rockford has not anticipated or discussed. You should consider carefully these and other risk factors, together with all of the other information included in Rockford's filings with the SEC and Rockford's periodic press releases, before you decide to buy or sell shares of Rockford's common stock.

As you consider these risk factors, Rockford also calls your attention to Rockford's statements about Forward Looking Statements and Risk Factors before Part I of this Annual Report.

Rockford's products may not satisfy shifting consumer demand or compete successfully with competitors' products.

Rockford's business is based primarily on the demand for aftermarket mobile audio products and on Rockford's ability to deliver products that provide powerful, high quality sound. If Rockford fails to introduce new products, misinterprets consumer preferences or fails to respond to changes in the marketplace, consumer demand for its products could decrease and its brands' images could suffer. In addition, Rockford's competitors may introduce superior designs or business strategies, undermining Rockford's distinctive image and its products' desirability. If any of these events occur, they could cause Rockford's sales to decline.

Aftermarket Mobile Audio Sales May Continue to Decline, Reducing the Potential Market Rockford is Seeking to Address

Aftermarket mobile audio sales have been soft over an extended period for many reasons, including the perceived difficulty of replacing newer OEM audio systems, the somewhat improved performance of OEM mobile audio systems and the availability of alternative audio products such as the iPod. Consumer spending for aftermarket mobile audio products is volatile and is affected by economic conditions such as:

- General business conditions;
- Employment levels, especially among Rockford's core consumers (who tend to be less experienced workers and are particularly subject to layoff if employment levels decline);
- Consumer confidence in future economic conditions;
- Energy prices; and
- Interest and tax rates.

The mobile audio aftermarket in the U.S. has suffered from a decline in overall sales since 2000, which has made it difficult for Rockford and for competitors to maintain sales. The efforts to maintain sales have eroded margins and led to greater competition to place inventory in dealers. The market for mobile audio products continues to be unpredictable and Rockford is not able to predict when or whether the decline in mobile aftermarket sales will end.

A decline in discretionary spending likely would reduce Rockford's sales.

Because mobile audio sales are highly discretionary, a recession in the general economy or a general decline in consumer spending is likely to significantly reduce Rockford's sales.

Rockford may lose market share and its brand image may erode as Rockford manages the distribution channels for its mobile audio products.

Rockford distributes Rockford's products both through specialty distribution channels (including specialty dealers who sell only mobile audio products and audio/video retailers) and through "big box" national retailers, such as Best Buy and Wal-Mart. Rockford is seeking to increase distribution of Rockford's products through each of these distribution channels. Rockford also sells its products or licenses its brand and technologies as standard or optional OEM systems in Nissan and Mitsubishi vehicle models and is working to expand its OEM sales. The distribution and marketing needs of these channels are sometimes in conflict so that, for example, Rockford's efforts to increase "big box" sales of its products may reduce the perceived value of its products to specialty retailers.

Rockford's distribution channels and strategies create significant risks that:

- *Rockford may alienate its specialty dealer base.* Some specialty dealers or audio/video retailers may react to Rockford's "big box" and OEM strategies by reducing their purchases or even replacing Rockford's products with competing products; and
- *Rockford's brand image may erode.* Selling in "big box" and OEM markets may erode Rockford's brand image, which could decrease Rockford's product prices and profit margins.

Rockford's inability to manage Rockford's distribution channels in a way that mitigates these risks may reduce its sales and profitability.

Any decrease in demand for Rockford amplifiers or speakers could significantly decrease sales.

A significant portion of Rockford's future revenue depends upon sales of Rockford's amplifier and speaker products. These two product lines collectively accounted for approximately 78.5% of Rockford's sales in 2007, 80.7% of Rockford's sales in 2006 and 79.2% of Rockford's sales in 2005. If sales of either of these two product types decline, results of operations could be adversely affected.

The loss of Best Buy or Nissan as a customer or significant reductions in their purchases of Rockford's products would reduce sales.

Best Buy and Nissan are significant customers, with Best Buy accounting for 23.4%, 22.6% and 19.2% of Rockford's sales in 2005, 2006 and 2007, respectively and Nissan accounting for 13.7%, 14.9% and 7.5% of Rockford sales in 2005, 2006 and 2007, respectively. Rockford anticipates that Best Buy and Nissan will continue to account for a significant portion of Rockford's sales for the foreseeable future, but neither is obligated to any long-term purchases. Both have considerable discretion to reduce, change or terminate purchases of Rockford's products. If Best Buy or Nissan significantly reduce or terminate their purchases of Rockford products Rockford's sales and operations are likely to decline.

Rockford may lose sales and market share if it is unable to compete successfully against current and future competition, including products offered by aftermarket suppliers and by auto manufacturers.

Competition could result in reduced margins on Rockford's products and loss of market share. Rockford's primary markets are very competitive, with only limited barriers to entry and large numbers of competitors. Rockford's principal mobile audio competitors include Alpine, Boston Acoustics, Infinity, JL Audio, Kenwood, Kicker, Monster Cable, MTX, Pioneer, Sony and Stinger.

Rockford also competes with automobile manufacturers who continue to integrate OEM audio systems with other electronic features in their vehicles and somewhat improve their sound quality. These changes increase the perceived difficulty of installing Rockford's aftermarket products, reduce consumers' perception of the need to improve their factory audio systems and have reduced demand for aftermarket mobile audio products. Rockford believes that the changes auto manufacturers have made in recent years have significantly reduced overall demand for aftermarket mobile audio systems.

If Rockford does not continue to develop, introduce and achieve market acceptance of new and enhanced products, sales may decrease.

To remain competitive, Rockford believes that it must regularly introduce new products, improve the performance of existing products and limit increases in prices or even reduce prices. Rockford's inability to do so in a timely manner could reduce sales and profitability.

In order to increase sales in current markets and gain footholds in new markets, Rockford must maintain and improve existing products, while developing and introducing new products. Rockford's new and enhanced products must respond to technological developments and changing consumer preferences.

Rockford may experience difficulties that delay or prevent the development, introduction or market acceptance of new or enhanced products. Rockford's move to outsourced manufacturing of more of its products may also delay the development of new products because of the added complexity of product development for outsourced products. Furthermore, Rockford may not detect and correct defects in products before it ships them to customers. This may result in loss of sales or delays in market acceptance.

Even after introduction, new or enhanced products may not satisfy consumer preferences and product failures may cause consumers to reject the new products. As a result, these products may not achieve market acceptance. In addition, competitors' new products and product enhancements may cause consumers to defer or forego purchases of Rockford's products.

Rockford's OEM sales and royalty revenue depends on demand for the vehicles in which Rockford's OEM systems are offered. A decline in demand for those automobiles is likely to reduce OEM sales and royalty revenue.

Rockford OEM systems are currently offered in select Nissan and Mitsubishi vehicles. In Nissan's line, Rockford systems are offered in many of Nissan's truck-based products, which have suffered declining sales because of increased gasoline prices and reduced consumer demand for large vehicles. A decline in demand for these vehicles would lead to a decline in Rockford's OEM sales and royalty revenue.

Seasonality of mobile audio sales causes Rockford's quarterly sales to fluctuate and may affect the trading price of its stock.

Rockford's sales are generally greater during the first and second quarters of each calendar year and lower during the third and fourth quarters, with its lowest sales typically occurring during the fourth quarter. As a result, after the announcement of Rockford's results of operations for the third and fourth quarters, Rockford's stock price may be lower than at other times of the year.

Rockford's financial results may fluctuate significantly, making financial forecasting difficult and making Rockford's stock price volatile.

Rockford's results of operations are difficult to predict and may fluctuate significantly from quarter to quarter. In some quarters, operating results may fall below expectations. Rockford's operating results are difficult to forecast for many reasons, some of which are outside of Rockford's control, including:

- The level of product, price and dealer competition;
- Size and timing of product orders and shipments, particularly by higher volume customers such as Best Buy, Wal-Mart, Nissan and Mitsubishi;
- Rockford's ability to develop new products and product enhancements that respond to changes in technology and consumer preferences while controlling costs;
- Weather conditions, which affect consumers' willingness to install products;
- Capacity and supply constraints or difficulties; and
- Timing of Rockford's marketing programs and those of its competitors.

As a result, investors should not rely on historical results as an indication of Rockford's future performance.

In addition, some of Rockford's expenses are fixed and cannot be reduced in the short term. Accordingly, if sales do not meet expectations, the results of operations are likely to be negatively and disproportionately affected. In this event, Rockford's stock price may fall dramatically.

Rockford relies upon debt financing for a substantial part of its working capital; defaults on its debt or the unavailability of additional financing could make it impossible to carry out Rockford's business as currently structured.

As at December 31, 2007, Rockford had \$3.5 million in outstanding debt under its senior credit facility and \$9.5 million of notes outstanding. Rockford is dependent on its senior credit facility and other financing given the working capital requirements of its business. If Rockford's financial performance fails to improve, or if other developments make financing unavailable on an economic basis, Rockford might not be able to continue its operations as they are currently structured. A restructuring would likely have a significant negative impact on operations, financial performance, and stock price.

If Rockford fails to manage its inventory effectively, Rockford could incur additional costs or lose sales.

Rockford customers have many brands to choose from when they decide to order products. If Rockford cannot deliver products quickly and reliably, customers will order from a competitor. Rockford must stock enough

inventory to fill orders promptly, which increases Rockford's financing requirements and the risk of inventory obsolescence. Competition has forced Rockford to shorten its product life cycles and more rapidly introduce new and enhanced products, while simultaneously sourcing more product overseas and carrying larger inventories. There is a significant risk that Rockford's inventory could become obsolete or that changes in demand could cause Rockford to hold excess inventory.

Rockford's product supplies and international operations may be harmed by factors including political instability, currency exchange rates and changes in regulations that govern international transactions.

The risks inherent in international trade may interfere with Rockford's supply of products, reduce Rockford's international sales and harm Rockford's business and the businesses of its distributors and suppliers. These risks include:

- Changes in tariff regulations;
- Political instability, war, terrorism and other political risks;
- Foreign currency exchange rate fluctuations;
- Establishing and maintaining relationships with local distributors and dealers;
- Lengthy shipping times and accounts receivable payment cycles;
- Import and export licensing requirements;
- Compliance with a variety of foreign laws and regulations, including unexpected changes in taxation and regulatory requirements;
- Greater difficulty in safeguarding intellectual property than in the U.S.; and
- Difficulty in staffing and managing geographically dispersed operations.

These and other risks may increase the relative price of Rockford's products compared to those manufactured in other countries, reducing the demand for its products.

Loss of an international distributor may disrupt Rockford's sales.

International customers accounted for 19.1% of Rockford's sales in 2007. For sales outside the U.S. and Canada Rockford relies on distributors, each of whom is responsible for one or more countries. Each distributor purchases and resells Rockford's products in its territories. When Rockford has disputes with a distributor, or changes its relationship with a distributor, it may disrupt the market for Rockford's products in that country and reduce sales. If Rockford changes a relationship with a distributor, Rockford may repurchase that distributor's inventory, which would also reduce Rockford's sales.

Currency fluctuations may reduce the profitability of Rockford's foreign sales.

In some cases, Rockford sells to Canadian dealers and distributors in Canadian dollars. In other international markets, although Rockford prices its products in dollars, currency fluctuations may make Rockford's products more expensive in local currency terms. Rockford does not trade in derivatives or other financial instruments to reduce currency risks. In some instances this will subject Rockford's earnings to fluctuations because Rockford is not protected against substantial currency fluctuations and its distributors may reduce product purchases because of currency fluctuations.

Currency fluctuations may increase the cost of Rockford's products.

In recent years, Rockford has sourced an increasing percentage of its finished goods, and parts for its products, from outside the United States. Most of these finished goods, raw materials and parts are sourced in the Far East, principally in China. Although most of these purchases are denominated in dollars, an extended decline in the value of the dollar may affect the terms and prices on which Rockford is able to purchase from its foreign suppliers and may, therefore, increase Rockford's costs.

If Rockford's supplies of finished goods or components are interrupted, it may be unable to deliver its products to its customers.

Rockford has transitioned most of its products to outsourced manufacturing, generally in Asia. Rockford's supply chain is also increasingly dependent on suppliers who are globally sourced. The supply process does not provide a backlog of finished goods, components or materials to satisfy short lead-time orders, to compensate for potential halts in supply or to replace products or components that are not available due to supplier issues or that do not conform to quality standards.

Rockford also does not have long-term price commitments from its suppliers and cost increases may reduce Rockford's margins or require Rockford to raise its prices to protect margins. Rockford cannot be certain that it could locate, within reasonable time frames, alternative sources of finished goods and components at similar prices and quality levels. This failure could result in increased costs, delays in its supply chain, an inability to fill purchase orders on a timely basis and a decrease in product availability at the retail level. This could cause Rockford to lose sales and damage Rockford's customer relationships.

Rockford depends on a few suppliers for a large portion of its products. Interruptions in their ability or willingness to deliver products would reduce sales and damage customer relationships.

Rockford relied on Edge Global Holdings, Kontion Manufacturing, and Sound Factor for approximately 24.6%, 19.6%, and 13.5% respectively, of its inventory purchases during 2007. If any significant supplier refuses or is unable to supply finished goods or components to Rockford, it would require substantial time to identify an alternative supplier and could create a shortage of finished goods and electronic components and parts. Such a shortage would reduce sales and damage customer relationships.

Rockford may be unable to retain and attract key employees, which could impair Rockford's business.

Rockford operates in highly competitive employment markets and cannot guarantee its continued success in retaining and attracting the employees it needs to develop, produce and market its products and manage its operations. Rockford's business strategy and operations depend, to a large extent, on Rockford's senior management team. Rockford does not have written employment contracts with any of its key employees. If key members of Rockford's management team are unable or unwilling to continue in their present positions, Rockford's ability to develop, introduce and sell Rockford's products could be negatively impacted.

If Rockford is unable to enforce or defend its ownership and use of intellectual property, Rockford's business may decline.

Rockford's future success may depend, in part, on Rockford's intellectual property. Rockford seeks to protect its intellectual property rights, but its actions may not adequately protect the rights covered by patents, patent applications, trademarks and other proprietary rights. Prosecution of Rockford's claims could be time consuming and costly. In addition, the intellectual property laws of some foreign countries do not protect Rockford's proprietary rights as do the laws of the U.S. Despite Rockford's efforts to protect its proprietary information, third parties may obtain, disclose or use proprietary information without authorization, which could adversely affect Rockford's business.

From time to time, third parties have alleged that Rockford infringes their proprietary rights. These claims or similar future claims could subject Rockford to significant liability for damages, result in the invalidation of its proprietary rights, limit its ability to use infringing intellectual property or force Rockford to license third-party technology rather than dispute the merits of an infringement claim. Even if Rockford prevails, any associated litigation could be time consuming and expensive and could result in the diversion of Rockford's time and resources.

Rockford could suffer from internal control deficiencies.

Rockford is a small company and is dependent upon a small number of officers and staff. If it suffers turnover of key employees or is otherwise unable to maintain its internal controls, Rockford may not be able to comply with its reporting obligations and its inability could reduce the market price of its stock.

Rockford's executive officers and directors retain substantial control of Rockford, which may limit the liquidity and market price of its common stock.

Rockford's officers and directors, and various shareholders affiliated with or related to two of Rockford's directors, Nicholas G. Bartol and Timothy C. Bartol, collectively held approximately 34% of Rockford's outstanding shares at March 12, 2008. These shareholders, if they act together, are able as a practical matter to control the outcome of matters submitted for shareholder action, including the election of a majority of Rockford's board of directors and the approval of significant corporate transactions. Consequently, these shareholders effectively control Rockford's management and affairs, which may limit the liquidity of its shares, discourage acquisition bids for Rockford and limit the price some investors will be willing to pay for Rockford's shares.

Virtually all of Rockford's shares are available for resale without significant restrictions. Their sale or potential sale may reduce Rockford's stock price.

Virtually all of Rockford's outstanding shares are available for resale under applicable securities laws. The market price of Rockford's common stock could decline as a result of sales of a large number of shares in the market or the perception that those sales could occur.

Rockford's anti-takeover provisions could affect the value of Rockford's stock.

Rockford's articles of incorporation and bylaws and Arizona law contain provisions that could discourage potential acquirers. For example, Rockford's board of directors may issue additional shares of common stock to an investor that supports the incumbent directors in order to make a takeover more difficult. This could deprive Rockford's shareholders of opportunities to sell its stock at above-market prices typical in many acquisitions.

Item 2. Properties

The following table contains information about Rockford's facilities as at December 31, 2007, all of which are leased. Rockford believes these properties are adequate for its business and operations.

<u>Function</u>	<u>Location</u>	<u>Approximate Square Footage</u>	<u>Lease Expiration</u>
Corporate headquarters and research and development	Tempe, Arizona	30,000	September 30, 2009
Training	Tempe, Arizona	10,000	September 30, 2010
Manufacturing and purchasing	Tempe, Arizona	22,000	December 31, 2008
Warehousing, sales and customer service	Tempe, Arizona	25,000	December 31, 2008
Warehousing	Gilbert, Arizona	91,000	March 31, 2009
Warehousing	Grand Rapids, Michigan	83,000	June 30, 2009
Total		<u>261,000</u>	

Item 3. Legal Proceedings

During January 2007, Rockford participated in a mediation seeking to settle the Fiori patent claim described in Rockford's Annual Reports for 2002, 2003, 2004 and 2005. The mediation resulted in a settlement of the matter. Rockford decided to settle the litigation because it concluded that the cost of litigating the matter through trial and appeal would have approached or even exceeded the amount of the settlement and that it was in Rockford's interest to eliminate the risks inherent in further litigation.

Under the Agreement, Rockford agreed to pay Mr. Fiori gross payments totaling \$1,613,000, as follows:

- \$750,000 was paid in February 2007, \$225,500 was paid on August 1, 2007, and \$212,500 was paid on February 1, 2008; and
- \$212,500 each will be paid on August 1, and December 1, 2008.

In the agreement Rockford also agreed to cease producing products using its proprietary TOPAZ technology as of December 31, 2007, and Rockford has done so as of that date. Rockford did not incur material costs, other than the product development costs it already expected to incur to replace the remaining products that used the technology, to make the changes required to comply with this agreement.

The agreement releases Rockford with respect to all claims of Mr. Fiori, his firm IET, and their successors and assigns for infringement of any patent Fiori or IET owns, for which they have applied, or to which they have enforcement rights. The agreement has resulted in the dismissal with prejudice of Mr. Fiori's lawsuit. As noted elsewhere in this report, Rockford has taken a charge of approximately \$1.5 million in its results for the fourth quarter of 2006 attributable to the settlement.

During 2007, Rockford continued to pursue collection of a judgment against its former distributor for Central and South America arising from a balance owed to Rockford and the distributor's claims that Rockford improperly terminated its distribution rights. The former distributor had undertaken legal actions in Panama that interfered with the ability of Rockford's new distributor for Central and South America to develop and service those markets. This interference was one of the causes of a decline in Rockford's sales in this territory in prior years. Rockford has initiated efforts to collect its U.S. judgment through proceedings in the U.S. and Panama. Rockford is unable to determine at this time when, or the extent to which, its efforts to collect on the judgment will be successful.

Rockford is and may continue to be a party to various lawsuits and arbitrations from time to time. As at December 31, 2007, Rockford was not a party to any legal proceedings that it believes are likely to have a material effect on its business.

Item 4. *Submission of Matters to a Vote of Security Holders*

No matters were submitted to a vote of security holders during the fourth quarter of 2007.

PART II

Item 5. Market for Registrant's Common Equity and Related Stockholder Matters and Issuer Purchases of Equity Securities

Rockford common stock has traded on The NASDAQ National Market System under the symbol "ROFO" since April 20, 2000, the date of its initial public offering. Prior to that time, there was no public market for its common stock. The following table sets forth the range of high and low sales prices for Rockford's common stock for the periods indicated:

	<u>High</u>	<u>Low</u>
For the quarter ended:		
December 31, 2007	\$2.19	\$1.57
September 30, 2007	\$2.38	\$1.59
June 30, 2007	\$2.88	\$1.84
March 31, 2007	\$2.85	\$2.17
December 31, 2006	\$3.50	\$1.48
September 30, 2006	\$4.19	\$3.20
June 30, 2006	\$4.19	\$3.21
March 31, 2006	\$4.20	\$2.86

As at March 12, 2008, there were approximately 110 holders of record of Rockford's common stock.

Rockford has never declared or paid any cash dividends on its common stock. Rockford currently intends to retain its earnings, if any, to finance its operations and, therefore, does not anticipate paying cash dividends on its common stock in the foreseeable future. Rockford's current credit agreement prohibits the payment of cash dividends and permits stock purchases up to \$1.5 million. Rockford used \$0.9 million of this purchase authority through December 31, 2007, for purchases under Rockford's stock repurchase program.

Equity Compensation Plan Information

<u>Plan Category</u>	<u>Number of Securities to be Issued Upon Exercise of Outstanding Options, Warrants and Rights</u> (a)	<u>Weighted Average Exercise Price of Outstanding Options, Warrants and Rights</u> (b)	<u>Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column (a))</u> (c)
Equity compensation plans approved by security holders	1,697,464	\$ 4.14	91,600
Equity compensation plans not approved by security holders	59,073	3.73	—
	<u>1,756,537</u>	<u>\$ 4.13</u>	<u>91,600</u>

Issuer Purchases of Equity Securities

<u>Period</u>	<u>Total Number of Shares Purchased</u>	<u>Average Price Paid per Share</u>	<u>Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs*</u>	<u>Maximum Number of Shares That May Yet be Purchased Under the Plans or Programs</u>
October 2007	50,000	\$ 2.06	50,000	420,000
November 2007	399,700	1.99	399,700	20,300
December 2007	—	—	—	20,300
Total	<u>449,700</u>	<u>\$ 2.00</u>	<u>449,700</u>	

Rockford has two publicly announced share repurchase programs. The first was announced on September 6, 2007, and is for up to 5% (or 470,000) of Rockford's common shares. All 449,700 shares purchased in the fourth quarter of 2007 were purchased under this first program and 20,300 shares remain authorized for repurchase under this program. The second share repurchase program was announced on February 21, 2008 and is for up to an additional 5% (or 450,000) of Rockford's common shares. These programs do not have a specified expiration date, but may be suspended or terminated at any time.

Item 6. Selected Financial Data

The following selected consolidated financial data should be read in conjunction with Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Continuing Operations” and Item 8, “Financial Statements and Supplementary Data.” The table contains selected consolidated financial data for the five years ended December 31, 2007 derived from Rockford’s audited consolidated financial statements.

	Years Ended December 31,				
	2003	2004	2005	2006	2007
	(In thousands, except per share data)				
Consolidated Statements of Operations:					
Net sales	\$157,728	\$160,857	\$135,682	\$102,776	\$88,745
Cost of goods sold	<u>109,446</u>	<u>129,092</u>	<u>96,231</u>	<u>73,919</u>	<u>59,868</u>
Gross profit	48,282	31,765	39,451	28,857	28,877
Operating expenses:					
Sales and marketing	28,823	27,461	22,845	16,772	13,273
General and administrative	17,470	25,782	13,913	16,753	11,215
Research and development	<u>7,149</u>	<u>6,415</u>	<u>2,823</u>	<u>3,218</u>	<u>2,817</u>
Total operating expenses	<u>53,442</u>	<u>59,658</u>	<u>39,581</u>	<u>36,743</u>	<u>27,305</u>
Operating income (loss)	(5,160)	(27,893)	(130)	(7,886)	1,572
Interest and other expense, net	<u>252</u>	<u>2,826</u>	<u>2,593</u>	<u>1,243</u>	<u>886</u>
Income (loss) from continuing operations before income taxes	(5,412)	(30,719)	(2,723)	(9,129)	686
Income tax expense (benefit)	<u>(2,483)</u>	<u>4,597</u>	<u>—</u>	<u>(437)</u>	<u>—</u>
Income (loss) from continuing operations	<u>(2,929)</u>	<u>(35,316)</u>	<u>(2,723)</u>	<u>(8,692)</u>	<u>686</u>
Discontinued operations:					
Loss from disposal of discontinued operations, net of taxes	—	(70)	(1,019)	—	—
Loss from discontinued operations, net of taxes	<u>(2,735)</u>	<u>(3,469)</u>	<u>(345)</u>	<u>(155)</u>	<u>—</u>
Total loss from discontinued operations	<u>(2,735)</u>	<u>(3,539)</u>	<u>(1,364)</u>	<u>(155)</u>	<u>—</u>
Net income (loss)	<u>\$ (5,664)</u>	<u>\$ (38,855)</u>	<u>\$ (4,087)</u>	<u>\$ (8,847)</u>	<u>\$ 686</u>
Income (loss) per common share:					
Income (loss) from continuing operations					
Basic	<u>\$ (0.33)</u>	<u>\$ (3.90)</u>	<u>\$ (0.29)</u>	<u>\$ (0.92)</u>	<u>\$ 0.07</u>
Diluted	<u>\$ (0.33)</u>	<u>\$ (3.90)</u>	<u>\$ (0.29)</u>	<u>\$ (0.92)</u>	<u>\$ 0.07</u>
Loss from discontinued operations					
Basic	<u>\$ (0.31)</u>	<u>\$ (0.39)</u>	<u>\$ (0.15)</u>	<u>\$ (0.02)</u>	<u>\$ 0.00</u>
Diluted	<u>\$ (0.31)</u>	<u>\$ (0.39)</u>	<u>\$ (0.15)</u>	<u>\$ (0.02)</u>	<u>\$ 0.00</u>
Net income (loss):					
Basic	<u>\$ (0.64)</u>	<u>\$ (4.29)</u>	<u>\$ (0.44)</u>	<u>\$ (0.94)</u>	<u>\$ 0.07</u>
Diluted	<u>\$ (0.64)</u>	<u>\$ (4.29)</u>	<u>\$ (0.44)</u>	<u>\$ (0.94)</u>	<u>\$ 0.07</u>
Weighted average shares:					
Basic	<u>8,866</u>	<u>9,066</u>	<u>9,258</u>	<u>9,388</u>	<u>9,325</u>
Diluted	<u>8,866</u>	<u>9,066</u>	<u>9,258</u>	<u>9,388</u>	<u>9,342</u>
Consolidated Balance Sheet Data:					
Working capital	\$ 38,138	\$ 25,776	\$ 23,217	\$ 16,479	\$17,110
Total assets	112,083	80,353	52,298	44,555	34,012
Current portion of long-term debt and capital lease obligations	24,382	18,204	6,109	11,402	4,235
Long-term debt and capital lease obligations	—	11,937	9,187	9,937	9,715
Total liabilities	48,393	57,768	33,667	34,310	24,066
Shareholders’ equity	63,207	22,585	18,631	10,245	9,946

Item 7. *Management's Discussion and Analysis of Financial Condition and Results of Continuing Operations*

This Analysis should be read in conjunction with the other sections of this Annual Report, including "Item 1: Business," "Item 6: Selected Financial Data," and "Item 8: Financial Statements and Supplementary Data." This Analysis does not reflect the potential impact of any divestitures, mergers, acquisitions or other business combinations that had not been completed as of the date of this report.

Results of Operations

Overview

Rockford is now focused almost entirely on its core mobile audio business. During 2008 and 2009 Rockford expects to work on improving penetration of the mobile audio markets and continuously improving its core operations.

Most of Rockford's products are now outsourced, with only limited internal assembly of amplifiers remaining as of the first quarter of 2008. Rockford expects to complete the outsourcing of amplifier assembly in 2008, allowing the removal late in the year and in 2009 of another layer of overhead in its manufacturing operations. With the completion of its outsourcing projects, and assuming only moderate changes in exchange rates and international trading conditions, Rockford anticipates that its 2008 and 2009 results will reflect a further reduction in its cost structure.

Rockford's sales are now focused on the mass retail, independent specialist, international distribution and OEM channels. In 2007 Rockford's aftermarket mobile audio sales were down, with decreases in both the mass retail and independent specialist channels, partly offset by an increase in international sales. The mobile audio aftermarket in the U.S. was down significantly, creating an environment in which competitors in the aftermarket channels continued aggressive pricing and promotional activity and in which Rockford's sales decreased.

Rockford is working to increase aftermarket sales and believes its new 2007 products perform better than the products Rockford had previously offered. Their improved performance has contributed positively to Rockford's sales efforts as dealers have found their installation to be easier and their operation to be more powerful and more reliable. Assuming a moderate decline in the overall mobile audio aftermarket, Rockford believes that it should be able to stabilize or even increase its aftermarket sales. If consumer spending as a whole decreases more significantly, Rockford expects the mobile audio aftermarket would also decline significantly and Rockford would be likely to suffer a decrease in its aftermarket sales.

In 2007 Rockford experienced a decline in OEM sales, due primarily to Nissan's introduction of a new Sentra model that had less Rockford content. If decreases in consumer spending significantly reduce Nissan and Mitsubishi vehicle sales, or if other changes in demand reduce sales of the particular vehicles in which Rockford's systems are offered, OEM sales may decline further.

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The following table shows, for the years indicated, selected consolidated statements of operations data expressed as a percentage of net sales:

	<u>Year Ended December 31</u>		
	<u>2005</u>	<u>2006</u>	<u>2007</u>
Net sales	100.0%	100.0%	100.0%
Cost of goods sold	<u>70.9</u>	<u>71.9</u>	<u>67.5</u>
Gross profit	29.1	28.1	32.5
Operating expenses:			
Sales and marketing	16.8	16.3	15.0
General and administrative	10.3	16.3	12.6
Research and development	<u>2.1</u>	<u>3.2</u>	<u>3.2</u>
Total operating expenses	<u>29.2</u>	<u>35.8</u>	<u>30.8</u>
Operating income (loss)	(0.1)	(7.7)	1.8
Interest and other expense, net	<u>1.9</u>	<u>1.2</u>	<u>1.0</u>
Income (loss) from continuing operations before income taxes	(2.0)	(8.9)	0.8
Income tax expense (benefit)	<u>—</u>	<u>(0.4)</u>	<u>—</u>
Income (loss) from continuing operations	(2.0)	(8.5)	0.8
Discontinued operations:			
Loss from disposal of discontinued operations	(0.7)	—	—
Loss from discontinued operations	<u>(0.3)</u>	<u>(0.1)</u>	<u>—</u>
Total loss from discontinued operations	<u>(1.0)</u>	<u>(0.1)</u>	<u>—</u>
Net income (loss)	<u>(3.0)%</u>	<u>(8.6)%</u>	<u>0.8%</u>

Cost of goods sold primarily consists of product costs, direct labor and manufacturing costs associated with production of Rockford's products as well as warranty, warehousing, freight-in and customer service expenses.

Sales and marketing expenses primarily consist of salaries, sales commissions, cost of advertising, trade shows, and freight-out expenses.

General and administrative expenses primarily consist of salaries, facilities and other costs of Rockford's accounting, finance, management information systems, administrative and executive departments, as well as legal, accounting and other professional fees.

Research and development expenses primarily consist of salaries associated with research and development personnel, prototyping and other costs related to new product development.

Geographic Distribution of Sales

Rockford's sales to external customers by geographic region were as follows:

<u>Region(1)</u>	<u>Year Ended December 31,</u>			
	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2007</u>
	(In thousands, excluding % column)			
United States	\$112,657	\$ 86,017	\$71,771	80.9%
Other Americas	9,438	8,007	7,193	8.1%
Europe	9,042	5,316	6,069	6.8%
Asia	<u>4,545</u>	<u>3,436</u>	<u>3,712</u>	<u>4.2%</u>
Total sales	<u>\$135,682</u>	<u>\$102,776</u>	<u>\$88,745</u>	<u>100.0%</u>

(1) Sales are attributed to geographic regions based on the location of customers. No single foreign country accounted for greater than 10% of Rockford's sales.

In the following discussion, certain increases or decreases may differ due to rounding.

Year Ended December 31, 2007 Compared to Year Ended December 31, 2006

Net Sales. Net sales decreased by \$14.0 million, or 13.7%, to \$88.7 million for 2007, from \$102.8 million for 2006. The decrease in sales was primarily attributable to lower sales to OEM, mass retail and independent specialist customers and to the elimination of sales of Rockford's Q-Logic enclosure product line which was sold on March 31, 2006. These reductions were partially offset by higher OEM royalty revenue and lower product returns. Royalty revenues fluctuate with consumer demand and automobile manufacturers production schedules, which can be volatile. OEM royalty revenues for 2007 and 2006 were \$6.3 million and \$2.6 million respectively.

U.S. sales decreased by \$14.2 million, or 16.6%, to \$71.8 million for 2007, from \$86.0 million for 2006. International sales increased by \$0.2 million, or 1.3%, to \$17.0 million for 2007, from \$16.8 million for 2006. The increase in international sales was primarily due to completion of the transition to a new distribution system in Europe and the launch of new 2007 Rockford Fosgate products, partly offset by the unfavorable impact on sales in Canada resulting from the weakness of the U.S. dollar in relation to the Canadian dollar.

Gross Profit. Gross profit remained flat at \$28.9 million for both 2007 and 2006. As a percent of sales, gross profit increased to 32.5% for 2007, from 28.1% for 2006. The increase in gross profit as a percent of sales is primarily due to higher royalty revenue, lower returns and a \$0.7 million charge related to future obligations for Rockford's vacated European warehouse facilities that was recorded in 2006. These improvements were partially offset by higher discounts offered on discontinued product lines.

Sales and Marketing Expenses. Sales and marketing expenses decreased by \$3.5 million, or 20.1%, to \$13.3 million for 2007 from \$16.8 million for 2006. As a percent of sales, sales and marketing expenses decreased to 15.0% for 2007 from 16.3% for 2006. The decrease was primarily due to lower sales commissions and reduced outbound freight resulting from lower sales, as well as reduced promotional activities.

General and Administrative Expenses. General and administrative expenses decreased by \$5.5 million or 33.1%, to \$11.2 million for 2007 from \$16.8 million for 2006. As a percent of sales, general and administrative expenses decreased to 12.6% for 2007 from 16.3% for 2006. The decrease in general and administrative expenses is primarily due to lower personnel related expenses, facilities costs and professional fees and was partially offset by a special charge of approximately \$1.1 million related to departing employees recorded in the first quarter of 2007. Most of this special charge arose from costs associated with the Retirement and Salary Continuation Agreement with Rockford's former CEO. General and administrative expenses for 2006 also included a legal settlement charge of approximately \$1.5 million to resolve the Fiori litigation that is discussed in Item 3 of this Annual Report and restructuring charges of approximately \$1.3 million related to severance costs.

Research and Development Expenses. Research and development expenses decreased by \$0.4 million, or 12.5%, to \$2.8 million for 2007, as compared to \$3.2 million for 2006. As a percent of sales, these expenses remained flat at 3.2% for both 2007 and 2006. The decrease in research and development expense is primarily related to costs incurred in 2006 associated with the launch of Rockford's new products in 2007.

Operating Income (Loss). Operating income (loss) improved by \$9.5 million, to \$1.6 million operating income for 2007 from a \$7.9 million operating loss for 2006. As a percent of sales, operating income was 1.8% for 2007, compared to an operating loss of 7.7% for 2006. This improvement in operating income (loss) is primarily due to lower operating expenses and higher gross margin as a percentage of net sales.

Interest and Other Expense, Net. Interest and other expense, net, primarily consists of interest expense and currency gains and losses. Interest and other expense, net, decreased by \$0.4 million or 28.7%, to \$0.9 million for 2007 from \$1.2 million for 2006. The decrease is primarily attributable to a fourth quarter 2007 currency gain of approximately \$418,000 resulting from the recognition of Rockford's previously unrealized cumulative transaction gains. Recognition was triggered by the dissolution of Rockford's European subsidiary.

Income Tax Expense (Benefit). Income tax expense from continuing operations was zero expense for 2007 and an income tax benefit from continuing operations of \$0.4 million for 2006. The effective income tax rates were 0.0% for 2007, and 4.9% for 2006. Rockford is not recording any tax expense (benefit) on income (losses) in 2007

and 2006 for financial reporting purposes. Rockford currently continues to maintain a valuation allowance reserve against all of its net deferred tax assets, which include net operating loss carryforwards. These loss carryforwards are likely to offset virtually all current period income tax expense until such time, if ever, that management believes that some portion of the reserved deferred tax asset become more likely than not recoverable.

Year Ended December 31, 2006 Compared to Year Ended December 31, 2005

Net Sales. Net sales decreased by \$32.9 million, or 24.3%, to \$102.8 million for 2006, from \$135.7 million for 2005. The decrease in sales was primarily attributable to lower sales of Rockford Fosgate and Lightning Audio branded products. The decrease is also partially due to the elimination of Rockford's Q-Logic enclosure product line for much of the year, and the elimination of domestic MB Quart and Omnifi branded products for all of the year. These decreases were partially offset by lower sales discounts and product returns.

U.S. sales decreased by \$26.7 million, or 23.6%, to \$86.0 million for 2006, from \$112.7 million for 2005. International sales decreased by \$6.2 million, or 27.0%, to \$16.8 million for 2006, from \$23.0 million for 2005. The decrease in international sales was primarily due to lower sales of Rockford Fosgate and Lighting Audio product lines. The transition to a new distribution model in Europe also contributed to this decrease.

Gross Profit. Gross profit decreased by \$10.6 million, or 26.9%, to \$28.9 million for 2006, from \$39.5 million for 2005. As a percent of sales, gross profit decreased to 28.1% for 2006, from 29.1% for 2005. This decrease was primarily due to lower net sales, higher manufacturing variances, and a \$0.7 million charge related to future obligations for Rockford's vacated European warehouse facility. The decrease was partially offset by lower cost of goods sold due to outsourcing, higher royalty revenue, and by the impairment of Q-Logic assets of \$0.8 million recorded in 2005.

Sales and Marketing Expenses. Sales and marketing expenses decreased by \$6.1 million, or 26.6%, to \$16.8 million for 2006 from \$22.9 million for 2005. As a percent of sales, sales and marketing expenses decreased to 16.3% for 2006 from 16.8% for 2005. The decrease in sales and marketing expense was primarily due to lower sales commissions, reduced outbound freight resulting from lower sales, lower trade show expenses and lower personnel related expenses.

General and Administrative Expenses. General and administrative expenses increased by \$2.8 million or 20.4%, to \$16.8 million for 2006 from \$13.9 million for 2005. As a percent of sales, general and administrative expenses increased to 16.3% for 2006 from 10.3% for 2005. The increase in general and administrative expenses is primarily due to a legal settlement charge of approximately \$1.5 million to resolve the Fiori litigation that is discussed in Item 3 of this Annual Report, a restructuring charge of approximately \$1.3 million for severance costs associated with a reorganization announced in August 2006 and the gain recognized from the sale of Rockford's rights to the MB Quart brand for North America in 2005. The increase was partially offset by lower personnel related expenses, facilities costs, and professional fees.

Research and Development Expenses. Research and development expenses increased by \$0.4 million, or 14.0%, to \$3.2 million for 2006 from \$2.8 million for 2005. As a percent of sales, these expenses increased to 3.2% for 2006, from 2.1% for 2005. The increase is primarily due to spending on the increased quantity of new product introductions planned for 2007.

Operating Loss From Continuing Operations. Operating loss increased by \$7.8 million, to a \$7.9 million operating loss for 2006 from a \$0.1 million loss for 2005. As a percent of sales, operating loss increased to a 7.7% operating loss for 2006, from a 0.1% operating loss for 2005. This increase in operating loss is primarily the result of the decrease in net sales and gross profit and the legal settlement and restructuring charges that contributed to increased General and Administrative Expenses. These items were partially offset by lower operating expenses as described above.

Interest and Other Expense. Interest and other expense primarily consists of interest expense and currency gains and losses. Interest and other expense decreased by \$1.4 million, or 52.1%, to \$1.2 million for 2006 from \$2.6 million for 2005. The decrease is primarily attributable to lower interest expense in 2006 due to lower average levels of borrowings, partially offset by higher effective borrowing rates.

Income Tax Expense (Benefit). The income tax benefit from continuing operations was \$0.4 million for 2006 and zero for 2005. The effective income tax rates were 4.9% for 2006 and 0.0% for 2005. Tax losses in 2006 were not benefited for financial reporting purposes. For 2005 and 2006 Rockford maintained a valuation allowance reserve against all of its net deferred tax assets.

Quarterly Results of Operations

Rockford’s sales on a quarterly basis reflect the seasonality of the mobile audio aftermarket business. Sales are generally greater during the first and second quarters of each calendar year and lower during the third and fourth quarters, with Rockford’s lowest sales typically occurring during the fourth quarter. Rockford’s consumer electronic chain and mass merchandise channels have seasonality that is somewhat different than the core business seasonality, with higher sales in the third and fourth quarters. Nevertheless, Rockford expects its business to remain seasonal for the foreseeable future.

The following tables show selected consolidated quarterly statements of operations data derived from Rockford’s unaudited consolidated financial statements for each of the eight quarters ended December 31, 2007. These unaudited financial results were prepared on a basis consistent with the audited financial statements and include all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of the consolidated results of operations for those periods. The results of operations for any quarter are not necessarily indicative of the results for any future period.

Consolidated Statement of Operations Data

	Three Months Ended							
	Mar. 31, 2006	June 30, 2006	Sept. 30, 2006	Dec. 31, 2006	Mar. 31, 2007	June 30, 2007	Sept. 30, 2007	Dec. 31, 2007
	(In thousands, except per share data)							
Net sales	\$29,928	\$31,668	\$21,217	\$19,963	\$26,372	\$26,740	\$18,695	\$16,938
Gross profit	7,858	10,373	6,016	4,610	7,880	8,398	6,278	6,321
Income (loss) from continuing operations	(2,059)	1,026	(2,919)	(4,740)	(867)	970	91	492
Income (loss) from discontinued operations	6	(114)	(47)	—	—	—	—	—
Net income (loss)	<u>\$ (2,053)</u>	<u>\$ 912</u>	<u>\$ (2,966)</u>	<u>\$ (4,740)</u>	<u>\$ (867)</u>	<u>\$ 970</u>	<u>\$ 91</u>	<u>\$ 492</u>
Net income (loss) per common share(1)								
Basic	<u>\$ (0.22)</u>	<u>\$ 0.09</u>	<u>\$ (0.32)</u>	<u>\$ (0.50)</u>	<u>\$ (0.09)</u>	<u>\$ 0.10</u>	<u>\$ 0.01</u>	<u>\$ 0.05</u>
Diluted	<u>\$ (0.22)</u>	<u>\$ 0.09</u>	<u>\$ (0.32)</u>	<u>\$ (0.50)</u>	<u>\$ (0.09)</u>	<u>\$ 0.10</u>	<u>\$ 0.01</u>	<u>\$ 0.05</u>

(1) The sum of quarterly net income (loss) per common share does not equal annual net income (loss) per common share due to changes in the weighted average number of common shares outstanding.

Liquidity and Capital Resources

Rockford has financed its business primarily using existing capital, cash flows from operations, and bank borrowings. Rockford’s cash flow generated from operations was \$8.9 million for 2007 compared to \$4.1 million of cash flow used in operations for 2006. Decreases in inventory were the primary source of cash during 2007. Decreases in accounts payable and reductions in the bank line of credit were the primary uses of cash during 2007.

Rockford entered into an asset-based credit facility with Wachovia Capital Financial Corporation (Western) as Agent and Wachovia Bank, National Association as Arranger on March 29, 2004 and as amended most recently on November 28, 2007. This credit facility, as amended, expires on March 24, 2011, is collateralized by substantially all of Rockford’s assets, is a \$20 million asset-based facility, and has a variable interest rate of LIBOR plus 200 basis

points or Prime. The balance on the facility and interest rate were \$3.5 million and 7.25% per annum, respectively, at December 31, 2007. At December 31, 2007, Rockford was in compliance with all applicable covenants.

Rockford has outstanding \$9.5 million of 4.5% convertible senior subordinated secured notes due 2009 and warrants to purchase 961,573 shares of common stock at \$3.73 per share. These items are outstanding under agreements effective on June 10, 2004 and as amended on November 12, 2004. The net proceeds of approximately \$9.5 million are allocated between the warrants and the notes based on their relative fair values. The value of the warrants was calculated using the Black-Scholes pricing model. The discount on the notes is being accreted ratably, over the term of the notes, to the \$9.5 million amount due at maturity. Debt issuance costs were capitalized and are being amortized over the life of the notes. The noteholders may convert the notes into Rockford's common stock at any time before their redemption, which at latest would be on the scheduled maturity date of June 10, 2009. The conversion price is \$4.61 per share. If fully converted, the notes will convert into 2,060,738 shares of Rockford's common stock. Rockford may, at its option, redeem all or any part of the notes from and after June 10, 2007, for a redemption price equal to the outstanding principal plus accrued interest. The noteholders have a second priority lien on certain Rockford assets.

Rockford anticipates, based on its cash flow forecast, that cash flow from operations at the expected level of operations for 2008 and available borrowings under its credit facility will be adequate to meet Rockford's requirements for current capital expenditures, working capital and interest payments for the next twelve months. Rockford does not expect asset sales will be a significant source of cash in 2008 or 2009.

At the redemption date for the outstanding notes on June 10, 2009, and assuming the noteholders do not convert the notes into shares, Rockford will be required to pay \$9.5 million to redeem the notes. Based on its current cash-flow forecasts Rockford anticipates that it will have available borrowings under its credit facility to complete this redemption. This availability could be impacted by adverse economic events and, if it is, Rockford may need to secure additional borrowings or equity to fund the required redemption.

Rockford had working capital of \$17.1 million at December 31, 2007, compared to \$16.5 million at December 31, 2006. The significant components of working capital at December 31, 2007 include:

- Rockford had no cash and cash equivalents at December 31, 2007 and December 31, 2006. Due to the daily sweep of cash by Wachovia Capital, described below, Rockford has reclassified cash and cash equivalents to net against its current debt balance.
- Rockford's net accounts receivable were \$15.9 million at December 31, 2007 compared to \$19.2 million at December 31, 2006. The decrease in accounts receivable balances is primarily due to the decrease in net sales in 2007 compared to 2006.
- Rockford's inventory position decreased from \$19.6 million at the end of 2006 to \$14.4 million at December 31, 2007. This inventory decrease was primarily due to the initial phases of outsourcing manufacturing, improved inventory turns and the reduction of end of life inventory during 2007.
- Accounts payable decreased \$1.3 million, from \$7.1 million at December 31, 2006 to \$5.8 million at December 31, 2007. This decrease was primarily due to lower purchase requirements resulting from lower sales.

The Wachovia Capital credit facility requires that Rockford maintain blocked lock box accounts whereby Wachovia Capital takes possession of all cash receipts on a daily basis and these amounts are applied to reduce Rockford's outstanding debt. In accordance with EITF 95-22: *Balance Sheet Classification of Borrowings Outstanding under Revolving Credit Agreements That Include both a Subjective Acceleration Clause and a Lock-Box Arrangement*, Rockford has recorded as short term the \$3.5 million and \$10.4 million outstanding balance as at December 31, 2007 and December 31, 2006, respectively, on the Wachovia Capital credit facility. The credit facility matures on March 29, 2011, and Rockford expects to maintain the credit facility for its entire term.

Investing activities used cash of \$0.4 million for 2007 and used cash of \$0.2 million for 2006. Capital expenditures, the primary use of cash from investing activities, were \$1.0 million for 2007 versus \$1.5 million for 2006. The primary source of cash from investing activities in 2006 and 2007 was primarily proceeds from the sale of Rockford's Q-Logic enclosure business and collections on the long term note receivable related to this sale.

Rockford's capital spending is primarily in tooling for specific product lines and computer hardware and software to support operations. Rockford does not anticipate significant changes in its capital spending requirements in 2008 or 2009.

Off Balance Sheet Arrangements

Rockford does not participate in transactions that generate relationships with unconsolidated entities or financial partnerships, such as entities referred to as structured finance or variable interest entities (VIEs), which would be established for the purpose of facilitating off-balance sheet arrangements. As of December 31, 2007, Rockford did not have any unconsolidated VIE's.

Rockford did not have any material outstanding noncancelable purchase obligations at December 31, 2007. Several of its sourcing agreements require Rockford to place monthly purchase orders, but do not require a minimum purchase quantity or dollar amount. Rockford does not anticipate significant liability in connection with these contractual requirements.

Critical Accounting Policies and Estimates

The methods, estimates and judgments Rockford uses in applying its accounting policies may have a significant impact on the results reported in its consolidated financial statements. Rockford evaluates its estimates and judgments on an on-going basis. Rockford bases its estimates on historical experience and assumptions that Rockford believes to be reasonable under the circumstances. Rockford's experience and assumptions form the basis for its judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may vary from what Rockford anticipates and different assumptions or estimates about the future could change its reported results.

Rockford believes the following accounting policies are the most critical to Rockford, in that they are important to the portrayal of Rockford's consolidated financial statements and they require Rockford's most difficult, subjective or complex judgments in the preparation of its consolidated financial statements:

Revenue Recognition. Rockford recognizes revenue pursuant to Staff Accounting Bulletin No. 104, *Revenue Recognition in Financial Statements*. Accordingly, Rockford recognizes revenue and records sales, net of related discounts, when all of the following criteria are met:

- Persuasive evidence of an arrangement exists;
- Ownership has transferred to the customer;
- The price to the customer is fixed or determinable; and
- Collectibility is reasonably assured.

Rockford sells almost all of its products F.O.B. place of shipment, so that upon shipment of products the above criteria are met and revenue is recognized. Rockford also records reductions to revenue for estimated customer returns and additional sales incentive offerings, such as growth and volume incentive rebates and prompt pay discounts, based on historical rates.

In addition, Rockford earns royalties by licensing its brand names and know-how to its customers for use in their products. Royalty revenue is recognized as the customer produces products utilizing Rockford's brand names and know-how based upon the terms of the agreement and the production information provided by the licensee. The royalties are included in net sales on the consolidated statement of operations.

Allowance for Doubtful Accounts. Rockford maintains an allowance for doubtful accounts, based on historical rates, for estimated losses resulting from the inability of its customers to make required payments. The assessment of customers' ability to pay generally includes direct contact with the customer, investigation into customers' financial status, as well as consideration of customers' payment history. Rockford assesses the reserve required through an account review process. Rockford further evaluates the results based upon comparisons of ending allowance balances to historical experience based on actual write-off history.

Inventory. Rockford carries inventory at the lower of cost or market, computed using the weighted average method. For purposes of the lower of cost or market calculations, Rockford writes down obsolete or unmarketable inventory by an amount equal to the difference between the cost of inventory and the estimated market value based upon assumptions about future demand and market conditions. Rockford reviews information such as quantity on hand, forecasted use, and inventory age to assist in this assessment.

Warranty. Rockford maintains a warranty reserve, based on historical rates, for costs associated with the repair or replacement of product that fails to meet its standard warranty against defects in material and workmanship. The estimate is based upon a trend analysis of historical costs and the number of units expected to be subject to warranty using historical estimated of number of units likely to be returned.

Income taxes. Rockford must make estimates and judgments in determining income tax expense for financial statement purposes. These estimates and judgments occur in the calculation of tax assets and liabilities, which arise from differences in the timing of recognition of revenue and expense for tax and financial statement purposes. Rockford must assess the likelihood that it will be able to recover Rockford's deferred tax assets and establish a valuation allowance for the portion of its deferred tax assets that it does not believe are more likely than not recoverable. Based on Rockford's review of its net deferred tax assets at December 31, 2007, it determined that a full valuation allowance was required.

Rockford adopted the provisions of FASB Interpretation No. 48 Accounting for Uncertainty in Income Taxes ("FIN 48") an interpretation of FASB Statement No. 109 ("SFAS 109") on January 1, 2007. Adoption had no net impact given that the approximately \$1.1 million adjustment reduced both Rockford's deferred tax assets and related valuation allowance. The future recognition of the \$1.1 million would not impact the effective income tax rate as long as Rockford maintains its full valuation allowance against its deferred tax assets. However, the recognition of such assets, along with a release in the valuation allowance could favorably affect the effective income tax rate.

Inflation. Inflation has not had a significant impact on Rockford's operations since it operates in a market that requires continuing price decreases and Rockford has historically been able to insist on continuing price decreases from its suppliers. Rising metal prices and increasing transportation costs may have an impact on Rockford's results in 2008, if Rockford is not able to secure concessions from its suppliers.

New Accounting Standards

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*. This statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007. Rockford does not expect the adoption of SFAS No. 157 will have a material impact on its consolidated financial statements.

In December 2007 the FASB issued SFAS No. 141R, *Business Combinations*, or SFAS 141R. SFAS 141R 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 statement to evaluate the nature and financial effects of the business combination. SFAS 141R is effective for financial statements issued for fiscal years beginning after December 15, 2008. Accordingly, any business combinations Rockford engages in will be recorded and disclosed following existing generally accepted accounting principles until January 1, 2009. Rockford is still assessing the impact of this standard on its future consolidated financial statements.

Item 8. *Financial Statements and Supplementary Data*

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders
Rockford Corporation

We have audited the accompanying consolidated balance sheets of Rockford Corporation and subsidiaries (collectively the “Company”) as of December 31, 2007 and 2006, and the related consolidated statements of operations, shareholders’ equity, and cash flows for each of the three years in the period ended December 31, 2007. These consolidated financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company’s internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Rockford Corporation and subsidiaries at December 31, 2007 and 2006, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2007, in conformity with U.S. generally accepted accounting principles.

As discussed in Note 8 to the consolidated financial statements, the Company adopted the provisions of Statement of Financial Accounting Standards No. 123 (Revised 2004), “Share-Based Payment,” on January 1, 2006, which changed its method of accounting for share-based payments.

/s/ Ernst & Young LLP

March 12, 2008
Phoenix, Arizona

ROCKFORD CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(In thousands, except share data)

	<u>December 31,</u>	
	<u>2006</u>	<u>2007</u>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ —	\$ —
Accounts receivable, less allowances of \$1,267 and \$929 at December 31, 2006 and 2007, respectively	19,242	15,885
Inventories	19,612	14,352
Prepaid expenses and other	1,998	1,224
Total current assets	40,852	31,461
Property and equipment, net	2,487	1,905
Other assets	1,216	646
Total assets	<u>\$ 44,555</u>	<u>\$ 34,012</u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 7,094	\$ 5,794
Accrued salaries and incentives	1,485	1,415
Accrued warranty and returns	2,199	1,267
Other accrued expenses	2,193	1,640
Current portion of capital leases and other long-term liabilities	1,002	760
Asset-based credit facility	10,400	3,475
Total current liabilities	24,373	14,351
Notes payable, less unaccrued discount of \$222 and \$130 at December 31, 2006 and 2007, respectively	9,278	9,582
Long-term portion of capital lease and other long-term liabilities	659	133
Total liabilities	34,310	24,066
Commitments and Contingencies (Note 10)		
Shareholders' equity		
Common stock, \$.01 par value. Authorized shares — 40,000,000 Issued shares — 9,390,970 and 9,395,720 shares at December 31, 2006 and 2007, respectively	94	94
Additional paid-in capital	37,995	38,319
Accumulated deficit	(28,255)	(27,569)
Accumulated other comprehensive income	411	—
Less: Treasury stock, at cost (449,700 shares at December 31, 2007)	—	(898)
Total shareholders' equity	10,245	9,946
Total liabilities and shareholders' equity	<u>\$ 44,555</u>	<u>\$ 34,012</u>

See accompanying notes.

ROCKFORD CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)

	Year Ended December 31,		
	2005	2006	2007
Net sales	\$135,682	\$102,776	\$88,745
Cost of goods sold	96,231	73,919	59,868
Gross profit	39,451	28,857	28,877
Operating expenses:			
Sales and marketing	22,845	16,772	13,273
General and administrative	13,913	16,753	11,215
Research and development	2,823	3,218	2,817
Total operating expenses	39,581	36,743	27,305
Operating income (loss)	(130)	(7,886)	1,572
Interest expense	2,009	1,366	1,423
Other expense (income)	584	(123)	(537)
Income (loss) from continuing operations before income taxes	(2,723)	(9,129)	686
Income tax benefit	—	(437)	—
Income (loss) from continuing operations	(2,723)	(8,692)	686
Discontinued operations:			
Loss from disposal of discontinued operations, net of taxes	(1,019)	—	—
Loss from discontinued operations, net of taxes	(345)	(155)	—
Total loss from discontinued operations	(1,364)	(155)	—
Net income (loss)	<u>\$ (4,087)</u>	<u>\$ (8,847)</u>	<u>\$ 686</u>
Income (loss) per common share:			
Income (loss) from continuing operations			
Basic	<u>\$ (0.29)</u>	<u>\$ (0.92)</u>	<u>\$ 0.07</u>
Diluted	<u>\$ (0.29)</u>	<u>\$ (0.92)</u>	<u>\$ 0.07</u>
Loss from discontinued operations			
Basic	<u>\$ (0.15)</u>	<u>\$ (0.02)</u>	<u>\$ 0.00</u>
Diluted	<u>\$ (0.15)</u>	<u>\$ (0.02)</u>	<u>\$ 0.00</u>
Net income (loss)			
Basic	<u>\$ (0.44)</u>	<u>\$ (0.94)</u>	<u>\$ 0.07</u>
Diluted	<u>\$ (0.44)</u>	<u>\$ (0.94)</u>	<u>\$ 0.07</u>
Weighted average shares:			
Basic	<u>9,258</u>	<u>9,388</u>	<u>9,325</u>
Diluted	<u>9,258</u>	<u>9,388</u>	<u>9,342</u>

See accompanying notes.

ROCKFORD CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(In thousands)

	Common Stock		Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Income	Treasury Stock		Total
	Shares	Amount				Number	Amount	
Balance at December 31, 2004	9,205	\$ 92	\$ 37,329	\$ (15,321)	\$ 485	—	\$ —	\$22,585
Currency translation	—	—	—	—	(88)	—	—	(88)
Net loss	—	—	—	(4,087)	—	—	—	(4,087)
Comprehensive loss	—	—	—	—	—	—	—	(4,175)
Exercise of stock options, including tax benefit of \$0	116	1	246	—	—	—	—	247
Issuance of shares for employee stock purchase plan	63	1	121	—	—	—	—	122
Repurchase of warrants issued with convertible notes	—	—	(148)	—	—	—	—	(148)
Balance at December 31, 2005	9,384	94	37,548	(19,408)	397	—	—	18,631
Currency translation	—	—	—	—	14	—	—	14
Net loss	—	—	—	(8,847)	—	—	—	(8,847)
Comprehensive loss	—	—	—	—	—	—	—	(8,833)
Exercise of stock options, including tax benefit of \$0	7	—	16	—	—	—	—	16
Share-based compensation	—	—	431	—	—	—	—	431
Balance at December 31, 2006	9,391	94	37,995	(25,255)	411	—	—	10,245
Currency translation	—	—	—	—	(411)	—	—	(411)
Net income	—	—	—	686	—	—	—	686
Comprehensive income	—	—	—	—	—	—	—	275
Exercise of stock options, including tax benefit of \$0	5	—	11	—	—	—	—	11
Share-based compensation	—	—	313	—	—	—	—	313
Purchase of treasury stock	—	—	—	—	—	450	(898)	(898)
Balance at December 31, 2007	9,396	\$ 94	\$ 38,319	\$ (27,569)	\$ —	450	\$ (898)	\$ 9,946

See accompanying notes.

ROCKFORD CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31,		
	2005	2006	2007
	(In thousands)		
Cash flow from continuing operating activities:			
Net income (loss)	\$ (4,087)	\$ (8,847)	\$ 686
Net loss from discontinued operations	(1,364)	(155)	—
Net income (loss) from continuing operations	(2,723)	(8,692)	686
Adjustments to reconcile net income (loss) from continuing operations to net cash provided by (used in) operating activities:			
Depreciation and amortization	3,891	2,555	1,849
Share based compensation expense	—	431	313
Loss on legal settlement and special charges	—	1,518	1,098
Gain on divestiture of business	—	(142)	—
Realized translation gain	—	—	(411)
Gain on sale of brand rights	(844)	—	—
Write-off of assets to fair market value	814	—	—
Net gain on buyback of notes and warrants	(112)	—	—
Loss (gain) on sale of property and equipment	44	153	(35)
Provision for doubtful accounts	388	856	111
Provision for inventory	549	974	507
Changes in operating assets and liabilities:			
Accounts receivable	6,457	3,300	3,245
Inventories	12,275	(2,768)	4,752
Prepaid expenses and other	361	2,271	739
Accounts payable	(4,683)	(2,534)	(1,301)
Accrued salaries and incentives	(85)	168	(573)
Accrued warranty and returns	(1,514)	(935)	(932)
Other accrued expenses	(2,120)	(1,279)	(1,107)
Net cash provided by (used in) operating activities	12,698	(4,124)	8,941
Cash flow from continuing investing activities:			
Purchases of property and equipment	(948)	(1,505)	(1,014)
Proceeds from sale of property and equipment	125	78	161
Net proceeds from disposal of assets	2,098	972	400
Proceeds from sale of brand rights and other assets	843	—	—
Increase (decrease) in other assets	(313)	263	31
Net cash provided by (used in) investing activities	1,805	(192)	(422)
Cash flow from continuing financing activities:			
Proceeds from (payments on) notes payable and warrants	(2,688)	—	317
Proceeds from bank debt and short term notes	139,394	114,765	86,047
Payments on bank debt and short term notes	(151,490)	(110,440)	(92,972)
Payments on capital lease obligations	—	(39)	(44)
Payments on litigation settlement	—	—	(980)
Proceeds from employee stock purchase plan	122	—	—
Purchase of treasury stock	—	—	(898)
Proceeds from exercise of stock options	247	16	11
Net cash provided by (used in) financing activities	(14,415)	4,302	(8,519)
Effect of exchange rate changes on cash from continuing operations	(88)	14	—
Net decrease in cash and cash equivalents from continuing operations	—	—	—
Net decrease in cash flow from discontinued operations	—	—	—
Cash and cash equivalents at beginning of year	—	—	—
Cash and cash equivalents at end of year	\$ —	\$ —	\$ —
Cash flow from discontinued operations:			
Cash flow provided by operating activities	\$ 54	\$ 34	\$ —
Cash flow used in investing activities	(54)	—	—
Cash flow provided by (used in) financing activities	—	(34)	—
Effect of exchange rate changes on cash	—	—	—
Net decrease in cash flow from discontinued operations	\$ —	\$ —	\$ —

See accompanying notes.

ROCKFORD CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Accounting Policies

Organization and Description of Business

Rockford Corporation and subsidiaries (“Rockford”) designs, assembles and distributes high performance mobile audio products, primarily under the Rockford Fosgate, Lightning Audio, and Rockford Acoustic Design brands.

Rockford was organized and incorporated under the laws of the State of Arizona on July 22, 1980. Corporate headquarters are located in Tempe, Arizona. Manufacturing is performed at facilities located in Tempe, Arizona and by third party manufacturers in Asia. Rockford uses warehouses located in Arizona and Michigan.

Principles of Consolidation

The consolidated financial statements include the accounts of Rockford and its wholly and majority owned subsidiaries. Intercompany accounts and transactions have been eliminated in consolidation.

Cash and Cash Equivalents

Cash and cash equivalents consist of cash and highly liquid investments with remaining maturities of three months or less when acquired. Rockford’s investments have consisted of commercial paper, certificates of deposit and money market accounts.

Fair Value of Financial Instruments

At December 31, 2007, Rockford has the following financial instruments: accounts receivable, accounts payable, accrued salaries and incentives, accrued warranty, other accrued expenses, notes payable, and long-term debt. The carrying value of accounts receivable, accounts payable, accrued salaries and incentives, accrued warranty, and other accrued expenses, approximates their fair value based on the liquidity of these financial instruments or based on their short-term nature. The carrying value of notes payable and long-term debt approximates fair value based on the market interest rates available to Rockford for debt of similar risk and maturities.

Revenue Recognition

Rockford recognizes revenue and records sales, net of related discounts, when all of the following criteria are met:

- Persuasive evidence of an arrangement exists;
- Ownership has transferred to the customer;
- The price to the customer is fixed or determinable; and
- Collectibility is reasonably assured.

Rockford also records reductions to revenue for estimated customer returns and additional sales incentive offerings, such as growth and volume incentive rebates and prompt pay discounts, based on historical rates.

In addition, Rockford earns royalties by licensing its brand names and know-how to its customers for use in their product. Royalty revenue is recognized as the customer produces products utilizing Rockford’s brand names and know-how based upon the term of the agreement and the production information provided by the licensee. The royalties are included in net sales on the consolidated statement of operations.

ROCKFORD CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Shipping and Handling Costs

Rockford records outbound product shipping costs as freight expense in sales and marketing expense. Freight expense for the years ended December 31, 2005, 2006 and 2007 was approximately \$5.4 million, \$3.3 million and \$2.8 million respectively.

Accounts Receivable and Allowances

Rockford sells its products principally to mobile audio dealers and distributors in North America, South America, Europe and Asia. Rockford also sells certain portions of its product line to major mass retailers in the United States and Canada. At December 31, 2006 and 2007, net accounts receivable includes approximately \$3.3 million and \$2.7 million respectively, due from international businesses.

Rockford maintains an allowance for doubtful accounts, based on historical rates, for estimated losses resulting from the inability of its customers to make required payments. Rockford has included in the allowance for accounts receivable at December 31, 2006 and 2007, approximately \$1.0 million, and \$0.8 million respectively, for doubtful accounts.

Rockford also maintains allowances for prompt pay and freight discounts, based on historical rates for discounts offered to customers. Rockford has included in its allowance for accounts receivable at December 31, 2006 and 2007, approximately \$0.3 million and \$0.1 million respectively, with respect to customers expected to use such discounts after year-end.

Inventories

Inventories consist principally of finished goods and raw materials of electronic and mechanical components used in the manufacturing of amplifiers, speaker systems and other finished goods. Inventories are carried at the lower of cost or market computed using the weighted average method. Rockford writes-down estimated obsolete or unmarketable inventory equal to the difference between the cost of inventory and the estimated market value based upon assumptions regarding future demand, average selling price, and market conditions.

Property and Equipment

Property and equipment is stated at cost. Depreciation and amortization are computed principally on the straight-line method for financial reporting purposes over a two to ten year life. Leasehold improvements are amortized on the straight-line method over the shorter period of the lease term or the estimated useful life of the asset.

Impairment of Long-Lived Assets

In accordance with the SFAS No. 144, *Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of*, Rockford records impairment losses on long-lived assets used in operations when events and circumstances indicate that the assets might be impaired and the undiscounted cash flows estimated to be generated by those assets are less than the carrying amounts of those assets. Impairment, if any, is based on the excess of the carrying amount over the fair value of those assets and is recorded in the period in which the determination is made.

Goodwill

Rockford accounts for acquired businesses under SFAS No. 141, *Business Combinations*, and SFAS No. 142, *Goodwill and Other Intangible Assets*. When Rockford accounts for acquired businesses as purchases, it allocates purchase prices to the assets, definite-lived intangible assets, and liabilities acquired based on the estimated fair values on the respective acquisition dates. Based on these values, Rockford allocates any excess purchase price over

ROCKFORD CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

the fair value of the net assets acquired to goodwill. Rockford has written off or impaired all remaining goodwill related to acquisitions.

Advertising

Rockford expenses advertising as incurred. Advertising expense for the years ended December 31, 2005, 2006 and 2007 was approximately \$0.8 million, \$0.6 million and \$0.2 million respectively. Such amounts are included in sales and marketing expenses in Rockford's Consolidated Statements of Operations.

Income Taxes

Rockford accounts for income taxes under the provisions of SFAS No. 109, *Accounting for Income Taxes*. Deferred tax assets and liabilities are recognized in order to account for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax laws (including rates) is recognized in income in the period that includes the enactment date.

Rockford assesses the likelihood that it will be able to recover its deferred tax assets. If recovery is not likely, Rockford must increase the provision, or decrease the benefit, by recording a valuation allowance against the deferred tax assets that it estimates will not ultimately be recoverable. As of December 31, 2007, Rockford had a full valuation allowance against its net deferred tax assets, as described in Note 7.

Rockford adopted the provisions of FASB Interpretation No. 48 Accounting for Uncertainty in Income Taxes ("FIN 48") an interpretation of FASB Statement No. 109 ("SFAS 109") on January 1, 2007. Adoption had no net impact given that the approximately \$1.1 million adjustment reduced both Rockford's deferred tax assets and the related valuation allowance. The future recognition of the \$1.1 million would not impact the effective income tax rate as long as Rockford maintains its full valuation allowance against its deferred tax assets. However, the recognition of such assets, along with a release in the valuation allowance, could favorably affect the effective income tax rate.

Product Warranty Cost and Service Returns

Rockford's return policy is to replace, repair or issue credit for product under warranty. Returns received during the current period are expensed as received and a reserve is maintained for future returns from current shipments. Management calculates the reserve using historical return rates by brand. These rates are reviewed and adjusted periodically as actual results become available.

A reconciliation of the warranty and returns reserve activity is as follows for the years ended December 31, 2005, 2006 and 2007.

	<u>2005</u>	<u>2006</u>	<u>2007</u>
	(In thousands)		
Balance at the beginning of year	\$ 4,789	\$ 3,185	\$ 2,199
Provision for warranties and returns	10,882	6,674	3,694
Net settlements made during the year	<u>(12,486)</u>	<u>(7,660)</u>	<u>(4,626)</u>
Balance at the end of the year	<u>\$ 3,185</u>	<u>\$ 2,199</u>	<u>\$ 1,267</u>

Income (Loss) per Common Share

Rockford reports income (loss) per common share in accordance with SFAS No. 128, *Earnings Per Share*. Diluted income per share includes the dilutive effects of options, warrants and convertible securities.

ROCKFORD CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Significant Customers

Rockford had sales to one customer representing 23.4%, 22.6% and 19.2% of net sales for the years ended December 31, 2005, 2006 and 2007, respectively and sales to another customer representing 13.7%, 14.9% and 7.5% of net sales for the year ended December 31, 2005, 2006 and 2007, respectively. These customers accounted for approximately 25.8% and 6.7% of the accounts receivable balance at December 31, 2006 and 20.8% and 6.1% at December 31, 2007.

Foreign Currency Translation

Rockford has translated the financial statements of foreign subsidiaries into U.S. dollars in accordance with SFAS No. 52, *Foreign Currency Translation*. All asset and liability accounts have been translated using the current exchange rates at the balance sheet date. Shareholders' equity accounts were translated at historical exchange rates. Amounts reported in the statements of operations have been translated using the average exchange rate for the year. The gains and losses resulting from the change in exchange rates from year-to-year have been reported separately as a component of shareholders' equity. The effect on the statements of operations of transaction gains and losses is insignificant. Rockford recorded in 2007 a currency gain of approximately \$411,000 due to the recognition of Rockford's previously unrealized cumulative translation gains triggered by the dissolution of its European subsidiary which was completed in December of 2007.

Stock Based Compensation

Rockford grants stock options for a fixed number of shares to employees with an exercise price equal to the fair market value of the shares at date of grant. Fair market value of the underlying shares is determined by the market price at the date of the grant. Prior to the adoption of SFAS 123R on January 1, 2006, Rockford accounted for stock options using the intrinsic value method, in accordance with Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees*, and related Interpretations. Rockford had adopted the disclosure-only provisions of SFAS No. 123, *Accounting for Stock-Based Compensation*, and accordingly, recognized no compensation expense for employee stock option grants. Stock option grants to non-employees were charged to expense based upon the fair value of the options granted.

Effective January 1, 2006 Rockford adopted SFAS No 123R using the "modified prospective" method permitted by SFAS No. 123R. In this method compensation costs are recognized beginning with the effective date based on the requirements of SFAS No. 123R for all share-based payments granted or modified after the effective date, and based on the requirements of SFAS No. 123 for all awards granted to employees prior to the effective date of SFAS No. 123R that remain unvested on the effective date. No share-based employee compensation cost has been reflected in net loss prior to the adoption of SFAS No. 123R. Results for prior periods have not been restated.

The following table represents the effect on net loss and loss per share if Rockford had applied during 2005 the fair value based method and recognition provisions of SFAS No. 123R, *Accounting for Stock-Based Compensation*, to stock-based employee compensation:

	<u>Year Ended December 31, 2005</u>
	<u>(In thousands except per share data)</u>
Net loss as reported	\$ (4,087)
Proforma SFAS No. 123R expense	(451)
Proforma net loss	<u>\$ (4,538)</u>
Proforma loss per common share	
Basic	<u>\$ (0.49)</u>
Diluted	<u>\$ (0.49)</u>

ROCKFORD CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

For purposes of proforma disclosure, the estimated fair value of the options is amortized to expense over the option's vesting period. See Note 8 for further discussion of Rockford's stock-based employee compensation.

Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. The actual results experienced by Rockford may differ from management's estimates.

New Accounting Pronouncements

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*. This statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007. Rockford does not expect the adoption of SFAS No. 157 will have a material impact on its consolidated financial statements.

In December 2007 the FASB issued SFAS No. 141R, *Business Combinations*, or SFAS 141R. SFAS 141R 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 statement to evaluate the nature and financial effects of the business combination. SFAS 141R is effective for financial statements issued for fiscal years beginning after December 15, 2008. Accordingly, any business combinations Rockford engages in will be recorded and disclosed following existing generally accepted accounting principles until January 1, 2009. Rockford is still assessing the impact of this standard on its future consolidated financial statements.

2. Discontinued Operations

MB Quart. Rockford placed its MB Quart GmbH subsidiary into receivership under German law in September of 2004. By instituting the receivership, Rockford relinquished any future benefit from the assets of this subsidiary. As a result, Rockford has treated the MB Quart GmbH operations as discontinued operations for all years presented.

The following represents the results of operations for MB Quart GmbH for the periods presented and are reported on Rockford's statements of operations as results from discontinued operations:

	<u>December 31, 2005</u> (In thousands)
Revenues	\$ —
Cost of sales	—
Operating expenses	63
Interest and other expense (income), net	—
Income tax benefit	—
Net loss	<u>\$ (63)</u>

Rockford Home Group. Prior to October 2005 Rockford operated its Rockford Home Group, a home audio business using the NHT (Now Hear This), Fosgate Audionics and Hafler brands. On October 18, 2005, Rockford sold the assets and liabilities of NHT for a cash purchase price of \$2.4 million. As a result of the sale Rockford recorded a net loss on the sale of approximately \$1.0 million, net of fees, which is included in loss from disposal of discontinued operations. At the closing, Rockford received approximately \$2.2 million and the remaining proceeds

ROCKFORD CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

of approximately \$0.2 million were placed into an escrow account that was available to pay claims, if any, of the Buyer relating to the representations made by Rockford in the Asset Purchase Agreement. There were no claims and the escrow amount was released to Rockford in October 2006.

In connection with the sale of NHT, Rockford assigned a lease to office space, located in Benicia, California, and used solely in NHT's operations, to the Buyer. As a condition of the assignment of the lease, the landlord required Rockford to guarantee the rental payments through October 2008, the lease termination date. As the buyer makes monthly lease payments, Rockford's obligation is reduced by those amounts. As of December 31, 2007, the future rental commitment under the original lease, and therefore the maximum potential exposure under the guarantee, was approximately \$0.2 million. Management believes the likelihood Rockford will have to perform under the guarantee is remote. No liability relating to the guarantee has been recorded in Rockford's financial statements as of December 31, 2006 and 2007.

Rockford discontinued the operations of its Fosgate Audionics and Hafler businesses at the time of the NHT sale. As a result of the October 2005 sale, Rockford has treated its Rockford Home Group operations as discontinued operations for all periods presented.

The following represents the results of operation for the Rockford Home Group for the periods presented and are reported on Rockford's Consolidated Statements of Operations as results from discontinued operations:

	<u>December 31,</u>	
	<u>2005</u>	<u>2006</u>
	(In thousands)	
Revenues	\$5,266	\$ 46
Cost of sales	3,165	201
Operating expenses	2,382	—
Interest and other expense (income), net	<u>1</u>	<u>—</u>
Net loss	<u>\$ (282)</u>	<u>\$ (155)</u>

3. Inventories

Inventories consisted of the following:

	<u>December 31,</u>	
	<u>2006</u>	<u>2007</u>
	(In thousands)	
Raw materials	\$ 4,801	\$ 3,564
Work in progress	563	246
Finished goods	<u>14,248</u>	<u>10,542</u>
	<u>\$19,612</u>	<u>\$14,352</u>

ROCKFORD CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

4. Property and Equipment

Property and equipment consisted of the following:

	December 31,	
	2006	2007
	(In thousands)	
Machinery and equipment	\$ 13,230	\$ 10,501
Tooling equipment	3,314	2,952
Leasehold improvements	2,838	2,861
Furniture and fixtures	297	297
Computer software and hardware	1,722	2,229
Construction in process	80	80
Assets under capital leases	182	182
	<u>21,663</u>	<u>19,102</u>
Less accumulated depreciation and amortization	<u>(19,176)</u>	<u>(17,197)</u>
	<u>\$ 2,487</u>	<u>\$ 1,905</u>

Depreciation expense was approximately \$3.1 million, \$2.2 million and \$1.5 million in 2005, 2006, and 2007, respectively. Depreciation of assets under capital leases is included in depreciation expense. Accumulated depreciation on assets under capital leases totaled \$46,000 at December 31, 2007.

5. Notes Payable and Long-Term Debt

Notes payable and long-term debt consisted of the following:

	December 31,	
	2006	2007
	(In thousands)	
Asset based credit facility	\$ 10,400	\$ 3,475
Convertible senior subordinated secured notes	9,500	9,500
Other	—	318
	<u>19,900</u>	<u>13,293</u>
Less debt discount	(222)	(130)
Less current portion	<u>(10,400)</u>	<u>(3,581)</u>
	<u>\$ 9,278</u>	<u>\$ 9,582</u>

Interest payments were approximately \$2.0 million, \$1.4 million and \$1.4 million for the years ended December 31, 2005, 2006 and 2007, respectively.

Rockford entered into an asset-based credit facility with Wachovia Capital Financial Corporation (Western) as Agent and Wachovia Bank, National Association as Arranger on March 29, 2004 and as amended most recently on November 28, 2007. This credit facility, as amended, is a \$20 million asset-based credit facility, has a term expiring on March 24, 2011, and is collateralized by substantially all of Rockford's assets. Under the agreement, pricing options based on LIBOR and prime rates are available to Rockford. The interest rate was 7.25% at December 31, 2007. As of December 31, 2007, Rockford was in compliance with all applicable covenants. The availability under the credit facility at December 31, 2007 was approximately \$9.4 million in excess of the outstanding balance of \$3.5 million.

ROCKFORD CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The Wachovia credit facility requires that Rockford maintain blocked lock box accounts, whereby Wachovia takes possession of all cash receipts on a daily basis and these amounts are applied to reduce Rockford's outstanding debt. In accordance with EITF 95-22: *Balance Sheet Classification of Borrowings Outstanding under Revolving Credit Agreements That Include both a Subjective Acceleration Clause and a Lock-Box Arrangement*, Rockford has recorded the \$10.4 million and \$3.5 million outstanding balances as of December 31, 2006 and 2007, respectively, on the Wachovia credit facility as short-term. Rockford expects to maintain the facility for its entire term.

Rockford has outstanding \$9.5 million of 4.5% convertible senior subordinated secured notes due 2009 and warrants to purchase 961,573 shares (plus 59,073 warrants issued to the placement agent in the original transaction) of common stock at \$3.73 per share. These items are outstanding under agreements effective on June 10, 2004 and as amended on November 12, 2004. The net proceeds of approximately \$9.5 million face value are allocated between the warrants and the notes based on their respective fair values. The value of the warrants was calculated using the Black-Scholes pricing model. The discount on the notes is being accreted ratably, over the term of the notes, to the \$9.5 million amount due at maturity. Debt issuance costs were capitalized and are being amortized over the life of the notes. The noteholders may convert the notes into Rockford's common stock at any time before their redemption, which at latest would be on the scheduled maturity date of June 10, 2009. The conversion price is \$4.61 per share. If fully converted, the notes will convert into 2,060,738 shares of Rockford's common stock. Rockford may, at its option, redeem all or any part of the notes from and after June 10, 2007, for a redemption price equal to the outstanding principal plus accrued interest. The noteholders also have a second priority lien on certain Rockford assets.

Rockford was in compliance with all applicable covenants under the indenture for the convertible notes as of December 31, 2007.

The aggregate principal payments due on long-term debt (including the remaining principal amount relating to the patent settlement, and the Wachovia credit facility that is classified as short term for the reasons described above) are as follows:

	<u>Years Ending December 31,</u> <u>(In thousands)</u>	
2008	\$	715
2009		9,609
2010		103
2011		3,475
2012		—
	<u>\$</u>	<u>13,902</u>

ROCKFORD CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

6. Leases

Rockford leases certain manufacturing, warehouse and office facilities, and computer hardware and software under noncancelable operating leases that expire in various years through December 2010.

Future minimum payments under noncancelable capital and operating leases with initial terms of one year or more consisted of the following at December 31, 2007:

	<u>Capital</u> <u>(In thousands)</u>	<u>Operating Leases</u> <u>(In thousands)</u>
2008	\$ 59	\$ 1,696
2009	59	726
2010	—	119
2011	—	6
2012	—	—
Thereafter	—	—
Total minimum lease payments	118	\$ 2,547
Less amount representing interest and taxes	19	
Total present value of capital obligation	99	
Less current portion	48	
Long-term obligation under capital leases	\$ 51	

Total rental expense for all operating leases was approximately \$3.2 million, \$2.3 million and \$1.8 million for the years ended December 31, 2005, 2006 and 2007 respectively.

7. Income Taxes

Rockford's deferred tax assets consisted of the following:

	<u>December 31,</u>	
	<u>2006</u>	<u>2007</u>
	<u>(In thousands)</u>	
Deferred tax assets Inventory basis	\$ 1,592	\$ 1,021
Basis in receivables	749	340
Book over tax depreciation	301	680
Accrued warranty	528	469
Net operating loss carryforward	15,827	17,261
Capital loss carryforward	—	945
Federal and state credit carryforwards	2,402	1,974
Accrued liabilities and other	514	719
Gross deferred tax assets	21,913	23,409
Valuation allowance	(21,913)	(23,409)
Net deferred tax assets	\$ —	\$ —

In 2005, 2006, and 2007 Rockford has maintained a valuation allowance recorded on the entire amount of its deferred tax assets. On January 1, 2007, the valuation allowance was reduced by \$1.1 million due to the adoption of a new accounting pronouncement that is described below in further detail. During 2007, the valuation allowance increased by \$2.6 million to an ending balance of \$23.4 million at December 31, 2007 primarily due to a projected

ROCKFORD CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

net operating loss for U.S. tax purposes. The valuation allowance includes approximately \$148,000 for net operating loss carryforwards that relate to stock option compensation expense and warrants expense for income tax reporting purposes. Any utilization of this portion of Rockford's net operating loss carryforwards would be recorded as an increase in additional paid in capital. Valuation allowances are subject to reversal in future years at such time as the actual benefits are utilized or operating profits become sustainable at a level that meets the recoverability criteria under SFAS 109 *Accounting for Income Tax*. The recoverability criteria in SFAS 109 requires a judgment whether it is more likely than not, based on an evaluation of positive and negative evidence, that a valuation allowance is not needed. If positive evidence of sufficient quality overcomes the negative evidence, Rockford would reverse all or a portion of the valuation allowance resulting in a decrease to income tax expense, or an income tax benefit, in the consolidated statement of operations. Rockford evaluates whether the deferred tax assets are realizable, and the need for valuation allowances, quarterly.

At December 31, 2007 Rockford had a net operating loss carryforward for United States federal income tax purposes of approximately \$47.8 million. Approximately \$45.9 million of this carryforward is from domestic operations and can be carried forward until it begins to expire in 2024. This carryforward results in a deferred tax asset of approximately \$15.6 million. Approximately \$1.9 million of the net operating loss carryforward is from international operations, is subject to an annual limitation under Section 382 and will begin to expire in 2011 if not utilized. This carryforward results in a deferred tax asset of approximately \$0.7 million. Rockford also has a deferred tax asset in the amount of \$1.0 million for state tax loss carryforwards. The state loss carryforwards begin to expire in 2008. Rockford has a capital loss carryforward for federal income tax purposes of \$2.8 million. This carryforward results in a deferred tax asset in the amount of \$0.9 million. This carryforward expires in 2012. Rockford also has approximately \$2.0 million of federal and state tax credits for alternative minimum tax and research and experimentation. The research and experimentation credits begin to expire in 2022 and 2017 for federal and state, respectively. However, the alternative minimum tax credits can be carried forward indefinitely. These total credits result in a deferred tax asset of approximately \$2.0 million.

A valuation allowance was recorded for the entire unreserved balance of net operating loss carryforwards and credits in 2007. Rockford has not recorded a benefit related to losses generated outside of the United States.

Federal and state income tax expense (benefit) consisted of the following:

	Year Ended December 31,		
	2005	2006	2007
	(In thousands)		
Current:			
Federal expense (benefit)	\$ —	\$(437)	\$ —
State expense (benefit)	—	—	—
Foreign expense	—	—	—
Total current expense (benefit)	—	(437)	—
Deferred:			
Federal expense (benefit)	—	—	—
State expense (benefit)	—	—	—
Foreign expense(benefit)	—	—	—
Total deferred expense (benefit)	—	—	—
Income tax expense (benefit)	<u>\$ —</u>	<u>\$(437)</u>	<u>\$ —</u>

ROCKFORD CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

A reconciliation of Rockford's effective income tax rate to the federal statutory rate follows:

	Year Ended December 31,		
	2005	2006	2007
	(In thousands)		
Federal statutory rate — continuing operations	\$(1,022)	\$(3,104)	\$ 233
Federal statutory rate — discontinued operations	(368)	(53)	—
State tax net of federal benefit	—	—	—
State tax operating loss carryforward	(552)	(408)	(136)
Nondeductible items	178	110	68
Amount not taxable due to dissolution of subsidiary	—	—	(2,531)
Tax benefit on disposal of domestic subsidiary stock	—	(1,008)	—
Federal and state tax credits	(1,100)	(367)	(138)
Loss of state net operating losses	—	267	—
Revision of contingency reserve	—	(437)	—
Increase in valuation allowance	3,177	4,378	2,567
Affiliate unbenefited losses	—	249	—
Other, net	(313)	(64)	(63)
Income tax benefit	<u>\$ —</u>	<u>\$ (437)</u>	<u>\$ —</u>

Rockford's income (loss) attributable to foreign operations amounted to approximately \$(8,000), \$(732,000) and \$(96,000) for years ended December 31, 2005, 2006 and 2007, respectively. Income (loss) attributable to domestic operations amounted to approximately \$(4,709,000), \$(8,116,000) and \$782,000 for the years ended December 31, 2005, 2006 and 2007, respectively.

In 2005, Rockford received refunds in the amount of \$0.8 million. In 2006, Rockford received refunds in the amount of \$0.5 million. In 2007, Rockford received a refund in the amount of \$18,000. The 2005 and 2006 refunds were primarily due to amended returns and carry backs of net operating losses into years in which Rockford was in a taxable position. The 2007 refund was due to an overpayment of tax from a prior year.

Rockford adopted the provisions of FASB Interpretation No. 48 Accounting for Uncertainty in Income Taxes ("FIN 48") an interpretation of FASB Statement No. 109 ("SFAS 109") on January 1, 2007. Adoption had no net impact given that the approximately \$1.1 million adjustment reduced both Rockford's deferred tax assets and the related valuation allowance. The future recognition of the \$1.1 million would not impact the effective income tax rate as long as Rockford maintains its full valuation allowance against its deferred tax assets. However, the recognition of such assets, along with a release in the valuation allowance, could favorably affect the effective income tax rate.

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

	2007 (In thousands)
Balance at beginning of year	\$ 1,071
Additions based on tax positions relating to current year	—
Additions for tax positions of prior years	—
Reductions for tax positions of prior years	—
Settlements	—
Balance at ending of year	<u>\$ 1,071</u>

ROCKFORD CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Rockford recognizes interest and penalties related to uncertain tax positions in income tax expense. As of December 31, 2007, Rockford has not recorded any related expense in its income statement for 2007. Rockford's 2003-2007 years remain subject to examination for federal income tax purposes, as well as for certain state taxing jurisdictions where Rockford operates. The statute of limitations for certain years may be extended if Rockford were to utilize certain of its carryover attributes from years outside of this range. Rockford does not expect the amount of unrecognized tax benefits to significantly increase or decrease over the next twelve months.

8. Common Stock Grants and Options

Rockford has provided stock option plans for selected employees, directors and consultants. Under the stock option plans, options to purchase common stock of Rockford will be granted to the selected employees, directors and consultants at the fair market value of the underlying common stock. The options generally have a term of ten years and become exercisable over three years commencing on the date of the grant. Under certain circumstances, Rockford has the right to repurchase common stock acquired under some of the options at their fair market value.

At December 31, 2007 Rockford had four active share-based employee compensation plans. Stock option awards granted from these plans are granted at the fair market value on the date of grant, and vest over a period determined at the time the options are granted, ranging from zero to three years, and have a maximum term of ten years. Some options provide for accelerated vesting if there is a change in control (as defined in the plans). When options under any of the plans are exercised, new shares of Rockford's common stock are issued. At December 31, 2007 there were 91,600 shares available for grant under these plans.

Prior to January 1, 2006 Rockford accounted for share-based employee compensation, including stock options, using the method prescribed in Accounting Principles Board opinion No. 25, "*Accounting for Stock Issued to Employees*" and related Interpretations ("APB Opinion No. 25"). Under APB Opinion No. 25 if stock options are granted at market price, no compensation cost is recognized, and a disclosure is made regarding the pro forma effect on net earnings assuming compensation cost had been recognized in accordance with SFAS No. 123, "*Accounting for Stock-Based Compensation*." In December 2004, the FASB issued SFAS No. 123R, which requires companies to measure and recognize compensation expense for all share-based payments at fair value. SFAS No. 123R eliminates the ability to account for share-based compensation transactions using APB Opinion No 25, and generally requires that such transactions be accounted for using prescribed fair-value based methods.

On December 21, 2005 Rockford's Board of Directors approved accelerating the vesting of certain out-of-the-money, unvested stock options held by current employees, including executive officers and directors. All stock options priced at or above \$5.70 were considered to be out-of-the-money. The acceleration was effective as of December 21, 2005. The acceleration of these options was done primarily to eliminate future compensation expense Rockford would otherwise recognize in its income statement with respect to these options upon the adoption of FAS 123R. The future expense that was eliminated was approximately \$0.3 million, of which approximately \$0.2 million is attributable to options held by executive officers and directors.

The adoption of SFAS No. 123R increased compensation expense for the years ended December 31, 2006 and 2007 by approximately \$0.4 million and \$0.3 million, respectively. This increased basic and diluted loss per share by \$0.05 and lowered basic and diluted income per share by \$0.04 for the years ended December 31, 2006 and 2007, respectively. The total value of stock option awards is expensed ratably over the service period of the employees receiving the awards. As of December 31, 2007, total unrecognized compensation cost related to non vested stock option awards was approximately \$0.3 million and the related weighted- average period over which these costs are expected to be recognized is approximately 1.6 years. The total fair value of options that vested during the years ended December 31, 2005, 2006, and 2007 was \$0.7 million, \$0.4 million and \$0.3 million, respectively.

Prior to the adoption of SFAS No. 123R, Rockford presented all tax benefits of deductions resulting from the exercise of stock options as operating cash flows in the condensed consolidated statements of cash flows. SFAS No. 123R requires the cash flows resulting from the tax benefits resulting from tax deductions in excess

ROCKFORD CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

of the compensation cost recognized for those options (excess tax benefits) to be classified as financing cash flows. There were no excess tax benefits for the years ended December 31, 2006 and 2007.

Prior to the adoption of SFAS 123R, proforma information regarding net loss and net loss per share was required by FAS No. 123, which also required that the information be determined as if Rockford had accounted for its employee stock options granted subsequent to December 31, 1994, under the fair value method of that Statement. The fair value of each stock option award was estimated on the date of the grant using the Black-Scholes option pricing model with the following weighted average assumptions for the years ended December 31:

	<u>2005</u>	<u>2006</u>	<u>2007</u>
Expected life of the award	5 years	5 years	5 years
Dividend yield	0%	0%	0%
Risk-free interest rate	4.5%	4.6%	5.1%
Expected volatility	0.46	0.47	0.48

Option activity under the stock option plans during the year ended December 31, 2007 was as follows:

	<u>Outstanding Options</u>		<u>Weighted Average Remaining Contractual Term</u>	<u>Aggregate Intrinsic Value</u>
	<u>Shares</u>	<u>Weighted Average Exercise Price</u>		
Outstanding at January 1, 2007	1,905,951	\$ 4.12		
Granted	70,000	2.45		
Exercised	(5,000)	2.15		
Expired	(273,487)	3.66		
Outstanding at December 31, 2007	<u>1,697,464</u>	<u>4.14</u>	<u>6.5 years</u>	<u>\$ —</u>
Exercisable at December 31, 2007	<u>1,380,937</u>	<u>\$ 4.48</u>	<u>6.0 years</u>	<u>\$ —</u>

The intrinsic value of options exercised during the years ended December 31, 2005, 2006, and 2007 was \$82,000, \$7,000 and \$2,000 respectively. Options to purchase 389,150 shares, 530,000 shares and 70,000 shares respectively were granted during the years ended December 31, 2005, 2006 and 2007. The weighted average fair value of options granted during the years ended December 31, 2005 and 2006 and 2007, was \$1.35, \$1.26 and \$1.17 respectively.

The following table summarizes information about stock options under the plans outstanding at December 31, 2007:

<u>Range of Exercise Prices</u>	<u>Options Outstanding</u>			<u>Options Exercisable</u>	
	<u>Number Outstanding at December 31, 2007</u>	<u>Weighted Average Remaining Contractual Life</u>	<u>Weighted Average Exercise Price</u>	<u>Number Outstanding at December 31, 2007</u>	<u>Weighted Average Exercise Price</u>
\$2.15 - \$2.90	1,029,800	8.1	\$ 2.48	763,773	\$ 2.47
\$3.41 - \$4.19	102,000	8.3	\$ 3.47	51,500	\$ 3.47
\$5.70 - \$7.68	501,164	3.4	\$ 6.80	501,164	\$ 6.80
\$11.00	64,500	2.3	\$ 11.00	64,500	\$ 11.00
	<u>1,697,464</u>			<u>1,380,937</u>	

ROCKFORD CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

9. Income (Loss) Per Share

	Year Ended December 31,		
	2005	2006	2007
(In thousands, except per share data)			
Numerator:			
Income (loss) from continuing operations	\$(2,723)	\$(8,692)	\$ 686
Plus:			
Income impact of assumed conversion of convertible debt	—	—	—
Income (loss) from continuing operations available to shareholders	(2,723)	(8,692)	686
Loss from discontinued operations	(1,364)	(155)	—
Net income (loss) available to shareholders	<u>\$(4,087)</u>	<u>\$(8,847)</u>	<u>\$ 686</u>
Denominator:			
Denominator for basic net income (loss) per share	9,258	9,388	9,325
Effect of dilutive securities:			
Employee stock options	—	—	17
Warrants	—	—	—
Dilutive potential common shares	—	—	17
Denominator for diluted net income (loss) per share	<u>9,258</u>	<u>9,388</u>	<u>9,342</u>
Income (loss) per common share:			
Income (loss) from continuing operations			
Basic	<u>\$ (0.29)</u>	<u>\$ (0.92)</u>	<u>\$ 0.07</u>
Diluted	<u>\$ (0.29)</u>	<u>\$ (0.92)</u>	<u>\$ 0.07</u>
Loss from discontinued operations			
Basic	<u>\$ (0.15)</u>	<u>\$ (0.02)</u>	<u>\$ 0.00</u>
Diluted	<u>\$ (0.15)</u>	<u>\$ (0.02)</u>	<u>\$ 0.00</u>
Net income (loss)			
Basic	<u>\$ (0.44)</u>	<u>\$ (0.94)</u>	<u>\$ 0.07</u>
Diluted	<u>\$ (0.44)</u>	<u>\$ (0.94)</u>	<u>\$ 0.07</u>

The effect of 108,269 and 162,901 employee stock options which would have increased net shares outstanding using the treasury stock method were not included in the diluted loss per share calculation for December 31, 2005 and 2006 respectively, as they were not dilutive due to the net loss for the periods.

Rockford also has \$9.5 million of 4.5% convertible senior subordinated secured notes due 2009 and warrants to purchase 961,573(excluding 59,073 warrants issued to the placement agent in the original transaction) shares of common stock at \$3.73 per share. The noteholders may convert the notes into the Rockford's common stock at any time before the scheduled maturity date of June 10, 2009. The conversion price was \$4.61 per share. If fully converted, the notes are scheduled to convert into 2,060,738 shares of Rockford's common stock. The convertible senior subordinated secured notes and warrants were not included in the diluted loss per share calculation for December 31, 2005 and 2006, as they were not dilutive due to the net loss for the periods and not included in the

ROCKFORD CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

diluted income per share calculation for December 31, 2007 as they were anti-dilutive. Rockford excluded the warrants in the diluted income per share calculations because the exercise price of the warrants exceeded the average market price of the stock.

Outstanding stock options with exercise prices (plus unearned compensation for unvested awards) greater than the average market price of Rockford's common stock during the period are excluded from the computation of diluted net income (loss) per share of common stock. A summary of the excluded amounts follows (in thousands, except exercise prices):

	<u>Year Ended December 31st</u>		
	<u>2005</u>	<u>2006</u>	<u>2007</u>
Outstanding options	912	888	1,430
Exercise price	\$6.27	\$6.04	\$ 4.51

10. Contingencies

Rockford is a party to legal proceedings arising in the ordinary course of business. Based upon advice from outside legal counsel, management is of the opinion the resolution of these matters will have no material effect on Rockford's consolidated financial position or results of operations.

During January 2007, Rockford settled a patent litigation case for payments totaling \$1,613,000. The settlement released Rockford with respect to all claims of the patent litigation case. The settlement resulted in a charge of approximately \$1.5 million in 2006.

11. Benefit Plan

Rockford has a 401(k) Retirement Savings Plan (Plan) covering substantially all employees who have completed six consecutive months of service without regard to hours of service. Under the terms of the Plan, employees may make voluntary contributions, subject to Internal Revenue Service limitations. Rockford will match employee contributions up to three percent of the employee's annual compensation. Additional contributions to the Plan can be made at the discretion of the Board of Directors. Contributions to the Plan during the year ended December 31, 2005, 2006 and 2007, were approximately \$0.5 million, \$0.4 million and \$0.3 million respectively.

12. Stock Purchase Program

In September 2007, Rockford's Board of Directors authorized a common share repurchase program that enables Rockford to purchase, in the open market and through negotiated transactions, up to 5%, or approximately 470,000 of its outstanding common shares. Rockford had repurchased 449,700 shares under this program as of December 31, 2007. A second share repurchase program was announced in February 2008 for up to an additional 5% or approximately 450,000 shares of Rockford's common shares. Rockford's current credit agreement permits stock purchases up to \$1.5 million. Rockford used \$0.9 million of this purchase authority through December 31, 2007, for purchases under Rockford's stock repurchase program.

ROCKFORD CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

13. Segment Information

Rockford operates its business almost exclusively under the mobile audio segment. Below is geographic information for Rockford's revenues:

<u>Region(1)</u>	<u>Year Ended December 31</u>			
	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>% 2007</u>
	(In thousands)			
United States	\$112,657	\$ 86,017	\$71,771	80.9%
Other Americas (includes Canada)	9,438	8,007	7,193	8.1%
Europe	9,042	5,316	6,069	6.8%
Asia	4,545	3,436	3,712	4.2%
Total sales to external customers	<u>\$135,682</u>	<u>\$102,776</u>	<u>\$88,745</u>	<u>100%</u>

(1) Revenues are attributed to geographic regions based on the location of customers.

For the years ended December 31, 2005, 2006 and 2007, sales to one customer accounted for 23.4%, 22.6% and 19.2% of total net sales, respectively and sales to another customer represented 13.7%, 14.9% and 7.5% of net sales for the years ended December 31, 2005, 2006 and 2007, respectively.

14. Disposal of Assets

Rockford recorded the following disposals of assets in 2005 and 2006:

MB Quart. Rockford assigned its North American brand rights for MB Quart in September of 2005 and recorded a gain of approximately \$0.8 million.

Q-Logic. Rockford sold the assets of its Q-Logic enclosures line of products on March 31, 2006 for \$1.75 million. At closing on March 31, 2006, Rockford received \$0.8 million of cash and a non-interest bearing note for \$1.0 million payable in 30 equal monthly payments beginning May 1, 2006. The note was discounted using Rockford's effective borrowing rate and recorded as a note receivable. Rockford adjusted the carrying value of its Q-Logic assets by recording an impairment charge to cost of goods sold of approximately \$0.8 million as of December 31, 2005.

ROCKFORD CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

15. Special Charges

During the first quarter of 2007 Rockford recorded a special charge of approximately \$1.1 million related to departing employees. The charge is primarily due to costs associated with the Retirement and Salary Continuation Agreement Rockford entered into with its former CEO.

During the second half of 2006, Rockford recorded a special charge of approximately \$1.3 million. This charge was in connection with costs associated with headcount reductions of approximately 100 positions. These included manufacturing, engineering, sales and general administrative positions. Employees immediately affected were notified and began receiving related payments. Remaining employees were given notification of expected termination dates for their respective positions. Payments for these individuals commenced upon their departure.

These charges increased general and administrative expenses. Rockford expects to complete all payments arising from these special charges by the quarter ending March 31, 2009. The following table summarizes the outstanding liabilities arising from these special charges at December 31, 2006, the changes in the twelve month period ending December 31, 2007, and the outstanding liabilities at December 31, 2007 (in thousands):

	Liability at December 31, 2006	Twelve Months Ended December 31, 2007			Liability at December 31, 2007
		Reserve Recorded	Payments	Adjustments To Reserve	
Post Employment Costs:	<u>\$615</u>	<u>\$1,174</u>	<u>\$(1,191)</u>	<u>\$(14)</u>	<u>\$584</u>

Item 9. *Changes In and Disagreements with Accountants on Accounting and Financial Disclosure*

None.

Item 9A. *Controls and Procedures*

Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures

Under the supervision and with the participation of Rockford's management, including its President, who is its principal executive officer, and its CFO, who is its principal financial officer, Rockford conducted an evaluation of its disclosure controls and procedures, as such term is defined under *Rule 13a-15(e)* promulgated under the Securities Exchange Act of 1934, as amended (the Exchange Act). Based on this evaluation, Rockford's President and Rockford's CFO concluded that Rockford's disclosure controls and procedures were effective as of its year ending December 31, 2007.

Management's Annual Report on Internal Control Over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in the *Exchange Act Rules 13a-15(f)*. A system of 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.

Under the supervision and with the participation of management, including the President and the CFO, Rockford's management has evaluated the effectiveness of its internal control over financial reporting as of December 31, 2007 based on the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this evaluation, Rockford's management has evaluated and concluded that Rockford's internal control over financial reporting was effective as of December 31, 2007.

This annual report does not include an attestation report of Rockford's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by Rockford's registered public accounting firm pursuant to temporary rules of the Securities and Exchange Commission that permit Rockford to provide only management's report in this annual report.

Changes in Internal Controls

Rockford is continuously seeking to improve the efficiency and effectiveness of its operations and of its internal controls. This results in modifications to its processes throughout the Company. However, there has been no change in its internal control over financial reporting that occurred during Rockford's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Rockford's internal control over financial reporting.

Item 9B. *Other Information*

None

PART III

Item 10. *Directors and Executive Officers and Corporate Governance*

The information required by this item with respect to items 401 and 405 of Regulation S-K is incorporated by reference to the sections entitled "Executive Officers and Board of Directors" and "Section 16(A) Beneficial Ownership Reporting Compliance" in the definitive Proxy Statement for Rockford's Annual Meeting of Stockholders to be held May 8, 2008.

Rockford has adopted a Code of Business Ethics and Policy that applies to its directors, officers and employees, including its principal executive officer, principal financial officer, principal accounting officer or

controller, or persons performing similar functions. The Code of Business Ethics and Policy is available on Rockford's Internet website at www.rockfordcorp.com. Rockford will post on its website information about any amendment to, or waiver from, any provision of the Code of Business Ethics and Policy that applies to its principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions.

Item 11. *Executive Compensation*

The information required by this item is incorporated by reference to the sections entitled "Executive Compensation" and "Director Compensation" in the definitive Proxy Statement for Rockford's Annual Meeting of Stockholders to be held May 8, 2008.

Item 12. *Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters*

The information required by this item is incorporated by reference to the section entitled "Principal Shareholders and Shareholdings of Officers and Directors," "Security Ownership of Certain Beneficial Owners," "Grants of Plan Based Awards During 2007," and "Outstanding Equity Awards at December 31, 2007" in the definitive Proxy Statement for Rockford's Annual Meeting of Stockholders to be held May 8, 2008.

Item 13. *Certain Relationships and Related Transactions*

The information required by this item is incorporated by reference to the sections entitled "Related Party Transactions" and "Director Independence" in the definitive Proxy Statement for Rockford's Annual Meeting of Stockholders to be held May 8, 2008.

Item 14. *Principal Accounting Fees and Services*

The information required by this item is incorporated by reference to the section entitled "Principal Accounting Fees and Services" in the definitive Proxy Statement for Rockford's Annual Meeting of Stockholders to be held May 8, 2008.

PART IV

Item 15. *Exhibits, Financial Statement Schedules*

- (a) 1. Financial Statements — See Index to Consolidated Financial Statements on page 26 of this report.
- (a) 2. Financial Statement Schedules — Financial Statement Schedules are excluded since they are either not applicable or the information is included in the Financial Statements.
- (a) 3. Exhibits — The exhibits listed on the accompanying Index to Exhibits immediately following the Financial Statements are filed as part, or hereby incorporated by reference into, this report.

Exhibits

<u>Exhibit Number</u>	<u>Description of Document</u>
3.1	Articles of Incorporation+
3.2	Restated Bylaws as amended through July 27, 2000++
3.3	Amendment to Articles of Incorporation filed on January 12, 1988+
3.4	Amendment to Articles of Incorporation filed on May 12, 1999+
3.5	Amendment to Articles of Incorporation filed on May 17, 1999+
3.7	Amendment to Articles of Incorporation filed on July 1, 1999+
4.1	Conformed Copy of Indenture dated as of June 10, 2004 between Rockford Corporation and BNY Western Trust Company###
4.2	Form of 4.5% Convertible Senior Subordinated Secured Note Due 2009###
4.3	Form of Warrant to Purchase Common Stock###
4.4	Conformed Copy of Registration Rights Agreement dated as of June 10, 2004 by and among Rockford Corporation, Piper Jaffray & Co. and the Buyers as defined therein###
4.5	Conformed Copy of Warrant Agent Agreement dated as of June 10, 2004 between Rockford Corporation and BNY Western Trust Company###
4.6	Conformed Copy of Security Agreement dated as of June 10, 2004 among Rockford Corporation, Audio Innovations, Inc. and BNY Western Trust Company###
4.7	Conformed Copy of Intercreditor Agreement dated as of June 10, 2004 by and among Congress Financial Corporation (Western), BNY Western Trust Company, Rockford Corporation and Audio Innovations, Inc.###
4.8	Conformed Copy of Global Amendment to Notes, Warrants, Indenture, Security Agreement, Warrant Agent Agreement and Registration Rights Agreement and Waiver of Event of Default dated as of November 12, 2004 by and among Rockford Corporation, Audio Innovations, Inc., BNY Western Trust Company and the persons listed on the Schedule of Holders attached thereto as Exhibit A#####
4.9	Conformed Copy of Amendment to Warrants, Warrant Agent Agreement and Registration Rights Agreement dated as of November 12, 2004, by and among Rockford Corporation, BNY Western Trust Company and Piper Jaffray & Co#####
10.62	Loan and Security Agreement among Rockford Corporation, Audio Innovations, Inc., Congress Financial Corporation (Western), and various Financial Institutions, dated March 29, 2004##
10.62.1	First Amendment to Loan and Security Agreement and Conditional Default Waiver among Congress Financial Corporation (Western), as a lender and as administrative and collateral agent for the lenders party to the Loan Agreement, Rockford Corporation, and Audio Innovations, Inc., dated as of June 10, 2004***
10.62.2	Second Amendment to Loan and Security Agreement among Congress Financial Corporation (Western) as a lender and as administrative and collateral agent for the lenders party to the Loan Agreement, Rockford Corporation and Audio Innovations, Inc., dated as of December 30, 2004***
10.63	Industrial Lease Agreement between Jerome A. and/or Cathy E. Reynolds and Rockford Corporation, dated as of May 1, 2003***
10.66	Securities Purchase Agreement dated as of June 10, 2004 between Rockford Corporation and the Buyers as defined therein#####
10.67	Third Amendment to Loan and Security Agreement, dated August 31, 2005, among Rockford, Rockford's wholly owned subsidiary Audio Innovations, Inc. ("AII"), and Wachovia Capital Finance Corporation (Western).**
10.70	Fourth amendment to Loan and Security Agreement and Consent, dated March 21, 2006, among Rockford, Rockford's wholly owned subsidiary Audio Innovations, Inc. ("AII"), and Wachovia Capital Finance Corporation (Western).****
10.74	Fifth amendment to Loan and Security Agreement and Consent, dated August 31, 2006, among Rockford, Rockford's wholly owned subsidiary Audio Innovations, Inc. ("AII"), and Wachovia Capital Finance Corporation (Western).****

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<u>Exhibit Number</u>	<u>Description of Document</u>
10.75	Agreement between Rockford and David Fiori dated February 22, 2007*****
10.76	Retirement and Salary Continuation Agreement between Rockford and W. Gary Suttle*****
10.77	Fifth Lease Amendment Between Centerpoint Properties Trust and Rockford Corporation, dated November 9, 2006*****
10.78	Sixth amendment to Loan and Security Agreement and Waiver, dated March 7, 2007, among Rockford, Rockford's wholly owned subsidiary Audio Innovations, Inc. ("AII"), and Wachovia Capital Finance Corporation (Western).*****
10.79	Seventh amendment to Loan and Security Agreement and Waiver, dated November 28, 2007, among Rockford, Rockford's wholly owned subsidiary Audio Innovations, Inc. ("AII"), and Wachovia Capital Finance Corporation (Western).
10.80	Revised form of Change of Control Agreement, entered into with 5 executive officers (Mr. Jackson, Mr. Vasek, Ms. Mott, Mr. Matson, and Mr. Carlsness).
21	List of Subsidiaries of Rockford Corporation
23.1	Consent of Independent Registered Public Accounting Firm
31.1	Certification pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 for W. Gary Suttle
31.2	Certification pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 for Richard G. Vasek
32	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

* Management contract or compensatory plan or arrangement

+ Previously filed with registration statement effective April 19, 2000 and/or amendments.

++ Previously filed on August 11, 2000 with Rockford's Quarterly Report on Form 10-Q for the quarter ended June 30, 2000.

+++ Previously filed on March 29, 2002 with Rockford's Annual Report on Form 10-K for the year ended December 30, 2001.

Previously filed on May 17, 2004 with Rockford's Quarterly Report on Form 10-Q for the quarter ended March 31, 2004.

Previously filed on June 15, 2004 with Rockford's Current Report on Form 8-K.

Previously filed on November 15, 2004 with Rockford's Current Report on Form 8-K.

Previously filed on June 15, 2004 as Exhibit 10.1 with Rockford's Current Report on Form 8-K.

** Previously filed on November 14, 2005, with Rockford's quarterly report on Form 10Q for the quarter ended September 30, 2005.

*** Previously filed on April 15, 2005 with Rockford's Annual Report on Form 10-K for the year ended December 31, 2004.

**** Previously filed on November 14, 2006, with Rockford's quarterly report on Form 10Q for the quarter ended September 30, 2006.

***** Previously filed on March 28, 2007, with Rockford's annual report on Form 10-K for the year ended December 31, 2006.

SIGNATURES

Pursuant to the requirements of the Section 13 or 15(d), as amended, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of Tempe, State of Arizona, on March 12, 2008.

ROCKFORD CORPORATION

By: /s/ WILLIAM R. JACKSON

William R. Jackson
President and Director

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, this Report has been signed by the following persons in the capacities and on the dates indicated:

<u>Name</u>	<u>Title</u>	<u>Date</u>
<u>/s/ WILLIAM R. JACKSON</u> William R. Jackson	President (Principal Executive Officer) and Director	March 12, 2008
<u>/s/ RICHARD G. VASEK</u> Richard G. Vasek	Vice President of Finance and Chief Financial Officer, Secretary (Principal Financial Officer)	March 12, 2008
<u>/s/ MARK E. BARRIERE</u> Mark E. Barriere	Corporate Controller (Principal Accounting Officer)	March 12, 2008
<u>/s/ JERRY E. GOLDRRESS</u> Jerry E. Goldress	Director	March 12, 2008
<u>/s/ TIMOTHY C. BARTOL</u> Timothy C. Bartol	Director	March 12, 2008
<u>/s/ NICHOLAS G. BARTOL</u> Nicholas G. Bartol	Director	March 12, 2008
<u>/s/ RALPH B. GODFREY</u> Ralph B. Godfrey	Director	March 12, 2008
<u>/s/ JOHN P. LLOYD</u> John P. Lloyd	Director	March 12, 2008

EXHIBIT INDEX

<u>Exhibit Number</u>	<u>Description of Document</u>
3.1	Articles of Incorporation+
3.2	Restated Bylaws as amended through July 27, 2000++
3.3	Amendment to Articles of Incorporation filed on January 12, 1988+
3.4	Amendment to Articles of Incorporation filed on May 12, 1999+
3.5	Amendment to Articles of Incorporation filed on May 17, 1999+
3.7	Amendment to Articles of Incorporation filed on July 1, 1999+
4.1	Conformed Copy of Indenture dated as of June 10, 2004 between Rockford Corporation and BNY Western Trust Company###
4.2	Form of 4.5% Convertible Senior Subordinated Secured Note Due 2009###
4.3	Form of Warrant to Purchase Common Stock###
4.4	Conformed Copy of Registration Rights Agreement dated as of June 10, 2004 by and among Rockford Corporation, Piper Jaffray & Co. and the Buyers as defined therein###
4.5	Conformed Copy of Warrant Agent Agreement dated as of June 10, 2004 between Rockford Corporation and BNY Western Trust Company###
4.6	Conformed Copy of Security Agreement dated as of June 10, 2004 among Rockford Corporation, Audio Innovations, Inc. and BNY Western Trust Company###
4.7	Conformed Copy of Intercreditor Agreement dated as of June 10, 2004 by and among Congress Financial Corporation (Western), BNY Western Trust Company, Rockford Corporation and Audio Innovations, Inc.###
4.8	Conformed Copy of Global Amendment to Notes, Warrants, Indenture, Security Agreement, Warrant Agent Agreement and Registration Rights Agreement and Waiver of Event of Default dated as of November 12, 2004 by and among Rockford Corporation, Audio Innovations, Inc., BNY Western Trust Company and the persons listed on the Schedule of Holders attached thereto as Exhibit A####
4.9	Conformed Copy of Amendment to Warrants, Warrant Agent Agreement and Registration Rights Agreement dated as of November 12, 2004, by and among Rockford Corporation, BNY Western Trust Company and Piper Jaffray & Co####
10.62	Loan and Security Agreement among Rockford Corporation, Audio Innovations, Inc., Congress Financial Corporation (Western), and various Financial Institutions, dated March 29, 2004##
10.62.1	First Amendment to Loan and Security Agreement and Conditional Default Waiver among Congress Financial Corporation (Western), as a lender and as administrative and collateral agent for the lenders party to the Loan Agreement, Rockford Corporation, and Audio Innovations, Inc., dated as of June 10, 2004***
10.62.2	Second Amendment to Loan and Security Agreement among Congress Financial Corporation (Western) as a lender and as administrative and collateral agent for the lenders party to the Loan Agreement, Rockford Corporation and Audio Innovations, Inc., dated as of December 30, 2004***
10.63	Industrial Lease Agreement between Jerome A. and/or Cathy E. Reynolds and Rockford Corporation, dated as of May 1, 2003***
10.66	Securities Purchase Agreement dated as of June 10, 2004 between Rockford Corporation and the Buyers as defined therein#####
10.67	Third Amendment to Loan and Security Agreement, dated August 31, 2005, among Rockford, Rockford's wholly owned subsidiary Audio Innovations, Inc. ("AII"), and Wachovia Capital Finance Corporation (Western).**
10.70	Fourth amendment to Loan and Security Agreement and Consent, dated March 21, 2006, among Rockford, Rockford's wholly owned subsidiary Audio Innovations, Inc. ("AII"), and Wachovia Capital Finance Corporation (Western).****
10.74	Fifth amendment to Loan and Security Agreement and Consent, dated August 31, 2006, among Rockford, Rockford's wholly owned subsidiary Audio Innovations, Inc. ("AII"), and Wachovia Capital Finance Corporation (Western).****
10.75	Agreement between Rockford and David Fiori dated February 22, 2007.*****

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<u>Exhibit Number</u>	<u>Description of Document</u>
10.76	Retirement and Salary Continuation Agreement between Rockford and W. Gary Suttle.*****
10.77	Fifth Lease Amendment Between Centerpoint Properties Trust and Rockford Corporation, dated November 9, 2006.*****
10.78	Sixth amendment to Loan and Security Agreement and Waiver, dated March 7, 2007, among Rockford, Rockford's wholly owned subsidiary Audio Innovations, Inc. ("AII"), and Wachovia Capital Finance Corporation (Western).*****
10.79	Seventh amendment to Loan and Security Agreement and Waiver, dated November 28, 2007, among Rockford, Rockford's wholly owned subsidiary Audio Innovations, Inc. ("AII"), and Wachovia Capital Finance Corporation (Western).
10.80	Revised form of Change of Control Agreement, entered into with 5 executive officers (Mr. Jackson, Mr. Vasek, Ms. Mott, Mr. Matson, and Mr. Carlsness).
21	List of Subsidiaries of Rockford Corporation
23.1	Consent of Independent Registered Public Accounting Firm
31.1	Certification pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 for W. Gary Suttle
31.2	Certification pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 for Richard G. Vasek
32	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

* Management contract or compensatory plan or arrangement

+ Previously filed with registration statement effective April 19, 2000 and/or amendments.

++ Previously filed on August 11, 2000 with Rockford's Quarterly Report on Form 10-Q for the quarter ended June 30, 2000.

+++ Previously filed on March 29, 2002 with Rockford's Annual Report on Form 10-K for the year ended December 30, 2001.

Previously filed on May 17, 2004 with Rockford's Quarterly Report on Form 10-Q for the quarter ended March 31, 2004.

Previously filed on June 15, 2004 with Rockford's Current Report on Form 8-K.

Previously filed on November 15, 2004 with Rockford's Current Report on Form 8-K.

Previously filed on June 15, 2004 as Exhibit 10.1 with Rockford's Current Report on Form 8-K.

** Previously filed on November 14, 2005, with Rockford's quarterly report on Form 10Q for the quarter ended September 30, 2005.

*** Previously filed on April 15, 2005 with Rockford's Annual Report on Form 10-K for the year ended December 31, 2004.

*** Previously filed on April 15, 2005 with Rockford's Annual Report on Form 10-K for the year ended December 31, 2004.

**** Previously filed on November 14, 2006, with Rockford's quarterly report on Form 10Q for the quarter ended September 30, 2006.

***** Previously filed on March 28, 2007, with Rockford's annual report on Form 10-K for the year ended December 31, 2006.

SEVENTH AMENDMENT TO LOAN AND SECURITY AGREEMENT

THIS SEVENTH AMENDMENT TO LOAN AND SECURITY AGREEMENT (this "Amendment"), dated as of November __, 2007, is entered into among WACHOVIA CAPITAL FINANCE CORPORATION (WESTERN), a California corporation formerly known as Congress Financial Corporation (Western) ("Agent"), as administrative and collateral agent for the Lenders party to the Loan Agreement (as defined below) from time to time ("Lenders"), WACHOVIA CAPITAL FINANCE CORPORATION (WESTERN), a California corporation formerly known as Congress Financial Corporation (Western), as a Lender ("Wachovia"), ROCKFORD CORPORATION, an Arizona corporation ("Borrower Agent"), and AUDIO INNOVATIONS, INC., an Oklahoma corporation ("AII" and together with Rockford, collectively, "Borrowers").

RECITALS

A. Agent, Wachovia, Wachovia Bank, National Association, as arranger, and Borrowers have previously entered into that certain Loan and Security Agreement dated March 29, 2004 as amended by the First Amendment to Loan and Security Agreement and Conditional Default Waiver dated as of June 10, 2004, the Second Amendment to Loan and Security Agreement dated as of December 30, 2004, the Third Amendment to Loan and Security Agreement dated as of August 31, 2005, the Fourth Amendment to Loan and Security Agreement and Consent dated as of March 21, 2006, the Fifth Amendment to Loan and Security Agreement dated as of August 31, 2006 and the Sixth Amendment to Loan and Security Agreement dated as of March 7, 2007 (the "Loan Agreement"), pursuant to which Wachovia has made certain loans and financial accommodations available to Borrowers. Terms used herein without definition shall have the meanings ascribed to them in the Loan Agreement.

B. Borrowers have requested Agent and Wachovia to amend the Loan Agreement in certain respects, and Agent and Wachovia are willing to accommodate such request on the terms and conditions set forth herein.

C. Borrowers are entering into this Amendment with the understanding and agreement that, except as specifically provided herein, none of Agent's or Lenders' rights or remedies as set forth in the Loan Agreement is being waived or modified by the terms of this Amendment.

AGREEMENT

NOW, THEREFORE, in consideration of the foregoing and the mutual covenants herein contained, and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereby agree as follows:

1. Amendments to Loan Agreement .

(a) Permanent Reserve . The amount of the Reserve established pursuant to Section 1 of the First Amendment to Loan and Security Agreement and Conditional Default Waiver dated as of June 10, 2004, as amended by the Third Amendment to Loan and Security Agreement dated as of August 31, 2005 and the Fifth Amendment to Loan and Security Agreement dated as of August 31, 2006, is hereby reduced to One Million Dollars (\$1,000,000). Such Reserve is a permanent Reserve under the Loan and Security Agreement and shall not be reduced or eliminated without the written consent of Agent, and will be referred to as the “Permanent Reserve”.

(b) Eligible In Transit Inventory . The amount “One Million Dollars (\$1,000,000)” in clause (m) of the definition of “Eligible Inventory” in Section 1.25 of the Loan Agreement (as amended by the Second Amendment to Loan and Security Agreement dated as of December 30, 2004) is hereby replaced with “Three Million Dollars (\$3,000,000)”.

(c) Eurodollar Rate Margin . The definition of “Eurodollar Rate Margin” in Section 1.34 of the Loan Agreement is hereby amended and restated to read in its entirety as follows:

“1.34 ‘ Eurodollar Rate Margin ’ shall mean five percent (5.00%) per annum; provided, that , on December 1, 2007, then on January 1, 2008, and on the first day of each fiscal quarter (March 1, July 1, October 1 and January 1) thereafter, the Eurodollar Rate Margin shall be adjusted as follows based upon the average daily Excess Availability during the immediately preceding sixty (60) days as determined by Agent after giving effect to the Permanent Reserve:

<u>Excess Availability</u>	<u>Eurodollar Rate Margin</u>
Equal to or greater than \$4,000,000	Two percent (2.00%)
Less than \$4,000,000 but equal to or greater than \$1,000,000	Two and one-half percent (2.50%)
Less than \$1,000,000	Three percent (3.00%)”

(d) Final Maturity Date . The definition of “Final Maturity Date” in Section 1.39 of the Loan Agreement is hereby amended and restated to read in its entirety as follows:

“1.39 ‘ Final Maturity Date ’ shall mean March 24, 2011, as such date may be extended from year to year pursuant to Section 14.1(a) hereof.”

(e) Letter of Credit Rate . The definition of “Letter of Credit Rate” in Section 1.56 of the Loan Agreement is hereby amended and restated to read in its entirety as follows:

“1.56 ‘ Letter of Credit Rate ’ shall mean five percent (5.00%) per annum; provided, that, on December 1, 2007, then on January 1, 2008, and on the first day of each fiscal quarter (March 1, July 1, October 1 and January 1) thereafter, the Letter of Credit Rate shall be adjusted as follows based upon the average daily Excess Availability during the immediately preceding sixty (60) days as determined by Agent after giving effect to the Permanent Reserve:

<u>Excess Availability</u>	<u>Eurodollar Rate Margin</u>
Equal to or greater than \$4,000,000	Two percent (2.00%)
Less than \$4,000,000 but equal to or greater than \$1,000,000	Two and one-half percent (2.50%)
Less than \$1,000,000	Three percent (3.00%)”

(f) Prime Rate Margin. The definition of “Prime Rate Margin” in Section 1.76 of the Loan Agreement is hereby amended and restated to read in its entirety as follows:

“7.76 ‘ Prime Rate Margin ’ shall mean one percent (1.00%) per annum; provided, that, on December 1, 2007, then on January 1, 2008, and on the first day of each fiscal quarter (March 1, July 1, October 1 and January 1) thereafter, the Prime Rate Margin shall be adjusted as follows based upon the average daily Excess Availability during the immediately preceding sixty (60) days as determined by Agent after giving effect to the Permanent Reserve:

<u>Excess Availability</u>	<u>Eurodollar Rate Margin</u>
Equal to or greater than \$4,000,000	Zero percent (0.00%)
Less than \$4,000,000 but equal to or greater than \$1,000,000	One-half of one percent (0.50%)
Less than \$1,000,000	One percent (1.00%)”

(g) Eurodollar Rate Loans. Clause (v) of Section 3.1 of the Loan Agreement is hereby amended and restated to read in its entirety as follows:

“(v) each Eurodollar Rate Loan must be in the amount of One Million Dollars (\$1,000,000) or an integral multiple of Five Hundred Thousand Dollars (\$500,000) in excess thereof,”

(h) Servicing Fee. The amount “Four Thousand Dollars (\$4,000)” in Section 3.4 of the Loan Agreement is hereby replaced with “Two Thousand Dollars (\$2,000)”.

(i) Unused Line Fee. The percentage “three-eighths of one percent (0.375%)” in Section 3.5 of the Loan Agreement is hereby replaced with “one-quarter of one percent (0.25%)”.

(j) Inventory Appraisals. Clause (d) of Section 7.3 of the Loan Agreement is hereby amended and restated to read in its entirety as follows:

“(d) upon Agent’s request, Borrowers shall, at their expense, no more than one (1) time in any twelve (12) month period if the average daily Excess Availability after giving effect to the Permanent Reserve exceeded \$3,000,000 during the sixty (60) days immediately preceding the subject request by Agent, and no more than two (2) times in any twelve (12) month period if the average daily Excess Availability after giving effect to the Permanent Reserve was equal to or less than \$3,000,000 during the sixty (60) days immediately preceding the subject request by Agent, but at any time or times as Agent may request on or after an Event of Default, deliver or cause to be delivered to Agent full written appraisals as to the Inventory in form, scope and methodology reasonably acceptable to Agent and by an appraiser reasonably acceptable to Agent, addressed to Agent and Lenders and upon which Agent and Lenders are expressly permitted to rely;”

(k) EBITDA. Section 9.17.1 of the Loan Agreement is hereby amended and restated to read in its entirety as follows:

“9.17.1 EBITDA. Borrowers and their Subsidiaries, on a consolidated basis, shall earn EBITDA, during each period of twelve (12) consecutive months ending on the last day of any fiscal quarter, of not less than \$4,000,000. Notwithstanding the foregoing, if on the last day of any of the foregoing periods, the Excess Availability before giving effect to the Permanent Reserve, minus the sum of (a) all of the Borrowers’ trade payables that are then more than thirty (30) days past due, plus (b) all of the Borrowers’ obligations and liabilities (other than trade payables) that are then past due, exceeds \$3,000,000, then Borrowers will not be required to comply with the foregoing minimum consolidated EBITDA covenant for the specific period then ending.

For the purposes hereof, ‘EBITDA’ shall mean the net income of Borrowers and their Subsidiaries determined on a consolidated basis in accordance with GAAP consistently applied, but excluding any extraordinary or one-time gains, plus (a) depreciation, amortization and other non-cash charges (to the extent deducted in the computation of such net income), plus (b) Interest Expense (to the extent deducted in the computation of such net income), plus (c) charges for federal, state, local and foreign income taxes (to the extent deducted in the computation of such income).”

(l) Early Termination Fee. Clauses (i) and (ii) of Section 14.1(c) of the Loan Agreement are hereby amended and restated to read in their entirety, and a new clause (iii) is hereby added to read in its entirety, as follows:

- | | |
|--|--|
| “(i) One percent (1.00%) of the Maximum Credit | On or before March 24, 2009 |
| (ii) One-half of one percent (0.50%) of the Maximum Credit | After March 24, 2009 but on or before March 24, 2010 |
| (iii) Zero | After March 24, 2010.” |

2. Consent.

(a) Notwithstanding anything to the contrary contained in Sections 9.10 and 9.11 of the Loan Agreement, Agent and Wachovia hereby consent to Borrower Agent fully or partially paying the principal balances owing on its 4.5% Convertible Senior Subordinated Secured Notes due 2009 and to Borrower Agent redeeming, purchasing or otherwise acquiring its Capital Stock, in consideration of its cash payments not to exceed \$1,500,000 in the aggregate, provided that in each case, (a) the Excess Availability, after giving effect to the Permanent Reserve and any such payment, would be greater than \$1,000,000 and (b) no Default or Event of Default has occurred and is continuing or would result therefrom. The foregoing consent shall apply only to the specific transactions described above and shall be subject to the conditions set forth above, and in all other respects, Agent and Lenders shall reserve and preserve their rights to require the Borrowers’ strict compliance with Sections 9.10 and 9.11 of the Loan Agreement and all other terms and provisions of the Financing Agreements.

(b) Notwithstanding anything to the contrary contained in the Loan Agreement or in any Guaranty and Security Agreement dated March 29, 2004 (a “Guaranty”), Agent and Wachovia hereby acknowledge that in order to simplify its corporate structure Borrower Agent is in the process of dissolving each of its subsidiaries, including AII and each Guarantor. Borrower Agent has determined that such subsidiaries no longer hold material assets and serve no continuing business purpose. Borrower Agent confirms and represents that, upon such dissolution, Borrower Agent will succeed to all of the assets of AII and each Guarantor and will assume all obligations to Agent and Lenders of AII and each Guarantor. In consideration of such confirmation and representation, Agent and Wachovia consent to the dissolution of the subsidiaries, including AII and each Guarantor. Upon completion of the dissolutions, the Loan Agreement is amended to remove each reference to AII and each Guarantor, so that all references to “Borrowers” will refer solely to Borrower Agent as the sole remaining entity in Borrower Agent’s corporate organization, and each Guaranty of the Guarantors is terminated and merged into the Loan Agreement.

3. Effectiveness of this Amendment. Agent must have received the following items, in form and content acceptable to Agent, before this Amendment is effective.

(a) Amendment; Acknowledgement. This Amendment and the attached Acknowledgement by Guarantors, each fully executed in a sufficient number of counterparts for distribution to all parties.

(b) Amendment Fee. An amendment fee in the amount of Fifty Thousand Dollars (\$50,000), which fee shall be paid to Agent by Borrowers on or before the date hereof and is fully earned as of the date hereof.

(c) Representations and Warranties. The representations and warranties set forth herein and in the Loan Agreement must be true and correct.

(d) Other Required Documentation. All other documents and legal matters in connection with the transactions contemplated by this Amendment shall have been delivered or executed or recorded and shall be in form and substance satisfactory to Agent.

4. Representations and Warranties. Each Borrower represents and warrants as follows:

(a) Authority. Such Borrower has the requisite corporate power and authority to execute and deliver this Amendment, and to perform its obligations hereunder and under the Financing Agreements (as amended or modified hereby) to which it is a party. The execution, delivery and performance by such Borrower of this Amendment have been duly approved by all necessary corporate action and no other corporate proceedings are necessary to consummate such transactions.

(b) Enforceability. This Amendment has been duly executed and delivered by such Borrower. This Amendment and each Financing Agreement (as amended or modified hereby) is the legal, valid and binding obligation of such Borrower, enforceable against such Borrower in accordance with its terms, and is in full force and effect.

(c) Representations and Warranties. The representations and warranties contained in each Financing Agreement (other than any such representations or warranties that, by their terms, are specifically made as of a date other than the date hereof) are correct on and as of the date hereof as though made on and as of the date hereof.

(d) Due Execution. The execution, delivery and performance of this Amendment are within the power of such Borrower, have been duly authorized by all necessary corporate action, have received all necessary governmental approval, if any, and do not contravene any law or any contractual restrictions binding on such Borrower.

(e) No Default. No event has occurred and is continuing that constitutes an Event of Default.

5. Choice of Law. The validity of this Amendment, its construction, interpretation and enforcement, and the rights of the parties hereunder, shall be determined under, governed by, and construed in accordance with the internal laws of the State of California governing contracts only to be performed in that State.

6. Counterparts. This Amendment may be executed in any number of counterparts and by different parties and separate counterparts, each of which when so executed and

delivered, shall be deemed an original, and all of which, when taken together, shall constitute one and the same instrument. Delivery of an executed counterpart of a signature page to this Amendment by telefacsimile shall be effective as delivery of a manually executed counterpart of this Amendment.

7. Reference to and Effect on the Financing Agreements .

(a) Upon and after the effectiveness of this Amendment, each reference in the Loan Agreement to “this Agreement”, “hereunder”, “hereof” or words of like import referring to the Loan Agreement, and each reference in the other Financing Agreements to “the Loan Agreement”, “thereof” or words of like import referring to the Loan Agreement, shall mean and be a reference to the Loan Agreement as modified and amended hereby.

(b) Except as specifically amended above, the Loan Agreement and all other Financing Agreements, are and shall continue to be in full force and effect and are hereby in all respects ratified and confirmed and shall constitute the legal, valid, binding and enforceable obligations of Borrowers to Agent and Lenders.

(c) The execution, delivery and effectiveness of this Amendment shall not, except as expressly provided herein, operate as a waiver of any right, power or remedy of Agent or any Lender under any of the Financing Agreements, nor constitute a waiver of any provision of any of the Financing Agreements.

(d) To the extent that any terms and conditions in any of the Financing Agreements shall contradict or be in conflict with any terms or conditions of the Loan Agreement, after giving effect to this Amendment, such terms and conditions are hereby deemed modified or amended accordingly to reflect the terms and conditions of the Loan Agreement as modified or amended hereby.

8. Integration . This Amendment and the Loan Agreement as amended, together with the other Financing Agreements, incorporates all negotiations of the parties hereto with respect to the subject matter hereof and is the final expression and agreement of the parties hereto with respect to the subject matter hereof.

9. Severability . In case any provision in this Amendment shall be invalid, illegal or unenforceable, such provision shall be severable from the remainder of this Amendment and the validity, legality and enforceability of the remaining provisions shall not in any way be affected or impaired thereby.

IN WITNESS WHEREOF, the parties have entered into this Amendment as of the date first above written.

ROCKFORD CORPORATION

By: _____
Name: _____
Title: _____

AUDIO INNOVATIONS, INC.

By: _____
Name: _____
Title: _____

WACHOVIA CAPITAL FINANCE
CORPORATION (WESTERN),
as Agent and as a Lender

By: _____
Name: _____
Title: _____

ACKNOWLEDGEMENT BY GUARANTORS

Dated as of November __, 2007

Each of the undersigned, being a guarantor (each a “Guarantor” and collectively, the “Guarantors”) under their Guaranty and Security Agreement dated March 29, 2004, made in favor of Agent and Lenders (as amended, modified or supplemented, the “Guaranty”) hereby acknowledges and agrees to the foregoing Seventh Amendment to Loan and Security Agreement (the “Amendment”) and confirms and agrees that the Guaranty is and shall continue to be, in full force and effect and is hereby ratified and confirmed in all respects except that, upon the effectiveness of, and on and after the date of the Amendment, each reference in the Guaranty to the Loan Agreement (as defined in the Amendment), “thereunder”, “thereof” or words of like import referring to the “Loan Agreement”, shall mean and be a reference to the Loan Agreement as amended or modified by the Amendment. Although Lender has informed Guarantors of the matters set forth above, and Guarantors have acknowledged the same, each Guarantor understands and agrees that Lender has no duty under the Loan Agreement, the Guaranty or any other agreement with any Guarantor to so notify any Guarantor or to seek such an acknowledgement, and nothing contained herein is intended to or shall create such a duty as to any advances or transaction hereafter.

ROCKFORD SINGAPORE CORPORATION

By: _____
Name: _____
Title: _____

ROCKFORD SALES.COM, INC.

By: _____
Name: _____
Title: _____

MB QUART SHANGHAI, INC.

By: _____
Name: _____
Title: _____

Non-Compete and Change in Control Agreement

This Agreement is between the individual named on the signature page of this Agreement (“Executive”) and Rockford Corporation, an Arizona corporation, (“Rockford”). Executive and Rockford agree as follows:

1 Background and Purpose

- 1.1 Executive’s Position. Executive is currently a member of Rockford’s senior management team, with the title identified on the signature page of this Agreement.
- 1.2 Confidential Information. Executive has access to confidential information that might be of substantial help to Rockford’s competitors, including information that could harm Rockford if used to compete with Rockford.
- 1.3 Potential Change of Control. Rockford is a public company and this position subjects Executive to significant risks associated with a change of control at Rockford. Subject to the limitations in this Agreement, Rockford desires to protect Executive from such risks.
- 1.4 Non-compete and Non-Disclosure. Rockford also desires to secure Executive’s promise not to disclose confidential information and not to compete with Rockford for a reasonable period after any termination of Executive’s employment.
- 1.5 Definitions. In this agreement, the following terms have the meanings given below:
 - (a) *Benefits Date* is the date Executive becomes entitled to receive Severance Benefits because an event occurs that satisfies the conditions stated in Section 2.1.
 - (b) *Business Reason* exists if any of the following occur:
 - (1) Executive acts with personal dishonesty, related to Executive’s responsibilities to Rockford, that results in Executive’s substantial and unjust personal enrichment,
 - (2) Executive is charged with committing a felony, other offense involving moral turpitude, or other offense that is injurious to Rockford or its reputation, and the Board finds that such charge has consequences for Rockford that create a Business Reason,

- (3) Executive's willful or gross misconduct is injurious to Rockford or its reputation,
- (4) Executive substantially breaches Executive's obligations and duties as a member of Rockford's senior management, or under any agreement with Rockford, and fails to correct the breach after reasonable notice from Rockford.
- (c) *Change of Control* means any merger, consolidation, sale of assets or other similar transaction or series of transactions involving Rockford, but excluding any transaction if
 - (1) Rockford's shareholders immediately before the transaction or series of transactions continue to own a majority of the combined voting power of the entity that survives the transaction, or
 - (2) Rockford directors who
 - (a) were Rockford directors immediately before the transaction or series of transaction; and
 - (b) continue to serve on the board of directors of the surviving entityconstitute a majority of the directors of that entity for not less than one year after the transaction.
- (d) *Competitive Business* means a business that manufactures or distributes mobile audio products that are competitive with the products Rockford (directly or through any division or subsidiary) manufactures or distributes during the term of Executive's employment at Rockford.
- (e) *Confidential Information* means trade secrets and other proprietary information that
 - (1) is not generally known to the public,
 - (2) Rockford has used, developed, or obtained, and
 - (3) relates to Rockford's business or the business of any Rockford customer or supplier.Confidential Information includes, but is not limited to, information contained in or about:

- Products or services,
- Fees, costs and pricing structure,
- Designs, drawings, and photographs,
- Analyses, formulae, and reports,
- Computer software, including operating systems, applications, databases, program listings, flow charts, manuals and documentation;
- Accounting and business methods,
- Inventions and new developments and methods, whether patentable or not and whether reduced to practice or not,
- Copyrightable works,
- Customers and customer lists, and
- all similar and related information in whatever form.

Confidential Information excludes information that is or was

- Rightfully known by Executive before Rockford employed Executive,
- Publicly available through no fault or action of Executive, or
- Published in a form generally available to the public through no fault or action of Executive.

(f) *Good Reason* exists if any of the following occur without Executive's consent and the notice and cure conditions stated below are satisfied:

- (1) Rockford substantially reduces Executive's overall scope of duties, authorities and responsibilities. Executive acknowledges that a new position in a larger combined company is not a reduction if it is in the same area of operations and involves a similar scope of management responsibility, even if the formal position is less senior within the larger combined company,
- (2) Rockford requires that Executive materially change Executive's place of employment. A change is not material if it involves a move of 50 miles or less from Executive's current business location, or
- (3) Rockford materially reduces Executive's base salary, except that it is not a material reduction in any year if
 - (a) Executive's base salary after the reduction is equal to or greater than the average of Executive's base

salary in the 3 years before the reduction minus 10 percent; or

- (b) a reduction in Executive's base salary that is consistent with a general reduction of pay across Rockford's senior management as a group due to poor financial performance or failure to meet financial objectives.

Good Reason exists only if:

- (x) Executive provides Rockford notice that at least one of the conditions described in this Section (f) exists within 90 days after the condition arises; and
 - (y) Rockford has a period of not less than 30 days nor more than 60 days to remedy the condition and Rockford does not do so; and
 - (z) Executive elects to terminate Executive's employment at Rockford within 10 days after Rockford's period to cure the condition expires.
- (g) *Rockford* means Rockford Corporation and any division, subsidiary, joint venture, or other business entity that Rockford owns directly or indirectly.
 - (h) *Severance Benefits* has the meaning given in Section 2.2.

2 **Change in Control Benefits .**

2.1 Right to Benefits . If, while this Agreement is in force:

- (a) Executive is an employee on the date of a Change of Control at Rockford, and
- (b) Within one year after the Change of Control, either
 - (1) Rockford terminates Executive's employment without a Business Reason, or
 - (2) Executive terminates Executive's employment with Good Reason

then Executive will receive the Severance Benefits. For purposes of this Agreement, termination of employment means separation from service as defined under Section 409A of the Code and regulations hereunder.

2.2 Severance Benefits. If the conditions in Section 2.1 are satisfied then Executive will receive the following Severance Benefits:

- (a) Payment of the larger of
 - (1) Executive's annual base salary and bonus as of the date of the Change of Control, or
 - (2) Executive's annual base salary and bonus as of the Benefits Date times the multiple stated on the signature page of this Agreement.

For purposes of this Section 2.2(a), the amount of Executive's bonus will be computed based on the average of the highest 2 bonuses paid to Executive during the 3 full years before Benefits Date (for example, if Executive's bonuses in the 3 years before the Benefits Date were \$30,000, \$10,000, and \$50,000, then Executive's bonus under this agreement is \$40,000).

- (b) Payment of Executive's vacation accrued through the Benefits Date,
- (c) Rockford will allow Executive to exercise all of the stock options Rockford has granted to Executive that are vested as of the Benefits Date in accordance with the terms of the stock option plan and the stock option grant given to Executive. In addition, to the extent Executive elects to be paid Executive's base salary in accordance with Rockford's ordinary payroll policies, Rockford will permit Executive's stock options to vest during the period when Rockford is paying the base salary component of Executive's Severance Benefits; provided that such options cannot be exercised later than the latest date in which they were otherwise exercisable under any circumstances, or the 10th anniversary of the original date of grant, if earlier. (This treatment will not require that Rockford permit Executive to participate in any other Rockford benefit programs), and
- (d) If required by COBRA, and only to the extent Executive elects under applicable COBRA procedures, continuation of Executive's group health benefits under Rockford's standard health benefit plans as of the Benefits Date until the earlier of:

- (1) the expiration of the period required by COBRA (generally 18 months, but may be longer if required by COBRA); or
- (2) the date Executive becomes eligible to be covered under a group health plan of another employer.

Rockford will reimburse Executive for the cost of Executive's group health benefits during this period.

2.3 Exclusivity. The Severance Benefits are exclusive. If there is a Change of Control and the conditions in Section 2.1 are satisfied, Rockford's sole obligation to Executive is to pay the Severance Benefits. Executive acknowledges that Executive is not entitled to any other benefits, compensation or other payments or rights upon termination and Executive releases all claims against Rockford relating to any termination under the conditions stated in Section 2.1.

2.4 Payment and Withholding.

- (a) At Executive's option, documented as described below, Rockford will pay the base salary component of Executive's Severance Benefits either:
 - (1) beginning on the 1st payroll period after Executive's termination of employment in accordance with Rockford's ordinary payroll policies over the period such payments would be made at Executive's base salary in the year before the Change of Control event (for example, if the multiple is two times base salary, such payments would be made over a two-year period), or
 - (2) any balance in a lump sum payable on the first day of any month elected by the Executive within the payment period described in (a), above.

An election under this Section 2.4(a) will be made when this Agreement is executed. Executive may change the election in the manner specified by Rockford, but it will be effective only if made not less than six months before a Change of Control.

- (b) The election under Section 2.4(a) is not available with respect to any amount that is subject to Section 409A. However, prior to a Change of Control, in accordance with transition rules under Section 409A, Executive may elect whether to receive any Severance Benefits that are based on base salary and subject to Section 409A in a lump sum or as salary continuation. Such

election, if made in 2007, will be valid for terminations occurring in 2008 or afterwards, and any election made in 2008 will be valid for any terminations occurring in 2009 and afterwards. Any additional election made after 2008 for amounts subject to Section 409A will be made in the time and manner required under Section 409A.

- (c) Absent an election under either Section 2.4(a) or 2.4(b), benefits will be paid under Section 2.4(a)(1).
- (d) Rockford will compute and pay the bonus component of Executive's Severance Benefits set forth in Section 2.2(a) at the time it computes and pays annual bonuses to its executive team, which will be during the period of January 1 through March 15 of the year after the year for which the current year bonus is earned, However, if the multiple set forth in this Agreement is 2 or more, one-half of the bonus amount will be paid during the period set forth in the previous sentence, and one-half will be paid during the period of January 1 through March 15 of the year following the first payment.
- (e) All payments of Severance Benefits are subject to withholding for applicable taxes.

3 **Other Terms of Employment .**

- 3.1 Agreement not Exclusive. This Agreement governs only Executive's rights to Severance Benefits if the conditions in Section 2.1 are satisfied and the other matters specifically addressed elsewhere in this Agreement. Other terms of Executive's employment are governed by Rockford's employee manual and general employment policies. Except for the express obligations stated in this Agreement, this Agreement does not change the terms of Rockford's employment of Executive.
- 3.2 Employment is At-Will. In particular, Rockford and Executive acknowledge that Executive's employment is and will continue to be at-will, as defined under applicable law. Either Rockford or Executive may terminate this Agreement and Executive's employment at any time for any reason by giving written notice of termination.
- 3.3 No General Severance Rights. This Agreement does not establish a general right to severance benefits. If Executive's employment ends for any reason other than the occurrence of a Benefits Date, Executive will receive only the payments and benefits due under Rockford's employee plans and policies as in effect at the time of termination and will not receive any Severance Benefits under this Agreement.

3.4 Other Agreements. Executive has signed the agreements and documents relating to Executive's employment at Rockford identified on the signature page to this Agreement. These documents discuss other terms of Executive's employment at Rockford. If there is any conflict between this Agreement and the other documents, this Agreement will control.

4 **Executive's Obligations**

4.1 Non-Competition and Non-Solicitation. During the term of Executive's employment at Rockford (including any period when Executive is treated as an employee under Rockford's stock option plans and Section 2.2(c)), and for one year after any termination of Executive's employment at Rockford, Executive will not:

- (a) Engage in, plan for, organize, work for, or assist, directly or indirectly, any Competitive Business. Executive will not violate this restriction if Executive owns less than 1% of a publicly traded company that competes with Rockford, so long as Executive has no active participation in its business,
- (b) Directly or indirectly
 - (1) induce or attempt to induce any Rockford employee to leave Rockford,
 - (2) induce or attempt to induce any Rockford customer, supplier, licensee or other business relation to cease doing business with Rockford, or
 - (3) interfere with the relationship between Rockford and any Rockford employee, customer, supplier, licensee or business relation.

4.2 Confidential Information. During and after the term of Executive's employment at Rockford, Executive will not disclose, use (either alone or with others), copy, or encourage anyone else to disclose to any other person or firm any of Rockford's Confidential Information unless the use, copying, or disclosure is:

- (a) within the scope of Executive's duties and responsibilities for Rockford,
- (b) done with Rockford's consent, or

- (c) required by law, but if Executive believes a disclosure is required by law then Executive will first give Rockford notice of the proposed disclosure and the opportunity to seek a protective order or take other action to maintain the confidentiality to the maximum extent the law permits.

Executive will take appropriate steps to safeguard the Confidential Information and prevent its inadvertent disclosure or theft.

- 4.3 Return of Documents . Upon termination of Executive's employment, or upon Rockford's request, Executive will return to Rockford all memoranda, notes, plans, records, documentation and other materials (including copies and information stored on computer) containing any of Rockford's Confidential Information. Executive will not make, retain, or give to any other person any copy or extract of any item Executive may be obligated to return to Rockford.
- 4.4 Actions . Executive acknowledges that it would be difficult to determine damages, and Rockford will not have an adequate remedy at law, if Executive breaches this Agreement. Accordingly, if Executive breaches this Agreement, Rockford may seek injunctive relief to enforce this Agreement. Nothing in this section limits or excludes any and all other rights, including rights to money damages, granted to Rockford in law or equity.

- 5 **Reformation and Severability** . If a section of this Agreement is deemed unreasonable as to time or scope by any court or arbitrator, then the court or arbitrator may modify the section so that it is reasonable and must then enforce the section as modified. If a section of this Agreement is deemed unreasonable by a court or arbitrator and cannot be modified so that it is reasonable, the section is severable from the remainder of this Agreement, which must be enforced according to its terms.

6 **Compliance with Section 409A**

- 6.1 Intent to Comply; Interpretation . Payments under this Agreement are intended to comply with or be exempt from Section 409A of the Code and this Agreement shall be interpreted to comply with Section 409A. For purposes of the Agreement, the salary continuation payments described in Section 2.4(a)(1) shall be treated as a series of separate payments.
- 6.2 Amounts Exempt from Section 409A . Because the payments under this Agreement are the result of an involuntary termination as defined under Section 409A, to the extent the payments under this Agreement are
 - (a) totally exempt from Section 409A; or

- (b) exempt up to the Applicable Amount and are paid within a period no later than the last day of the second taxable year following the Executive's termination of employment,

Executive may make the election in Section 2.4(a) with respect to such exempt payments and such payments will be paid without regard to the six-month delay described in Section 6.3 below, if applicable. As used in this Agreement, "Applicable Amount" means two times the lesser of:

- (A) Executive's annualized compensation for the year prior to Executive's termination (as adjusted and within the meaning of Section 409A of the Code); or
- (B) the maximum amount that may be taken into account under a qualified plan in accordance with Section 401(a)(17) of the Code for the year in which Executive's employment is terminated.

6.3 Six-month Delay for Certain "specified employees." Any payments under this Agreement that are paid to a "specified employee" as defined under Section 409A and that are not exempt as an involuntary severance payment, short-term deferral, nontaxable or exempt health care benefit, or otherwise, shall be paid no earlier than the first day of the seventh month after the Executive's termination of employment ("Delayed Payment Date"). Any non-exempt lump sum payment delayed under the previous sentence shall be paid on the Delayed Payment Date. Salary continuation payments shall be made in accordance with the schedule set forth in this Agreement, and with respect to the total of such payments, the Applicable Amount shall be paid first, followed by non-exempt amounts in excess of the Applicable Amount, but in no event will amounts in excess of the Applicable Amount be paid before the Delayed Payment Date. If a delay of payment is required under the preceding sentence, any delayed payments that were otherwise due before the Delayed Payment Date under this Agreement will be made to the Executive in a lump sum on the Delayed Payment Date.

7 **Term and Termination .**

- 7.1 Term. This Agreement is effective during the term while Rockford employs Executive. This Agreement is also effective after termination of Executive's employment to the extent any of its terms require performance after termination.
- 7.2 Termination. At any time before:

- (a) Rockford enters into an agreement that would result in a Change of Control, or
- (b) Any other event occurs that results in an actual Change of Control

Rockford's board of directors may terminate this Agreement for any reason other than as restricted in the next sentence. Rockford's board of directors may not terminate this Agreement in anticipation of, or to facilitate, a Change of Control. In connection with any termination, Rockford's board of directors must resolve in good faith that the termination is not in anticipation of, or to facilitate, a Change of Control. Termination is effective when Rockford gives Executive notice of the board's vote to terminate.

8 **Miscellaneous .**

8.1 Non-delegation of Executive's Rights. Executive's obligations, rights and benefits under this Agreement are personal and may not be delegated, assigned, or transferred without written consent from Rockford.

8.2 Notices. Notices are effective:

- (a) upon delivery to the recipient if sent in person, by e-mail, or by facsimile, or
- (b) three days after mailing, certified or registered mail, return receipt requested.

Notices must be sent to the addresses stated on the signature page of this Agreement. A party may change its address by giving notice of the new address.

8.3 Governing Law. Arizona law will govern this Agreement.

8.4 Attorneys' Fees. In any proceeding arising out of this Agreement the prevailing party is entitled to reasonable attorneys' fees, costs and other expenses incurred in connection with such proceeding. Rockford will pay amounts due Executive under this provision, if any, on or before the end of the year after Rockford is declared legally obligated by a court or other forum of applicable jurisdiction to make such payments (and after any period for appeal expires or any appeal is completed and affirms the obligation to pay), and this provision shall exist for the life of the Executive.

8.5 Arbitration. Disputes arising out of this Agreement or out of Executive's employment at Rockford will be submitted to binding arbitration in

metropolitan Phoenix, Arizona, before a single arbitrator or, if the parties cannot agree upon a single arbitrator, before a panel of three arbitrators, one selected by each party (within 10 days after notice of a dispute and failure to agree upon a single arbitrator) and a third appointed by the arbitrators selected by the parties. The selection of arbitrators and all arbitration proceedings will be in accordance with the rules for commercial arbitration of the American Arbitration Association, as amended to the date of the proceedings, and judgment upon the award may be entered in any court having jurisdiction. The arbitrators must render a decision within 30 days after their appointment and may award the costs of arbitration as they see fit.

- 8.6 Amendment and Waiver. The parties may amend this Agreement, and a party may waive another party's obligations under this Agreement, but the amendment or waiver must be in writing and signed by all parties to this Agreement. If a party waives any breach, the waiver applies only to the specific breach waived. It will not waive any other breach (including a subsequent breach of the same obligation).
- 8.7 Counterparts. The parties may execute this Agreement in counterparts. Each counterpart will be deemed an original, but all counterparts together constitute one and the same instrument.
- 8.8 Termination of Prior Agreement. Rockford and Executive are parties to a Change of Control Agreement covering substantially the same subject matter as this Agreement and dated the date indicated on the signature page (the "Prior Agreement"). This Agreement is intended to supercede the Prior Agreement and the parties agree that the Prior Agreement is terminated in all respects.

[Remainder of Page Intentionally Left Blank]

9 **Execution and Effective Date** . This Agreement is executed and effective on _____, 2007.

Rockford Corporation, an Arizona corporation

By _____
President

Address: 600 S. Rockford Dr.
Tempe, AZ 85281
Phone: (480) 967 - 3565
Fax: (480) ___ - ___

Executive

Signature

Printed Name

Address: _____

Phone: (480) ___ - ___

Fax: (480) ___ - ___

Title: _____

Salary Multiple under Section 2.2: _____

Other agreements and documents relating to Executive's employment:

- Employee Agreement (relating to Invention ownership and disclosure), signed on _____, ____.
- Offer Letter signed on _____, ____.

Date of Prior Change of Control Agreement (terminated by this Agreement): _____, 20__.

SUBSIDIARIES

- MB Quart Shanghai, Inc., an Arizona corporation
- Rockford Foreign Sales Corporation, a Barbados corporation
- Rockford Sales.Com, Inc., an Arizona corporation
- Rockford Singapore Corporation, an Arizona corporation

Consent of Independent Registered Public Accounting Firm

We consent to the incorporation by reference in the Registration Statements (Forms S-8 Nos. 333-48076, 333-101010 and 333-134164) pertaining to Rockford's Stock Option Plans and in the Registration Statement (Form S-3 No. 333-117315) of Rockford Corporation of our report dated March 12, 2008, with respect to the consolidated financial statements of Rockford Corporation included in this Annual Report (Form 10-K) for the year ended December 31, 2007.

/s/ Ernst & Young LLP

Phoenix, Arizona
March 12, 2008

CERTIFICATION PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, William R. Jackson, certify that:

1. I have reviewed this annual report on Form 10-K of Rockford Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report, except to the extent affected by the material weaknesses disclosed in Item 9A of this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under the Company's supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under the Company's supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report the Company's conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on the Company's most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ William R. Jackson

William R. Jackson
President
Principal Executive Officer

Date: March 12, 2008

CERTIFICATION PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Richard G. Vasek, certify that:

1. I have reviewed this annual report on Form 10-K of Rockford Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report, except to the extent affected by the material weaknesses disclosed in Item 9A of this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under the Company's supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under the Company's supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report the Company's conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on the Company's most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ Richard G. Vasek

 Richard G. Vasek
 Chief Financial Officer
 Principal Financial Officer

Date: March 12, 2008

**Certification of Periodic Financial
Report Pursuant to 18 U.S.C. Section 1350**

Pursuant to 18 U.S.C. Section 1350, as adopted in Section 906 of the Sarbanes-Oxley Act of 2002, William R. Jackson, Rockford's President, and Richard G. Vasek, Rockford's Chief Financial Officer, each certifies with respect to Rockford Corporation's Annual Report on Form 10-K for the year ended December 31, 2007, that:

- the report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- information contained in the report fairly presents, in all material respects, Rockford's financial condition and results of operations.

Date: March 12, 2008

/s/ William R. Jackson
William R. Jackson
President

Date: March 12, 2008

/s/ Richard G. Vasek
Richard G. Vasek
Chief Financial Officer