



FORM 10-Q

COMARCO INC - CMRO

Filed: December 12, 2008 (period: October 31, 2008)

Quarterly report which provides a continuing view of a company's financial position

Table of Contents

[10-Q - FORM 10-Q \(FOR THE QUARTERLY PERIOD ENDED OCTOBER 31, 2008\)](#)

[PART I](#)

- [ITEM 1.](#) [FINANCIAL STATEMENTS \(Unaudited\)](#)
- [ITEM 1.](#) [FINANCIAL STATEMENTS](#)
- [ITEM 2.](#) [MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL
CONDITION AND RESULTS OF OPERATIONS](#)
- [ITEM 3.](#) [QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT
MARKET RISK](#)
- [ITEM 4.](#) [CONTROLS AND PROCEDURES](#)

[PART II](#)

- [ITEM 1.](#) [LEGAL PROCEEDINGS](#)
 - [ITEM 2.](#) [UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF
PROCEEDS](#)
 - [ITEM 3.](#) [DEFAULTS UPON SENIOR SECURITIES](#)
 - [ITEM 4.](#) [SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS](#)
 - [ITEM 5.](#) [OTHER INFORMATION](#)
 - [ITEM 6.](#) [EXHIBITS](#)
- [SIGNATURES](#)
- [EXHIBIT INDEX](#)
- [EX-10.2 \(2005 EQUITY INCENTIVE PLAN\)](#)
-
- [EX-31.1 \(PRINCIPAL EXECUTIVE OFFICER CERTIFICATION PURSUANT TO
SECTION 302\)](#)
- [EX-31.2 \(PRINCIPAL FINANCIAL OFFICER CERTIFICATION PURSUANT TO
SECTION 302\)](#)
- [EX-32.1 \(PRINCIPAL EXECUTIVE OFFICER CERTIFICATION PURSUANT TO
SECTION 906\)](#)
- [EX-32.2 \(PRINCIPAL FINANCIAL OFFICER CERTIFICATION PURSUANT TO
SECTION 906\)](#)

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

FORM 10-Q

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

For the quarterly period ended

OCTOBER 31, 2008

OR

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

For the transition period from _____ to _____

Commission file number 0-5449

COMARCO, INC.
(Exact name of registrant as specified in its charter)

California
(State or other jurisdiction of
incorporation or organization)

95-2088894
(I.R.S. Employer
Identification No.)

25541 Commercentre Drive, Lake Forest, California 92630
(Address of principal executive offices and zip code)

(949) 599-7400
(Registrant's telephone number, including area code)

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

Yes No

Indicate by check mark whether the registrant 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.

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

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

Yes No

The registrant had 7,326,671 shares of common stock outstanding as of December 5, 2008.

COMARCO, INC. AND SUBSIDIARIES
QUARTERLY REPORT ON FORM 10-Q
FOR THE THREE AND NINE MONTHS ENDED OCTOBER 31, 2008
TABLE OF CONTENTS

	<u>Page</u>
PART I — FINANCIAL INFORMATION	
ITEM 1. FINANCIAL STATEMENTS (Unaudited)	
Condensed Consolidated Balance Sheets as of October 31, 2008 and January 31, 2008	3
Condensed Consolidated Statements of Operations for the Three and Nine Months Ended October 31, 2008 and 2007	4
Condensed Consolidated Statements of Cash Flows for the Nine Months Ended October 31, 2008 and 2007	5
Notes to Condensed Consolidated Financial Statements	6
ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS	20
ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK	35
ITEM 4. CONTROLS AND PROCEDURES	36
PART II — OTHER INFORMATION	
ITEM 1. LEGAL PROCEEDINGS	37
ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS	37
ITEM 3. DEFAULTS UPON SENIOR SECURITIES	38
ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS	38
ITEM 5. OTHER INFORMATION	38
ITEM 6. EXHIBITS	38
SIGNATURES	39

PART I — FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

COMARCO, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)
(In thousands, except share amounts)

	October 31, 2008	January 31, 2008 (A)
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 7,607	\$ 17,011
Short-term investments	—	336
Accounts receivable, net of reserves of \$49 and \$43	4,222	2,979
Inventory, net of reserves of \$671 and \$577	4,793	2,659
Current assets of discontinued operations	—	3,572
Other current assets	776	718
Total current assets	17,398	27,275
Property and equipment, net	2,058	2,572
Software development costs, net	688	—
Acquired intangible assets, net	408	525
Goodwill	1,898	1,898
Restricted cash	250	250
Non-current assets of discontinued operations	—	28
Other assets	4	33
Total assets	\$ 22,704	\$ 32,581
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	\$ 1,231	\$ 803
Deferred revenue	1,843	1,776
Deferred compensation	—	336
Current liabilities of discontinued operations	—	1,366
Accrued liabilities	4,741	5,271
Total current liabilities	7,815	9,552
Tax liability: FIN 48	86	86
Deferred rent	419	573
Non-current liabilities of discontinued operations	—	3
Deferred revenue, net of current portion	1,026	1,552
Total liabilities	9,346	11,766
Commitments, Contingencies, and Subsequent Events		
Stockholders' Equity:		
Preferred stock, no par value, 10,000,000 shares authorized; no shares issued or outstanding at October 31, 2008 and January 31, 2008, respectively	—	—
Common stock, \$0.10 par value, 50,625,000 shares authorized; 7,326,671 shares issued and outstanding at October 31, 2008 and January 31, 2008, respectively	733	733
Additional paid-in capital	14,642	14,434
(Accumulated deficit) retained earnings	(2,017)	5,648
Total stockholders' equity	13,358	20,815
Total liabilities and stockholders' equity	\$ 22,704	\$ 32,581

(A) Derived from the audited consolidated financial statements as of January 31, 2008.

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

[Table of Contents](#)

COMARCO, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
(In thousands, except per share amounts)

	Three Months Ended		Nine Months Ended	
	October 31,		October 31,	
	2008	2007	2008	2007
Revenue	\$ 4,236	\$ 3,099	\$ 21,763	\$ 8,184
Cost of revenue	3,777	2,817	14,898	6,905
Gross profit	459	282	6,865	1,279
Selling, general, and administrative expenses	3,100	2,428	10,294	7,011
Engineering and support expenses	1,825	2,176	5,954	6,096
	4,925	4,604	16,248	13,107
Operating loss	(4,466)	(4,322)	(9,383)	(11,828)
Other income, net	25	207	105	699
Gain on sale of equipment, net	—	—	—	321
Gain on sale of investment in SwissQual, net	—	308	—	577
Loss from continuing operations before income taxes	(4,441)	(3,807)	(9,278)	(10,231)
Income tax benefit	32	815	632	1,818
Net loss from continuing operations	(4,409)	(2,992)	(8,646)	(8,413)
Income from discontinued operations, net of income taxes	50	411	981	1,996
Net loss	\$ (4,359)	\$ (2,581)	\$ (7,665)	\$ (6,417)
Basic and diluted income (loss) per share:				
Net loss from continuing operations	\$ (0.60)	\$ (0.41)	\$ (1.18)	\$ (1.14)
Net income from discontinued operations	0.01	0.06	0.13	0.27
	\$ (0.59)	\$ (0.35)	\$ (1.05)	\$ (0.87)
Weighted average common shares outstanding:				
Basic	7,327	7,327	7,327	7,342
Diluted	7,327	7,327	7,327	7,342
Common shares outstanding	7,327	7,327	7,327	7,327

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

[Table of Contents](#)

COMARCO, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(In thousands)

	Nine Months Ended October 31,	
	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss from continuing operations	\$ (8,646)	\$ (8,413)
Adjustments to reconcile net loss from continuing operations to net cash used in operating activities:		
Depreciation and amortization	1,246	1,634
Loss (gain) on sale/retirement of property and equipment	25	(298)
Gain on sale of investment in SwissQual, net	—	(577)
Stock based compensation expense	208	427
Deferred income taxes	—	(483)
Provision for doubtful accounts receivable	15	6
Provision for obsolete inventory	35	79
Changes in operating assets and liabilities:		
Accounts receivable	(1,258)	4,575
Inventory	(2,169)	151
Other assets	(29)	(578)
Accounts payable	428	(209)
Deferred revenue	(459)	(698)
Deferred rent	(154)	(142)
Accrued liabilities	(530)	(1,673)
Net cash used in continuing operating activities	(11,288)	(6,199)
Net cash provided by discontinued operating activities	3,212	5,149
Net cash used in operating activities	(8,076)	(1,050)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sales of property and equipment	3	361
Purchases of property and equipment	(561)	(409)
Acquired intangible assets	(82)	—
Software development costs	(688)	—
Proceeds from sale of investment in SwissQual, net	—	577
Net cash provided by (used in) continuing investing activities	(1,328)	529
Net cash used in discontinued investing activities	—	(3)
Net cash provided by (used in) investing activities	(1,328)	526
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net proceeds from issuance of common stock	—	84
Dividends paid	—	(7,371)
Purchase and retirement of common stock	—	(386)
Net cash used in financing activities	—	(7,673)
Net decrease in cash and cash equivalents	(9,404)	(8,197)
Cash and cash equivalents, beginning of period	17,011	26,360
Cash and cash equivalents, end of period	\$ 7,607	\$ 18,163
Supplemental disclosures of cash flow information:		
Cash paid for interest	\$ —	\$ 8
Cash paid for income taxes, net of refunds	\$ 18	\$ 724

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

COMARCO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

1. Organization

Comarco, Inc., through its subsidiary Comarco Wireless Technologies, Inc. (collectively, “we,” “Comarco,” or “the Company”), is a leading designer and manufacturer of external mobile power adapters used to power and charge notebook computers, mobile phones, BlackBerry® smartphones, iPods®, and other handheld devices. Comarco is also a provider of wireless test solutions for the wireless industry. Our operations consist solely of the operations of Comarco Wireless Technologies, Inc. (“CWT”), which was incorporated in the State of Delaware in September 1993. Comarco, Inc. is a California corporation whose common stock has been publicly traded since 1971 when it was spun-off from Genge Industries, Inc.

2. Summary of Significant Accounting Policies

Basis of Presentation:

The interim condensed consolidated financial statements of Comarco included herein have been prepared without audit in accordance with accounting principles generally accepted in the United States of America for interim information and with the instructions for Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. The Company believes that the disclosures are adequate to make the information presented not misleading when read in conjunction with the audited consolidated financial statements included in the Company’s annual report on Form 10-K for the year ended January 31, 2008. The unaudited, interim condensed financial information presented herein reflects all adjustments, consisting of normal recurring accruals and discontinued operations adjustments, which are, in the opinion of management, necessary for a fair presentation of the results for the interim periods presented. The results for the three and nine months ended October 31, 2008 are not necessarily indicative of the results to be expected for the fiscal year ending January 31, 2009.

Principles of Consolidation:

The unaudited interim condensed consolidated financial statements of the Company include the accounts of Comarco, Inc. and CWT. All material intercompany balances, transactions, and profits and losses have been eliminated.

Use of Estimates:

The preparation of unaudited interim condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the unaudited interim condensed consolidated financial statements, and the reported amounts of revenue and expenses during the period reported. Actual results could materially differ from those estimates.

Certain accounting principles require subjective and complex judgments to be used in the preparation of financial statements. Accordingly, a different financial presentation could result depending on the judgments, estimates, or assumptions that are used. Such estimates and assumptions include, but are not specifically limited to, those required in the valuation of long-lived assets, revenue recognition, allowance for doubtful accounts, capitalization and amortization of software development costs, reserves for inventory obsolescence, valuation allowances for deferred tax assets, and determination of stock based compensation.

Reclassifications:

Certain prior period balances have been reclassified to conform to the current period presentation.

COMARCO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

3. Discontinued Operations

On July 10, 2008, the Company executed an asset purchase agreement to sell the assets of its call box business for \$2.7 million in cash. The transaction closed on July 10, 2008 and accordingly, the Company recorded a pre-tax gain on the sale in the amount of \$382,000 during the second quarter. In accordance with the provisions of Statement of Financial Accounting Standard ("SFAS") No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," the results of the call box business are now presented as discontinued operations for all periods in the unaudited interim condensed consolidated financial statements.

During the third quarter of fiscal 2009, the Company recorded an additional pre-tax gain on the sale of the call box business of \$150,000 in conjunction with the execution of a subcontractor agreement that provides for a monthly cash payment of \$12,500 to the Company from the buyer of the call box business over a 12-month period. Offsetting the gain of \$150,000 in the third quarter were additional pre-tax expenses incurred relating to the sale of the business of approximately \$68,000.

Operating results of the discontinued operations are as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	October 31,		October 31,	
	2008	2007	2008	2007
Revenues	\$ —	\$ 1,915	\$ 3,680	\$ 8,165
Income from discontinued operations:				
Gain on sale, net of taxes of \$32,000 and \$182,000	\$ 50	\$ —	\$ 282	\$ —
Income from discontinued operations, before taxes	—	666	1,149	3,287
Income tax expense	—	(255)	(450)	(1,291)
Total income from discontinued operations	\$ 50	\$ 411	\$ 981	\$ 1,996

Income from discontinued operations consists of direct revenues and direct expenses of the call box business, including cost of revenues, as well as other fixed and allocated costs to the extent that such costs will be eliminated as a result of the transaction. The Company historically allocated certain fixed manufacturing costs, indirect engineering costs, and corporate overhead based upon analysis of actual percentage shares of Company costs and expenses to each of its three businesses. The two remaining businesses, ChargeSource and WTS, now reflect allocations of the amounts previously allocated to the call box business segment.

COMARCO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

Assets and liabilities related to discontinued operations at January 31, 2008 consisted of the following (in thousands):

	January 31, 2008
Assets:	
Accounts receivable, net	\$ 1,749
Inventory, net	1,807
Other current assets	16
Current assets of discontinued operations	3,572
Property and equipment, net	14
Other assets	14
Assets of discontinued operations	\$ 3,600
Liabilities:	
Accounts payable	\$ 487
Deferred revenue	445
Accrued liabilities	434
Total current liabilities	1,366
Deferred revenue, net of current portion	3
Liabilities of discontinued operations	\$ 1,369

4. Stock-Based Compensation

The Company grants stock options for a fixed number of shares to employees with an exercise price equal to the fair value of the shares at the date of grant.

As of February 1, 2006, the Company adopted SFAS No. 123R, "Share-Based Payment" ("SFAS 123R"), using the modified prospective method, which requires measurement of compensation cost for all stock awards at fair value on date of grant and recognition of compensation over the service period for awards expected to vest. The fair value of stock options is determined using the Black-Scholes valuation model, which is consistent with the Company's valuation techniques previously utilized for options in footnote disclosures required under SFAS 123, and requires the input of subjective assumptions. These assumptions include estimating the length of time employees will retain their vested stock options before exercising them (the "expected term"), the estimated volatility of our common stock price over the expected term, and the number of options that will ultimately not complete their vesting requirements ("forfeitures"). Changes in these subjective assumptions can materially affect the estimate of fair value of stock-based compensation and, consequently, the related amount recognized as an expense on the consolidated statements of operations. As required under the accounting rules, the Company reviews its valuation assumptions at each grant date and, as a result, is likely to change its valuation assumptions used to value employee stock-based awards granted in future periods. The values derived from using the Black-Scholes model are recognized as expense over the vesting period, net of estimated forfeitures. The estimation of stock awards that will ultimately vest requires significant judgment. Actual results, and future changes in estimates, may materially differ from the Company's current estimates.

COMARCO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

The compensation expense recognized under SFAS 123R is summarized in the table below (in thousands except per share amounts):

	<u>Three Months Ended</u> <u>October 31,</u>		<u>Nine Months Ended</u> <u>October 31,</u>	
	<u>2008</u>	<u>2007</u>	<u>2008</u>	<u>2007</u>
Compensation expense relating to SFAS 123R	\$ 16	\$ 167	\$ 208	\$ 427
Impact on diluted earnings per share	\$ (0.00)	\$ (0.02)	\$ (0.03)	\$ (0.06)

The total compensation cost related to nonvested awards not yet recognized is approximately \$504,000, which will be expensed over a weighted average remaining life of 16.6 months.

The fair value of options granted under the Company's stock option plans during the nine months ended October 31, 2008 and 2007 was estimated on the date of grant using the Black-Scholes option-pricing model utilizing the following weighted average assumptions:

	<u>Nine Months Ended</u> <u>October 31,</u>	
	<u>2008</u>	<u>2007</u>
Weighted average risk-free interest rate	3.0%	4.8%
Expected life (in years)	5.9	5.8
Expected stock volatility	38.1%	40.1%
Dividend yield	None	None
Expected forfeitures	8.2%	10.6%

Comarco, Inc. has stock-based compensation plans under which outside directors and certain employees receive stock options. The employee stock option plans and a director stock option plan provide that officers, key employees, and directors may be granted options to purchase shares of common stock of the Company at not less than 100 percent of the fair market value at the date of grant, unless the optionee is a 10 percent shareholder of the Company, in which case the price must not be less than 110 percent of the fair market value. The total number of shares that may be granted under these plans is 3,354,337.

The Company's Director Stock Option Plan (the "Director Plan") expires in December 2010, and the Company's former employee stock option plan (the "Employee Plan") expired during May 2005. During December 2005, the Board of Directors approved and adopted a new equity incentive plan (the "2005 Plan") covering 450,000 shares of our common stock. The 2005 Plan was approved by the Company's shareholders at its annual shareholders' meeting in June 2006, and subsequently amended at its annual shareholders' meeting in June 2008 to increase the number of shares issuable under the plan from 450,000 shares to 1,100,000 shares. Under the 2005 Plan, the Company may grant stock options, stock appreciation rights, restricted stock, restricted stock units, and performance based awards. Under all plans, the options are exercisable in installments determined by the compensation committee of the Company's Board of Directors unless vesting occurs based on achievement of performance measures, as defined. The options of the Director Plan and the Employee Plan expire as determined by the Compensation Committee, but no later than ten years and one week after the date of grant (five years for 10 percent shareholders). The options of the 2005 Plan expire as determined by the Compensation Committee, but no later than ten years after the date of grant (five years for 10 percent shareholders).

[Table of Contents](#)

COMARCO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

Transactions and other information related to these plans for the nine months ended October 31, 2008 are summarized below:

	Outstanding Options	
	Number of Shares	Weighted-Average Exercise Price
Balance, January 31, 2008	842,000	\$ 11.59
Options granted	45,000	4.57
Options canceled or expired	(471,500)	12.02
Options exercised	—	—
Balance, October 31, 2008	<u>415,500</u>	<u>\$ 10.33</u>

The average fair value of each of the options granted during the nine months ended October 31, 2008 was \$1.88. As of October 31, 2008, the stock options outstanding have no intrinsic value, based on a closing market price of \$1.15 per share on October 31, 2008. The following table summarizes information about the Company's stock options outstanding at October 31, 2008:

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Number Outstanding	Weighted-Avg. Remaining Contractual Life	Weighted-Avg. Exercise Price	Number Exercisable	Weighted-Avg. Exercise Price
\$3.91 to 9.89	257,500	5.74	\$ 7.15	179,750	\$ 7.69
10.43 to 12.41	72,000	6.35	10.77	57,000	10.86
13.21 to 17.50	30,500	2.00	14.77	30,500	14.77
19.33 to 23.67	55,500	1.55	22.08	55,500	22.08
	<u>415,500</u>	5.02 years	10.33	<u>322,750</u>	11.39

Stock options exercisable at October 31, 2008 were 322,750 at a weighted-average exercise price of \$11.39. At October 31, 2008, shares available for future grants under the 2005 Plan were 939,500 and under the Director Plan were 625.

On November 12, 2008, the Board of Directors granted 750,000 stock options under the 2005 Plan to certain employees at an exercise price of \$1.09 per share (see Note 16).

As of October 31, 2008, CWT also had a subsidiary stock option plan. Under this plan, officers and key employees of CWT could have been granted options to purchase up to 600,000 shares of common stock of CWT at not less than 100 percent of the fair market value at the date of grant.

As of October 31, 2008, the Company owned all of the 3,353,000 outstanding shares of CWT common stock. During the three and nine months ended October 31, 2008, no options were granted or exercised under the CWT option plan. Although the plan had 198,000 shares available for future grant at October 31, 2008, no options were outstanding under this plan. Subsequent to October 31, 2008, the Company's Board of Directors took action to terminate the CWT stock option plan.

5. Recent Accounting Pronouncements

In March 2008, the Financial Accounting Standards Board ("FASB") issued SFAS No. 161, "Disclosures about Derivative Instruments and Hedging Activities – An Amendment of SFAS No. 133" ("SFAS No. 161"). SFAS No. 161 seeks to improve financial reporting for derivative instruments and hedging activities by requiring enhanced disclosures regarding their impact on financial position, financial performance, and cash flows. To achieve this increased transparency, SFAS No. 161 requires (1) the disclosure of the fair value of derivative instruments and

COMARCO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

gains and losses in a tabular format; (2) the disclosure of derivative features that are credit risk-related; and (3) cross-referencing within the footnotes. SFAS No. 161 is effective prospectively for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early application permitted. The Company is in the process of evaluating the new disclosure requirements under SFAS No. 161, but does not expect adoption of SFAS No. 161 to have an impact on its consolidated financial statements.

In May 2008, the FASB issued SFAS No. 162, "The Hierarchy of Generally Accepted Accounting Principles." This Statement identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of nongovernmental entities that are presented in conformity with U.S. GAAP (the GAAP hierarchy). This Statement will not have a material effect on the Company's consolidated results of operations or financial position.

6. Stockholders' Equity

During 1992, the Company's Board of Directors authorized a stock repurchase program of up to 3.0 million shares of the Company's common stock. From program inception through October 31, 2008, the Company repurchased approximately 2.7 million shares for an average price of \$8.20 per share. During the three and nine months ended October 31, 2008, the Company did not repurchase any shares of common stock. During the three months ended October 31, 2007, the Company did not repurchase any shares of common stock. During the nine months ended October 31, 2007, the Company repurchased 57,637 shares of common stock at an average price of \$6.70 per share.

7. Earnings (Loss) Per Share

The Company calculates net earnings (loss) per share by dividing net income (loss) by the weighted-average number of common shares outstanding during the reporting period. Diluted earnings (loss) per share reflects the effects of potentially dilutive securities. Since the Company incurred a net loss for the three and nine months ended October 31, 2008 and 2007, basic and diluted loss per share were the same because the inclusion of potential common shares related to outstanding stock options in the calculation would have been antidilutive.

Potential common shares of 0 and 1,366 have been excluded from diluted weighted average common shares for the three and nine months ended October 31, 2007, as the effect would have been antidilutive. There were no potentially dilutive common shares related to outstanding stock options for the three and nine months ended October 31, 2008.

The following table presents reconciliations of the numerators and denominators of the basic and diluted earnings (loss) per share computations for net income (loss). In the tables below, "Net income or loss" represents the numerator and "Shares" represents the denominator (in thousands, except per share amounts):

[Table of Contents](#)

COMARCO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

	Three Months Ended		Nine Months Ended	
	October 31,		October 31,	
	2008	2007	2008	2007
Basic and diluted:				
Net loss from continuing operations	\$ (4,409)	\$ (2,992)	\$ (8,646)	\$ (8,413)
Weighted average shares outstanding	<u>7,327</u>	<u>7,327</u>	<u>7,327</u>	<u>7,342</u>
Basic and diluted loss per share from continuing operations	<u>\$ (0.60)</u>	<u>\$ (0.41)</u>	<u>\$ (1.18)</u>	<u>\$ (1.14)</u>
Net income from discontinued operations	\$ 50	\$ 411	\$ 981	\$ 1,996
Weighted average shares outstanding	<u>7,327</u>	<u>7,327</u>	<u>7,327</u>	<u>7,342</u>
Basic and diluted earnings per share from discontinued operations	<u>\$ 0.01</u>	<u>\$ 0.06</u>	<u>\$ 0.13</u>	<u>\$ 0.27</u>
Net loss	\$ (4,359)	\$ (2,581)	\$ (7,665)	\$ (6,417)
Weighted average shares outstanding	<u>7,327</u>	<u>7,327</u>	<u>7,327</u>	<u>7,342</u>
Basic and diluted loss per share	<u>\$ (0.59)</u>	<u>\$ (0.35)</u>	<u>\$ (1.05)</u>	<u>\$ (0.87)</u>

8. Customer Concentrations

A significant portion of the Company's revenue is derived from a limited number of customers. The customers providing 10 percent or more of the Company's revenue for the periods presented below are listed here:

	Three Months Ended October 31,			
	2008	(In thousands)		2007
Total revenue	<u>\$4,236</u>	<u>100%</u>	<u>\$3,099</u>	<u>100%</u>
Customer concentration:				
Lenovo Information Products Co., Ltd.	2,521	60%	—	—
Trust International B.V.	521	12%	—	—
Kensington Technology Group	<u>125</u>	<u>3%</u>	<u>1,780</u>	<u>57%</u>
	<u>\$3,167</u>	<u>75%</u>	<u>\$1,780</u>	<u>57%</u>

[Table of Contents](#)

COMARCO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

	Nine Months Ended October 31,			
	2008		2007	
	(In thousands)			
Total revenue	\$21,763	100%	\$8,184	100%
Customer concentration:				
AT&T Wireless Services	8,577	39%	—	—
Verizon Wireless	969	5%	2,484	30%
Lenovo Information Products Co., Ltd.	8,447	39%	—	—
Kensington Technology Group	946	4%	2,431	30%
	<u>\$18,939</u>	<u>87%</u>	<u>\$4,915</u>	<u>60%</u>

The AT&T revenue amount reported above for the nine months ended October 31, 2008 is net of \$2.2 million in revenue sharing due to Ascom (Schwiez) AG (“Ascom”) and net of assessed sales tax and deferred revenue.

In November 2006, the Company entered into a development and sales agreement with Ascom whereby Ascom receives 30 percent to 40 percent of the revenue on jointly developed products, less associated hardware costs. During the first quarter of fiscal 2009, the Company sold the first jointly developed product, the Symphony™ Multi, to AT&T, and associated revenue sharing amounts have been paid to Ascom.

The Verizon Wireless revenue amounts reported above are net of \$38,000 and \$704,000 of revenue sharing amounts payable to SwissQual AG (“SwissQual”) for the nine months ended October 31, 2008 and 2007, respectively.

The customers comprising 10 percent or more of the Company’s gross accounts receivable at either October 31, 2008 or January 31, 2008 are listed below (in thousands):

	October 31,		January 31,	
	2008		2008	
Total gross accounts receivable	\$ 4,271	100%	\$ 3,022	100%
Customer concentration:				
Lenovo Information Products Co., Ltd.	2,614	61%	—	—
Trust International B.V.	521	12%	—	—
Kensington Technology Group	11	1%	1,209	40%
	<u>\$ 3,146</u>	<u>74%</u>	<u>\$ 1,209</u>	<u>40%</u>

9. Inventory

Inventory, net of reserves, consists of the following (in thousands):

	October 31,	January 31,
	2008	2008
Raw materials	\$ 2,872	\$ 2,018
Work in process	75	146
Finished goods	1,846	495
	<u>\$ 4,793</u>	<u>\$ 2,659</u>

COMARCO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

10. Software Development Costs, Net

Software development costs consist of the following (in thousands):

	October 31, 2008	January 31, 2008
Capitalized software development costs	\$ 688	\$ 8,444
Less: accumulated amortization	—	(8,444)
	<u>\$ 688</u>	<u>\$ —</u>

The Company capitalized software development costs in the amount of \$353,000 and \$688,000 during the three and nine months ended October 31, 2008, respectively. The Company did not capitalize software development costs during the comparable periods of the prior fiscal year. Amortization of software development costs for the nine months ended October 31, 2008 and 2007 totaled \$0 and \$224,000, respectively, and have been reported in cost of revenue in the accompanying unaudited interim condensed consolidated financial statements. Amortization of software development costs for the three months ended October 31, 2008 and 2007 totaled \$0 and \$20,000, respectively. During the first quarter of fiscal 2009, the Company retired fully amortized capitalized software development costs of \$8.4 million from its books. The engineering costs capitalized during fiscal 2009 relate to our WTS Opti product currently under development, and therefore the Company is uncertain when capitalization of costs will cease and amortization will begin. During the third quarter of fiscal 2009, the Company also began capitalizing software development related to our WTS QuOTA product upon completion of a working model.

11. Goodwill and Acquired Intangible Assets, Net

Goodwill and acquired intangible assets consist of the following (in thousands):

	October 31, 2008	January 31, 2008
Goodwill	<u>\$ 1,898</u>	<u>\$ 1,898</u>
Acquired intangible assets:		
Definite-lived intangible assets:		
License rights	\$ 82	\$ 1,440
Intellectual property rights	1,244	1,244
	1,326	2,684
Less: accumulated amortization	(918)	(2,159)
	<u>\$ 408</u>	<u>\$ 525</u>

During the first quarter of fiscal 2009, fully amortized license rights related to mobile phone technologies in the amount of \$1.4 million were retired.

The following table presents goodwill by reportable segment (in thousands):

	ChargeSource®	Wireless Test Solutions	Total
Balance as of October 31, 2008	<u>\$ —</u>	<u>\$ 1,898</u>	<u>\$ 1,898</u>
Balance as of January 31, 2008	<u>\$ —</u>	<u>\$ 1,898</u>	<u>\$ 1,898</u>

[Table of Contents](#)

COMARCO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

The following table presents the future expected amortization of the definite-lived intangible assets (in thousands):

	<u>Amortization Expense</u>
Fiscal year:	
2009	\$ 61
2010	178
2011	126
2012	43
Total estimated amortization expense	<u>\$ 408</u>

Amortization of definite-lived acquired intangible assets for the three months ended October 31, 2008 and 2007 totaled \$69,000 and \$66,000, respectively. For the nine months ended October 31, 2008 and 2007, amortization of definite-lived acquired intangible assets totaled \$198,000 and \$244,000, respectively. The Company ceased amortizing goodwill beginning February 1, 2002 upon adoption of SFAS No. 142, "Goodwill and Other Intangible Assets."

12. Warranty Arrangements

Standard Warranty

The Company records an accrual for estimated warranty costs as products are sold. Warranty costs are estimated based on periodic analysis of historical experience. Changes in the estimated warranty accruals are recorded when the change in estimate is identified. A summary of the standard warranty accrual activity is shown in the table below (in thousands):

	<u>Nine Months Ended October 31,</u>	
	<u>2008</u>	<u>2007</u>
Beginning balance	\$ 46	\$ 113
Accruals for warranties issued during the period	106	30
Utilization	(70)	(100)
	<u>\$ 82</u>	<u>\$ 43</u>

Embedded Post Contract Support and Warranty

The Company defers revenue relating to its WTS product sales for post contract support and warranty for the term of the maintenance commitment made at the time of the sale, generally one year. A summary of the post contract support and warranty activity is shown in the table below (in thousands):

	<u>Nine Months Ended October 31,</u>	
	<u>2008</u>	<u>2007</u>
Beginning balance	\$ 200	\$ 551
Deferral of revenue for new contracts	811	335
Recognition of revenue	(532)	(647)
	<u>\$ 479</u>	<u>\$ 239</u>

COMARCO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

Extended Post Contract Support and Warranty

Revenue for the Company's extended post contract support and warranty contracts is deferred and recognized on a straight line basis over the contract period, typically one to four years. Costs incurred under separately priced extended warranty arrangements are expensed as incurred. A summary of the extended post contract support and warranty activity is shown in the table below (in thousands):

	Nine Months Ended October 31,	
	2008	2007
Beginning balance	\$ 2,437	\$ 2,952
Deferral of revenue for new contracts	187	617
Recognition of revenue	(704)	(906)
	<u>\$ 1,920</u>	<u>\$ 2,663</u>

13. Supplemental Disclosures of Cash Flow Information and Noncash Investing and Financing Activities

In the first quarter of fiscal 2008, 16,125 stock options were exercised as net exercises and therefore no cash was received upon exercise. The number of shares of Company common stock issued as a result of these net exercises totaled 2,671.

14. Business Segment Information

The Company has two reportable operating segments: ChargeSource[®] and Wireless Test Solutions.

The ChargeSource[®] segment designs mobile power products for notebook computers, cellular telephones, PDAs, and other handheld devices.

The Wireless Test Solutions segment designs and manufactures hardware and software tools for use by wireless carriers, equipment vendors, and others. Radio frequency engineers, professional technicians, and others use these tools to design, deploy, and optimize wireless networks, and to verify the performance of the wireless networks once deployed.

Performance measurement and resource allocation for the reportable segments are based on many factors. The primary financial measures used are revenue and gross profit. The revenue, gross profit, gross margin, and total assets attributable to these segments are as follows (in thousands, except percentages):

	Three Months Ended October 31, 2008		
	ChargeSource [®]	Wireless Test Solutions	Total
Revenue	\$ 3,236	\$ 1,000	\$ 4,236
Cost of revenue	3,237	540	3,777
Gross profit (loss)	\$ (1)	\$ 460	\$ 459
Gross margin	0.0%	46.0%	10.8%

[Table of Contents](#)

COMARCO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

	Nine Months Ended October 31, 2008		
	ChargeSource®	Wireless Test Solutions	Total
Revenue	\$ 10,215	\$ 11,548	\$ 21,763
Cost of revenue	10,403	4,495	14,898
Gross profit (loss)	\$ (188)	\$ 7,053	\$ 6,865
Gross margin	(1.8%)	61.1%	31.5%

	Three Months Ended October 31, 2007		
	ChargeSource®	Wireless Test Solutions	Total
Revenue	\$ 1,893	\$ 1,206	\$ 3,099
Cost of revenue	2,153	664	2,817
Gross profit (loss)	\$ (260)	\$ 542	\$ 282
Gross margin	(13.7%)	44.9%	9.1%

	Nine Months Ended October 31, 2007		
	ChargeSource®	Wireless Test Solutions	Total
Revenue	\$ 2,980	\$ 5,204	\$ 8,184
Cost of revenue	4,009	2,896	6,905
Gross profit (loss)	\$ (1,029)	\$ 2,308	\$ 1,279
Gross margin	(34.5%)	44.3%	15.6%

	ChargeSource®	Wireless Test Solutions	Assets of Discontinued Operations	Corporate	Total
Assets at October 31, 2008	\$ 6,701	\$ 6,169	\$ —	\$ 9,834	\$ 22,704
Assets at January 31, 2008	\$ 2,972	\$ 6,292	\$ 3,600	\$ 19,717	\$ 32,581

The following table presents revenue by geographic region for the three and nine months ended October 31, 2008 and 2007 (in thousands):

Revenue by Region:

(in thousands)	Three Months Ended October 31,		Nine Months Ended October 31,	
	2008	2007	2008	2007
North America	\$ 958	\$ 2,017	\$ 11,115	\$ 5,539
Europe	696	604	1,505	1,218
Asia	2,531	210	8,787	552
Latin America	51	268	356	875
	<u>\$ 4,236</u>	<u>\$ 3,099</u>	<u>\$ 21,763</u>	<u>\$ 8,184</u>

COMARCO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

15. Commitments and Contingencies

Purchase Commitments with Suppliers

The Company generally issues purchase orders to its suppliers with delivery dates from four to six weeks from the purchase order date. In addition, the Company regularly provides significant suppliers with rolling six-month forecasts of material and finished goods requirements for planning and long-lead time parts procurement purposes only. The Company is committed to accepting delivery of materials pursuant to its purchase orders subject to various contract provisions that allow it to delay receipt of such order or allow it to cancel orders beyond certain agreed lead times. Such cancellations may or may not include cancellation costs payable by the Company. In the past, the Company has been required to take delivery of materials from its suppliers that were in excess of its requirements and the Company has previously recognized charges and expenses related to such excess material. If the Company is unable to adequately manage its suppliers and adjust such commitments for changes in demand, it may incur additional inventory expenses related to excess and obsolete inventory. Such expenses could have a material adverse effect on the Company's business, results of operations, and financial position.

Executive Severance Commitments

The Company has severance compensation agreements with several key executives. These agreements require the Company to pay these executives, in the event of a termination of employment following a change of control of the Company, the amount of their then current annual base salary and the amount of any bonus amount the executive would have achieved for the current year. The exact amount of this contingent obligation is not known and accordingly has not been recorded in the unaudited interim condensed consolidated financial statements. During the nine months ended October 31, 2008, severance of approximately \$1.0 million was incurred relating to the departure of three corporate officers. No severance accruals were made during the three months ended October 31, 2008.

Letter of Credit

In May 2006, the Company obtained a \$500,000 letter of credit from US Bank pursuant to a lease provision for the Company's corporate office, which was relocated in August 2006. In November 2007, the letter of credit was reduced to \$250,000 pursuant to the provisions of the lease. The letter of credit is secured by a certificate of deposit with a 6-month maturity, which is reflected as restricted cash on the condensed consolidated balance sheets.

Legal Contingencies

On June 8, 2007, iGo, Inc. (formerly Mobility Electronics, Inc.) ("iGo") filed a complaint against Comarco and its subsidiary CWT in the United States District Court for the Eastern District of Texas, Case No. 5:07cv84, alleging that two iGo patents are infringed by the mechanical keying arrangement between power adapters and programming tips used by the Company in its mobile power products sold through its distributors and sold to a computer maker. The complaint seeks an unspecified amount of treble damages and injunctive relief. The Company has denied liability and countersued alleging that iGo breached a settlement agreement (the "Settlement Agreement") entered into between the parties in 2003 settling a previous patent infringement lawsuit, and that iGo is liable for infringement of at least three of the Company's patents. iGo has denied liability and amended its claims to further allege that the Company breached the Settlement Agreement by asserting claims against iGo. The Company has denied liability as to the additional claim made by iGo. On March 5, 2008, both parties attended mediation without reaching a settlement.

On June 25, 2008, the parties jointly requested that the U.S. District Court for the Eastern District of Texas (the "Texas Court") transfer the lawsuit to the U.S. District Court for the District of Arizona, the court in which the parties' previous patent infringement lawsuit had been filed (the "Arizona Court"). The parties' joint request also sought, following transfer, a stay of proceedings until January 2009 so that the parties could pursue settlement. On June 30, 2008, the Texas Court granted the parties' joint request for transfer, transferring the lawsuit to the Arizona Court under the terms and conditions requested, including the stay, Action No. CV 08-1224-PHX-MHM.

COMARCO, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

On November 30, 2007, SwissQual filed a lawsuit against CWT in the United States District Court for the Central District of California, Case No. cv-07-07819, alleging fraud, intentional interference with prospective economic advantage, breach of contract, trademark infringement, unfair competition, trade secret misappropriation, and seeking declaratory relief relating to the Distribution and Sales Agreement dated December 15, 2005 between the parties.

The Company answered SwissQual's complaint and denied any and all liability. In addition, the Company asserted counterclaims against SwissQual alleging breach of contract, breach of the covenant of good faith and fair dealing, trade secret misappropriation, intentional interference with prospective economic advantage, negligent interference with prospective economic advantage, unfair competition, conversion, unjust enrichment/restitution, an accounting for money owed due to SwissQual's misconduct and seeking declaratory relief relating to SwissQual's failure to comply with its support obligations, indemnity, and trademark ownership.

On November 26, 2008, the Company entered into a Settlement Agreement and Release of Claims (the "Settlement Agreement") with SwissQual pursuant to which the parties agreed to dismiss their respective claims and counterclaims against each other. Among other terms, the Settlement Agreement contains general releases between the parties. As a result, this lawsuit has been dismissed with prejudice.

The outcome of the iGo matter remains neither determinable nor estimable. The Company believes it has meritorious defenses to the matter described above and intends to vigorously defend this action. In addition to the pending matter described above, the Company is from time to time involved in various legal proceedings incidental to the conduct of its business. The Company believes that the outcome of all such legal proceedings will not in the aggregate have a material adverse effect on its consolidated results of operations and financial position.

16. Subsequent Events

As previously announced, the Company entered into an Asset Purchase Agreement on September 26, 2008 with Ascom Holding AG and its subsidiary Ascom Inc. to sell the WTS business and related assets. Comarco's shareholders approved the transaction on November 26, 2008 with approximately 85 percent of the Company's shareholders voting in favor of the transaction. The transaction is expected to close on January 5, 2009, following the satisfaction or waiver of the remaining closing conditions to the obligations of the parties to the Asset Purchase Agreement.

The aggregate purchase price to be paid to Comarco in connection with the transaction is \$12,750,000 in cash, with \$1,775,000 of the proceeds expected to be placed in escrow. Of the amounts placed in escrow, \$1,275,000 will be held for one year from the closing date as security for general indemnification rights and \$500,000 will be held for two years from the date of close as security for excluded liabilities.

On November 12, 2008, the Company's Board of Directors granted 750,000 stock options under the 2005 Plan, as amended, to certain employees at an exercise price of \$1.09 per share. The options granted have 60 percent vesting ratably over the first four anniversaries of the grant date and 40 percent vesting when the daily close price of Comarco's stock is \$5.00 or greater for 90 consecutive days, if at all.

In November 2008, the Company's Board of Directors executed Unanimous Written Consents to terminate the CWT Stock Option Plan and the Comarco, Inc. Deferred Compensation Plan.

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

The following discussion and analysis should be read in conjunction with our unaudited interim condensed consolidated financial statements and the related notes and other financial information appearing elsewhere in this quarterly report on Form 10-Q.

Forward-Looking Statements

This report, including the following discussion and analysis, contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Words such as “expects,” “anticipates,” “intends,” “plans,” “believes,” “seeks,” and “estimates,” and similar expressions or variations of such words are intended to identify forward-looking statements, but are not deemed to represent an all-inclusive means of identifying forward-looking statements included in this report. Additionally, statements concerning future matters are forward-looking statements.

These forward-looking statements reflect current views about our plans, strategies, and prospects, but can only be based on facts and factors currently known by us. Consequently, forward-looking statements are inherently subject to risks and uncertainties, and actual results and outcomes may differ materially from the results and outcomes discussed in or anticipated by the forward-looking statements.

Forward-looking statements in this report include those related to our objectives; our products and the availability of future products; our sales, revenues, and costs; the timing of fulfillment of purchase orders and completion of projects; demand for our products; the sufficiency of our cash and cash equivalent balances; our ability to obtain debt or equity financing; and the anticipated closing of the sale of substantially all of our wireless test solutions (“WTS”) assets, including the timing thereof, and the estimated net proceeds from such anticipated transaction. Many important factors may cause the Company’s actual results to differ materially from those discussed in any such forward-looking statements, including but not limited to the effects of consolidation in the wireless communications industry; the current economic slowdown which adversely impacts our customers’ demand for our products and services and the difficulty of accurately estimating demand; our reliance on a limited number of customers for a significant portion of our revenue; increased competition; fluctuation in demand for our products; our ability to develop and introduce new products successfully; the risk of third parties infringing our intellectual property; difficulties and delays associated with our efforts to obtain cost reductions and to reduce the time to market for our ChargeSource products; general economic, political, and market conditions; risks associated with the volatility and uncertainty in the capital markets that may adversely impact our results of operations and our ability to raise additional capital; the risk that the proposed sale of WTS assets may fail to close for any reason, including the failure to satisfy the remaining closing conditions, and that actual taxes and transaction costs and fees may exceed our estimates; and litigation. Although we believe that the assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate and, therefore, we cannot assure that the results contemplated in forward-looking statements will be realized in the timeframe anticipated or at all. In light of the significant uncertainties inherent in the forward-looking information included herein, the inclusion of such information should not be regarded as a representation by us or any other person that our objectives or plans will be achieved. Accordingly, investors are cautioned not to place undue reliance on our forward-looking statements. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law.

In addition to the risks, uncertainties, and other factors discussed elsewhere in this Form 10-Q, the risks, uncertainties, and other factors that could cause or contribute to actual results differing materially from those expressed or implied in any forward-looking statements include, without limitation, those set forth under Part I, Item 1A “Risk Factors” in the Company’s Annual Report on Form 10-K for the fiscal year ended January 31, 2008 filed with the SEC, those contained in the Company’s other filings with the SEC, and those set forth above. For these forward-looking statements, we claim the protection of the safe harbor for forward-looking statements in Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934.

[Table of Contents](#)

Basis of Presentation

The financial information presented in this report is not audited and is not necessarily indicative of our future consolidated financial position, results of operations, or cash flow. Our fiscal year ends on January 31 and our fiscal quarters end on April 30, July 31, and October 31. Unless otherwise stated, all dates refer to our fiscal year and fiscal periods.

Executive Summary

Comarco, Inc., through its subsidiary Comarco Wireless Technologies, Inc. (collectively, “we,” “Comarco,” or the “Company”), is a leading designer and manufacturer of external mobile power adapters used to power and charge notebook computers, mobile phones, BlackBerry® smartphones, iPods®, and other handheld devices. Comarco is also a provider of wireless test solutions for the wireless industry. Our operations consist solely of the operations of Comarco Wireless Technologies, Inc. (“CWT”).

Our revenue and related cash flows are primarily derived from sales of our ChargeSource® products and wireless test solutions (“WTS”) products. We have two reportable segments: ChargeSource® and WTS. Performance measurement and resource allocation for the reportable segments are based on many factors and the primary financial measures utilized are revenue and gross profit. See “Business Segment Information” in Note 14 of the Notes to Condensed Consolidated Financial Statements included in Part I, Item 1 of this report.

The following table sets forth our revenue for the business segments for the three and nine months ended October 31, 2008 and 2007:

	Three Months Ended October 31,			Nine Months Ended October 31,		
	2008 (in thousands)	2007 (in thousands)	% Change	2008 (in thousands)	2007 (in thousands)	% Change
Revenue:						
ChargeSource®	\$ 3,236	\$ 1,893	71%	\$ 10,215	\$ 2,980	243%
WTS	<u>1,000</u>	<u>1,206</u>	(17%)	<u>11,548</u>	<u>5,204</u>	122%
	<u>\$ 4,236</u>	<u>\$ 3,099</u>	37%	<u>\$ 21,763</u>	<u>\$ 8,184</u>	166%

Management currently considers the following events, trends, and uncertainties to be important to understanding our two business segments and corresponding operating results for the three and nine months ended October 31, 2008.

ChargeSource®

- During the first quarter of fiscal 2008, we entered into a non-exclusive distribution arrangement with Kensington Technology Group (“Kensington”), thereby terminating our exclusive distribution agreement. Under the non-exclusive agreement, we have the right to penetrate all channels with multiple partners and Kensington has the right to purchase our products without volume minimums. Kensington is also able to purchase mobile power products from our competitors.
- In late January 2008, we began volume production of a small form factor 90-watt alternating current/direct current (“AC/DC”) external power adapter designed to the stringent specifications of Lenovo, a leading notebook computer original equipment manufacturer (“OEM”) headquartered in Beijing, China. This product is currently being marketed and sold as an OEM-branded aftermarket accessory.
- During the first quarter of fiscal 2009, we entered into an additional non-exclusive distribution agreement with Trust International B.V. (“Trust”) for our ChargeSource® products. We began

Table of Contents

shipping to Trust during the third quarter of fiscal 2009 and recorded revenue of \$0.5 million during the third quarter as a result of such sales.

- ChargeSource[®] revenue for the third quarter of fiscal 2009 increased to \$3.2 million compared to \$1.9 million for the third quarter of fiscal 2008. ChargeSource[®] revenue for the nine months ended October 31, 2008 increased to \$10.2 million compared to \$3.0 million for the comparable prior fiscal year period. Sequentially, for the second and third quarters of fiscal 2009, ChargeSource[®] revenue remained flat.
- The current level of ChargeSource[®] sales is insufficient to fully absorb our fixed manufacturing and supply chain overhead. We believe that our ability to drive increased sales is dependent upon, among others, the following factors:
 - Successful development and release for manufacture of certain AC and AC/DC external power adapter products designed to address the requirements of our retail and OEM accessories channels;
 - Securing additional OEM customers and retail distribution partners under non-exclusive arrangements;
 - Market and customer acceptance of our new products expected to be available by early fiscal 2010;
 - Successfully executing our cost reduction initiatives, which include reducing our component costs; and
 - Reducing manufacturing lead-time from demand to delivery.
- Our ChargeSource[®] products are based on proprietary patented construction technology that enables the production of slim and light power sources which can charge low power and high power mobile devices simultaneously from standard wall outlets, as well as power outlets in airplanes, cars, and other modes of transportation. Our new power adapter designed for the retail market was made available in the third quarter of fiscal 2009, and we shipped our first units of these new adapters to Trust.

Wireless Test Solutions

- During fiscal 2007, we entered into a cooperative alliance with Ascom (Schweiz) AG (“Ascom”), a leading specialist in wireless onsite communications solutions based in Switzerland, to develop, market, and support next-generation wireless network QoS, optimization, and test measurement systems. Together we have developed harmonized test and measurement systems and solutions for 3G and 4G wireless standards. These harmonized products and solutions are now available to the worldwide marketplace.
- Late in the fourth quarter of fiscal 2008, we received a purchase order from AT&T valued at approximately \$10.1 million for the Symphony™ Multi system, jointly developed by Ascom and Comarco. We began delivery on this order during the first quarter of fiscal 2009, and completed delivery during the second quarter of fiscal 2009. We generated revenue during the first half of fiscal 2009 relating to this order of \$8.2 million, net of revenue sharing payable to Ascom of \$1.9 million. This excludes amounts deferred relating to post-contract support and warranty. Since receiving this original order from AT&T, we have continued to receive and deliver on additional purchase orders for single systems.
- Demand for our next-generation mobile test equipment remains unpredictable. Although we are encouraged by interest we have received for the Symphony™ Multi system, the timing and amount of anticipated orders from our customer base remains uncertain. WTS revenue for the nine months ended October 31, 2008 increased \$6.3 million compared to the comparable period of the prior fiscal year due to the deliveries on the AT&T order during the first six months of fiscal 2009 discussed above. Revenue for the three months ended October 31, 2008 decreased \$0.2 million from the comparable period of the prior year, reflective of the current economic downturn and the unpredictable demand in

Table of Contents

this market. We expect our ability to compete on a global basis to be driven by our ability to offer products that cover all current wireless technologies, as well as the timely integration of new technology and functionality into our product platform.

- On September 26, 2008, we entered into an Asset Purchase Agreement to sell substantially all of our WTS assets to Ascom for a cash payment of \$12,750,000, with \$1,775,000 of the proceeds expected to be placed in escrow. At a special shareholders meeting held on November 26, 2008, the proposal to approve the anticipated asset sale was approved by approximately 85 percent of our shareholders. The Asset Purchase Agreement for the transaction provides that the closing of the contemplated asset sale is to take place on January 5, 2009, following the satisfaction or waiver of the remaining closing conditions to the obligations of the parties to the purchase agreement, or such other time as agreed upon by the parties.

Critical Accounting Policies

Management's Discussion and Analysis of Financial Condition and Results of Operations is based upon our unaudited interim condensed consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these unaudited interim condensed consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, and expenses, and related disclosure of contingent assets and liabilities. Management bases its estimates on historical experience and on various other assumptions that it believes to be reasonable under the circumstances. The results of these estimates form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ materially from our estimates.

An accounting policy is deemed to be critical if it requires an accounting estimate to be made based on assumptions about matters that are highly uncertain at the time the estimate is made, and if different estimates that reasonably could have been used or changes in the accounting estimate that are reasonably likely to occur could materially change the financial statements. No events occurred or circumstances changed during the three and nine months ended October 31, 2008 that required us to test goodwill for impairment. Management believes there have been no significant changes during the three and nine months ended October 31, 2008 to the items that we disclosed as our critical accounting policies and estimates in Management's Discussion and Analysis of Financial Condition and Results of Operations in our annual report on Form 10-K for the fiscal year ended January 31, 2008.

Results of Operations

Consolidated

Revenue

<i>(in thousands except change)</i>	Three Months Ended October 31,		Nine Months Ended October 31,		Year over Year % Change	
	2008	2007	2008	2007	Three Months	Nine Months
Revenue:						
Products	\$ 4,222	\$ 3,053	\$ 21,720	\$ 7,971	38%	172%
Services	14	46	43	213	(70%)	(80%)
	<u>\$ 4,236</u>	<u>\$ 3,099</u>	<u>\$ 21,763</u>	<u>\$ 8,184</u>	37%	166%
Operating loss	<u>\$ (4,466)</u>	<u>\$ (4,322)</u>	<u>\$ (9,383)</u>	<u>\$ (11,828)</u>		

[Table of Contents](#)*Revenue by Region*

<i>(in thousands except change)</i>	<u>Three Months Ended October 31,</u>		<u>Nine Months Ended October 31,</u>		<u>Year over Year % Change</u>	
	<u>2008</u>	<u>2007</u>	<u>2008</u>	<u>2007</u>	<u>Three Months</u>	<u>Nine Months</u>
Revenue:						
North America	\$ 958	\$ 2,017	\$ 11,115	\$ 5,539	(53%)	101%
Europe	696	604	1,505	1,218	15%	24%
Asia	2,531	210	8,787	552	1,105%	1,492%
Latin America	51	268	356	875	(81%)	(59%)
	<u>\$ 4,236</u>	<u>\$ 3,099</u>	<u>\$ 21,763</u>	<u>\$ 8,184</u>	37%	166%

Revenue for the three and nine months ended October 31, 2008 increased by \$1.1 million, or 37 percent, and \$13.6 million, or 166 percent, respectively, compared to the corresponding periods of fiscal 2007. The increase is primarily attributable to an increase in revenue in our ChargeSource[®] business of \$1.3 million for the three months ended October 31, 2008. The increase in revenue for the nine months ended October 31, 2008 is attributable to ChargeSource[®] and WTS revenue increases of \$7.2 million and \$6.3 million, respectively, compared to the same periods of the prior fiscal year. The increase in ChargeSource[®] revenue relates primarily to shipments to Lenovo that began in late January 2008 and sales to Trust of approximately \$0.5 million in the third quarter of fiscal 2009. The year to date increase in WTS revenue primarily relates to deliveries in the first and second quarters of fiscal 2009 of the Symphony[™] Multi units sold to AT&T.

[Table of Contents](#)

Cost of Revenue and Gross Margin

<i>(in thousands except margin and change)</i>	Three Months Ended October 31,				Nine Months Ended October 31,				Year over Year % Change	
	2008		2007		2008		2007		Three Months	Nine Months
	% of Related Revenue	% of Related Revenue	% of Related Revenue	% of Related Revenue	% of Related Revenue	% of Related Revenue				
Cost of revenue:										
Products	\$3,777	89%	\$2,717	89%	\$14,779	68%	\$6,440	81%	39%	129%
Amortization – software development	—	—	20	1%	—	—	212	3%	(100%)	(100%)
	<u>3,777</u>	<u>89%</u>	<u>2,737</u>	<u>90%</u>	<u>14,779</u>	<u>68%</u>	<u>6,652</u>	<u>84%</u>	38%	122%
Services	—	—	80	174%	119	277%	253	119%	(100%)	(53%)
	<u>\$3,777</u>	<u>89%</u>	<u>\$2,817</u>	<u>91%</u>	<u>\$14,898</u>	<u>69%</u>	<u>\$6,905</u>	<u>84%</u>	34%	116%

	Three Months Ended October 31,		Nine Months Ended October 31,		Year over Year ppt Change	
	2008	2007	2008	2007	Three Months	Nine Months
	Gross margin:					
Products	11%	10%	32%	16%	1	16
Services	—	(74%)	(177%)	(19%)	74	(158)
Combined gross margin	11%	9%	31%	16%	2	15

Cost of revenue for the three and nine months ended October 31, 2008 increased by \$1.0 million, or 34 percent, and \$8.0 million, or 116 percent, respectively, compared to the corresponding periods of fiscal 2008. These increases are consistent with the revenue increases for the three and nine months ended October 31, 2008. Combined gross margin is comparable for the three months ended October 31, 2008 compared to the prior year period. Combined gross margin for the nine months ended October 31, 2008 increased 15 percentage points from 16 percent to 31 percent compared to the comparable period of the prior year. As combined revenues increase, the Company is better able to absorb its fixed manufacturing overhead.

[Table of Contents](#)

Operating Costs and Expenses

<i>(in thousands except change)</i>	Three Months Ended October 31,				Nine Months Ended October 31,				Year over Year % Change	
	2008		2007		2008		2007		Three Months	Nine Months
		% of Revenue		% of Revenue		% of Revenue		% of Revenue		
Operating expenses:										
SG&A expenses	\$ 964	23%	\$1,131	37%	\$ 4,289	20%	\$ 3,229	40%	(15%)	33%
Allocated corporate overhead	2,136	50%	1,297	42%	6,005	28%	3,782	46%	65%	59%
Gross engineering and support expenses	2,177	51%	2,176	70%	6,642	30%	6,096	74%	—	9%
Capitalized software development	(352)	(8%)	—	—	(688)	(3%)	—	—	—	—
	<u>\$4,925</u>	<u>116%</u>	<u>\$4,604</u>	<u>149%</u>	<u>\$16,248</u>	<u>75%</u>	<u>\$13,107</u>	<u>160%</u>	7%	24%

Selling, general, and administrative expenses for the three months ended October 31, 2008 decreased \$0.2 million, or 15 percent, compared to the corresponding period of fiscal 2008. Selling, general, and administrative expenses for the nine months ended October 31, 2008 increased \$1.1 million, or 33 percent, compared to the corresponding period of fiscal 2008. The increase was primarily caused by increased legal fees for the nine months ended October 31, 2008 related to the SwissQual and iGo litigation described in Note 15 of the Notes to Condensed Consolidated Financial Statements included in Part I, Item 1 of this report.

Allocated corporate overhead consists of salaries and other personnel-related expenses of our accounting and finance, human resources and benefits, and other administrative personnel, as well as professional fees, directors' fees, and other costs and expenses attributable to being a public company. These costs are typically allocated to our two segments based on each business's percentage share of total Company costs and expenses. Allocated corporate overhead increased \$0.8 million and \$2.2 million, respectively, for the three and nine months ended October 31, 2008. The increase for the three months ended October 31, 2008 relates primarily to increased legal fees, compared to the corresponding period of fiscal 2008, in support of the pending sale of our WTS assets to Ascom. The increase of \$2.2 million for the nine months ended October 31, 2008 relates to \$1.0 million of non-recurring severance costs as well as increased legal fees of \$1.0 million and increased consulting fees of \$0.3 million compared to the same period of fiscal 2008.

Gross engineering and support expenses generally consist of salaries, employer paid benefits, and other personnel related costs of our hardware and software design engineers and testing and product support personnel, as well as facility and IT costs, professional and consulting fees, lab costs, material usages, and travel and related costs incurred in the development and support of our products. Engineering and support costs remained flat during the three months ended October 31, 2008 compared to the corresponding period of fiscal 2008. Engineering and support expenses for the nine months ended October 31, 2008 increased \$0.5 million, or 9 percent, compared to the corresponding period of fiscal 2008. This increase is primarily due to increased ChargeSource® engineering expenses, consisting of material usage and lab fees in support of our on-going efforts to develop new products for our retail and OEM accessories channels.

We capitalize costs incurred for the development of software embedded in our WTS products subsequent to establishing technological feasibility. These capitalized costs are subject to an ongoing assessment of recoverability based on anticipated future revenue and changes in hardware and software technologies. Costs that are capitalized include direct labor and related overhead. During the three and nine months ended October 31, 2008, we capitalized

[Table of Contents](#)

software development costs related to Opti and QuOTA in the amount of \$352,000 and \$688,000, respectively. During the corresponding periods of fiscal 2008 we did not capitalize any software product development costs.

Other Income, net

Other income, net, consists primarily of interest income earned on invested cash balances. Interest income earned on invested cash balances for the three and nine months ended October 31, 2008 totaled \$25,000 and \$105,000, respectively. For the three and nine months ended October 31, 2007, interest income totaled \$207,000 and \$699,000, respectively. The current year decrease in interest income is due to decreased invested cash balances and decreased interest rates earned on invested cash balances.

Gain on Sale of Equipment, net

The gain on sale of equipment recorded during the first quarter of fiscal 2008 relates to the sale of WTS equipment, the majority of which was previously leased to outsourced engineering services providers. No similar transactions occurred during fiscal 2009.

Gain on Sale of Investment in SwissQual, net

For the three and nine months ended October 31, 2007, we received additional consideration totaling \$0.3 million and \$0.6 million, respectively, net of transaction costs, from Spirent plc, the acquirer of our 18 percent interest in SwissQual AG.

Income Tax Expense

Significant management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities, and any required valuation allowance. The Company continues to have a fully reserved deferred tax asset. This valuation allowance was previously established based on management's overall assessment of risks and uncertainties related to our future ability to realize, and hence, utilize certain deferred tax assets, primarily consisting of net operating losses and carry forward temporary differences. Due to the losses in the current fiscal year, the adjusted net deferred tax assets remain fully reserved as of October 31, 2008. In accordance with paragraph 140 of Statement of Financial Accounting Standard No. 109, "Accounting for Income Taxes," a tax benefit has been recorded utilizing a combined effective rate of 39.2 percent and 38.3 percent for the three and nine months ended October 31, 2008 and the three and nine months ended October 31, 2007, respectively, to reflect the utilization of losses from current operations to offset the gain and income from discontinued operations.

The Company adopted FIN 48, "Accounting for Uncertainty in Income Taxes – An Interpretation of FASB Statement No. 109," on February 1, 2007. As a result of the adoption of FIN 48, the Company recorded an \$86,000 decrease in retained earnings and increased non-current liabilities by \$86,000. The FIN 48 liability recorded during the first quarter of fiscal 2008 had not changed as of October 31, 2008.

[Table of Contents](#)**Discontinued Operations, net of income taxes***Income from Discontinued Operations*

<i>(in thousands except change)</i>	<u>Three Months Ended October 31,</u>		<u>Nine Months Ended October 31,</u>		<u>Year over Year % Change</u>	
	<u>2008</u>	<u>2007</u>	<u>2008</u>	<u>2007</u>	<u>Three Months</u>	<u>Nine Months</u>
Revenues	\$ —	\$ 1,915	\$ 3,680	\$ 8,165	(100%)	(55%)
Income from discontinued operations:						
Gain on sale, net of income taxes of \$32,000 and \$182,000	\$ 50	\$ —	\$ 282	\$ —	100%	100%
Income from discontinued operations, before taxes	—	666	1,149	3,287	(100%)	(65%)
Income tax expense	—	(255)	(450)	(1,291)	100%	65%
Income from discontinued operations	\$ 50	\$ 411	\$ 981	\$ 1,996	(88%)	(51%)

The sale of the call box business was completed on July 10, 2008, which resulted in a pre-tax gain of \$382,000. The call box business experienced a decline in revenues and income for the nine months ended October 31, 2008 as compared to the corresponding period of the prior fiscal year due to the completion of non-recurring contracts to upgrade emergency call boxes from analog to digital. Additionally, the call box business was only operated for five months during fiscal 2009. The Company historically allocated certain fixed manufacturing costs, indirect engineering costs, and corporate overhead based upon analysis of actual percentage share of Company costs and expenses to each of its three businesses. The two remaining businesses presented below now reflect allocations of the amounts previously allocated to the call box business segment.

During the third quarter of fiscal 2009, the Company recorded an additional pre-tax gain on the sale of the call box business of \$150,000 in conjunction with the execution of a subcontractor agreement that provides for a monthly cash payment of \$12,500 to the Company from the buyer of the call box business over a 12-month period. Offsetting the gain of \$150,000 in the third quarter were additional pre-tax expenses incurred relating to the sale of the business of approximately \$68,000.

ChargeSource[®]*Revenue*

<i>(in thousands except change)</i>	<u>Three Months Ended October 31,</u>		<u>Nine Months Ended October 31,</u>		<u>Year over Year % Change</u>	
	<u>2008</u>	<u>2007</u>	<u>2008</u>	<u>2007</u>	<u>Three Months</u>	<u>Nine Months</u>
Revenue:						
Products	\$ 3,236	\$ 1,893	\$ 10,215	\$ 2,980	71%	243%
Services	—	—	—	—	—	—
	\$ 3,236	\$ 1,893	\$ 10,215	\$ 2,980	71%	243%
Operating loss	\$ (2,532)	\$ (2,287)	\$ (8,327)	\$ (5,824)		

[Table of Contents](#)

Revenue by Region

<i>(in thousands except change)</i>	Three Months Ended October 31,		Nine Months Ended October 31,		Year over Year % Change	
	2008	2007	2008	2007	Three Months	Nine Months
	Revenue:					
North America	\$ 74	\$ 1,355	\$ 466	\$ 1,906	(95%)	(76%)
Europe	647	513	1,329	1,049	26%	27%
Asia	2,515	25	8,420	25	9,960%	33,580%
Latin America	—	—	—	—	—	—
	<u>\$ 3,236</u>	<u>\$ 1,893</u>	<u>\$ 10,215</u>	<u>\$ 2,980</u>	71%	243%

Revenue by Customer

<i>(in thousands except change)</i>	Three Months Ended October 31,		Nine Months Ended October 31,		Year over Year % Change					
	2008	2007	2008	2007	Three Months	Nine Months				
	% of Revenue	% of Revenue	% of Revenue	% of Revenue						
Revenue:										
Kensington	\$ 125	4%	\$1,780	94%	\$ 946	9%	\$2,431	82%	(93%)	(61%)
Lenovo	2,521	78%	—	—	8,447	83%	—	—	—	—
Trust	521	16%	—	—	530	5%	—	—	—	—
Other	69	2%	113	6%	292	3%	549	18%	(39%)	(47%)
	<u>\$3,236</u>	<u>100%</u>	<u>\$1,893</u>	<u>100%</u>	<u>\$10,215</u>	<u>100%</u>	<u>\$2,980</u>	<u>100%</u>	71%	243%

Revenue for ChargeSource[®] for the three and nine months ended October 31, 2008 increased by \$1.3 million, or 71 percent, and \$7.2 million, or 243 percent, respectively, compared to corresponding periods of fiscal 2008. The increase in revenue relates primarily to shipments to Lenovo that began in late January 2008 and sales to Trust in the third quarter of fiscal 2009. During the three and nine months ended October 31, 2008, we shipped approximately 52,000 and 171,000 90-watt adapters, respectively, and 8,000 and 32,000 120-watt adapters, respectively. Sales to Lenovo expanded our presence in the Asia-Pacific market.

Cost of Revenue and Gross Margin

<i>(in thousands except change)</i>	Three Months Ended October 31,		Nine Months Ended October 31,		Year over Year % Change					
	2008	2007	2008	2007	Three Months	Nine Months				
	% of Revenue	% of Revenue	% of Revenue	% of Revenue						
Cost of revenue:										
Products	\$3,237	100%	\$2,153	114%	\$10,403	102%	\$4,009	135%	50%	159%
Amortization – software development	—	—	—	—	—	—	—	—	—	—
Services	3,237	100%	2,153	114%	10,403	102%	4,009	135%	50%	159%
	<u>\$3,237</u>	<u>100%</u>	<u>\$2,153</u>	<u>114%</u>	<u>\$10,403</u>	<u>102%</u>	<u>\$4,009</u>	<u>135%</u>	50%	159%

	Three Months Ended October 31,		Nine Months Ended October 31,		Year over Year ppt Change	
	2008	2007	2008	2007	Three Months	Nine Months
	Gross margin:					
Products	—	(14%)	(2%)	(35%)	14	33
Services	—	—	—	—	—	—
Combined gross margin	—	(14%)	(2%)	(35%)	14	33

Table of Contents

Cost of revenue for the three and nine months ended October 31, 2008 increased by \$1.1 million, or 50 percent, and \$6.4 million, or 159 percent, respectively, compared to the corresponding periods of fiscal 2008. The increase in cost of revenue is primarily due to the increase in revenue for the three and nine months ended October 31, 2008 compared to the corresponding periods of the prior fiscal year. The current level of ChargeSource[®] revenue is insufficient to fully absorb our fixed manufacturing overhead. Cost of revenue for the three and nine months ended October 31, 2008 included approximately \$0.2 million and \$1.0 million, respectively, of under-absorbed fixed manufacturing overhead. Cost of revenue for the three and nine months ended October 31, 2007 included approximately \$0.5 million and \$1.6 million of under-absorbed fixed manufacturing overhead. As revenues increase, the amount of under-absorption of fixed manufacturing costs decreases.

Operating Costs and Expenses

<i>(in thousands except change)</i>	Three Months Ended October 31,				Nine Months Ended October 31,				Year over Year % Change	
	2008		2007		2008		2007		Three Months	Nine Months
	% of Revenue	% of Revenue	% of Revenue	% of Revenue	% of Revenue	% of Revenue				
Operating expenses:										
SG&A expenses	\$ 443	14%	\$ 634	33%	\$2,540	25%	\$1,440	48%	(30%)	76%
Allocated corporate overhead	1,358	42%	720	38%	3,546	35%	1,700	57%	89%	109%
Gross engineering and support expenses	730	22%	673	36%	2,053	20%	1,655	56%	9%	24%
	<u>\$2,531</u>	<u>78%</u>	<u>\$2,027</u>	<u>107%</u>	<u>\$8,139</u>	<u>80%</u>	<u>\$4,795</u>	<u>161%</u>	<u>25%</u>	<u>70%</u>

Selling, general, and administrative expenses generally consist of salaries, employer paid benefits, commissions and other personnel related costs of our management, sales, marketing, and administrative personnel, facility and IT costs, professional fees, advertising, promotions, printed media, and travel directly attributable to our ChargeSource[®] business. Selling, general, and administrative expenses in the three months ended October 31, 2008 decreased by approximately \$0.2 million, or 30 percent, when compared to the three months ended October 31, 2007. Selling, general, and administrative expenses in the nine months ended October 31, 2008 increased by approximately \$1.1 million, or 76 percent, compared to the corresponding period of fiscal 2008. The increase in expenses for the 2009 fiscal year to date period is primarily due to increased legal fees related to the iGo litigation (see Note 15 of the Notes to Condensed Consolidated Financial Statements included in Part 1, Item 1 of this report). The decrease in expenses for the third quarter of fiscal 2009 compared to the prior year comparable period is primarily due to reduced legal fees due to the stay of proceedings obtained on June 30, 2008.

See the section above entitled "Consolidated" under the caption "Operating Costs and Expenses" for a discussion of allocated corporate overhead.

Gross engineering and support expenses generally consist of salaries, employer paid benefits, and other personnel related costs of our electrical and mechanical design engineers and testing and product support personnel, as well as facility and IT costs, professional and consulting fees, lab costs, material usages, and travel and related costs incurred in the development and support of our ChargeSource[®] business. Engineering and support expenses for the three and nine months ended October 31, 2008 increased \$0.1 million, or 9 percent, and \$0.4 million, or 24 percent, respectively, compared to the corresponding prior year periods. The increase in gross engineering and support expenses is due to increased material usages and lab costs as new products are currently in development.

[Table of Contents](#)

Wireless Test Solutions (“WTS”)

Revenue

<i>(in thousands except change)</i>	Three Months Ended October 31,		Nine Months Ended October 31,		Year over Year % Change	
	2008	2007	2008	2007	Three Months	Nine Months
	Revenue:					
Products	\$ 986	\$ 1,160	\$ 11,505	\$ 4,991	(15%)	131%
Services	14	46	43	213	(70%)	(80%)
	<u>\$ 1,000</u>	<u>\$ 1,206</u>	<u>\$ 11,548</u>	<u>\$ 5,204</u>	(17%)	122%
Operating loss	\$ (1,934)	\$ (2,035)	\$ (1,056)	\$ (6,004)		

Revenue by Region

<i>(in thousands except change)</i>	Three Months Ended October 31,		Nine Months Ended October 31,		Year over Year % Change	
	2008	2007	2008	2007	Three Months	Nine Months
	Revenue:					
North America	\$ 884	\$ 662	\$ 10,649	\$ 3,633	34%	193%
Europe	49	91	176	169	(46%)	4%
Asia	16	185	367	527	(91%)	(30%)
Latin America	51	268	356	875	(81%)	(59%)
	<u>\$ 1,000</u>	<u>\$ 1,206</u>	<u>\$ 11,548</u>	<u>\$ 5,204</u>	(17%)	122%

Revenue for the three months ended October 31, 2008 decreased by \$0.2 million, or 17 percent, compared to the corresponding period of fiscal 2008. The third quarter revenue decrease is a reflection of the current general economic downturn as well as delays in customer’s capital spending and is reflective of the unpredictable nature of our WTS business.

Revenue for the nine months ended October 31, 2008 increased by \$6.3 million, or 122 percent, compared to the corresponding period of fiscal 2008. The fiscal 2009 increase in revenue is due to the Symphony™ Multi units sold to AT&T. The revenue recognized on this single order totaled \$8.2 million, net of revenue sharing of \$1.9 million. This excludes amounts deferred relating to post-contract support and warranty.

Cost of Revenue and Gross Margin

<i>(in thousands except margin and change)</i>	Three Months Ended October 31,				Nine Months Ended October 31,				Year over Year % Change	
	2008		2007		2008		2007		Three Months	Nine Months
	\$	% of Related Revenue	\$	% of Related Revenue	\$	% of Related Revenue	\$	% of Related Revenue		
Cost of revenue:										
Products	\$540	55%	\$564	49%	\$4,376	38%	\$2,431	49%	(4%)	80%
Amortization – software development	—	—	20	2%	—	—	212	4%	(100%)	(100%)
	540	55%	584	50%	4,376	38%	2,643	53%	(8%)	66%
Services	—	—	80	174%	119	277%	253	119%	(100%)	(53%)
	<u>\$540</u>	<u>54%</u>	<u>\$664</u>	<u>55%</u>	<u>\$4,495</u>	<u>39%</u>	<u>\$2,896</u>	<u>56%</u>	(19%)	55%

[Table of Contents](#)

	Three Months Ended October 31,		Nine Months Ended October 31,		Year over Year ppt Change	
	2008	2007	2008	2007	Three Months	Nine Months
	Gross margin:					
Products	45%	50%	62%	47%	(5)	15
Services	100%	(74%)	(177%)	(19%)	174	(158)
Combined gross margin	46%	45%	61%	44%	1	17

Cost of revenue for the three months ended October 31, 2008 decreased by \$0.1 million, or 19 percent, compared to the corresponding period of fiscal 2008. The decrease in cost of revenue is consistent with the decrease in revenue for the same period. The gross margin for the third quarter of fiscal 2009 remained flat in comparison to the third quarter of fiscal 2008. Cost of revenue for the nine months ended October 31, 2008 increased by \$1.6 million, or 55 percent, compared to the corresponding period of fiscal 2008. The increase in cost of revenue for the year to date period is driven by increased sales volume. The cost of services relates to amortization on Seven.Five units previously leased. The combined gross margin increased by 1 and 17 percentage points in the three and nine months ended October 31, 2008, respectively, compared to the corresponding periods of the prior fiscal year because the increased revenue allows for greater absorption of fixed manufacturing overhead expenses. Additionally, the Company incurred amortization of software development costs of \$0.2 million during the nine months ended October 31, 2007 and had no similar expense during fiscal 2009.

Operating Costs and Expenses

<i>(in thousands except change)</i>	Three Months Ended October 31,				Nine Months Ended October 31,				Year over Year % Change	
	2008		2007		2008		2007		Three Months	Nine Months
	% of Revenue	% of Revenue	% of Revenue	% of Revenue	% of Revenue	% of Revenue	% of Revenue	% of Revenue	Three Months	Nine Months
Operating expenses:										
SG&A expenses	\$ 521	52%	\$ 497	41%	\$1,749	15%	\$1,789	35%	5%	(2%)
Allocated corporate overhead	778	78%	577	48%	2,459	21%	2,082	40%	35%	18%
Gross engineering and support expenses	1,447	144%	1,503	125%	4,589	40%	4,441	85%	(4%)	3%
Capitalized software development costs	(352)	(35%)	—	—	(688)	(6%)	—	—	—	—
	<u>\$2,394</u>	<u>239%</u>	<u>\$2,577</u>	<u>214%</u>	<u>\$8,109</u>	<u>70%</u>	<u>\$8,312</u>	<u>160%</u>	<u>(7%)</u>	<u>(2%)</u>

Selling, general, and administrative expenses generally consist of salaries, employer paid benefits, commissions and other personnel related costs of our sales, marketing, and support personnel, facility and IT costs, professional fees, advertising, promotions, printed media, and travel directly attributable to our WTS business. The selling, general, and administrative expenses incurred for the three and nine months ended October 31, 2008 are consistent with the prior period.

See the section above entitled “Consolidated” under the caption “Operating Costs and Expenses” for a discussion of allocated corporate overhead.

Gross engineering and support expenses generally consist of salaries, employer paid benefits, and other personnel related costs of our hardware and software design engineers and testing and product support personnel, as well as facility and IT costs, professional and consulting fees, lab costs, material usages, and travel and related costs

Table of Contents

incurred in the development and support of our WTS business. Engineering and support costs for the three and nine months ended October 31, 2008 were consistent with amounts incurred in the respective prior period.

We capitalize costs incurred for the development of software embedded in our WTS products subsequent to establishing technological feasibility. These capitalized costs are subject to an ongoing assessment of recoverability based on anticipated future revenue and changes in hardware and software technologies. Costs that are capitalized include direct labor and related overhead. We capitalized software development costs in the three and nine months ended October 31, 2008 in the amount of \$352,000 and \$688,000, respectively, related to Opti product development, as well as QuOTA development that we began capitalizing in the third quarter of fiscal 2009. We did not capitalize any software development costs in the three and nine months ended October 31, 2007.

Liquidity and Capital Resources

Cash and cash equivalents at October 31, 2008 decreased \$9.4 million to \$7.6 million as compared to \$17.0 million at January 31, 2008. The following table is a summary of our Condensed Consolidated Statements of Cash Flows.

	Nine Months Ended	
	October 31,	
	2008	2007
	(in thousands)	
Cash provided by (used in):		
Operating activities	\$ (8,076)	\$ (1,050)
Investing activities	(1,328)	526
Financing activities	—	(7,673)

Operating Activities

Cash used in operating activities of \$8.1 million for the nine months ended October 31, 2008 was driven by our net loss from continuing operations of \$8.7 million partially offset by non-cash depreciation and amortization of \$1.2 million and cash provided by discontinued operations of \$3.2 million, including proceeds of \$2.7 million from the sale of our call box business in July 2008. Additionally, our cash flow declined due to increases in accounts receivable and inventory balances of \$1.3 million and \$2.2 million, respectively.

Included in our year to date loss is non-recurring severance costs totaling \$1.0 million. Additionally, our receivable balance has grown as a result of increased sales for the third quarter of fiscal 2009 compared to the same period of the prior fiscal year. The increase in inventory is due to filling our ChargeSource® contract manufacturer's warehouse with a minimum 10-day supply of finished goods inventory.

Cash used in operating activities of \$1.1 million for the nine months ended October 31, 2007 was driven by our net loss from continuing operations of \$8.4 million, a decrease in deferred revenue of \$0.7 million, and a reduction in accrued liabilities of \$1.7 million, primarily due to vendor payments for inventory, income taxes and the distribution of incentive compensation. These decreases were offset primarily by cash generated from discontinued operations of \$5.1 million and collection of accounts receivable of \$4.6 million.

Investing Activities

During the nine months ended October 31, 2008, we purchased \$0.6 million of property and equipment, primarily tooling, and equipment used for the manufacture of our ChargeSource® products. We also capitalized software development costs incurred related to our WTS Opti and QuOTA product development in the amount of \$0.7 million.

During the nine months ended October 31, 2007 we received \$0.4 million relating primarily to the sale of WTS equipment that had been previously leased, and we collected \$0.6 million in contingent consideration from

[Table of Contents](#)

SwissQual relating to the January 2006 sale to Spirent. During the first nine months of fiscal 2008 we spent \$0.4 million of capitalized expenditures, mostly relating to tooling and other equipment for ChargeSource .

Financing Activities

During the nine months ended October 31, 2008, the Company did not engage in any financing activities. During the first quarter of fiscal 2008 we declared and paid a special dividend of \$1 per share of our outstanding common stock for a total payment of \$7.4 million. During the nine months ended October 31, 2007, we repurchased approximately 58,000 shares in the open market for a total cost of \$0.4 million, or an average price of \$6.70 per share.

We believe that the proceeds we expect to receive from the contemplated sale of the WTS assets (see Note 16 of the Notes to Condensed Consolidated Financial Statements included in Part I, Item 1 of this report), together with our existing cash and cash equivalent balances, will provide us sufficient funds to satisfy our cash requirements for the next 12 months. If the anticipated proceeds contemplated from the sale of the WTS assets together with our existing cash and cash equivalent balances do not satisfy our cash requirements, or if the contemplated sale of the WTS assets does not occur as we expect, we expect that we will need to implement further cost reduction strategies or attempt to raise additional capital through debt or the issuance of additional equity. We are unable at this time to predict the impact that the recent disruption in the financial and credit markets may have on our ability to raise such additional capital or the probability of our success should we need to attempt to raise additional capital.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Currency Risk

We are exposed to the risk of changes in currency exchange rates. As of October 31, 2008, we had no material accounts receivable denominated in foreign currencies. Our standard terms require customers to pay for our products and services in U.S. dollars. For those orders denominated in foreign currencies, we may limit our exposure to losses from foreign currency transactions through forward foreign exchange contracts. To date, sales denominated in foreign currencies have not been significant and we have not entered into any foreign exchange contracts.

Interest Rate Sensitivity

The primary objective of our investment activities is to preserve principal while at the same time maximizing the income we receive from our investments without significantly increasing risk. Some of the securities that we have invested in may be subject to market risk. This means that a change in prevailing interest rates may cause the principal amount of the investment to fluctuate. For example, if we hold a security that was issued with a fixed interest rate at the then-prevailing rate and the prevailing interest rate later rises, the principal amount of our investment will probably decline in value. To minimize this risk, we maintain a significant portion of our cash balances in money market funds. In general, money market funds are not subject to interest rate risk because the interest paid on such funds fluctuates with the prevailing interest rate.

We do not hold any derivative financial instruments.

Our cash and cash equivalents have maturities dates of three months or less and the fair value approximates the carrying value in our condensed consolidated financial statements.

Equity Price Risk

Our short-term investments consist of balances maintained in a non-qualified deferred compensation plan funded by our executives and directors. We value these investments using the closing market value for the last day of each month. These investments are subject to market price volatility. We reflect these investments on our condensed consolidated balance sheet at their market value, with the unrealized gains and losses reflected as adjustments to both short-term investments and the deferred compensation liability.

Due to the inherent risk associated with some of our investments, and in light of current stock market conditions, we may incur future losses on the sales, write-downs, or write-offs of our investments. We do not currently hedge against equity price changes.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in the periodic reports that we file or submit with the SEC under the Securities Exchange Act of 1934 is recorded, processed, summarized, and reported within the time periods specified in the rules and forms of the SEC, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report on Form 10-Q. Based upon this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report on Form 10-Q.

Changes in Internal Control Over Financial Reporting

“Internal control over financial reporting” is a process designed by, or under the supervision of, the issuer’s principal executive and financial officers, and effected by the issuer’s board of directors, management, and other personnel, 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 and includes those policies and procedures that:

- (1) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the issuer;
- (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the issuer are being made only in accordance with authorizations of management and directors of the issuer; and
- (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the issuer’s assets that could have a material effect on the financial statements.

There was no change in our internal control over financial reporting during the fiscal quarter ended October 31, 2008 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II — OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

On June 8, 2007, iGo, Inc. (formerly Mobility Electronics, Inc.) (“iGo”) filed a complaint against us and our subsidiary CWT in the United States District Court for the Eastern District of Texas, Case No. 5:07cv84, alleging that two iGo patents are infringed by the mechanical keying arrangement between power adapters and programming tips used by us in the mobile power products sold through our distributors and sold to a computer maker. The complaint seeks an unspecified amount of treble damages and injunctive relief. We have denied liability and countersued alleging that iGo breached a settlement agreement (the “Settlement Agreement”) entered into between the parties in 2003 settling a previous patent infringement lawsuit, and that iGo is liable for infringement of at least three of our patents. iGo has denied liability and amended its claims to further allege that we breached the Settlement Agreement by asserting claims against iGo. We have denied liability as to the additional claim made by iGo. On March 5, 2008, both parties attended mediation without reaching a settlement.

On June 25, 2008, the parties jointly requested that the U.S. District Court for the Eastern District of Texas (the “Texas Court”) transfer the lawsuit to the U.S. District Court for the District of Arizona, the court in which the parties’ previous patent infringement lawsuit had been filed (the “Arizona Court”). The parties’ joint request also sought, following transfer, a stay of proceedings until January 2009 so that the parties could pursue settlement. On June 30, 2008, the Texas Court granted the parties’ joint request for transfer, transferring the lawsuit to the Arizona Court under the terms and conditions requested, including the stay, Action No. CV 08-1224-PHX-MHM.

On November 30, 2007, SwissQual filed a lawsuit against our subsidiary CWT in the United States District Court for the Central District of California, Case No. cv-07-07819, alleging fraud, intentional interference with prospective economic advantage, breach of contract, trademark infringement, unfair competition, trade secret misappropriation, and seeking declaratory relief relating to the Distribution and Sales Agreement dated December 15, 2005 between the parties.

We have answered SwissQual’s complaint and denied any and all liability. In addition, we asserted counterclaims against SwissQual alleging breach of contract, breach of the covenant of good faith and fair dealing, trade secret misappropriation, intentional interference with prospective economic advantage, negligent interference with prospective economic advantage, unfair competition, conversion, unjust enrichment/restitution, an accounting for money owed due to SwissQual’s misconduct and seeking declaratory relief relating to SwissQual’s failure to comply with its support obligations, indemnity, and trademark ownership.

On November 26, 2008, we entered into a Settlement Agreement and Release of Claims (the “Settlement Agreement”) with SwissQual pursuant to which the parties agreed to dismiss their respective claims and counterclaims against each other. Among other terms, the Settlement Agreement contains general releases between the parties. As a result, this lawsuit has been dismissed with prejudice.

The outcome of the iGo matter remains neither determinable nor estimable. We believe we have meritorious defenses to the matter described above and intend to vigorously defend this action. In addition to the pending matter described above, we are from time to time involved in various legal proceedings incidental to the conduct of our business. We believe that the outcome of all such legal proceedings will not in the aggregate have a material adverse effect on our consolidated results of operations and financial position.

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

None.

[Table of Contents](#)

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

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

None.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

- 2.1 Asset Purchase Agreement by and among Comarco, Inc., Comarco Wireless Technologies, Inc., Ascom Holding AG and Ascom Inc. dated as of September 26, 2008 (incorporated by reference to Exhibit 2.1 of the Company's Current Report on Form 8-K filed with the SEC on September 29, 2008)
- 10.1 Form of Escrow Agreement by and among Comarco, Inc., Comarco Wireless Technologies, Inc., Ascom Holding AG, Ascom Inc. and U.S. Bank National Association (incorporated by reference to Exhibit 99.1 of the Company's Current Report on Form 8-K filed with the SEC on September 29, 2008)
- 10.2 2005 Equity Incentive Plan, As Amended, is filed herewith
- 31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized.

COMARCO, INC.

Date: December 12, 2008

/s/ Samuel M. Inman, III
Samuel M. Inman, III
President and Chief Executive Officer

Date: December 12, 2008

/s/ Winston E. Hickman
Winston E. Hickman
Vice President and Chief Financial Officer

EXHIBIT INDEX

<u>Exhibit Number</u>	<u>Description</u>
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31.1	Principal Executive Officer Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
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COMARCO, INC.
2005 EQUITY INCENTIVE PLAN, AS AMENDED

1. Purpose	1
2. Definitions	1
3. Term of the Plan	4
4. Stock Subject to the Plan	4
5. Administration	4
6. Authorization of Grants	4
7. Specific Terms of Awards	6
8. Adjustment Provisions	10
9. Change of Control	11
10. Settlement of Awards	12
11. Reservation of Stock	13
12. Limitation of Rights in Stock; No Special Service Rights	13
13. Unfunded Status of Plan	14
14. Nonexclusivity of the Plan	14
15. Termination and Amendment of the Plan	14
16. Notices and Other Communications	15
17. Governing Law	15

COMARCO, INC.

2005 Equity Incentive Plan, As Amended

1. Purpose

This Plan is intended to encourage ownership of Stock by employees, consultants and directors of the Company and its Affiliates and to provide additional incentive for them to promote the success of the Company's business. The Plan is intended to be an incentive stock option plan within the meaning of Section 422 of the Code, but not all Awards are required to be Incentive Options. This Plan constitutes an amendment, restatement and continuation in its entirety of the Company's 2005 Employee Stock Option Plan retroactive to the date of the Board's approval of that option plan on December 7, 2005 and shall take account of and govern any options granted under that option plan.

2. Definitions

As used in this Plan, the following terms shall have the following meanings:

2.1 Accelerate, Accelerated, and Acceleration, means: (a) when used with respect to an Option or Stock Appreciation Right, that as of the time of reference the Option or Stock Appreciation Right will become exercisable with respect to some or all of the shares of Stock for which it was not then otherwise exercisable by its terms; (b) when used with respect to Restricted Stock or Restricted Stock Units, that the Risk of Forfeiture otherwise applicable to the Stock or Units shall expire with respect to some or all of the shares of Restricted Stock or Units then still otherwise subject to the Risk of Forfeiture; and (c) when used with respect to Performance Units, that the applicable Performance Goals shall be deemed to have been met as to some or all of the Units.

2.2 Acquisition means a merger or consolidation of the Company with or into another person or the sale, transfer, or other disposition of all or substantially all of the Company's assets to one or more other persons in a single transaction or series of related transactions.

2.3 Affiliate means any corporation, partnership, limited liability company, business trust, or other entity controlling, controlled by or under common control with the Company.

2.4 Award means any grant or sale pursuant to the Plan of Options, Stock Appreciation Rights, Performance Units, Restricted Stock, Restricted Stock Units, or Stock Grants.

2.5 Award Agreement means an agreement between the Company and the recipient of an Award, setting forth the terms and conditions of the Award.

2.6 Board means the Company's Board of Directors.

2.7 Change of Control means the occurrence of any of the following after the date of the approval of the Plan by the Board:

(a) an Acquisition, unless securities possessing more than 50% of the total combined voting power of the survivor's or acquiror's outstanding securities (or the securities of any parent thereof) are held by a person or persons who held securities possessing more than 50% of the total combined voting power of the Company's outstanding securities immediately prior to that transaction, or

(b) any person or group of persons (within the meaning of Section 13(d)(3) of the Securities Exchange Act of 1934, as amended and in effect from time to time) directly or indirectly acquires, including but not limited to by means of a merger or consolidation, beneficial ownership (determined pursuant to Securities and Exchange Commission Rule 13d-3 promulgated under the said Exchange Act) of securities possessing more than 50% of the total combined voting power of the Company's outstanding securities, other than (i) the Company or an Affiliate, (ii) an employee benefit plan of the Company or any of its Affiliates, (iii) a trustee or other fiduciary holding securities under an employee benefit plan of the

Company or any of its Affiliates, or (iv) an underwriter temporarily holding securities pursuant to an offering of such securities, or

(c) over a period of 36 consecutive months or less, there is a change in the composition of the Board such that a majority of the Board members (rounded up to the next whole number, if a fraction) ceases, by reason of one or more proxy contests for the election of Board members, to be composed of individuals who either (i) have been Board members continuously since the beginning of that period, or (ii) have been elected or nominated for election as Board members during such period by at least a majority of the Board members described in the preceding clause (i) who were still in office at the time that election or nomination was approved by the Board.

2.8 Code means the Internal Revenue Code of 1986, as amended from time to time, or any successor statute thereto, and any regulations issued from time to time thereunder.

2.9 Committee means any committee of the Board delegated responsibility by the Board for the administration of the Plan, as provided in Section 5 of the Plan. For any period during which no such committee is in existence "Committee" shall mean the Board and all authority and responsibility assigned to the Committee under the Plan shall be exercised, if at all, by the Board.

2.10 Company means Comarco, Inc., a corporation organized under the laws of the State of California.

2.11 Covered Employee means an employee who is a "covered employee" within the meaning of Section 162(m) of the Code.

2.12 Grant Date means the date as of which an Option is granted, as determined under Section 7.1(a).

2.13 Incentive Option means an Option which by its terms is to be treated as an "incentive stock option" within the meaning of Section 422 of the Code.

2.14 Market Value means a value established by the Committee on the basis of actual transactions on or about the Grant Date or other relevant date in stock on any established securities market on which the Stock is then readily tradable, or in the absence of such transactions, the value of a share of stock on the relevant date as determined by the Committee.

2.15 Nonstatutory Option means any Option that is not an Incentive Option.

2.16 Option means an option to purchase shares of Stock.

2.17 Optionee means a Participant to whom an Option shall have been granted under the Plan.

2.18 Participant means any holder of an outstanding Award under the Plan.

2.19 Performance Criteria means the criteria that the Committee selects for purposes of establishing the Performance Goal or Performance Goals for a Participant for a Performance Period. The Performance Criteria used to establish Performance Goals are limited to: (i) cash flow (before or after dividends), (ii) earnings per share (including, without limitation, earnings before interest, taxes, depreciation and amortization), (iii) stock price, (iv) return on equity, (v) stockholder return or total stockholder return, (vi) return on capital (including, without limitation, return on total capital or return on invested capital), (vii) return on investment, (viii) return on assets or net assets, (ix) market capitalization, (x) economic value added, (xi) debt leverage (debt to capital), (xii) revenue, (xiii) sales or net sales, (xiv) backlog, (xv) income, pre-tax income or net income, (xvi) operating income or pre-tax profit, (xvii) operating profit, net operating profit or economic profit, (xviii) gross margin, operating margin or profit margin, (xix) return on operating revenue or return on operating assets, (xx) cash from operations, (xxi) operating ratio, (xxii) operating revenue, (xxiii) market share improvement, (xxiv) general and administrative expenses or (xxv) customer service.

2.20 Performance Goals means, for a Performance Period, the written goal or goals established by the Committee for the Performance Period based upon the Performance Criteria. The Performance Goals may be expressed in terms of overall Company performance or the performance of a division, business unit, subsidiary, or an individual, either individually, alternatively or in any combination, applied to either the Company as a whole or to a business unit or Affiliate, either individually, alternatively or in any combination, and measured either quarterly, annually or cumulatively over a period of years, on an absolute basis or relative to a pre-established target, to previous years' results or to a designated comparison group, in each case as specified by the Committee. The Committee will, in the manner and within the time prescribed by Section 162(m) of the Code in the case of Qualified Performance-Based Awards, objectively define the manner of calculating the Performance Goal or Goals it selects to use for such Performance Period for such Participant. To the extent consistent with Section 162(m) of the Code, the Committee may appropriately adjust any evaluation of performance against a Performance Goal to exclude any of the following events that occurs during a performance period: (i) asset write-downs, (ii) litigation, claims, judgments or settlements, (iii) the effect of changes in tax law, accounting principles or other such laws or provisions affecting reported results, (iv) accruals for reorganization and restructuring programs and (v) any extraordinary, unusual, non-recurring or non-comparable items (A) as described in Accounting Principles Board Opinion No. 30, (B) as described in management's discussion and analysis of financial condition and results of operations appearing in the Company's Annual Report to stockholders for the applicable year, or (C) publicly announced by the Company in a press release or conference call relating to the Company's results of operations or financial condition for a completed quarterly or annual fiscal period.

2.21 Performance Period means the one or more periods of time, which may be of varying and overlapping durations, selected by the Committee, over which the attainment of one or more Performance Goals will be measured for purposes of determining a Participant's right to, and the payment of, a Performance Unit.

2.22 Performance Unit means a right granted to a Participant under Section 7.5, to receive cash, Stock or other Awards, the payment of which is contingent on achieving Performance Goals established by the Committee.

2.23 Plan means this 2005 Equity Incentive Plan of the Company, as amended from time to time, and including any attachments or addenda hereto.

2.24 Qualified Performance-Based Awards means Awards intended to qualify as "performance-based compensation" under Section 162(m) of the Code.

2.25 Restricted Stock means a grant or sale of shares of Stock to a Participant subject to a Risk of Forfeiture.

2.26 Restricted Stock Units means rights to receive shares of Stock at the close of a Restriction Period, subject to a Risk of Forfeiture.

2.27 Restriction Period means the period of time, established by the Committee in connection with an Award of Restricted Stock or Restricted Stock Units, during which the shares of Restricted Stock are subject to a Risk of Forfeiture described in the applicable Award Agreement.

2.28 Risk of Forfeiture means a limitation on the right of the Participant to retain Restricted Stock or Restricted Stock Units, including a right in the Company to reacquire shares of Restricted Stock at less than their then Market Value, arising because of the occurrence or non-occurrence of specified events or conditions.

2.29 Stock means common stock of the Company, and such other securities as may be substituted for Stock pursuant to Section 8.

2.30 Stock Appreciation Right means a right to receive any excess in the Market Value of shares of Stock (except as otherwise provided in Section 7.2(c)) over a specified exercise price.

2.31 Stock Grant means the grant of shares of Stock not subject to restrictions or other forfeiture conditions.

2.32 Ten Percent Owner means a person who owns, or is deemed within the meaning of Section 422(b)(6) of the Code to own, stock possessing more than 10% of the total combined voting power of all classes of stock of the Company (or any parent or subsidiary corporations of the Company, as defined in Sections 424(e) and (f), respectively, of the Code). Whether a person is a Ten Percent Owner shall be determined with respect to an Option based on the facts existing immediately prior to the Grant Date of the Option.

3. Term of the Plan

Unless the Plan shall have been earlier terminated by the Board, Awards may be granted under this Plan at any time in the period commencing on December 7, 2005 and ending immediately prior to December 7, 2015. Awards granted pursuant to the Plan within that period shall not expire solely by reason of the termination of the Plan. Awards of Options granted prior to stockholder approval of the Plan may not be exercised prior to the receipt of such approval.

4. Stock Subject to the Plan

At no time shall the number of shares of Stock issued pursuant to or subject to outstanding Awards granted under the Plan (including pursuant to Incentive Options), nor the number of shares of Stock issued pursuant to Incentive Options, exceed one million one hundred thousand (1,100,000) shares of Stock; *subject, however,* to the provisions of Section 8 of the Plan. For purposes of applying the foregoing limitation, if any Option or Stock Appreciation Right expires, terminates, or is cancelled for any reason without having been exercised in full, or if any other Award is forfeited by the recipient or repurchased at less than its Market Value, the shares not purchased by the Optionee or which are forfeited by the recipient or repurchased shall again be available for Awards to be granted under the Plan. In addition, settlement of any Award shall not count against the foregoing limitations except to the extent settled in the form of Stock.

5. Administration

The Plan shall be administered by the Committee; *provided, however,* that at any time and on any one or more occasions the Board may itself exercise any of the powers and responsibilities assigned the Committee under the Plan and when so acting shall have the benefit of all of the provisions of the Plan pertaining to the Committee's exercise of its authorities hereunder. Subject to the provisions of the Plan, the Committee shall have complete authority, in its discretion, to make or to select the manner of making all determinations with respect to each Award to be granted by the Company under the Plan including the employee, consultant or director to receive the Award and the form of Award. In making such determinations, the Committee may take into account the nature of the services rendered by the respective employees, consultants, and directors, their present and potential contributions to the success of the Company and its Affiliates, and such other factors as the Committee in its discretion shall deem relevant. Subject to the provisions of the Plan, the Committee shall also have complete authority to interpret the Plan, to prescribe, amend and rescind rules and regulations relating to it, to determine the terms and provisions of the respective Award Agreements (which need not be identical), and to make all other determinations necessary or advisable for the administration of the Plan. The Committee's determinations made in good faith on matters referred to in the Plan shall be final, binding and conclusive on all persons having or claiming any interest under the Plan or an Award made pursuant hereto.

6. Authorization of Grants

6.1 Eligibility. The Committee may grant from time to time and at any time prior to the termination of the Plan one or more Awards, either alone or in combination with any other Awards, to

(a) any employee of or consultant to one or more of the Company and its Affiliates (including any such employee or consultant who is also a member of the Board or any board of directors (or similar governing authority) of any Affiliate), and

(b) any non-employee member of the Board or of any board of directors (or similar governing authority) of any Affiliate.

However, only employees of the Company, and of any parent or subsidiary corporations of the Company, as defined in Sections 424(e) and (f), respectively, of the Code, shall be eligible for the grant of an Incentive Option. Further, in no event shall the number of shares of Stock covered by Options or other Awards granted to any one person in any one calendar year exceed 25% of the aggregate number of shares of Stock subject to the Plan.

6.2 General Terms of Awards. Each grant of an Award shall be subject to all applicable terms and conditions of the Plan (including but not limited to any specific terms and conditions applicable to that type of Award set out in the following Section), and such other terms and conditions, not inconsistent with the terms of the Plan, as the Committee may prescribe. No prospective Participant shall have any rights with respect to an Award, unless and until such Participant has executed an agreement evidencing the Award, delivered a fully executed copy thereof to the Company, and otherwise complied with the applicable terms and conditions of such Award.

6.3 Effect of Termination of Employment, Etc. Unless the Committee shall provide otherwise with respect to any Award, if the Participant's employment or other association with the Company and its Affiliates ends for any reason, including because of the Participant's employer ceasing to be an Affiliate, (a) any outstanding Award of the Participant, other than an Option or SAR, shall be forfeited or otherwise subject to return to or repurchase by the Company on the terms specified in the applicable Award Agreement and (b) any outstanding Option or SAR of the Participant shall cease to be exercisable in any respect not later than whichever of the following may apply:

(1) one year following the termination of Optionee's employment or other association with the Company and its Affiliates on account of disability (within the meaning of Section 22(e)(3) of the Code);

(2) one year following the Optionee's death, in the event the Optionee dies while still employed or associated with the Company or its Affiliate or within three (3) months following his or her termination of employment or association; and

(3) unless (1) or (2) applies or becomes applicable, three (3) months (twelve (12) months in the case of nonemployee directors) following his or her termination of employment or association with the Company and its Affiliates for any other reason, including because of the Optionee's employer ceasing to be an Affiliate.

For the period an Option or SAR remains exercisable following any termination of employment or association with the Company and its Affiliates, such Option or SAR shall be exercisable only to the extent exercisable at the date of that event. Military or sick leave or other bona fide leave shall not be deemed a termination of employment or other association, *provided* that it does not exceed the longer of ninety (90) days or the period during which the absent Participant's reemployment rights, if any, are guaranteed by statute or by contract.

6.4 Non-Transferability of Awards. Except as otherwise provided in this Section 6.4, Awards shall not be transferable, and no Award or interest therein may be sold, transferred, pledged, assigned, or otherwise alienated or hypothecated, other than by will or by the laws of descent and distribution. All of a Participant's rights in any Award may be exercised during the life of the Participant only by the Participant or the Participant's legal representative. However, the Committee may, at or after the grant of an Award of a Nonstatutory Option, or shares of Restricted Stock, provide that such Award may be transferred by the recipient to a family member; *provided, however*, that any such transfer is without payment of any consideration whatsoever and that no transfer shall be valid unless first approved by the Committee, acting in its sole discretion. For this purpose, "family member" means any child, stepchild, grandchild, parent,

stepparent, spouse, former spouse, sibling, niece, nephew, mother-in-law, father-in-law, son-in-law, daughter-in-law, brother-in-law, or sister-in-law, including adoptive relationships, any person sharing the employee's household (other than a tenant or employee), a trust in which the foregoing persons have more than fifty (50) percent of the beneficial interests, a foundation in which the foregoing persons (or the Participant) control the management of assets, and any other entity in which these persons (or the Participant) own more than fifty (50) percent of the voting interests.

7. Specific Terms of Awards

7.1 Options.

(a)Date of Grant. The granting of an Option shall take place at the time specified in the Award Agreement. Only if expressly so provided in the applicable Award Agreement shall the Grant Date be the date on which the Award Agreement shall have been duly executed and delivered by the Company and the Optionee.

(b)Exercise Price. The price at which shares of Stock may be acquired under each Option shall be not less than 100% of the Market Value of Stock on the Grant Date, or not less than 110% of the Market Value of Stock on the Grant Date in the case of any Incentive Option granted to an Optionee is a Ten Percent Owner.

(c)Option Period. No Option may be exercised on or after the tenth anniversary of the Grant Date, or on or after the fifth anniversary of the Grant Date in the case of any Incentive Option granted to an Optionee is a Ten Percent Owner.

(d)Exercisability. An Option may be immediately exercisable or become exercisable in such installments, cumulative or non-cumulative, as the Committee may determine. In the case of an Option not otherwise immediately exercisable in full, the Committee may Accelerate such Option in whole or in part at any time; *provided, however*, that in the case of an Incentive Option, any such Acceleration of the Option would not cause the Option to fail to comply with the provisions of Section 422 of the Code or the Optionee consents to the Acceleration.

(e)Method of Exercise. An Option may be exercised by the Optionee giving written notice, in the manner provided in Section 16, specifying the number of shares with respect to which the Option is then being exercised. The notice shall be accompanied by payment in an amount equal to the exercise price of the shares to be purchased in the form of (i) cash or check payable to the order of the Company or (ii) any other lawful means authorized by the Committee (including exercise for the net number of shares available or delivery to the Company of shares of Stock having a Market Value equal to the exercise price of the shares to be purchased). As long as the Stock is traded on an established market, if authorized by the Committee, payment of any exercise price may also be made through and under the terms and conditions of any formal cashless exercise program authorized by the Company entailing the sale of the Stock subject to an Option in a brokered transaction (other than to the Company). Receipt by the Company of such notice and payment in any authorized or combination of authorized means shall constitute the exercise of the Option. Within thirty (30) days thereafter but subject to the remaining provisions of the Plan, the Company shall deliver or cause to be delivered to the Optionee or his agent a certificate or certificates for the number of shares then being purchased. Such shares shall be fully paid and nonassessable.

(f)Limit on Incentive Option Characterization. An Incentive Option shall be considered to be an Incentive Option only to the extent that the number of shares of Stock for which the Option first becomes exercisable in a calendar year do not have an aggregate Market Value (as of the date of the grant of the Option) in excess of the "current limit". The current limit for any Optionee for any calendar year shall be \$100,000 *minus* the aggregate Market Value at the date of grant of the number of shares of Stock available for purchase for the first time in the same year under each other Incentive Option previously granted to the Optionee under the Plan, and under each other incentive stock option previously granted to the Optionee under any other incentive stock option plan of the Company and its Affiliates, after December 31, 1986. Any shares of Stock which would cause the foregoing limit to be violated shall be

deemed to have been granted under a separate Nonstatutory Option, otherwise identical in its terms to those of the Incentive Option.

(g)Notification of Disposition. Each person exercising any Incentive Option granted under the Plan shall be deemed to have covenanted with the Company to report to the Company any disposition of such shares prior to the expiration of the holding periods specified by Section 422(a)(1) of the Code and, if and to the extent that the realization of income in such a disposition imposes upon the Company federal, state, local or other withholding tax requirements, or any such withholding is required to secure for the Company an otherwise available tax deduction, to remit to the Company an amount in cash sufficient to satisfy those requirements.

7.2 Stock Appreciation Rights.

(a)Tandem or Stand-Alone. Stock Appreciation Rights may be granted in tandem with an Option (at or, in the case of a Nonstatutory Option, after, the award of the Option), or alone and unrelated to an Option. Stock Appreciation Rights in tandem with an Option shall terminate to the extent that the related Option is exercised, and the related Option shall terminate to the extent that the tandem Stock Appreciation Rights are exercised.

(b)Exercise Price. Stock Appreciation Rights shall have an exercise price of not less than the Market Value of the Stock on the date of award, or in the case of Stock Appreciation Rights in tandem with Options, the exercise price of the related Option.

(c)Other Terms. Except as the Committee may deem inappropriate or inapplicable in the circumstances, Stock Appreciation Rights shall be subject to terms and conditions substantially similar to those applicable to a Nonstatutory Option. In addition, an SAR related to an Option which can only be exercised during limited periods following a Change of Control may entitle the Participant to receive an amount based upon the highest price paid or offered for Stock in any transaction relating to the Change of Control or paid during the thirty (30) day period immediately preceding the occurrence of the Change of Control in any transaction reported in the stock market in which the Stock is normally traded.

7.3 Restricted Stock.

(a)Purchase Price. Shares of Restricted Stock shall be issued under the Plan for such consideration, in cash, other property or services, or any combination thereof, as is determined by the Committee.

(b)Issuance of Certificates. Each Participant receiving a Restricted Stock Award, subject to subsection (c) below, shall be issued a stock certificate in respect of such shares of Restricted Stock. Such certificate shall be registered in the name of such Participant, and, if applicable, shall bear an appropriate legend referring to the terms, conditions, and restrictions applicable to such Award substantially in the following form:

The transferability of this certificate and the shares represented by this certificate are subject to the terms and conditions of Comarco, Inc. 2005 Equity Incentive Plan and an Award Agreement entered into by the registered owner and Comarco, Inc. Copies of such Plan and Agreement are on file in the offices of Comarco, Inc.

(c)Escrow of Shares. The Committee may require that the stock certificates evidencing shares of Restricted Stock be held in custody by a designated escrow agent (which may but need not be the Company) until the restrictions thereon shall have lapsed, and that the Participant deliver a stock power, endorsed in blank, relating to the Stock covered by such Award.

(d)Restrictions and Restriction Period. During the Restriction Period applicable to shares of Restricted Stock, such shares shall be subject to limitations on transferability and a Risk of Forfeiture arising on the basis of such conditions related to the performance of services, Company or Affiliate performance or otherwise as the Committee may determine and provide for in the applicable Award

Agreement. Any such Risk of Forfeiture may be waived or terminated, or the Restriction Period shortened, at any time by the Committee on such basis as it deems appropriate.

(e) Rights Pending Lapse of Risk of Forfeiture or Forfeiture of Award. Except as otherwise provided in the Plan or the applicable Award Agreement, at all times prior to lapse of any Risk of Forfeiture applicable to, or forfeiture of, an Award of Restricted Stock, the Participant shall have all of the rights of a stockholder of the Company, including the right to vote, and the right to receive any dividends with respect to, the shares of Restricted Stock. The Committee, as determined at the time of Award, may permit or require the payment of cash dividends to be deferred and, if the Committee so determines, reinvested in additional Restricted Stock to the extent shares are available under Section 4.

(f) Lapse of Restrictions. If and when the Restriction Period expires without a prior forfeiture of the Restricted Stock, the certificates for such shares shall be delivered to the Participant promptly if not theretofore so delivered.

7.4 Restricted Stock Units.

(a) Character. Each Restricted Stock Unit shall entitle the recipient to a share of Stock at a close of such Restriction Period as the Committee may establish and subject to a Risk of Forfeiture arising on the basis of such conditions relating to the performance of services, Company or Affiliate performance or otherwise as the Committee may determine and provide for in the applicable Award Agreement. Any such Risk of Forfeiture may be waived or terminated, or the Restriction Period shortened, at any time by the Committee on such basis as it deems appropriate.

(b) Form and Timing of Payment. Payment of earned Restricted Stock Units shall be made in a single lump sum following the close of the applicable Restriction Period. At the discretion of the Committee, Participants may be entitled to receive payments equivalent to any dividends declared with respect to Stock referenced in grants of Restricted Stock Units but only following the close of the applicable Restriction Period and then only if the underlying Stock shall have been earned. Unless the Committee shall provide otherwise, any such dividend equivalents shall be paid, if at all, without interest or other earnings.

7.5 Performance Units.

(a) Character. Each Performance Unit shall entitle the recipient to the value of a specified number of shares of Stock, over the initial value for such number of shares, if any, established by the Committee at the time of grant, at the close of a specified Performance Period to the extent specified Performance Goals shall have been achieved.

(b) Earning of Performance Units. The Committee shall set Performance Goals in its discretion which, depending on the extent to which they are met within the applicable Performance Period, will determine the number and value of Performance Units that will be paid out to the Participant. After the applicable Performance Period has ended, the holder of Performance Units shall be entitled to receive payout on the number and value of Performance Units earned by the Participant over the Performance Period, to be determined as a function of the extent to which the corresponding Performance Goals have been achieved.

(c) Form and Timing of Payment. Payment of earned Performance Units shall be made in a single lump sum following the close of the applicable Performance Period. At the discretion of the Committee, Participants may be entitled to receive any dividends declared with respect to Stock which have been earned in connection with grants of Performance Units which have been earned, but not yet distributed to Participants. The Committee may permit or, if it so provides at grant require, a Participant to defer such Participant's receipt of the payment of cash or the delivery of Stock that would otherwise be due to such Participant by virtue of the satisfaction of any requirements or goals with respect to Performance Units. If any such deferral election is required or permitted, the Committee shall establish rules and procedures for such payment deferrals.

7.6 Stock Grants. Stock Grants shall be awarded solely in recognition of significant contributions to the success of the Company or its Affiliates, in lieu of compensation otherwise already due and in such other limited circumstances as the Committee deems appropriate. Stock Grants shall be made without forfeiture conditions of any kind.

7.7 Qualified Performance-Based Awards.

(a) Purpose. The purpose of this Section 7.7 is to provide the Committee the ability to qualify Awards as “performance-based compensation” under Section 162(m) of the Code. If the Committee, in its discretion, decides to grant an Award as a Qualified Performance-Based Award, the provisions of this Section 7.7 will control over any contrary provision contained in the Plan. In the course of granting any Award, the Committee may specifically designate the Award as intended to qualify as a Qualified Performance-Based Award. However, no Award shall be considered to have failed to qualify as a Qualified Performance-Based Award solely because the Award is not expressly designated as a Qualified Performance-Based Award, if the Award otherwise satisfies the provisions of this Section 7.7 and the requirements of Section 162(m) of the Code and the regulations promulgated thereunder applicable to “performance-based compensation.”

(b) Authority. All grants of Awards intended to qualify as Qualified Performance-Based Awards and determination of terms applicable thereto shall be made by the Committee or, if not all of the members thereof qualify as “outside directors” within the meaning of applicable IRS regulations under Section 162 of the Code, a subcommittee of the Committee consisting of such of the members of the Committee as do so qualify. Any action by such a subcommittee shall be considered the action of the Committee for purposes of the Plan.

(c) Applicability. This Section 7.7 will apply only to those Covered Employees, or to those persons who the Committee determines are reasonably likely to become Covered Employees in the period covered by an Award, selected by the Committee to receive Qualified Performance-Based Awards. The Committee may, in its discretion, grant Awards to Covered Employees that do not satisfy the requirements of this Section 7.7.

(d) Discretion of Committee with Respect to Qualified Performance-Based Awards. Options may be granted as Qualified Performance-Based Awards in accordance with Section 7.1, except that the exercise price of any Option intended to qualify as a Qualified Performance-Based Award shall in no event be less than the Market Value of the Stock on the date of grant. With regard to other Awards intended to qualify as Qualified Performance-Based Awards, such as Restricted Stock, Restricted Stock Units, or Performance Units, the Committee will have full discretion to select the length of any applicable Restriction Period or Performance Period, the kind and/or level of the applicable Performance Goal, and whether the Performance Goal is to apply to the Company, a Subsidiary or any division or business unit or to the individual. Any Performance Goal or Goals applicable to Qualified Performance-Based Awards shall be objective, shall be established not later than ninety (90) days after the beginning of any applicable Performance Period (or at such other date as may be required or permitted for “performance-based compensation” under Section 162(m) of the Code) and shall otherwise meet the requirements of Section 162(m) of the Code, including the requirement that the outcome of the Performance Goal or Goals be substantially uncertain (as defined in the regulations under Section 162(m) of the Code) at the time established.

(e) Payment of Qualified Performance-Based Awards. A Participant will be eligible to receive payment under a Qualified Performance-Based Award which is subject to achievement of a Performance Goal or Goals only if the applicable Performance Goal or Goals period are achieved within the applicable Performance Period, as determined by the Committee. In determining the actual size of an individual Qualified Performance-Based Award, the Committee may reduce or eliminate the amount of the Qualified Performance-Based Award earned for the Performance Period, if in its sole and absolute discretion, such reduction or elimination is appropriate.

(f) Maximum Award Payable. The maximum Qualified Performance-Based Award payment to any one Participant under the Plan for a Performance Period is the number of shares of Stock set forth in

Section 4 above, or if the Qualified Performance-Based Award is paid in cash, that number of shares multiplied by the Market Value of the Stock as of the date the Qualified Performance-Based Award is granted.

(g)Limitation on Adjustments for Certain Events. No adjustment of any Qualified Performance-Based Award pursuant to Section 8 shall be made except on such basis, if any, as will not cause such Award to provide other than “performance-based compensation” within the meaning of Section 162(m) of the Code.

7.8Awards to Participants Outside the United States. The Committee may modify the terms of any Award under the Plan granted to a Participant who is, at the time of grant or during the term of the Award, resident or primarily employed outside of the United States in any manner deemed by the Committee to be necessary or appropriate in order that the Award shall conform to laws, regulations, and customs of the country in which the Participant is then resident or primarily employed, or so that the value and other benefits of the Award to the Participant, as affected by foreign tax laws and other restrictions applicable as a result of the Participant’s residence or employment abroad, shall be comparable to the value of such an Award to a Participant who is resident or primarily employed in the United States. The Committee may establish supplements to, or amendments, restatements, or alternative versions of the Plan for the purpose of granting and administering any such modified Award. No such modification, supplement, amendment, restatement or alternative version may increase the share limit of Section 4.

8. Adjustment Provisions

8.1Adjustment for Corporate Actions. All of the share numbers set forth in the Plan reflect the capital structure of the Company as of the date of the Board’s initial adoption of the Plan. Subject to Section 8.2, if subsequent to that date the outstanding shares of Stock (or any other securities covered by the Plan by reason of the prior application of this Section) are increased, decreased, or exchanged for a different number or kind of shares or other securities, or if additional shares or new or different shares or other securities are distributed with respect to shares of Stock, through merger, consolidation, sale of all or substantially all the property of the Company, reorganization, recapitalization, reclassification, stock dividend, stock split, reverse stock split, or other similar distribution with respect to such shares of Stock, an appropriate and proportionate adjustment will be made in (i) the maximum numbers and kinds of shares provided in Section 4, (ii) the numbers and kinds of shares or other securities subject to the then outstanding Awards, (iii) the exercise price for each share or other unit of any other securities subject to then outstanding Options and Stock Appreciation Rights (without change in the aggregate purchase price as to which such Options or Rights remain exercisable), and (iv) the repurchase price of each share of Restricted Stock then subject to a Risk of Forfeiture in the form of a Company repurchase right.

8.2Treatment in Acquisitions. Subject to any provisions of then outstanding Awards granting greater rights to the holders thereof, in the event of an Acquisition in which outstanding Awards are not Accelerated in full pursuant to Section 9, any then outstanding Awards shall nevertheless Accelerate to the extent not assumed or replaced by the successor or acquiring entity or parent thereof by comparable Awards referencing shares of the capital stock of the successor or acquiring entity or parent thereof, and thereafter (or after a reasonable period following the Acquisition, as determined by the Committee) terminate. As to any one or more outstanding Awards, however, the Committee may also, either in advance of an Acquisition or at the time thereof and upon such terms as it may deem appropriate, provide for the Acceleration of such outstanding Awards or in lieu thereof provide for the termination of the Award in exchange for a cash payment in an amount equal to the difference between the Market Value of the shares of Stock covered by the Award and the aggregated exercise price (if any) of the Award. Each outstanding Award that is assumed in connection with an Acquisition, or is otherwise to continue in effect subsequent to the Acquisition, will be appropriately adjusted, immediately after the Acquisition, as to the number and class of securities and other relevant terms in accordance with Section 8.1.

8.3Dissolution or Liquidation. Upon dissolution or liquidation of the Company, other than as part of an Acquisition or similar transaction, each outstanding Option and SAR shall terminate, but the Optionee or SAR holder (if at the time in the employ of or other associated with the Company or any of its

Affiliates) shall have the right, immediately prior to the dissolution or liquidation, to exercise the Option or SAR to the extent exercisable on the date of dissolution or liquidation.

8.4 Adjustment of Awards Upon the Occurrence of Certain Unusual or Nonrecurring Events. In the event of any corporate action not specifically covered by the preceding Sections, including but not limited to an extraordinary cash distribution on Stock, a corporate separation or other reorganization or liquidation, the Committee may make such adjustment of outstanding Awards and their terms, if any, as it, in its sole discretion, may deem equitable and appropriate in the circumstances.

8.5 Related Matters. Any adjustment in Awards made pursuant to this Section 8 shall be determined and made, if at all, by the Committee and shall include any correlative modification of terms, including of Option exercise prices, rates of vesting or exercisability, Risks of Forfeiture, applicable repurchase prices for Restricted Stock, and Performance Goals and other financial objectives which the Committee may deem necessary or appropriate so as to ensure the rights of the Participants in their respective Awards are not substantially diminished nor enlarged as a result of the adjustment and corporate action other than as expressly contemplated in this Section 8. No fraction of a share shall be purchasable or deliverable upon exercise, but in the event any adjustment hereunder of the number of shares covered by an Award shall cause such number to include a fraction of a share, such number of shares shall be adjusted to the nearest smaller whole number of shares. No adjustment of an Option exercise price per share pursuant to this Section 8 shall result in an exercise price which is less than the par value of the Stock.

9. Change of Control

Except as otherwise provided below, upon the occurrence of a Change of Control:

(a) any and all Options and Stock Appreciation Rights not already exercisable in full shall continue to vest and become exercisable after the Change of Control in accordance with the terms of the Plan and the applicable Award Agreement; *provided, however*, that such Options and Stock Appreciation Rights shall Accelerate in full upon any termination of the Participant's employment or other association with the Company and its Affiliates (or any successor thereto) by the Company or its Affiliate (or any successor), other than for cause, within one year following the Change of Control and;

(b) any Restricted Stock and Restricted Stock Units still subject to a Risk of Forfeiture at the date of the Change of Control which Risk is not based on achievement of Performance Goals shall continue to vest after the Change of Control in accordance with the terms of the Plan and the applicable Award Agreement; *provided, however*, that such Restricted Stock and Restricted Stock Units shall Accelerate in full upon any termination of the Participant's employment or other association with the Company and its Affiliates (or any successor thereto) by the Company or its Affiliate (or any successor), other than for cause, within one year following the Change of Control; and

(c) all outstanding Awards of Restricted Stock and Restricted Stock Units conditioned on the achievement of Performance Goals and the target payout opportunities attainable under outstanding Performance Units shall be deemed to have been satisfied as of the effective date of the Change of Control as to a pro rata number of shares based on the assumed achievement of all relevant Performance Goals and the length of time within the Performance Period which has elapsed prior to the Change of Control and the balance forfeited. All such Awards of Performance Units, Restricted Stock Units shall be paid to the extent earned to Participants in accordance with their terms within thirty (30) days following the effective date of the Change of Control.

None of the foregoing shall apply, however, (i) in the case of a Qualified Performance-Based Award specifically designated as such by the Committee at the time of grant (except to the extent allowed by Section 162(m) of the Code), (ii) in the case of any Award pursuant to an Award Agreement requiring other or additional terms upon a Change of Control (or similar event), or (iii) if specifically prohibited under applicable laws, or by the rules and regulations of any governing governmental agencies or national securities exchanges.

10. Settlement of Awards

10.1 In General. Options and Restricted Stock shall be settled in accordance with their terms. All other Awards may be settled in cash, Stock, or other Awards, or a combination thereof, as determined by the Committee at or after grant and subject to any contrary Award Agreement. The Committee may not require settlement of any Award in Stock pursuant to the immediately preceding sentence to the extent issuance of such Stock would be prohibited or unreasonably delayed by reason of any other provision of the Plan.

10.2 Violation of Law. Notwithstanding any other provision of the Plan or the relevant Award Agreement, if, at any time, in the reasonable opinion of the Company, the issuance of shares of Stock covered by an Award may constitute a violation of law, then the Company may delay such issuance and the delivery of a certificate for such shares until (i) approval shall have been obtained from such governmental agencies, other than the Securities and Exchange Commission, as may be required under any applicable law, rule, or regulation and (ii) in the case where such issuance would constitute a violation of a law administered by or a regulation of the Securities and Exchange Commission, one of the following conditions shall have been satisfied:

(a) the shares are at the time of the issue of such shares effectively registered under the Securities Act of 1933; or

(b) the Company shall have determined, on such basis as it deems appropriate (including an opinion of counsel in form and substance satisfactory to the Company) that the sale, transfer, assignment, pledge, encumbrance or other disposition of such shares or such beneficial interest, as the case may be, does not require registration under the Securities Act of 1933, as amended or any applicable State securities laws.

The Company shall make all reasonable efforts to bring about the occurrence of said events.

10.3 Corporate Restrictions on Rights in Stock. Any Stock to be issued pursuant to Awards granted under the Plan shall be subject to all restrictions upon the transfer thereof which may be now or hereafter imposed by the charter, certificate or articles, and by-laws, of the Company.

10.4 Investment Representations. The Company shall be under no obligation to issue any shares covered by any Award unless the shares to be issued pursuant to Awards granted under the Plan have been effectively registered under the Securities Act of 1933, as amended, or the Participant shall have made such written representations to the Company (upon which the Company believes it may reasonably rely) as the Company may deem necessary or appropriate for purposes of confirming that the issuance of such shares will be exempt from the registration requirements of that Act and any applicable state securities laws and otherwise in compliance with all applicable laws, rules and regulations, including but not limited to that the Participant is acquiring the shares for his or her own account for the purpose of investment and not with a view to, or for sale in connection with, the distribution of any such shares.

10.5 Registration. If the Company shall deem it necessary or desirable to register under the Securities Act of 1933, as amended or other applicable statutes any shares of Stock issued or to be issued pursuant to Awards granted under the Plan, or to qualify any such shares of Stock for exemption from the Securities Act of 1933, as amended or other applicable statutes, then the Company shall take such action at its own expense. The Company may require from each recipient of an Award, or each holder of shares of Stock acquired pursuant to the Plan, such information in writing for use in any registration statement, prospectus, preliminary prospectus or offering circular as is reasonably necessary for that purpose and may require reasonable indemnity to the Company and its officers and directors from that holder against all losses, claims, damage and liabilities arising from use of the information so furnished and caused by any untrue statement of any material fact therein or caused by the omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading in the light of the circumstances under which they were made. In addition, the Company may require of any such person that he or she agree that, without the prior written consent of the Company or the managing underwriter in any public offering of shares of Stock, he or she will not sell, make any short sale of, loan, grant any option for the purchase of, pledge or otherwise encumber, or otherwise dispose of, any shares of Stock during the 180 day period commencing on the effective date of the registration statement relating to the underwritten

public offering of securities. Without limiting the generality of the foregoing provisions of this Section 10.5, if in connection with any underwritten public offering of securities of the Company the managing underwriter of such offering requires that the Company's directors and officers enter into a lock-up agreement containing provisions that are more restrictive than the provisions set forth in the preceding sentence, then (a) each holder of shares of Stock acquired pursuant to the Plan (regardless of whether such person has complied or complies with the provisions of clause (b) below) shall be bound by, and shall be deemed to have agreed to, the same lock-up terms as those to which the Company's directors and officers are required to adhere; and (b) at the request of the Company or such managing underwriter, each such person shall execute and deliver a lock-up agreement in form and substance equivalent to that which is required to be executed by the Company's directors and officers.

10.6 Placement of Legends; Stop Orders; etc. Each share of Stock to be issued pursuant to Awards granted under the Plan may bear a reference to the investment representation made in accordance with Section 10.4 in addition to any other applicable restriction under the Plan and the terms of the Award and to the fact that no registration statement has been filed with the Securities and Exchange Commission in respect to such shares of Stock. All certificates for shares of Stock or other securities delivered under the Plan shall be subject to such stock transfer orders and other restrictions as the Committee may deem advisable under the rules, regulations, and other requirements of any stock exchange upon which the Stock is then listed, and any applicable federal or state securities law, and the Committee may cause a legend or legends to be put on any such certificates to make appropriate reference to such restrictions.

10.7 Tax Withholding. Whenever shares of Stock are issued or to be issued pursuant to Awards granted under the Plan, the Company shall have the right to require the recipient to remit to the Company an amount sufficient to satisfy federal, state, local or other withholding tax requirements if, when, and to the extent required by law (whether so required to secure for the Company an otherwise available tax deduction or otherwise) prior to the delivery of any certificate or certificates for such shares. The obligations of the Company under the Plan shall be conditional on satisfaction of all such withholding obligations and the Company shall, to the extent permitted by law, have the right to deduct any such taxes from any payment of any kind otherwise due to the recipient of an Award. However, in such cases Participants may elect, subject to the approval of the Committee, acting in its sole discretion, to satisfy an applicable withholding requirement, in whole or in part, by having the Company withhold shares to satisfy their tax obligations. Participants may only elect to have Shares withheld having a Market Value on the date the tax is to be determined equal to the minimum statutory total tax which could be imposed on the transaction. All elections shall be irrevocable, made in writing, signed by the Participant, and shall be subject to any restrictions or limitations that the Committee deems appropriate.

11. Reservation of Stock

The Company shall at all times during the term of the Plan and any outstanding Awards granted hereunder reserve or otherwise keep available such number of shares of Stock as will be sufficient to satisfy the requirements of the Plan (if then in effect) and the Awards and shall pay all fees and expenses necessarily incurred by the Company in connection therewith.

12. Limitation of Rights in Stock; No Special Service Rights

A Participant shall not be deemed for any purpose to be a stockholder of the Company with respect to any of the shares of Stock subject to an Award, unless and until a certificate shall have been issued therefor and delivered to the Participant or his agent. Any Stock to be issued pursuant to Awards granted under the Plan shall be subject to all restrictions upon the transfer thereof which may be now or hereafter imposed by the Certificate of Incorporation and the By-laws of the Company. Nothing contained in the Plan or in any Award Agreement shall confer upon any recipient of an Award any right with respect to the continuation of his or her employment or other association with the Company (or any Affiliate), or interfere in any way with the right of the Company (or any Affiliate), subject to the terms of any separate employment or consulting agreement or provision of law or corporate charter, certificate or articles, or by-laws, to the contrary, at any time to terminate such employment or consulting agreement or to increase or decrease, or otherwise adjust, the other terms and conditions of the recipient's employment or other association with the Company and its Affiliates.

13. Unfunded Status of Plan

The Plan is intended to constitute an “unfunded” plan for incentive compensation, and the Plan is not intended to constitute a plan subject to the provisions of the Employee Retirement Income Security Act of 1974, as amended. With respect to any payments not yet made to a Participant by the Company, nothing contained herein shall give any such Participant any rights that are greater than those of a general creditor of the Company. In its sole discretion, the Committee may authorize the creation of trusts or other arrangements to meet the obligations created under the Plan to deliver Stock or payments with respect to Options, Stock Appreciation Rights and other Awards hereunder, *provided, however*, that the existence of such trusts or other arrangements is consistent with the unfunded status of the Plan.

14. Nonexclusivity of the Plan

Neither the adoption of the Plan by the Board nor the submission of the Plan to the stockholders of the Company shall be construed as creating any limitations on the power of the Board to adopt such other incentive arrangements as it may deem desirable, including without limitation, the granting of stock options and restricted stock other than under the Plan, and such arrangements may be either applicable generally or only in specific cases.

15. Termination and Amendment of the Plan

The Board may at any time terminate the Plan or make such modifications of the Plan as it shall deem advisable. Unless the Board otherwise expressly provides, no amendment of the Plan shall affect the terms of any Award outstanding on the date of such amendment.

The Committee may amend the terms of any Award theretofore granted, prospectively or retroactively, provided that the Award as amended is consistent with the terms of the Plan. Also within the limitations of the Plan, the Committee may modify, extend or assume outstanding Awards or may accept the cancellation of outstanding Awards or of outstanding stock options or other equity-based compensation awards granted by another issuer in return for the grant of new Awards for the same or a different number of shares and on the same or different terms and conditions (including but not limited to the exercise price of any Option). Furthermore, the Committee may at any time (a) offer to buy out for a payment in cash or cash equivalents an Award previously granted or (b) authorize the recipient of an Award to elect to cash out an Award previously granted, in either case at such time and based upon such terms and conditions as the Committee shall establish; provided, however, that the per share exercise price of any Option bought out or cashed out shall not be greater than the Market Value of a share of Stock on such date unless the buy out or cash out of such Option is approved by the shareholders of the Company or is otherwise authorized in connection with a Change of Control; and

Notwithstanding the foregoing, however, neither the Board nor the Committee shall reduce the exercise price of any outstanding Option or SAR, or the purchase price of any Restricted Stock, or cancel and reissue any Award at a lower exercise or purchase price, unless such action is approved by the shareholders of the Company or results from the application of the adjustment provisions of Article 8 of the Plan. In addition, no amendment or modification of the Plan by the Board, or of an outstanding Award by the Committee, shall impair the rights of the recipient of any Award outstanding on the date of such amendment or modification or such Award, as the case may be, without the Participant’s consent; *provided, however*, that no such consent shall be required if (i) the Board or Committee, as the case may be, determines in its sole discretion and prior to the date of any Change of Control that such amendment or alteration either is required or advisable in order for the Company, the Plan or the Award to satisfy any law or regulation, including without limitation the provisions of Section 409A of the Code or to meet the requirements of or avoid adverse financial accounting consequences under any accounting standard, or (ii) the Board or Committee, as the case may be, determines in its sole discretion that such amendment or alteration is not reasonably likely to significantly diminish the benefits provided under the Award, or that any such diminution has been adequately compensated.

16. Notices and Other Communications

Any notice, demand, request or other communication hereunder to any party shall be deemed to be sufficient if contained in a written instrument delivered in person or duly sent by first class registered, certified or overnight mail, postage prepaid, or telecopied with a confirmation copy by regular, certified or overnight mail, addressed or telecopied, as the case may be, (i) if to the recipient of an Award, at his or her residence address last filed with the Company and (ii) if to the Company, at its principal place of business, addressed to the attention of its Treasurer, or to such other address or telecopier number, as the case may be, as the addressee may have designated by notice to the addressor. All such notices, requests, demands and other communications shall be deemed to have been received: (i) in the case of personal delivery, on the date of such delivery; (ii) in the case of mailing, when received by the addressee; and (iii) in the case of facsimile transmission, when confirmed by facsimile machine report.

17. Governing Law

The Plan and all Award Agreements and actions taken thereunder shall be governed, interpreted and enforced in accordance with the laws of the State of California without regard to the conflict of laws principles thereof.

**Certification of Chief Executive Officer
Pursuant to Section 302 of the
Sarbanes-Oxley Act of 2002**

I, Samuel M. Inman, III, Chief Executive Officer of Comarco, Inc., certify that:

1. I have reviewed this quarterly report on Form 10-Q of Comarco, Inc.;
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;
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 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 our 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 our 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 our 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 our 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.

Date: December 12, 2008

/s/ Samuel M. Inman, III
Samuel M. Inman, III
Chief Executive Officer

**Certification of Chief Financial Officer
Pursuant to Section 302 of the
Sarbanes-Oxley Act of 2002**

I, Winston E. Hickman, Chief Financial Officer of Comarco, Inc., certify that:

1. I have reviewed this quarterly report on Form 10-Q of Comarco, Inc.;
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;
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 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 our 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 our 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 our 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 our 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.

Date: December 12, 2008

/s/ Winston E. Hickman
Winston E. Hickman
Chief Financial Officer

**Certification of Chief Executive Officer
Pursuant to Section 906 of the
Sarbanes-Oxley Act of 2002**

In connection with this quarterly report on Form 10-Q of Comarco, Inc., I, Samuel M. Inman, III, Chief Executive Officer of Comarco, Inc., certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge:

1. The report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in this report fairly presents, in all material respects, the financial condition and results of operations of Comarco, Inc.

Date: December 12, 2008

/s/ Samuel M. Inman, III
Samuel M. Inman, III
Chief Executive Officer

The foregoing certification is being furnished to the Securities and Exchange Commission as part of the accompanying report on Form 10-Q. A signed original copy of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

**Certification of Chief Financial Officer
Pursuant to Section 906 of the
Sarbanes-Oxley Act of 2002**

In connection with this quarterly report on Form 10-Q of Comarco, Inc., I, Winston E. Hickman, Chief Financial Officer of Comarco, Inc., certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge:

1. The report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in this report fairly presents, in all material respects, the financial condition and results of operations of Comarco, Inc.

Date: December 12, 2008

/s/ Winston E. Hickman

Winston E. Hickman
Chief Financial Officer

The foregoing certification is being furnished to the Securities and Exchange Commission as part of the accompanying report on Form 10-Q. A signed original copy of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

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