

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-KSB

(Mark One)

☒ ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended JUNE 30, 1998  
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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 0-7219  
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GENTNER COMMUNICATIONS CORPORATION  
(Name of small business issuer in its charter)

UTAH  
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87-0398877  
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(State or other jurisdiction of  
incorporation or organization)

(I.R.S. Employer  
Identification No.)

1825 RESEARCH WAY, SALT LAKE CITY, UTAH  
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84119  
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(Address of principal executive offices)

(Zip Code)

Issuer's telephone number (801) 975-7200

Securities registered under Section 12(b) of the Exchange Act:

TITLE OF EACH CLASS -----	NAME OF EACH EXCHANGE ON WHICH REGISTERED -----
None	None

Securities registered under Section 12(g) of the Exchange Act:

COMMON STOCK, \$0.001 PAR VALUE  
(Title of class)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 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 ☐

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B contained in this form, and no disclosure will be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of the Form 10-KSB or any amendment to this Form 10-KSB. ☒

The issuer's revenues for its most recent fiscal year ended June 30, 1998 were \$17,267,886.

The aggregate market value of the voting stock held by non-affiliates is approximately \$10,700,000 at September 1, 1998. This value was computed by reference to the price at which the stock traded (\$1.88) on September 1, 1998 (which date is within 60 days of the filing of this Form 10-KSB).

The number of shares outstanding of the issuer's Common Stock as of September 1, 1998 was 7,750,095.

## PART I

### ITEM 1. BUSINESS

#### OVERVIEW

Gentner Communications Corporation (the "Company") was organized under the laws of the State of Utah on July 8, 1981 as Gentner Engineering Company, Inc. On March 26, 1985, Gentner Engineering Company went public by way of a reverse purchase when a shell corporation, Insular, Inc. (incorporated in Utah on July 8, 1983), acquired Gentner Engineering and changed its name to Gentner Electronics Corporation. On July 1, 1991, Gentner Electronics Corporation changed its name to Gentner Communications Corporation to more accurately reflect the expanding nature of its business.

The Company develops, markets and distributes products for the broadcast, audioconferencing and assistive listening markets. Until 1991, the Company's primary business was the sale of studio and transmitter related equipment to broadcast facilities. Since then, the Company has applied its core digital technology to the development of products for the telecommunications and assistive listening markets. In addition, the Company offers a conference calling service.

The Company initially began selling its products to the telephone interface portion of the broadcast market. This product line is primarily used to put callers on the air for call-in talk shows. Additionally, the Company sells remote facilities management systems that help engineers monitor and control remote transmitter sites for the broadcast market. During fiscal year 1998, the broadcast market accounted for 36% of the Company's total sales.

In 1991, using the technological expertise gained in the broadcast market, the Company commenced marketing products specifically developed for the audioconferencing market. The Company's audio teleconferencing products provide users with a natural, two-way method of conversation without the cut-offs, distortion, and noise associated with traditional speakerphones. Teleconferencing products are installed in conference rooms, courtrooms, and distance learning facilities. In fiscal 1993, the Company enhanced its telecommunication offerings with Gentner Conference Call(SM) (1-800 LETS MEET(R)), a comprehensive conference calling service. Sales of products and services to the teleconferencing market accounted for 51% of the Company's total sales during fiscal 1998.

The Company also has other sources of revenue that account for the remaining 13% of sales, which include assistive listening products, product repair and various other products.

#### BUSINESS STRATEGY

For fiscal year 1999, the Company plans to increase its efforts in the areas of remote facilities management and international business. To accomplish this, it has created two distinct business divisions, Remote Facilities Management and Gentner Products and Services, as well as an international sales and marketing team. Each has undergone extensive research to ensure that its markets offer growth opportunities that are congruent with the Company's overall objectives.

The Remote Facilities Management (RFM) division is focused on increasing the Company's share of the broadcast market as well as expanding RFM product lines into complementary markets such as the communications industry and government services.

The Gentner Products and Services division is responsible for the following areas: Room System Audioconferencers, Assistive Listening Systems, Conference Call Services, and Educational Services. Through this division the Company intends to broaden its product and service offerings in the conferencing market by providing a greater share of technology and service solutions.

The Company's products and services help businesses facilitate group communication, avoid wasted travel time, solve problems through group input, and get faster results. Sales growth is expected to come through growth in conference calling services, new equipment introductions and enhancements, increased international distribution, and an increase in the total number of dealers/distributors.

The Company's international sales and marketing team is dedicated exclusively to the development of a distribution channel of dealers throughout the world. The major product lines promoted in international markets are room system products, telephone interface products and RFM products.

## PRODUCTS AND SERVICES

### Telephone Interface Products

The Company continues to market and develop new products and enhancements for its telephone interface product line. The Company has developed strong brand awareness in this market and has experienced continued sales growth. While domestic growth for telephone interface products is limited by the small size of the market, the international market is expanding and continues to offer strong growth opportunities.

The Company's telephone interface product line offers a full selection of products ranging from simple single-line couplers, which enable users to send and receive audio over a single telephone line, to computerized multiple-line systems used in talk-show programs. An example of the computerized multi-line system is the Company's TS612, which it began selling in fiscal 1995. Using the TS612, talk-show hosts can screen calls, bring callers on-air, conference several callers together, or monitor whether callers are on hold or talking to the show's producer. The Company currently has a 60% share of the domestic telephone interface market, with potential for the largest growth in international markets.

### Remote Site Control Products

RFM products help broadcasters fulfill legal requirements for monitoring and controlling their transmitters, which are often located in remote areas such as on mountaintops. The Company's products provide monitoring of conditions at the transmitter site and permit users to make adjustments to transmitters by remote control. Components of the system offer users the option of monitoring and making such adjustments using either a desktop computer or touch-tone telephone. In fiscal 1997, the Company began shipping the GSC3000 product series. These hardware and software products are designed to augment the Company's existing transmitter site control products by permitting station managers to monitor several different sites using the same equipment. The GSC3000 has enjoyed better-than-expected sales performance.

### Room System Audioconferencing Products

In 1991, the Company applied the digital technology developed in its broadcast telephone products to develop a line of audio teleconferencing products that is used in conference rooms, distance learning facilities and court rooms. These products are used to provide high quality audio teleconferencing, improving the audio quality of speakerphones, video teleconferencing products, and sound systems. The Company's products are used, for example, by the North Carolina and Indiana school systems as the audio portion of their video teleconferencing system in distance learning classes. The Company's products are also used by the Federal Bankruptcy Courts in San Jose for audio teleconferencing and sound reinforcement. The Company has become well known for these types of quality products.

Recently the Company introduced and began shipping a new line of audioconferencing products under the brand name of Audio Perfect(TM). The Audio Perfect(TM) product line currently consists of the AP800, AP10 and AP Tools.

The AP800 is a comprehensive room audio control system designed to excel in the most demanding acoustic environments and routing configurations. Typical applications include hotel and convention center conference rooms, courtrooms, corporate boardrooms and distance learning facilities. It is also used for integrating audio with video conferencing systems.

The AP800 performs the combined functions of several audio devices, including an eight-channel automatic microphone mixer, a 12 X 12 matrix mixer, an audio processor, an equalizer and an audio network controller. It also functions as an echo canceller using a new digital technology called Distributed Echo Cancellation(TM) (D.E.C.). Before D.E.C., only one echo canceller was used to eliminate acoustic echo during a call. With D.E.C., an echo canceller, an equalizer and an audio processor are placed on every microphone input, yielding crystal-clear audio in a greater variety of environments.

The AP10 is used with the AP800 as a telephone interface to connect audioconferencing participants via a telephone line. Each Audio Perfect(TM) system can be expanded to interface with up to eight AP800's and 16 AP10's, providing a network of up to 16 phone lines, 32 line inputs, and 64 microphones, all operating as a single unit.

AP Tools is PC-based software designed to enhance the Audio Perfect(TM) family of products. AP Tools simplifies the set-up, configuration and operation of the Audio Perfect(TM) system by employing a graphic user interface. The graphic orientation provides access to the same features available via the front panel controls of the AP800 and AP10, but does so in a manner that is more user-friendly. AP Tools can control an entire Audio Perfect(TM) system using only one serial connection, and can communicate with AP units both locally and remotely via modem.

The Company believes that its Audio Perfect(TM) product line will provide its customers with significantly better performance with less equipment and complexity. The Company also believes there is a much larger market for its new line of teleconferencing products, particularly when combined with the Company's conference calling service.

#### Assistive Listening Products

In March 1993, the Company began shipping its Assistive Listening System (ALS) products. These products help the Company's customers comply with the Americans with Disabilities Act (ADA) by provide amplified audio for hearing impaired people in public places such as theaters, houses of worship, schools, courtrooms, stadiums and arenas.

#### Conference Calling Service

In February 1993, the Company launched its conference calling service to provide customers with a complete offering of teleconferencing solutions. Gentner Conference Call(SM) (1-800 LETS MEET(R)) can connect many different telephone callers worldwide with superior service and excellent clarity. The Company saw significant growth from this segment during the last fiscal year as a result of hiring a dedicated sales force to target businesses that need conference calling services. The Company believes opportunity exists in pursuing vertical markets for its products and services in conference rooms, distance learning facilities and courtrooms. The Company believes these vertical markets will be responsive to a higher level of quality and service, which it can provide with its premium products and services.

#### MARKETS

##### Teleconferencing Market

The Company believes that there is significant growth potential in the U.S. teleconferencing market. Frost & Sullivan, an international marketing consulting company that publishes market research reports, projects the teleconferencing market to grow to over \$24 billion by 2003.

The teleconferencing market is made up of the audio, video and data conferencing segments. Sales to the audio segment of the market represented approximately 51% of total Company sales in fiscal 1998. During fiscal 1998, the Company entered the data conferencing market by partnering with Broadband Associates, Inc. to add Broadband's "M.Show(TM)" distance presentation service to its portfolio of conference calling services. The Company expects to realize increased revenue from this service during fiscal 1999. Although the Company designs and manufactures audio equipment that works in connection with the videoconferencing segment, it specializes in the audio portion of the teleconferencing market.

Products and services sold by all companies to the teleconferencing market include terminal equipment, telephone bridge equipment, and conference calling services and transmission services. The Company's primary focus is in the terminal equipment and conference calling service categories.

The Company believes that the audioconferencing segment of the teleconferencing market provides significant sales growth potential for the future, and plans to continue providing solutions to businesses and other end users through the sale of teleconferencing equipment and services.

#### Broadcast Market

For fiscal 1998, the broadcast market, which is served by telephone interface and remote facilities management products, generated 36% of the Company's total sales. The Company's products are targeted and sold to radio and television stations, broadcast networks and other professional audio customers.

The Company believes that the worldwide market for its telephone interface and site control products is approximately \$40 million. The Company believes it has a worldwide market share of approximately 15%. The United States is considered to be the predominant segment of the worldwide broadcast market, with over 12,000 radio and television stations in operation. The Company estimates that the U.S. market will grow at an average annual rate of approximately 5%.

The Company's products are sold to upgrade studios and transmitter sites. Although little new broadcast-station construction has taken place in the United States over the past several years (due to the limited number of frequencies that become available at any given time), the Company believes that it will continue to experience growth in the broadcast market through international opportunities and as product innovations allow broadcast stations to upgrade their existing equipment and reduce operating costs.

The Company has also noted a recent organizational shift in the broadcast industry, as an increasing number of stations have come under consolidated ownership and/or management control. The Company expects this trend to continue over the next few years, and believes its broadcast products are especially suited to provide sales growth during this trend as its newer site control products provide centralized monitoring and control of several facilities.

The Company has traditionally concentrated its efforts on selling its products in the United States. However, while the United States is considered to be the largest single broadcast market segment in the world, it is believed to represent only 20% of the total worldwide broadcast market. The international broadcast market is expanding as a result of government deregulation and privatization of stations and the increasing number of frequencies available for commercial use. In 1991, the Company began focusing efforts on expanding its international market share and has appointed dealers located in key areas around the world (see "Description of Business-Distribution"). Such international broadcast sales accounted for 26% of all sales by the Company to the broadcast market in fiscal year 1998.

#### Other Markets

In addition to broadcast and teleconferencing markets, the Company's products are sold into other markets, primarily the professional audio market. The professional audio market includes sound contractors who install audio and other equipment in churches, schools, auditoriums and other large facilities. The Company sells its products into this market generally through the same manufacturers' representatives and dealers that represent the Company in the teleconferencing market. The products sold to this market are primarily the telephone interface products, teleconferencing products and ALS products.

## MARKETING AND SALES

Teleconferencing systems sales efforts are primarily aimed at audio/visual equipment dealers and consultants. These companies, in turn, provide audio solutions to end users in applications such as audio and video corporate boardroom systems, distance learning facilities, telemedicine examination and diagnosis systems, and court rooms. The Company reaches these end users through a sales representative and dealer network that regularly interacts with potential end users in the target market. The Company actively participates alongside this network at communication forums, trade shows and industry promotions. The Company intends to reinforce those efforts and increase sales by remaining involved in the distribution network and to offer training through "Gentner University" (an educational and training setting where dealers can obtain training on the Company's products and services).

Historically, the Company relied on its existing sales force and outside representative network to sell its conference calling service. During fiscal year 1998, the Company continued to increase its direct sales staff in an effort to increase sales for the Company's services and to work in tandem with its dealer network. The Company believes that it has the potential to cross-sell its products and services by partnering with key dealers. The Company believes its strategic advantage is that it can provide higher quality products and services as a package for organizations that require premium, mission critical solutions for their teleconferencing needs.

Additionally, the Company has currently formed, and is pursuing additional, strategic alliances with companies promoting Internet technologies. The Company believes that through these strategic alliances it will not only have the opportunity to sell its own services, but also to re-sell the services of its strategic partners.

Due to the large size of the conferencing market and its potential for intense competition, the marketing of teleconferencing products and services will continue to require substantial marketing resources and research and development efforts. To this end, the Company will continue to seek highly trained and experienced personnel. Additionally, the Company has aggressively focused on research and development to create an expanded and, what the Company believes to be a technologically superior line of products. The Company's strategy continues to be to sell its teleconferencing products through national and international dealers who focus on integrating conferencing facilities for organizations.

Sales efforts for the Company's telephone interface and RFM products focus on the domestic and international sale of these products through a worldwide network of dealers. Such efforts have included a combination of product catalogs, trade shows, telemarketing, direct mail, trade advertising, fax on demand, an Internet Web-page and direct selling. The Company will continue to support dealers with product information, brochures and data sheets, and has been increasing its activities aimed at garnering the attention of end users. The Company will continue to sponsor sales promotions to encourage dealers to feature the Company's products, and will also focus more on end-user interaction efforts. The Company will also continue to exhibit its products at high-profile industry trade shows to ensure that its products remain highly visible to dealers and broadcasters.

## TECHNICAL SUPPORT

Technical support, which is generally conducted over the telephone and sometimes on site, provides timely, interactive help to customers needing operational or technical assistance with their products. The Company's technical support team regularly communicates with the Company's engineering and manufacturing groups to ensure that customer feedback can be directed toward initiating product improvements and incorporated into future products. The technical support team provides a vital role in solving customer problems and building customer confidence. The Company has focused its resources to ensure that strong technical support to its customers remains a competitive advantage.

## WARRANTY AND SERVICE

The Company provides a one-year warranty on its products, which covers both parts and labor. The Company, at its option, repairs or replaces products that are defective during the warranty period if the proper preventative maintenance procedures have been followed by customers. Repairs that are necessitated by misuse of such products or that are required outside the warranty period are not covered by the Company's warranty.

In case of a defective product, the customer typically returns it to the Company's facility in Salt Lake City, Utah. The Company's service personnel then replace or repair the defective item and ship it back to the customer. Generally, all servicing is done at the Company's plant, and the Company charges its customers a fee for those service items that are not covered by warranty. The Company does not offer its customers any formal written service contracts.

## DISTRIBUTION

### Teleconferencing Products

The Company sells its teleconferencing systems and components through independent audio/visual equipment dealers and consultants. The Company also uses a national network of independent sales representatives. Currently, most of the Company's teleconferencing system sales are in the United States. The Company's primary strategy for foreign expansion is to establish dealers and master distributors in markets where it believes there is a growing need for products and services of the type offered by the Company.

The Company distributes products to the professional audio market via this same network of sales representatives and to independent sound contractors. These products include the Company's Assistive Listening Systems (ALS) product line.

### Teleconferencing Services

The Company primarily sells its conference calling service through telemarketing directly to end users, and continues to expand its activities and the number of employees in this area. The Company utilizes this sales force in selling certain teleconferencing products directly to end-users. The Company also sells services through its product dealers and independent representatives and provides wholesale conference calling services to several long distance companies.

### Telephone Interface and Remote Facilities Management Products

The Company's telephone interface and RFM products are generally sold in the United States through non-exclusive, independent broadcast equipment dealers. End users generally place orders with a dealer by calling a toll free number. The market is highly competitive, and it is not unusual for a customer to call several dealers to get the best possible price. Once a customer orders equipment, a dealer orders the product from the Company to be shipped directly to the customer or, in some instances, ships the product to the customer from the dealer's inventory.

The Company's has several dealers that are also manufacturers of communications systems and equipment. The largest of these is the Company's predominant dealer in the Broadcast market and is believed by the Company to be the dominant supplier of equipment for radio stations in the United States. Sales to this dealer represent a significant portion of Company sales, accounting for approximately 7% of the Company's total sales in fiscal 1998, and 12% and 11% during fiscal 1997 and fiscal 1996 respectively. However, the Company believes that if it were to lose this dealer, it could sell its products to end-customers either directly or through other dealers.

With respect to international sales, the Company has established, and continues to establish, international relationships with dealers for its broadcast products in Europe, Canada, Asia, the South Pacific and Latin America.

## COMPETITION

The principal competitive factors in the Company's markets include innovative product design, product quality, established customer relationships, name recognition, distribution and price.

The Company believes that its ability to successfully compete in the teleconferencing market is essential to the Company's growth and development. There are other companies with substantial financial, technical, manufacturing and marketing

resources currently engaged in the development and marketing of similar products and services. Some of these companies have launched products competitive with those being developed and manufactured by the Company. However, the Company has used its core digital technology to produce what it believes to be superior audio teleconferencing systems and equipment. The Company believes it is the only provider of both high-end teleconferencing products and mission critical conference calling services, and feels it can uniquely position itself in the rapidly expanding teleconferencing market.

In the telephone interface and RFM markets, the Company has several competitors in each of its product lines. There is not, however, any single competitor who directly competes with the Company in all such product lines. Although some of the Company's competitors are smaller in terms of annual revenues and capitalization, such competitors usually focus on a single product line. They can therefore devote their resources to products that are directly competitive with, and which may adversely impact sales of, the Company's products. However, the Company's name is well known with respect to its products. This advantage, coupled with the Company's size, will likely enable it to preserve and increase its market share.

#### RESEARCH AND PRODUCT DEVELOPMENT

The Company is highly committed to research and product development. The Company views its investment in research and product development as a key ingredient to long-term business success. The Company expended \$1,142,605, \$1,046,757 and \$929,132 on research and product development in the fiscal years ended June 30, 1998, 1997 and 1996, respectively.

The Company is continually developing new products and services. Current research and product development efforts are focused on the teleconferencing system products, broadcast telephone interface products and enhancements to the RFM product family. The Company also invests resources in refining existing products. Moreover, the Company continues to allocate resources to obtain and maintain product regulatory compliance, both domestically and internationally.

The Company's core technological competencies include many areas of telecommunications and telephone acoustic echo cancellation. The Company's capability to use Digital Signal Processing (DSP) technology to perform audio processing operations is also a core competency. This technology is critical to the performance of the Company's products.

The Company maintains an internal computer aided design (CAD) team. This team creates the necessary electrical schematics, printed circuit board designs, mechanical designs, and manufacturing documentation to support the research and product development efforts. The Company's CAD and product design teams use networked computing systems and sophisticated software programs to facilitate all aspects of product development.

The Company believes that ongoing development of its core technological competencies is vitally important to future sales.

#### PATENT AND PROPRIETARY RIGHTS

Trade secrets, proprietary information, and technical know-how are important to the Company's scientific and commercial success. The Company currently relies on a combination of trade secrets and nondisclosure agreements to establish and protect its proprietary rights in its products.

The Company currently holds a federal registered servicemark for 1-800 LETS MEET(R), and federal registered trademarks for GENTNER(R), and "GENTNER(R)" (as both the name and logo). In addition to these registered servicemarks and trademarks, the Company has federal applications pending for the following trademarks: AUDIO PERFECT(TM), and DISTRIBUTED ECHO CANCELLATION(TM). In addition, the Company has federal applications pending for the following servicemarks: WE PUT THE WORLD ON SPEAKING TERMS(SM), and COMMUNICATION AUDIT PROCESS(SM).



## GOVERNMENT REGULATION

The Company designs and manufactures its equipment in accordance with the technical design standards of the Federal Communications Commission (FCC) Part 15 and Part 68. Part 15 of the FCC Rules governs the levels of electromagnetic radiation emanating from commercial computing equipment. The Company endeavors to conform all of its products covered by Part 15 of the FCC Rules based on testing performed at a FCC approved testing facility. Part 68 of the FCC Rules sets forth standards for telephone equipment that is intended to be connected to the Public Switch Telephone Network (PSTN) used within the United States. The Company's applicable telecommunications products are tested by an independent testing laboratory and are registered with the FCC.

The Company also designs and manufactures its equipment pursuant to industry product safety standards. The Canadian Standards Association (CSA), an approved Nationally Recognized Testing Laboratory (NRTL) under direction of the Occupational Safety and Health Administration (OSHA), tests all products and performs quarterly audits for continuing compliance to applicable safety standards.

Several of the Company's products are currently registered for sale in various international markets. The Company must conform to design standards similar to those of the FCC and CSA in each of the foreign countries in which the products are sold.

## MANUFACTURING

The Company currently manufactures and/or assembles its products using purchased or leased manufacturing equipment. The equipment presently being used will continue to be utilized for several years. The Company's manufacturing facility incorporates modern, modular assembly work stations and work accessories that enhance the efficiency and quality of the manufacturing process. In July 1996, the Company installed a surface-mount assembly line, which has reduced manufacturing costs, and increased production efficiencies and capacity. Toward the end of fiscal 1998, the Company completely overhauled its manufacturing floor process, decreasing the manufacturing cycle time by two-thirds and improving the efficiency of raw materials management. The new process will enable the Company to more effectively meet the demand generated by increasing sales.

If sales continue to increase substantially, the Company may be required to invest in additional manufacturing equipment. Subject to financial considerations, the Company does not believe it would experience any difficulty in obtaining any additional equipment that might be needed as a result of any substantial sales increase (see "Management's Discussion and Analysis--Financial Condition and Liquidity").

The Company generally purchases its assembly components from distributors, but also buys a limited amount directly from local fabricators. Its principal suppliers are Avnet, Arrow Electronics, Bell Industries, Standard Supply Company, Precise Metal Products Company, and Precision Technology.

The Company's general policy is to have a minimum of two vendor sources. Many of the components utilized are bonded by certain distributors and manufacturers. This bonding process places ordered products on the distributors' shelves until the Company requires the products. This allows the Company to reduce its inventory while maintaining available stock.

The Company's ALS products are manufactured in Taiwan and shipped to its facility to complete the packaging before shipping to its customers.

The Company uses a real time computer system to monitor its manufacturing process, which allows the Company to utilize cost accounting for each product and to monitor profitability in each phase of the manufacturing process. The software is covered under a maintenance contract that allows for new version upgrades. The Company has developed an extensive software back-up system that provides for daily back-ups housed in a fireproof safe as well as biweekly backups in an off-site storage facility.

## Telecommunications and Information Systems

The Company has become heavily reliant on its telecommunications and information systems (network) in order to conduct its day-to-day operations. Failure of the network for an extended amount of time could be detrimental to the Company's ongoing business (see "Risk Factors"). As such, the Company is establishing and will continue to develop an infrastructure that can support and enhance growth, reduce down time and improve operational efficiencies. Network features aimed at these objectives include pre-wiring of the Company's building for ease of changes and new installations; several different back-up power sources to guard against power failure; redundant equipment and circuit cards for some equipment; alarm systems and monitoring equipment; and a temperature controlled network room. In addition, the Company backs up its electronic data daily in case of catastrophic failure.

The Company is now focused on making its network fully scalable to accommodate expected growth. Especially noteworthy is that as conference calling service revenues grow, the network structure must expand at the same rate.

## EMPLOYEES

As of June 30, 1998, the Company had 143 employees, all of which were employed on a full-time basis. None of the Company's employees are subject to a collective bargaining agreement.

## ITEM 2. PROPERTIES

All of the Company's operations, including its executive offices, conference call service, product sales, research and development, and manufacturing, are conducted in a 40,000 square-foot facility located south of Salt Lake City (the "Research Way facility"). The Research Way facility is a modern building leased by the Company. The base monthly rent for this facility currently is approximately \$22,400. The facility is in good condition and the Company believes the facility will be reasonably adequate to meet its immediate needs. Monthly rents are scheduled to increase ratably over the next 10 years. The new facilities will allow the Company to grow steadily during this time, as the landlord has granted certain expansion options to the Company with respect to adjacent building space.

## ITEM 3. LEGAL PROCEEDINGS

There are no pending legal proceedings.

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

No matter was submitted to a vote of security holders of the Company during the quarter ended June 30, 1998.

## PART II

## ITEM 5. MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

The Company's common stock is traded in the over-the-counter market on the NASDAQ System under the symbol "GTNR." The following table sets forth quotations for the common stock for the last two fiscal years.

1998 ----	High ----	Low ---
First Quarter	\$1.06	\$0.75
Second Quarter	1.56	0.97
Third Quarter	1.50	0.91
Fourth Quarter	2.75	1.28
1997		
First Quarter	\$1.06	\$0.75
Second Quarter	0.94	0.69
Third Quarter	0.97	0.66
Fourth Quarter	0.78	0.59

The above inter-dealer quotations were obtained from the National Association of Securities Dealers (NASD), do not reflect markups, markdowns, or commissions, and may not represent actual transactions.

As of September 1, 1998, there were approximately 3,500 holders of common stock of the Company.

The Company does not pay a cash dividend and does not anticipate doing so in the foreseeable future. Currently, the Company's line of credit prohibits the payment of dividends. The Company intends to retain earnings for future capital requirements, growth and product development.

## ITEM 6. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

## RESULTS OF OPERATIONS

Year Ended June 30, 1998 Compared to Year Ended June 30, 1997.

Sales for the year ended June 30, 1998 ("fiscal 1998") increased 29% compared to the prior fiscal year ended June 30, 1997. This increase is mainly due to the strong growth of sales in the teleconferencing market, but growth in revenues from the broadcast market also contributed to the increase.

Revenues from the teleconferencing market increased 67% during fiscal 1998 as compared to fiscal 1997. Product sales increased 55% mainly due to the introduction of the Audio Perfect(TM) product line and an increase in the sales of GT724 audio conferencing systems. The Audio Perfect(TM) product line began shipping in April of 1998. These products use a new digital technology called Distributed Echo Cancellation(TM) and incorporate several functional devices including automatic microphone mixing, echo cancellation, audio routing, audio equalization and audio processing into a single device. The Company will get more of the revenue associated with a room installation as a result of the expanded applications. The Company's conference calling service, 1-800 LETS MEET(SM), experienced sales growth of 117% for fiscal 1998 as compared to fiscal 1997. This growth is a result of the Company expanding its

sales staff, who are aggressively marketing its conference calling service. This service is being marketed not only to corporate clients, but also to long distance telephone service providers for resale.

Sales in the broadcast market grew 7% in fiscal 1998 compared to the previous fiscal year. In this market, Remote Facilities Management (formerly known as Remote Site Control) grew significantly (36%), mainly due to large sales of the GSC3000. The GSC3000 allows broadcasters to monitor and control many transmitter sites from one location. Sales to the television market and the introduction of the Voice Interface also contributed to the increased sales of the GSC3000. The Voice Interface allows an engineer to call the remote equipment from any telephone, check on its status, and make adjustment using only the telephone. Sales to Telephone Interface customers dropped slightly (4%). Even though domestic sales of Telephone Interface products dropped, international sales are showing strong growth with a 51% increase in fiscal 1998 sales compared to fiscal 1997.

During fiscal 1998, sales of products that are not in either the Broadcast or Teleconferencing markets ("Other Products") changed less than 1%. Within Other Products, sales of Assistive Listening Systems ("ALS") increased 23%. Non-ALS Other Products sales declined, and are expected to continue to decline.

The Company's gross profit margin increased to 52% in fiscal 1998. It was 48% in fiscal 1997. This increase is primarily due to price increases at the beginning of this fiscal year, aggressive vendor pricing, new products with higher gross profit margins, a different product mix and increased efficiencies in the manufacturing process.

The Company's operating expenses increased 10% when comparing fiscal 1998 to fiscal 1997. Most of the increase in operating expenses came in the General and Administrative area. Product Development expenses also increased.

General and Administrative expenses increased 23% in fiscal 1998 as compared to the previous fiscal year. The one-time expense of the severance package of the former CEO contributed to the increase. Facility expenses also increased as a result of moving into a larger facility in November of 1996.

Sales and Marketing expenses for fiscal 1998 only increased 2% from fiscal 1997. A major expense increase in this area came from commissions, which was a direct result of increased sales. However, this was offset from the Company reducing other expenses by bringing all advertising development in house and closely monitoring other advertising expenses.

Product Development costs increased 9% in fiscal 1998 as compared to fiscal 1997. This was mainly due to increased personnel and product compliance activities. The Company increased R&D personnel so that each engineer can specialize in a specific product area. The Company believes it will improve the development cycle by having specialized engineers.

Interest expense increased 23% when comparing fiscal 1998 to fiscal 1997 due to increased debt balances used to finance the facility expansion.

Year Ended June 30, 1997 Compared to Year Ended June 30, 1996.

Sales for the year ended June 30, 1997 ("fiscal 1997") increased 17% compared to the prior fiscal year ended June 30, 1996. This increase is due to the Company focusing on its core businesses: Teleconferencing products and services, Remote Facilities Management and Telephone Interface products.

Product and conference calling service revenues to the teleconferencing market increased 29% during fiscal year 1997 as compared to fiscal year 1996. Product sales increased 20% primarily due to sales of the GT724 audio teleconferencing system. The Company started shipping this product in the beginning of the fiscal year and sales have remained strong during the entire year. The GT724 system is used in conference rooms, distance learning facilities and courtrooms. The Company's conference calling service increased 93% in fiscal year 1997 over fiscal 1996. This significant increase is due to the Company hiring a dedicated, direct sales force and due to aggressive marketing campaigns during the year. The Company is focused on providing premium, mission critical conference calling services for conference rooms, distance learning facilities and courtrooms.

Sales in the broadcast market grew 20% in fiscal year 1997 as compared to fiscal year 1996. In the Telephone Interface segment, the Company introduced a new product line late in the fiscal year, unveiling the new digital hybrid line at the National Association of Broadcasters show in April 1997. Shipments began in June 1997. Remote Facilities Management sales grew significantly when the Company began shipping the GSC3000 Remote Facilities Management product line in November 1996. The GSC3000 monitors and adjust settings at one or more remote transmitter sites, or an engineer can adjust the settings via a personal computer. Historically, the Company's Remote Facilities Management products have sold primarily in the radio market, but the GSC3000 has been accepted in the television market, resulting in increased sales.

During fiscal 1997, other product sales experienced a 37% decrease as compared to fiscal 1996 as the Company's primary focus was on its core business lines. The Company stopped selling Audio Processing products and has seen decreased sales in the audio routing and distribution and portable teleconferencing products. The Company believes these product lines have taken focus and resources away from its core businesses and expects to see these continue to decline.

The Company's gross profit margin increased to 48% in fiscal 1997 as compared to 45% in fiscal 1996. This improvement in gross profit margin can be attributed to higher margin product mix, product pricing and the in-house surface mount manufacturing technology the Company began using in fiscal 1997. The Company continues to work towards increasing its gross profit margin. For products, the Company has recently increased prices and is working to reduce actual manufacturing costs. However, the Company's conference calling service has a lower gross profit margin, which, as it becomes a higher percentage of total sales, could negatively impact the Company's overall gross profit margin.

For the year ending June 30, 1997, the Company's operating expenses increased 40% compared to the previous fiscal year. As previously reported, the Company invested significantly in its infrastructure during fiscal 1997 in an effort to prepare for future growth. Sales and Marketing expenses increased 49%, General and Administrative expenses increased 43% and Product Development expenses increase 13% when comparing fiscal 1997 to fiscal year 1996.

The Company underwent some significant changes in its Sales and Marketing area in fiscal 1997. It hired its first Vice President of Sales and Marketing to focus specifically on increasing sales. The Company also hired a direct sales force to sell its conference calling service, incurred one time marketing expenses regarding its conference calling service, hired internal marketing people and invested significantly in market research prior to developing new products. All these events contributed to the increase in sales and marketing expenses and the Company believes these initiatives will help sustain long-term sales growth.

General and Administrative expenses increased 43% in fiscal 1997 as compared to fiscal 1996. Most of this increase is due to the Company expanding its facility, doubling the square footage. Occupancy costs increased significantly, as well as other costs associated with expanding operations (human resources and information systems management). The Company feels this investment in the infrastructure will sustain long term growth as it moves forward.

During fiscal 1997, Product Development expenses increased 13% as compared to fiscal 1996. This increase is a result of hiring additional engineers to focus on specific product areas. The Company also expended significant resources in developing new teleconferencing and site control products.

Interest expense increased 6% when comparing fiscal 1997 to fiscal 1996 due to increased borrowing requirements to fund growth. This increased borrowing occurred toward the end of the fiscal year when the Company finalized the financing required for the facility expansion.

#### FINANCIAL CONDITION AND LIQUIDITY

The Company's financial condition grew stronger in fiscal year 1998. The Company's current ratio was 3.0:1 at the end of fiscal 1998 as compared to 2.2:1 at the end of fiscal 1997. Inventories increased 18% and accounts receivable increased 4% during fiscal 1998 as a result of higher sales. Cash on hand increased due to strong positive cash flows from operations. These changes all contribute to the financial strength of the Company.

The Company has an outstanding revolving line of credit of \$2.0 million, which is secured by the Company's accounts receivable and inventory. The interest rate on the line of credit is a variable interest rate (anywhere from three to five percentage points over the London Interbank Offered Rate (LIBOR)). There was no outstanding balance on June 30, 1998. The line of credit expires in December of 1998.

As described in the notes to the financial statements, the Company has certain commitments relating to capital expenditures. These commitments are in the form of obligations classified as long-term debt and capital leases, both related to the financing of furniture and equipment. Together, the current obligation on these commitments was \$639,214 in fiscal 1998 and will be \$625,459 in fiscal 1999.

The Company continued to experience positive cash flows in fiscal 1998. Higher sales and closely managing the operating expenses provided positive operational cash flows for the Company. As sales continue to increase, the Company anticipates that it can achieve its business plan through a combination of internally generated funds and short-term and/or long-term borrowing, if necessary.

#### FORWARD LOOKING STATEMENTS AND RISK FACTORS

To the extent any statement presented herein deals with information that is not historical, such statement is necessarily forward looking. As such, it is subject to occurrence of many events outside of the Company's control. These occurrences could cause the Company's results to differ materially from those anticipated. A sample listing of such occurrences follows:

##### Competition - Rapid Technological Change

The Broadcast, Teleconferencing and ALS markets are highly competitive and characterized by rapid technological change. The Company's future performance will depend in large part upon its ability to remain competitive and to develop and market new products and services in these markets. The Company competes with businesses having substantial financial, research and development, manufacturing, marketing and other resources.

The markets in which the Company competes have historically involved the introduction of new and technologically advanced products and services that cost less or perform better. If the Company is not competitive in its research and development efforts, its products may become obsolete or be priced above competitive levels.

Although management believes that based on their performance and price, its products are attractive to customers, there can be no assurance that competitors will not introduce comparable or technologically superior products, which are priced more favorably than the Company's products.

##### Marketing

The Company has experience in marketing its products. However, it is subject to all of the risks inherent in the sale and marketing of current and new products and services in an evolving marketplace. The Company must effectively allocate its resources to the marketing and sale of these products through diverse channels of distribution. The Company's strategy is to establish distribution channels and direct selling efforts in markets where it believes there is a growing need for its products and services. There can be no assurance that this strategy will prove successful.

##### Dependence on Distribution Network

The Company markets its products primarily through a network of representatives, dealers and master distributors. All of the Company's agreements retaining such representatives and dealers are non-exclusive and terminable at will by either party. Although the Company believes that its relationships with such representatives and dealers are good, there can be no assurance that any of such representatives or dealers will continue to offer the Company's products.

Price discounts are based on performance. However, there are no obligations on the part of such representatives and dealers to provide any specified level of support to the Company's products or to devote any specific time, resources or efforts to the marketing of the Company's products. There are no prohibitions on dealers offering products that are competitive with those of the Company. Most dealers do offer competitive products. The Company reserves the right to maintain house accounts, which are for products sold direct. The loss of a majority or all representatives or dealers could have a material adverse effect on the Company's business.

#### Limited Capitalization

As of June 30, 1998, the Company had \$715,325 in cash and \$3,908,943 in working capital. The Company may be required to seek additional financing if anticipated levels of revenue are not realized, if higher than anticipated costs are incurred in the development, manufacture or marketing of the Company's products, or if product demand exceeds expected levels. There can be no assurance that any additional financing thereby necessitated will be available on acceptable terms, or at all.

In addition, the Company's revolving \$2 million line of credit matures in December of 1998 and there can be no assurance that the Company will be able to extend the maturity date of the line of credit or obtain a replacement line of credit from another commercial institution. The Company had no outstanding balance payable on the line of credit as of June 30, 1998. To the extent the line of credit is not extended or replaced and cash from operations is unavailable to pay the indebtedness then outstanding under the line of credit, the Company may be required to seek additional financing.

#### Telecommunications and Information Systems (Network)

The Company is highly reliant on its network equipment, data and software to support all functions of the Company. The Company's conference calling service relies 100% on the network for its revenues. While the Company endeavors to provide for failures in the network by providing back up systems and procedures, there is no guarantee that these back up systems and procedures will operate satisfactorily in an emergency. Should the Company experience such a failure, it could seriously jeopardize its ability to continue operations. In particular, should the Company's conference calling service experience even a short term interruption of its network, its ongoing customers may choose a different provider.

#### Dependence Upon Key Employees

The Company is substantially dependent upon certain of its employees, including Frances M. Flood, a Director, President and Chief Executive Officer and a stockholder of the Company. The loss of Ms. Flood by the Company could have a material adverse effect on the Company. The Company currently has in place a key person life insurance policy on the life of Ms. Flood in the amount of \$1,000,000.

The Company is also dependent upon Brooks Gibbs, Director of Technology. Due to his technological expertise and product familiarity, the loss of Mr. Gibbs by the Company could have a material adverse effect on the Company. The Company currently has in place a key person life insurance policy on the life of Mr. Gibbs in the amount of \$1,000,000.

#### Dependence on Supplier and Single Source of Supply

The Company does not have written agreements with any suppliers. Furthermore, certain digital microprocessor chips used in connection with the Company's products can only be obtained from a single manufacturer and the Company is dependent upon the ability of this manufacturer to deliver such chips to the Company's suppliers so that they can meet the Company's delivery schedules. The Company does not have a written commitment from such suppliers to fulfill the Company's future requirements. The Company's suppliers maintain an inventory of such chips, but there can be no assurance that such chips will always be readily available, available at reasonable prices, available in sufficient quantities, or deliverable in a timely fashion. If such chips or other key components become unavailable, it is likely that the Company will experience delays, which could be significant, in production and delivery of its products unless and until the Company can otherwise procure the required component or components at competitive prices, if at all. The lack of availability of these components could have a materially adverse effect on the Company.

Although the Company believes that most of the key components required for the production of its products are currently available in sufficient production quantities, there can be no assurance that they will remain available. Furthermore, suppliers of some of these components are currently or may become competitors of the Company, which might also affect the availability of key components to the Company. It is possible that other components required in the future may necessitate custom fabrication in accordance with specifications developed or to be developed by the Company. Also, in the event the Company, or any of the manufacturers whose products the Company expects to utilize in the manufacture of its products, is unable to develop or acquire components in a timely fashion, the Company's ability to achieve production yields, revenues and net income will be adversely affected.

#### Lack of Patent Protection

The Company currently relies on a combination of trade secret and nondisclosure agreements to establish and protect its proprietary rights in its products. There can be no assurance that others will not independently develop similar technologies, or duplicate or design around aspects of the Company's technology. The Company believes that its products and other proprietary rights do not infringe any proprietary rights of third parties. There can be no assurance, however, that third parties will not assert infringement claims in the future.

#### Government Funding and Regulation

In the teleconferencing market, the Company is dependent on government funding to place its distance learning sales and courtroom equipment sales. In the event government funding was stopped, these sales would be negatively impacted. Additionally, many of the Company's products are regulated by governmental regulations. New regulations could significantly impact sales.

#### Dividends Unlikely

The Company has never paid cash dividends on its securities and does not intend to declare or pay cash dividends in the foreseeable future. Earnings are expected to be retained to finance and expand its business. Furthermore, the Company's revolving line of credit prohibits the payment of dividends on its Common Stock.

#### Potential Dilutive Effect of Outstanding Options and Possible Negative Effect of Future Financing

The Company has outstanding options. The outstanding options are issued under the Company's 1990 Incentive Plan and the 1998 Stock Option Plan, which includes options to purchase up to 1,700,000 shares of Common Stock granted or available for grant. Holders of these options are given an opportunity to profit from a rise in the market price of the Company's Common Stock with a resulting dilution in the interests of the other stockholders. The holders of the options may exercise them at a time when the Company might be able to obtain additional capital through a new offering of securities on terms more favorable than those provided therein.

#### Possible Control by Officers and Directors

The officers and directors of the Company together had beneficial ownership of approximately 24.6% of the Common Stock (including options that are currently exercisable or exercisable within sixty (60) days) of the Company as of September 1, 1998. This significant holding in the aggregate place the officers and directors in a position, when acting together, to effectively control the Company (see "Security Ownership of Certain Beneficial Owners and Management").

#### Year 2000

The Company is continuing to assess the impact of the Year 2000 issue\* on its information technology ("IT") and non-IT systems and believes that certain software and hardware currently in use will have to be upgraded. To date, the Company has assessed approximately 100% of its existing IT systems and 80% of its existing non-IT systems. The Company estimates a cost of \$50,000 to upgrade existing systems so that they are Year 2000 compatible. None of that cost has been incurred so far. To date, the Company has identified two of its systems that will have to be upgraded. None of these upgrades have taken place yet, but all upgrades are scheduled for completion by November 30, 1998. There should be no



significant interruptions to the business caused by the upgrade process. However, if these upgrades are not completed in a timely manner, the impact on the operations of the Company could be material. The Company plans to finance these upgrades with operating income.

The first system so far identified as requiring upgrading is the internal phone system, including the voice mail system. The software and hardware to upgrade this system will be purchased so that the system will be upgraded to meet a scheduled completion date of the end of October of 1998. The estimated cost of this software and hardware is \$50,000. The second system identified to date is the conference calling bridge. This system is essential to the Company's conference calling service. It is scheduled for upgrading in November of 1998. The manufacturer is furnishing the software to the Company at no cost.

The Company is in the process of determining through direct contacts whether its material vendors and suppliers, and its larger customers are Year 2000 compliant. To date, no major customer or supplier that the Company contacted has any Year 2000 compliance problems that would significantly impact the operations of the Company.

At the present time, the company believes that a reasonably likely worst case scenario involving a Year 2000 event would be in a non-IT system affecting the Company's manufacturing process. Such an event could result in the suspension of the affected portion of the manufacturing process until such a problem is corrected. However, the Company believes that as it continues its Year 2000 assessment the risk of such an event will decrease.

The Company currently is in the process of developing contingency plans for dealing with Year 2000 issues, including the worst case scenario just described. Those plans are scheduled to be complete and in place by the end of fiscal 1999.

The Company has performed a Year 2000 compliance review of its product line. To date, the company has addressed all existing Year 2000 compliance issues on products.

The costs of the projects and the dates on which the Company believes it will complete the Year 2000 upgrades are based on management's best estimates at this time, which were derived utilizing numerous assumptions of future events, including the continued availability of certain resources and other factors. However, there can be no guarantees that these estimates will be achieved, that personnel trained in this area will be available at a reasonable cost, or that we will locate and correct all relevant computer codes and similar uncertainties.

\* The "Year 2000 Problem" has arisen because many computer programs were written using only the last two digits to refer to a year (i.e. "98" for 1998). Therefore, these computer programs may not properly recognize the year 2000. If not corrected, many computer applications could fail or create erroneous results.

#### New Accounting Pronouncements

In 1997, the Financial Accounting Standards Board ("FASB") issued SFAS No. 128, "Earnings per Share." SFAS 128 replaced the calculation of primary and fully diluted earnings (loss) per share with basic and diluted earnings (loss) per share. Unlike primary earnings (loss) per share, basic earnings (loss) per share excludes any dilutive effects of options, warrants and convertible securities. Diluted earnings (loss) per share is very similar to the previously reported fully diluted earnings (loss) per share. All earnings (loss) per share amounts for all periods have been presented, and where appropriate, restated to conform to the SFAS 128 requirements.

In June 1997, FASB issued SFAS No. 130, "Reporting Comprehensive Income", which established standards for reporting and display of "Comprehensive Income" which is the total of net income and all other non-owner changes in stockholders' equity and its components. SFAS 130 is effective for fiscal years beginning after December 15, 1997 with earlier application permitted. The Company will adopt the standard in fiscal 1999 and does not expect comprehensive income it differ significantly from previously reported net income.

In June 1997, the FASB also issued SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information." SFAS 131, which supersedes SFAS Nos. 14, 18, 24 and 30, establishes new standards for segment reporting in which reportable segments are based on the same criteria on which management disaggregates a business for making operating decisions and assessing performance. SFAS 131 is effective for fiscal years beginning after December 15, 1997 with earlier application permitted. The Company will adopt the standard in fiscal 1999 and is currently analyzing the impact this new standard will have on previously reported information.

## ITEM 7. FINANCIAL STATEMENTS

### Index to Financial Statements

Report of Independent Auditors

Balance Sheets for June 30, 1998 and 1997.

Statements of Operations for fiscal years ended June 30, 1998, 1997 and 1996.

Statements of Cash Flows for fiscal years ended June 30, 1998, 1997 and 1996.

Statements of Shareholders' Equity for fiscal years ended June 30, 1998, 1997 and 1996.

Notes to Financial Statements

## Report of Independent Auditors

The Board of Directors and Shareholders  
GENTNER COMMUNICATIONS CORPORATION

We have audited the accompanying balance sheets of Gentner Communications Corporation as of June 30, 1998 and 1997, and the related statements of operations, shareholders' equity, and cash flows for each of the three years in the period ended June 30, 1998. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Gentner Communications Corporation at June 30, 1998 and 1997, and the results of its operations and its cash flows for each of the three years in the period ended June 30, 1998, in conformity with generally accepted accounting principles.

/s/ Ernst & Young, L.L.P.

Salt Lake City, Utah  
July 31, 1998

## GENTNER COMMUNICATIONS CORPORATION

## BALANCE SHEETS

	June 30,	
	1998	1997
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents .....	\$ 715,325	\$ 63,992
Accounts receivable, less allowances of \$246,000 in 1998, and \$115,000 in 1997 .....	1,743,390	1,682,254
Inventory .....	3,154,983	2,668,761
Deferred taxes .....	40,000	--
Other current assets .....	174,667	136,177
Total current assets .....	5,828,365	4,551,184
Property and equipment, net .....	2,320,336	2,493,287
Related party note receivable .....	126,505	139,000
Other assets, net .....	36,534	152,383
Total assets .....	\$ 8,311,740	\$ 7,335,854
	=====	=====
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current liabilities:		
Notes payable .....	\$ --	\$ 722,997
Accounts payable .....	537,202	471,072
Accrued compensation and other benefits .....	486,658	197,209
Other accrued expenses .....	372,823	159,237
Current portion of long-term debt .....	285,630	257,164
Current portion of capital lease obligations .....	237,109	254,951
Total current liabilities .....	1,919,422	2,062,630
Long-term debt .....	402,584	687,274
Capital lease obligations .....	752,728	784,354
Total liabilities .....	3,074,734	3,534,258
Shareholders' equity:		
Common stock, 50,000,000 shares authorized, par value \$.001, 7,698,523 and 7,663,405 shares issued and outstanding at June 30, 1998 and 1997 .....	7,699	7,663
Additional paid-in capital .....	4,454,407	4,423,482
Retained earnings (accumulated deficit) .....	774,900	(629,549)
Total shareholders' equity .....	5,237,006	3,801,596
Total liabilities and shareholders' equity .....	\$ 8,311,740	\$ 7,335,854
	=====	=====

See accompanying notes

## GENTNER COMMUNICATIONS CORPORATION

## STATEMENTS OF OPERATIONS

	Years ended June 30,		
	1998	1997	1996
Net Sales .....	\$ 17,267,886	\$ 13,371,851	\$ 11,469,155
Cost of goods sold .....	8,347,300	6,874,590	6,279,775
Gross profit .....	8,920,586	6,497,261	5,189,380
Operating expenses:			
Marketing and selling .....	3,649,876	3,572,882	2,394,415
General and administrative .....	2,470,949	2,006,998	1,406,786
Research and product development .....	1,142,605	1,046,757	929,132
Total operating expenses .....	7,263,430	6,626,637	4,730,333
Operating income (loss) .....	1,657,156	(129,376)	459,047
Other income (expense):			
Interest income .....	13,475	7,836	1,988
Interest expense .....	(240,371)	(196,176)	(185,676)
Other, net .....	13,189	(18,282)	7,525
Total other income (expense) .....	(213,707)	(206,622)	(176,163)
Income (loss) before income taxes .....	1,443,449	(335,998)	282,884
Provision for income taxes .....	39,000	36,900	900
Net income (loss) .....	\$ 1,404,449	\$ (372,898)	\$ 281,984
	=====	=====	=====
Basic earnings (loss) per common share .....	\$ 0.18	\$ (0.05)	\$ 0.04
	=====	=====	=====
Diluted earnings (loss) per common share ...	\$ 0.18	\$ (0.05)	\$ 0.04
	=====	=====	=====

See accompanying notes

## GENTNER COMMUNICATIONS CORPORATION

## STATEMENT OF CASH FLOWS

	Years ended June 30,		
	1998	1997	1996
Cash flows from operating activities:			
Net income (loss) .....	\$ 1,404,449	\$ (372,898)	\$ 281,984
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Depreciation and amortization of property and equipment .....	678,501	621,024	513,781
Amortization of other assets .....	41,383	52,654	41,258
Deferred income tax .....	(40,000)	--	--
Gain (loss) on investments .....	(1,785)	21,378	(36,895)
Other .....	--	36,000	21,339
Changes in operating assets and liabilities:			
Accounts receivable .....	(61,136)	(125,818)	87,940
Inventory .....	(486,222)	561,004	95,101
Other current assets .....	(38,490)	(24,434)	(31,975)
Accounts payable and other accrued expenses ....	569,165	29,621	(443,252)
Net cash provided by operating activities ....	2,065,865	798,531	529,281
Cash flows from investing activities:			
Purchases of property and equipment .....	(313,050)	(623,949)	(176,743)
Issuance of note receivable .....	--	(147,327)	--
Repayment of note receivable .....	12,495	8,327	60,320
Decrease (increase) in other assets .....	76,251	(108,541)	139
Net cash used in investing activities .....	(224,304)	(871,490)	(116,284)
Cash flows from financing activities:			
Proceeds from issuance of common stock .....	3,366	736	--
Exercise of warrants and employee stock options .....	27,595	--	142,313
Net borrowings (repayments) under line of credit .....	(722,997)	(193,044)	(308,959)
Net financing of trade payables with short-term notes .....	--	--	(283,687)
Proceeds from issuance of long-term debt .....	--	566,906	400,000
Principal payments of capital lease obligations .....	(241,968)	(238,378)	(135,825)
Principal payments of long-term debt .....	(256,224)	(213,032)	(132,314)
Net cash used in financing activities .....	(1,190,228)	(76,812)	(318,472)
Net increase (decrease) in cash .....	651,333	(149,771)	94,525
Cash at the beginning of the year .....	63,992	213,763	119,238
Cash at the end of the year .....	\$ 715,325	\$ 63,992	\$ 213,763
	=====	=====	=====
Supplemental disclosure of cash flow information:			
Property and equipment financed by capital leases ....	\$ 192,500	\$ 975,732	\$ 25,490
Income taxes paid .....	\$ (28,000)	\$ (12,800)	\$ (25,900)
Interest paid .....	\$ (241,371)	\$ (193,500)	\$ (194,148)

See accompanying notes

GENTNER COMMUNICATIONS CORPORATION  
STATEMENTS OF SHAREHOLDERS' EQUITY

	Common Stock		Additional Paid-In Capital	Retained Earnings (Accumulated Deficit)	Total Shareholder's Equity
	Shares	Amount			
Balances at June 30, 1995 .....	7,455,375	\$ 7,455	\$4,244,641	\$ (538,635)	\$3,713,461
Exercise of employee stock options .....	207,000	207	142,106	--	142,313
Tax benefits allocated to contributed capital .....	--	--	36,000	--	36,000
Net income .....	--	--	--	281,984	281,984
Balances at June 30, 1996.....	7,662,375	7,662	4,422,747	(256,651)	4,173,758
Issuance of common stock .....	1,030	1	735	--	736
Net loss .....	--	--	--	(372,898)	(372,898)
Balances at June 30, 1997.....	7,663,405	7,663	4,423,482	(629,549)	3,801,596
Exercise of employee stock options .....	32,000	32	27,563	--	27,595
Issuance of common stock .....	3,118	4	3,362	--	3,366
Net income .....	--	--	--	1,404,449	1,404,449
Balances at June 30, 1998 .....	7,698,523	\$ 7,699	\$ 4,454,407	\$ 774,900	\$5,237,006
	=====	=====	=====	=====	=====

See accompanying notes

## GENTNER COMMUNICATIONS CORPORATION

## NOTES TO FINANCIAL STATEMENTS

## 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

## ORGANIZATION

Gentner Communications Corporation (the "Company"), designs and manufactures high-technology electronic equipment for the Teleconferencing, Telephone Interface and Remote Facilities Management markets. The Company also provides domestic and international conference calling services. The Company grants credit without requiring collateral to substantially all its customers within these markets.

## SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Cash Equivalents - The Company considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents.

Inventory - Inventories are stated at the lower of cost (first-in, first-out) or market.

Revenue Recognition - Revenue from product sales is recognized at the time product is shipped, net of allowances for returns and uncollectible accounts. Revenue from service sales is recognized at the time the service is rendered, net of allowances for uncollectible accounts.

Property and Equipment - Property and equipment are stated at cost. Depreciation and amortization are provided over the estimated useful lives of the respective assets using the straight-line method. In fiscal 1997, the Company adopted the provisions of Statement of Financial Accounting Standards (SFAS) No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of" without a significant impact to operating results, financial position or cash flow.

Other Assets - Other assets consist principally of deposits, insurance policy cash values, capitalized software costs, purchased technology and certain other intangible assets. The Company amortizes software costs, purchased technology and intangible assets on a straight-line basis over periods ranging from three to ten years. Accumulated amortization was \$209,626 and \$168,243 at June 30, 1998 and 1999, respectively. The Company performs an evaluation of these amounts on a periodic basis to determine that the recorded costs are not in excess of their net realizable value.

Earnings (Loss) ("FASB") Per Common Share - In 1997, the Financial Accounting Standards Board issued SFAS No. 128, "Earnings per Share." SFAS 128 replaced the calculation of primary and fully diluted earnings (loss) per share with basic and diluted earnings (loss) per share. Unlike primary earnings (loss) per share, basic earnings (loss) per share excludes any dilutive effects of options, warrants and convertible securities. Diluted earnings (loss) per share is very similar to the previously reported fully diluted earnings (loss) per share. All earnings (loss) per share amounts for all periods have been presented, and where appropriate, restated to conform to the SFAS 128 requirements.



The following table sets forth the computation of basic and diluted net income (loss) per share:

	June 30		
	1998	1997	1996
Numerator:			
Net income (loss)	\$1,404,449	\$ (372,898)	\$ 281,984
	=====	=====	=====
Denominator for basic net income (loss) per share - weighted average shares:	7,679,985	7,662,494	7,639,637
Dilutive common stock equivalents using treasury stock method:	280,267	630,532	129,086
	-----	-----	-----
	7,960,252	8,293,026	7,768,723
	=====	=====	=====
Basic net income (loss) per share	\$ 0.18	\$ (0.05)	\$ 0.04
	=====	=====	=====
Diluted net income (loss) per share	\$ 0.18	\$ (0.05)	\$ 0.04
	=====	=====	=====

Options to purchase 20,000 shares of common stock were outstanding as of June 30, 1998, but were not included in the computation of diluted earnings per share as the effect would be antidilutive.

Research and Product Development Costs - Research and product development costs are expensed as incurred.

Software Development Costs - The Company capitalizes a portion of its software development costs. Both capitalized software development costs and purchased software costs are amortized on a straight-line basis over the estimated useful life of three years or the ratio of current revenue to the total current and anticipated future revenue, whichever provides for greater amortization. Amortization generally commences when shipments of the related products begin. Amortization expense recorded during the respective years ended June 30, 1998, 1997 and 1996 was \$18,608, \$31,900 and \$31,900. Unamortized costs are stated at the lower of cost or net realizable value and are included in other assets net of accumulated amortization of \$95,700 in 1998, \$77,100 in 1997 and \$45,200 in 1996.

Income Taxes - The Company provides for income taxes based on the liability method which requires the recognition of deferred tax assets and liabilities based on differences between financial reporting and tax bases of assets and liabilities measured using enacted tax rates and laws that are expected to be in effect when the differences are expected to reverse.

Use of Estimates - The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts in the financial statements and these accompanying notes. Actual results could differ from those estimates.

Stock Based Compensation - The Company adopted SFAS 123 "Accounting for Stock Based Compensation," effective July 1, 1996. SFAS 123 defines a fair value-based method of accounting for and measuring compensation expense related to stock based compensation plans and encourages adoption of the new standard. However, the statement allows entities to continue to measure compensation expense for stock-based plans using the intrinsic value-based method prescribed by APB Opinion No. 25, "Accounting for Stock Issued to Employees". The Company has elected to continue to account for stock-based compensation plans using the provisions of APB Opinion No. 25. Pro forma footnote disclosure of net income has been made as if the fair value based method of accounting defined in the statement had been applied.

Advertising Expenses - Advertising expenses are expensed as incurred. Advertising expense for fiscal years 1998, 1997 and 1996 totaled \$229,629, \$598,500 and \$331,300, respectively.

New Accounting Pronouncements - In June 1997, the FASB issued SFAS No. 130, "Reporting Comprehensive Income", which established standards for reporting and display of "Comprehensive Income" which is the total of net income and all other non-owner changes in stockholders' equity and its components. SFAS 130 is effective for fiscal years beginning after December 15, 1997 with

earlier application permitted. The Company will adopt the standard in fiscal 1999 and does not expect comprehensive income to differ significantly from previously reported net income.

In June 1997, the FASB also issued SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information." SFAS 131, which supersedes SFAS Nos. 14, 18, 24 and 30, establishes new standards for segment reporting in which reportable segments are based on the same criteria on which management disaggregates a business for making operating decisions and assessing performance. SFAS 131 is effective for fiscal years beginning after December 15, 1997 with earlier application permitted. The Company will adopt the standard in fiscal 1999 and is currently analyzing the impact this new standard will have on previously reported information.

Reclassifications - Certain 1997 and 1996 amounts have been reclassified to conform with the current year presentation.

## 2. SIGNIFICANT CUSTOMER

The Company sells a substantial portion of its products to a major distributor in the Telephone Interface and Remote Facilities Management product areas. For the fiscal years ended June 30, 1998, 1997 and 1996, sales to this distributor aggregated to \$1,228,278 (7%), \$1,551,811 (12%) and \$1,223,438 (11%), respectively. At the end of those years amounts due from this customer were \$23,248, \$77,920 and \$80,983, respectively.

## 3. FINANCIAL INSTRUMENTS

The carrying values of cash and cash equivalents, the note receivable, accounts receivable and payable, the Company's line of credit and accrued liabilities all approximate fair value due to the short-term maturities of these assets and liabilities. The carrying values of virtually all long-term notes payable also approximate fair value because applicable interest rates fluctuate based on market conditions.

## 4. INVENTORY

Inventory is summarized as follows:

	June 30,	
	1998	1997
Raw materials	\$1,014,732	\$ 897,481
Work in progress	524,313	648,712
Finished goods	1,615,938	1,122,568
Total Inventory	<u>\$3,154,983</u>	<u>\$2,668,761</u>

## 5. PROPERTY AND EQUIPMENT

Major classifications of property and equipment and estimated useful lives are as follows:

	June 30,	
	1998	1997
Office furniture and equipment - 5 to 10 years.....	\$ 3,357,347	\$ 3,174,708
Manufacturing and test equipment - 5 to 10 years.....	1,708,857	1,616,125
Telephone bridging equipment - 10 years.....	731,750	593,070
Vehicles - 3 to 5 years.....	33,862	22,318
	<u>5,831,816</u>	<u>5,406,221</u>
Accumulated depreciation and amortization.....	<u>(3,511,480)</u>	<u>(2,912,934)</u>
Net property and equipment.....	<u>\$ 2,320,336</u>	<u>\$ 2,493,287</u>

## 6. LINE OF CREDIT

The Company maintains a revolving line of credit (no outstanding balance on \$2.0 million available at June 30, 1998, and \$722,997 was outstanding on \$2.5 million available at June 30, 1997) with a commercial bank that expires December 24, 1998 and which the Company anticipates renewing beyond that date. Borrowings accrue interest at a rate of anywhere from three to five percent over the London Interbank Offered Rate (LIBOR). The borrowing rate was 9.15% as of June 30, 1998. The weighted average interest rate as of June 30, 1998, 1997 and 1996, respectively, was 10.8%, 11.0% and 9.8%. The terms of the line of credit prohibit the payment of dividends and require the Company to maintain other defined financial ratios and restrictive covenants. No compensating balance arrangements are required.

## 7. LONG TERM DEBT

Long-term debt consists of the following:

	June 30,	
	1998	1997
	----	----
1.5% over prime note due to a financial institution, with monthly payments of \$5,846 through July 1999, secured generally by manufacturing and test equipment (on June 30, 1998, the interest rate was 10.7%)	\$ 82,809	\$ 140,983
9.25% note to a financial institution, with monthly payments of \$8,069, through February 2001, secured generally by equipment, furniture and other assets	220,073	292,849
11.5% note due to a financial institution, with monthly payments of \$14,851, through December 2000, secured generally by furniture	385,332	510,606
	-----	-----
	688,214	944,438
Less current portion	(285,630)	(257,164)
	-----	-----
Total long term debt	\$ 402,584	\$ 687,274
	=====	=====

Annual principal installments of long-term debt are \$285,630, \$263,980 and \$138,604 for the years ending June 30, 1999, 2000 and 2001, respectively.

## 8. LEASES

The Company has entered into capital leases with finance companies to finance the purchase of certain furniture and equipment. Property and equipment under capital leases are as follows:

	June 30,	
	1998	1997
	----	----
Office furniture and equipment.....	\$ 890,360	\$ 842,238
Manufacturing and test equipment.....	524,917	496,718
Telephone bridging equipment.....	600,250	477,042
Vehicles.....	33,862	22,318
	-----	-----
	2,049,389	1,838,316
Accumulated depreciation and amortization.....	(1,099,093)	(810,477)
	-----	-----
Net property and equipment under capital leases.....	\$ 950,296	\$1,027,839
	=====	=====

Future minimum lease payments under capital leases and noncancelable operating leases with initial terms of one year or more are as follows:

	Capital	Operating
	-----	-----
For years ending June 30:		
1999.....	\$ 353,584	\$ 277,318
2000.....	361,479	267,680
2001.....	336,861	265,752
2002.....	202,014	265,752
2003.....	29,562	265,752
Thereafter.....	0	1,063,008
	-----	-----
Total minimum lease payments.....	1,283,500	\$2,405,262
		=====
Less use taxes.....	(76,636)	
	-----	
Net minimum lease payments.....	1,206,864	
Less amount representing interest.....	(217,027)	
	-----	
Present value of net minimum lease payments.....	989,837	
Less current portion.....	(237,109)	
	-----	
Capital lease obligation.....	\$ 752,728	
	=====	

Certain operating leases contain escalation clauses based on the consumer price index. Rental expense, which was composed of minimum rentals under operating lease obligations, was \$265,759, \$245,996 and \$144,877 for the years ended June 30, 1998, 1997 and 1996, respectively. The Company's operating lease on its facility, which expires 2007, provides for renewal options extending the terms an additional ten years. Rates charged would be at prevailing market rates at the time of renewal.

#### 9. ROYALTY AGREEMENTS

The Company is a general partner in two limited partnerships, Gentner Research Ltd. ("GRL") and Gentner Research II, Ltd. ("GR2L"), both related parties. GRL sold the proprietary interest in a remote control product line to the Company in exchange for royalty agreements in 1987 and 1988. Royalty expense under the agreements with GRL for the years ended June 30, 1998, 1997 and 1996, was \$43,500, \$45,100 and \$29,400, respectively. In fiscal 1997, GR2L sold the proprietary interest in a new Remote Facilities Management product to the Company in exchange for a royalty agreement. Royalty expense under this agreement with GR2L for the years ended June 30, 1998 and 1997 was \$54,810 and \$36,588, respectively. As of June 30, 1998 and 1997, GR2L owed the Company \$126,505 and \$139,000, respectively, which is a note receivable from the partnership to the Company. The terms of the note are such that 50% of all the royalty proceeds will be applied to the payment of the note's principle and interest first. The note is payable in full on April 30, 2001, and the interest rate on the note is equal to the Company's cost of short term funds.

#### 10. INCOME TAXES

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's deferred tax liabilities and assets are as follows:

	1998	1997
	----	----
Deferred tax liabilities:		
Tax over book depreciation.....	\$229,000	\$164,000
Unamortized software costs.....	--	7,000
	-----	-----
Total deferred tax liabilities.....	229,000	171,000

Deferred tax assets:		
Unamortized software costs .....	11,000	--
Accounts receivable and other reserves ..	70,000	29,000
Inventory reserves .....	35,000	34,000
Product warranty accruals .....	8,000	8,000
Net operating loss carryforwards .....	--	504,000
Tax credit carryforwards .....	304,000	245,000
	-----	-----
Total deferred tax assets .....	428,000	820,000
Valuation allowance for deferred tax assets	(159,000)	(649,000)
	-----	-----
Net deferred tax assets .....	269,000	171,000
	-----	-----
Net deferred taxes .....	\$ 40,000	\$ --
	=====	=====

Significant components of the provision for income taxes are as follows:

	Years Ended June 30,		
	1998	1997	1996
	----	----	----
Current:			
Federal .....	\$ 69,000	\$ --	\$ --
State .....	6,000	900	900
Tax benefits allocated to contributed capital .....	4,000	--	36,000
	-----	-----	-----
Total current .....	79,000	900	36,900
Deferred:			
Federal .....	(36,500)	33,000	(33,000)
State .....	(3,500)	3,000	(3,000)
	-----	-----	-----
Total deferred .....	(40,000)	36,000	(36,000)
	-----	-----	-----
	\$ 39,000	\$ 36,900	\$ 900
	=====	=====	=====

The provision for federal income taxes was reduced due to the use of approximately \$1,300,000, \$1,000,000 and \$1,100,000 in net operating loss benefits in 1998, 1997 and 1996, respectively.

The reconciliation of income tax computed at the U.S. federal statutory tax rates to income tax expense is as follows:

	Years Ended June 30,		
	1998	1997	1996
	----	----	----
Tax at federal statutory rate .....	34.0%	(34.0)%	34.0%
Increase (reduction) in computed tax rate resulting from:			
State income tax, net of federal effect .....	3.3	(3.5)	3.2
Valuation allowance .....	(33.9)	45.8	(14.9)
Federal income tax credits generated .....	(4.0)	--	(20.9)
Statutory tax disallowance of entertainment expenses ..	0.2	1.0	0.8
Nondeductible life insurance premiums .....	0.1	--	0.3
Utilization of capital loss carryforward .....	--	--	(2.1)
Nondeductible intangible asset amortization and other	3.0	0.6	(0.1)
	-----	-----	-----
	2.7%	9.9%	0.3%
	=====	=====	=====

At June 30, 1998, for income tax purposes the Company had research and development tax credit carryforwards of approximately \$289,000 that expire beginning in 2004.

## 11. STOCK OPTIONS

The Company's 1990 Incentive Plan ("1990 Plan") has shares of common stock available for issuance to employees and directors. Provisions of the 1990 Plan include the granting of stock options. Stock options vest over a five year period at 10%, 15%, 20%, 25% and 30% per year over years one through five. Additionally, the plan has some performance based



options that vest on net income goals for fiscal years 1998 to 2000. The Company also has a 1998 Stock Option Plan ("1998 Plan"). Provisions of the 1998 Plan include the granting of stock options. Currently the vesting schedule is performance based where options will vest based on an earnings per share goal for the next five years. Under the 1998 Plan, there are 1,700,000 shares available. The 1998 Plan expires June 10, 2008, or when all the shares available under the plan have been issued. Information for the fiscal years 1996 through 1998 with respect to the Plans is as follows:

Stock Options	Number of Shares	Weighted Average Exercise Price
	-----	-----
Outstanding at June 30, 1995	490,000	\$0.74
Options granted	140,000	0.84
Options expired and canceled	(23,000)	0.82
Options exercised	(207,000)	0.69
	-----	
Outstanding at June 30, 1996	400,000	0.80
Options granted	605,000	0.79
Options expired and canceled	(55,000)	0.72
	-----	
Outstanding at June 30, 1997	950,000	0.80
Options granted	1,193,000	2.05
Options expired and canceled	(258,000)	0.80
Options exercised	(32,000)	0.74
	-----	
Outstanding at June 30, 1998	1,853,000	\$1.61
	=====	

The following table summarized information about stock options outstanding at June 30, 1998 under the Plans:

Exercise Price Range	Options Outstanding at June 30, 1998	Options Outstanding		Options Exercisable	
		Weighted Average Contractual Remaining Life	Weighted Average Exercise Price	Options Exercisable at June 30, 1998	Weighted Average Exercise Price
		-----	-----	-----	-----
\$0.69 to \$0.84	1,018,000	4.7 years	\$0.76	580,500	\$0.75
\$1.81	20,000	2.0 years	\$1.81	20,000	\$1.81
\$2.66	815,000	6.0 years	\$2.66		
	-----			-----	
Total	1,853,000			600,500	
	=====			=====	

There were 1,085,000 options available for future grant at June 30, 1998. The following are the options exercisable at the corresponding weighted average exercise price at June 30, 1998, 1997 and 1996, respectively: 600,500 at \$0.79; 284,000 at \$0.78; and 209,500 at \$0.78.

On June 30, 1993 the Company registered with the Securities and Exchange Commission all shares of common stock previously issued or issuable under the 1990 Plan.

The Company applies Accounting Principles Board Opinion No. 25 "Accounting for Stock Issued to Employees" and related interpretations in accounting for its plan. No compensation expense has been recognized for the stock option plan because the exercise price of the options equals the market price of the underlying stock on the date of the grant. If compensation expense for the Company's stock based compensation plan had been determined consistent with SFAS 123 "Accounting and Disclosure of Stock-based Compensation", the Company's net income (loss) would have been the pro forma amount indicated below:

	Fiscal Year 1998 ----	Fiscal Year 1997 ----
Net Income (Loss)		
As Reported	\$1,404,449	\$(372,898)
earnings per share	\$ 0.18	\$ (0.05)
Pro Forma	\$1,223,317	\$(460,116)
earnings per share	\$ 0.15	\$ (0.06)

The pro forma results above are not likely to be representative of the effects of applying SFAS 123 on reported net income (loss) for future years as these amounts only reflect the expense from two years.

The weighted average fair value (as defined by SFAS 123) of each option granted in fiscal 1998, 1997 and 1996 is estimated as \$1.24, \$0.43 and \$0.36, respectively, on the date of grant using the Black-Scholes model with the following weighted average assumptions: expected dividend yield, 0%; risk-free interest rate, 5.5% to 6.0% expected price volatility, 55.1% to 84.8%; and expected life of options, 3 to 5 years.

## 12. WARRANTS

During 1991, the Company filed a registration statement with the Securities and Exchange Commission in connection with a secondary public offering of 1,437,500 units. Each unit consisted of three shares of common stock and two redeemable common stock purchase warrants. As of June 30, 1998 there were no warrants outstanding, as all warrants expired on September 22, 1997. No warrants were exercised during fiscal 1998, 1997 or 1996.

## 13. INTERNATIONAL SALES

The Company provides products to the Telephone Interface and Remote Facilities Management markets, and products to the Teleconferencing markets. These products are all distributed from, and designed, manufactured, and serviced at the Company's facilities in Salt Lake City, Utah. The Company uses either master distributors or international dealers to facilitate its international sales. Currently, the Company's products are distributed to at least thirty-five different countries.

The Company ships products to unaffiliated distributors in worldwide markets. In fiscal 1998, 1997 and 1996, respectively, such international sales were \$2,581,700, \$2,183,000 and \$1,454,000 and accounted for 15%, 15% and 13% of total sales. During those years, the Company shipped the following amounts, respectively, to the following areas: Canada - \$798,800, \$724,000 and \$357,900; Asia - \$513,300, \$451,400 and \$519,000; Europe - \$817,400, \$580,600 and \$361,000; Latin America - \$252,100, \$158,800 and \$31,300; Other Areas - \$200,100, \$268,200 and \$183,900.

## 14. RETIREMENT SAVINGS AND PROFIT SHARING PLAN

The Company has a 401(k) retirement savings and profit sharing plan to which it makes discretionary matching contributions, as authorized by the Board of Directors. All full-time employees who are at least 21 years of age and have a minimum of six months of service with the Company at the plan date are eligible to participate in the plan. Matching contributions, if made, are based upon amounts participating employees contribute to the plan. The Company's retirement plan contributions for the 1998, 1997 and 1996 fiscal years totaled \$31,000, \$0 and \$16,000, respectively.

## ITEM 8. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None exist.



## PART III

ITEM 9. DIRECTORS, EXECUTIVE OFFICERS, PROMOTERS AND CONTROL PERSONS; COMPLIANCE  
WITH SECTION 16(a) OF THE EXCHANGE ACT

## DIRECTORS AND EXECUTIVE OFFICERS

## Directors

The following individuals are currently directors of the Company:

Name -----	Age ---	Principal Occupation -----	Director Since -----
Frances M. Flood	42	Chief Executive Officer and President	1998
Edward Dallin Bagley*	60	Attorney	1994
Brad R. Baldwin	43	President and Chief Executive Officer of Bank One, Utah	1988
Edward N. Bagley*	86	Vice President of Smith Barney and Chairman of the Board of Mining Services International	1993
Dwight H. Egan	45	President and Chief Executive Officer of Broadcast International, Inc.	1994
K. Bradford Romney	42	Assistant Business Unit Manager, Small Business Networking Operation, Intel Corporation	1994

\* Edward N. Bagley and Edward Dallin Bagley are father and son, respectively.

Frances M. Flood has been a Director of the Company since June of 1998. Ms. Flood joined the Company in October 1996 as Vice-President of Sales and Marketing. She was named President in December 1997 and Chief Executive Officer in June 1998. Prior to joining the Company, Ms. Flood was Area Director of Sales and Marketing for Ernst & Young, LLP, an international accounting and consulting firm. Ms. Flood has nearly twenty-five years experience in sales, marketing, change management, international business and finance.

Edward Dallin Bagley has been a Director of the Company since April 1994. Previously, Mr. Bagley served as a Director of the Company from April 1987 to July 1991. Mr. Bagley began practicing law in 1965. During the past six years, Mr. Bagley has served as Vice President of National Financial, a computer back-up accounting firm for health clubs. Mr. Bagley is also currently a director of Tunex International, a chain of automotive engine performance and service centers. Mr. Bagley received a Juris Doctorate in 1965 from the University of Utah College of Law.

Brad R. Baldwin has been a Director of the Company since September 1988. Since October 1, 1994, Mr. Baldwin has served as President and Chief Executive Officer of Bank One, Utah, a commercial bank headquartered in Salt Lake City,

Utah. Mr. Baldwin served as Senior Vice President and General Counsel of Bank One from 1988 until his appointment as President and CEO. From 1981 to 1988, Mr. Baldwin was engaged in the general practice of law at the firm of Biele, Haslam & Hatch in Salt Lake City, Utah. Mr. Baldwin received a Juris Doctorate in 1980 from the University of Washington.

Edward N. Bagley has been a Director of the Company since January 1993. Mr. Bagley is currently Vice President of Smith Barney, with whom he has been associated since 1971. Mr. Bagley has worked in the investment industry since 1934. Mr. Bagley is also Chairman of the Board of Directors of Mining Services International, a publicly held developer of explosives technology and suppliers of chemicals to the mining industry, located in Salt Lake City, Utah. He received a bachelors degree from Utah State University in 1933.

Dwight H. Egan has been a Director of the Company since November 1994. Mr. Egan is currently the President and Chief Executive Officer of Broadcast International, Inc., a satellite communications and business information company located in Midvale, Utah. He is also currently a director of Data Broadcasting Corp., the parent of Broadcast International, Inc. Mr. Egan has served as an officer of Broadcast International since November 1985.

K. Bradford Romney has been a Director of the Company since November 1994. He currently serves as Assistant Business Unit Manager of the Small Business Networking Operation for Intel Corporation. From 1991 until its sale to Intel Corporation in October 1997, Mr. Romney served as President and Chief Executive Officer of Dayna Communications, Inc., a small business computer networking company based in Salt Lake City, Utah. Prior to that, he served as Executive Vice President of Dayna, beginning in 1986. From 1982 to 1986, Mr. Romney was Executive Vice-President of Keith Romney Associates. The former chairman of the Utah Information Technologies Association, Mr. Romney received a Juris Doctorate and a Masters of Business Administration degree from Brigham Young University in 1982.

#### Director Compensation and Committees

All directors serve until their successors are elected and have qualified. Each board member received options to purchase 25,000 shares of the Company's Common Stock as compensation for services rendered through June 30, 1998. Employee directors receive no additional compensation for serving on the Board.

The Board of Directors has three committees, the Executive, Audit and Compensation Committees. The Executive Committee is composed of Ms. Frances M. Flood, Mr. Brad R. Baldwin and Mr. Dwight H. Egan. The Audit Committee is currently composed of Mr. Brad R. Baldwin, Mr. Edward Dallin Bagley, Edward N. Bagley, Dwight H. Egan and Mr. K. Bradford Romney. The Compensation Committee is currently composed of Mr. Brad R. Baldwin, Mr. Edward Dallin Bagley, Edward N. Bagley, K. Bradford Romney and Mr. Dwight H. Egan. The Executive Committee exercises all the powers and authority of the Board of Directors in the management of the business and affairs of the Company except those which by statute, Articles of Incorporation or By-laws are reserved to the Board of Directors. The Audit Committee is authorized to review proposals of the Company's auditors regarding annual audits, recommend the engagement or discharge of the Company's auditors, review recommendations of such auditors concerning accounting principles and the adequacy of internal controls and accounting procedures and practices, to review the scope of the annual audit, to approve or disapprove each professional service or type of service other than standard auditing services to be provided by the auditors, and to review and discuss the audited financial statements with the auditors. The Compensation Committee makes recommendations to the Board of Directors regarding remuneration of the executive officers and directors of the Company and administers the incentive plans for directors, officers and key employees.

#### Meetings of the Board of Directors and Committees

The Board of Directors held eight meetings during the last fiscal year. The Executive Committee held no formal meetings during the last fiscal year. The Audit Committee held no formal meetings during the last fiscal year. The Compensation Committee held two meetings during the last fiscal year.

## Executive Officers and Significant Employee

The executive officers of the Company are as follows:

Name ----	Age ---	Position -----
Frances M. Flood	42	President and Chief Executive Officer
Susie S. Strohm	38	Vice President of Finance

For the biography of Ms. Flood, see "Directors."

Susie S. Strohm became Vice President of Finance in 1997. In 1996, Ms. Strohm joined the Company as its Controller. She is responsible for all the Company's accounting, financial and tax planning, financial and management reporting and SEC filings. Prior to joining the Company, Ms. Strohm was the Controller for Newspaper Agency Corporation in Salt Lake City, Utah. She graduated from the University of Utah with a Bachelor of Science degree in Accounting, and received her Masters of Business Administration degree from Westminster College.

The significant employee of the Company is:

Name ----	Age ---	Position -----
Brooks Gibbs	39	Director of Technology

Brooks Gibbs was named Director of Technologies for Gentner Communications in January of 1998. He has been with Gentner for 10 years serving in Product Management, Sales, Marketing and Customer Service areas. He is responsible for coordination of the company's strategic technical direction, product development, manufacturing and technical service and support. Prior to joining the Company Mr. Gibbs was a lead project design engineer for Centro Corporation, a systems design and integration company. Mr. Gibbs has over eighteen years of communications product development and product management experience.

## COMPLIANCE WITH SECTION 16(a) OF THE SECURITIES EXCHANGE ACT

Section 16(a) of the Securities Exchange Act of 1934, as amended, requires the Company's directors and executive officers, and persons who own more than 10% of a registered class of the Company's equity securities to file with the Securities and Exchange Commission initial reports of ownership and reports of changes of ownership of equity securities of the Company. Officers, directors and greater than 10% shareholders are required to furnish the Company with copies of all Section 16(a) forms they file.

To the Company's knowledge, persons as defined above have complied with all applicable section 16(a) requirements during the preceding fiscal year.

## ITEM 10. EXECUTIVE COMPENSATION

## SUMMARY COMPENSATION

The following table sets forth the compensation of the Chief Executive Officer of the Company and the other most highly compensated executive officers of the Company for each of the Company's last three fiscal years whose total salary and bonus for the year ended June 30, 1998 exceeded \$100,000, for services rendered in all capacities to the Company during such fiscal years.

## SUMMARY COMPENSATION TABLE

Name and Position	Year	Annual Compensation			Long Term Compensation			
		Salary	Bonus	Other Annual Compensation	Awards		Payouts	
					Securities Restricted Stock Awards	Underlying Options /SARS	LTIP Payouts	All Other Compensation(1)
Frances M. Flood	Fiscal							
CEO & President(2)	97-98	\$117,310	\$16,649	None	None	None	None	None
	Fiscal 96-97	\$ 70,657	\$ 8,903	None	None	None	None	None
Russell D. Gentner Former Chairman, CEO, & President	Fiscal 97-98	\$122,950	\$18,711	\$96,403(3)	None	None	None	None
	Fiscal 96-97	\$162,240	\$11,760	None	None	None	None	None
	Fiscal 95-96	\$156,756	None	None	None	None	None	\$890

(1) These amounts reflect the Company's contributions to the deferred compensation plan (401(k) plan).

(2) Ms. Flood did not join the Company until fiscal 96-97.

(3) This includes a severance package.

## STOCK OPTIONS/SARS

The following table sets forth the stock option and SAR grants to the named executive officers for the last fiscal year:

OPTION/SAR GRANTS IN FISCAL YEAR ENDED JUNE 30, 1998  
(INDIVIDUAL GRANTS)

Name and Position	Number of Securities Underlying Options/SARS Granted (#)	Percent of Total Options /SARS Granted to Employees in Fiscal Year	Exercise or Base Price (\$/Sh)	Expiration Date
Frances M. Flood CEO & President	181,000	14%	\$0.75 to \$2.66	6/30/2004
Russell D. Gentner Former Chairman, CEO & President	87,000	7%	\$0.75	6/30/2004

## AGGREGATED STOCK OPTION/SAR EXERCISES

The following table sets forth the aggregated stock options and SARs exercised by the named executive officers in fiscal 1998 and the year-end value of unexercised options and SARs:

AGGREGATED OPTION/SAR EXERCISES IN FISCAL YEAR ENDED JUNE 30, 1998  
AND FISCAL YEAR-END OPTION/SAR VALUES

Name and Position	Shares Acquired on Exercise(#)	Value Realized(\$)	Number of Securities Underlying Unexercised Options/SARs at FY-End (#) Exercisable/ Unexercisable	Value of Unexercised In-The-Money Options/SARs at FY-End (\$) Exercisable/ Unexercisable
Frances M. Flood CEO & President	0	\$0	39,000/301,000	\$30,000/\$128,250
Russell D. Gentner Former Chairman, CEO, & President	0	\$0	0	\$0

## ITEM 11. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table sets forth certain information regarding ownership of the Common Stock of the Company as of September 1, 1998 by (i) each person known to the Company to be the beneficial owner of more than 5% of the outstanding Common Stock of the Company, (ii) each director of the Company, (iii) the Chief Executive Officer and each other executive officer of the Company whose salary and bonus for the year ended June 30, 1998 exceeded \$100,000, and (iv) all executive officers and directors of the Company as a group. Each person has sole investment and voting power with respect to the shares indicated, subject to community property laws where applicable, except as otherwise indicated below. The address for each beneficial owner is in care of the Company, 1825 Research Way, Salt Lake City, Utah 84119, unless otherwise indicated.

Names of Beneficial Owners	Amount of Beneficial Ownership(1)	Percentage of Class(2)
Edward Dallin Bagley	1,394,335(3)	17.2%
Watson Investment Group	389,000(4)	5.0%
Edward N. Bagley	312,333(5)	4.0%
Brad R. Baldwin	130,166(6)	1.7%
Frances M. Flood	78,477(7)	1.0%
Dwight H. Egan	55,000(8)	0.7%
K. Bradford Romney, Jr	55,000(8)	0.7%
Directors and Executive Officers as a Group (7 people)	2,059,282(3)(5)(6)(7)(8)(9)	24.6%

- (1) For each shareholder, the calculation of percentage of beneficial ownership is based on 7,750,095 shares of Common Stock outstanding as of September 1, 1998 and shares of Common Stock subject to options held by the shareholder that are currently exercisable or exercisable within 60 days of September 1, 1998.
- (2) The percentage ownership for any person is calculated assuming that all the stock that could be acquired by that person within 60 days by option exercise or otherwise, is in fact outstanding and that no other stockholder has exercised a similar right to acquire additional shares.
- (3) Director. Includes: 922,285 shares owned directly; 100,000 shares owned by a corporation controlled by Mr. Bagley; 50 shares owned by Mr. Bagley's wife as custodian for one of Mr. Bagley's daughters; and options to purchase 372,000 shares that are exercisable within 60 days. On September 9, 1998, Mr. Bagley exercised the options referred to in this footnote. Excludes: 50 shares owned by another of Mr. Bagley's daughters; and shares owned by the Bagley Family Revocable Trust, all of which Mr. Bagley disclaims beneficial ownership.
- (4) Beneficial owner. Includes: shares held by an investment partnership, a non-US investment company, and several managed accounts, as to all of which Mr. Watson has sole investment authority. Mr. Watson's address is 237 Park Avenue, Suite 801, New York, NY 10017.
- (5) Director. Includes: 257,333 shares owned by the Bagley Family Revocable Trust, of which Mr. Bagley is a co-trustee with his wife; and options to purchase 55,000 shares that are exercisable within 60 days. Excludes: shares held or controlled by Mr. Bagley's son (Edward Dallin Bagley) and granddaughters as described in footnote 3 above, all of which Mr. Edward N. Bagley disclaims beneficial ownership.
- (6) Director. Includes: 65,166 shares owned directly; options to purchase 60,000 shares that are exercisable within 60 days; and 5,000 shares owned by Mr. Baldwin's wife.
- (7) President, CEO and Director. Includes: 49,229 shares owned directly; options to purchase 29,248 shares that are exercisable within 60 days.
- (8) Includes: options to acquire 55,000 shares that are exercisable within 60 days.
- (9) Includes: an additional 27,251 shares owned directly by one additional officer; and options to purchase 6,720 shares that are exercisable within 60 days by that officer.

#### ITEM 12. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

Gentner Research Ltd. ("GRL"), is a related limited partnership, formed on August 1985, in which the Company is the general partner and Russell Gentner, Edward Dallin Bagley and, among other unrelated parties, certain members of their families, are the limited partners. In 1987 and 1988, GRL sold to the Company proprietary interests in the VRC-1000 (now VRC-2000), VRC-1000 Modem (now VRC-2000) and Digital Hybrid in exchange for royalty payments. Royalty expense recognized by the Company for the years ending June 30, 1998 and 1997 was \$43,500 and \$45,100 respectively. The following directors and/or executive officers and members of their immediate families have purchased the following interests in GRL:

Russell D. Gentner (Former Pres/CEO/Director).....	5.21%
Edward Dallin Bagley (Director).....	10.42%
Edward N. Bagley (Director).....	5.21%
Hyrum S. Gentner (father of Russell Gentner).....	5.21%
Robert O. Baldwin (father of Brad Baldwin).....	10.42%

The Company has also formed a second related limited partnership, Gentner Research II, Ltd. ("GR2L"), also in which it acts as general partner. In fiscal year 1997, GR2L sold proprietary interest in the GSC3000 to the Company in exchange for royalty payments. Royalty expense with GR2L for the years ending June 30, 1998 and 1997 was \$54,810 and \$36,588. The following directors and/or executive officers and members of their immediate families have purchased the following interests in GR2L:

Brad R. Baldwin (Director).....	3.19%
Robert O. Baldwin (father of Brad Baldwin).....	9.58%
Hyrum S. Gentner (father of Russell Gentner).....	3.19%
Edward D. Bagley (Director).....	6.39%
Edward N. Bagley (Director, Father of Edward D. Bagley).....	6.39%

## ITEM 13. EXHIBITS AND REPORTS ON FORM 8-K

## EXHIBITS REQUIRED BY ITEM 601 OF REGULATION S-B

The following exhibits are hereby incorporated by reference from the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 1989. The exhibit numbers shown are those in the 1989 Form 10-K as originally filed.

EXHIBIT NUMBER - - - - -	DESCRIPTION - - - - -
3.1(1)(2)	Articles of Incorporation and all amendments thereto through March 1, 1988. (Page 10)
10.4(1)(2)	VRC-1000 Purchase Agreement between Gentner Engineering Company, Inc. (a former subsidiary of the Company which was merged into the Company) and Gentner Research Ltd., dated January 1, 1987. (Page 71)

The following exhibits are hereby incorporated by reference from the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 1991. The exhibit numbers shown are those in the 1991 Form 10-K as originally filed.

EXHIBIT NUMBER - - - - -	DESCRIPTION - - - - -
3.1(1)(2)	Amendment to Articles of Incorporation, dated July 1, 1991. (Page 65)
10.1(1)(2)	Internal Modem Purchase Agreement between Gentner Engineering Company, Inc. and Gentner Research, Ltd., dated October 12, 1987. (Page 69)
10.2(1)(2)	Digital Hybrid Purchase Agreement between Gentner Engineering, Inc. and Gentner Research, Ltd., dated September 8, 1988. (Page 74)

The following documents are hereby incorporated by reference from the Company's Form 10-KSB for the fiscal year ended June 30, 1993. The exhibit numbers shown are those in the 1993 Form 10-KSB as originally filed.

EXHIBIT NUMBER - - - - -	DESCRIPTION - - - - -
3(1)(2)	Bylaws, as amended on August 24, 1993. (Page 16)

The following documents are hereby incorporated by reference from the Company's Form 10-KSB for the fiscal year ended June 30, 1996. The exhibit numbers shown are those in the 1996 Form 10-KSB as originally filed.

EXHIBIT NUMBER - - - - -	DESCRIPTION - - - - -
10(1)(2)(3)	1990 Incentive Plan, as amended August 7, 1996 (Page 40)

The following documents are hereby incorporated by reference from the Company's Form 10-KSB for the fiscal year ended June 30, 1997. The exhibit numbers shown are those in the 1997 Form 10-KSB as originally filed.

EXHIBIT NUMBER - - - - -	DESCRIPTION - - - - -
10.1(1)(2)	Commercial Credit and Security Agreement, and Promissory Note, between Company and First Security Bank, N.A. (original aggregate amount of \$2,500,000) (Page 7)
10.2(1)(2)(3)	1997 Employee Stock Purchase Plan (Page 37)
10.3(1)(2)	Promissory Note in favor of Safeco Credit Company (\$419,000) (Page 52)
10.4(1)(2)	Commercial Credit and Security Agreement, and Promissory Note, between Company and First Security Bank (\$322,716.55) (Page 53)
10.5(1)(2)	Lease between Company and Valley American Investment Company (Page 71)

The following documents are filed as exhibits to this Form 10-KSB.

EXHIBIT NUMBER - - - - -	DESCRIPTION - - - - -
10.1(3)	1998 Stock Option Plan & Form of Grant
10.2	Modification Agreement dated as of December 24, 1997, between First Security Bank, N.A. and the Company
23	Consent of Ernst & Young LLP, Independent Auditors
27	Financial Data Schedule

(1) Denotes exhibits specifically incorporated into this Form 10-KSB by reference to other filings pursuant to the provisions of Rule 12B-32 under the Securities Exchange Act of 1934.

(2) Denotes exhibits specifically incorporated into this Form 10-KSB by reference, pursuant to Regulation S-B, Item 10(f)(2). These documents are located under File No. 0-17219 and are located at the Securities and Exchange Commission, Public Reference Branch, 450 South 5th St., N.W., Washington, DC 20549.

(3) Identifies management or compensatory plans, contracts or arrangements.

#### REPORTS ON FORM 8-K

The Company filed no reports on Form 8-K during the latest fiscal quarter.



## SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the Company caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

## GENTNER COMMUNICATIONS CORPORATION

September 28, 1998

By: /s/ Frances M. Flood  
 -----  
 Frances M. Flood  
 Chief Executive Officer

In accordance with the Exchange Act, this report has been signed below by the following persons on behalf of the Company and in the capacities and on the dates indicated.

Signature -----	Title -----	Date ----
/s/ Frances M. Flood - ----- Frances M. Flood	Director, President and Chief Executive Officer (Principal Executive Officer)	September 28, 1998
/s/ Susie Strohm - ----- Susie Strohm	Vice President - Finance (Principal Financial and Accounting Officer)	September 28, 1998

## POWER OF ATTORNEY

Know all men by these presents, that each person whose signature appears below constitutes and appoints each of Frances M. Flood and Susie Strohm, jointly and severally, his true and lawful attorney in fact and agent, with full power of substitution for him and in his name, place and stead, in any and all capacities, to sign any or all amendments to this report on Form 10-KSB and to file the same, with all exhibits thereto and other documents in connection therewith with the Securities and Exchange Commission, hereby ratifying and confirming all that each said attorney in fact or his substitute or substitutes may do or cause to be done by virtue hereof.

Signature - -----	Title -----	Date ----
/s/ Edward Dallin Bagley - ----- Edward Dallin Bagley	Director	September 28, 1998
/s/ Brad R. Baldwin - ----- Brad R. Baldwin	Director	September 28, 1998
/s/ Edward N. Bagley - ----- Edward N. Bagley	Director	September 28, 1998
/s/ K. Bradford Romney - ----- K. Bradford Romney	Director	September 28, 1998
/s/ Dwight H. Egan - ----- Dwight H. Egan	Director	September 28, 1998

## EXHIBIT INDEX

EXHIBIT NUMBER - - - - -	DESCRIPTION - - - - -
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27	Financial Data Schedule

Grant No. \_\_\_\_\_

## GENTNER COMMUNICATIONS CORPORATION

## STOCK OPTION GRANT

OPTIONEE: \_\_\_\_\_

ADDRESS: \_\_\_\_\_

GRANT DATE: \_\_\_\_\_

EXERCISE PRICE: \$\_\_\_\_\_ per share

NUMBER OF OPTION SHARES: \_\_\_\_\_ shares

EXPIRATION DATE: \_\_\_\_\_

TYPE OF OPTION: \_\_\_\_\_ Incentive Option \_\_\_\_\_ Non-Statutory Option

EXERCISE SCHEDULE: The option shall become exercisable annually with respect to a percentage of one-fifth (1/5) of the total Option Shares upon the Corporation's achieving annual increases in earnings per share ("EPS") in the five fiscal years 1999-2003, as set forth on Schedule 1 attached. The annual increase in EPS and the number of Options to become exercisable shall be determined by the Administrator within forty-five (45) days of the end of the fiscal year and shall be determined based on the Corporation's audited financial statements for such fiscal year. For purposes of determining EPS, the Administrator may, in its discretion, exclude or otherwise adjust annual EPS due to the occurrence of an extraordinary event during the fiscal year. Extraordinary events shall include the merger of the Corporation, the Corporation's acquisition of all or substantially all assets or stock of another company, the sale of all or substantially all assets or stock of the Corporation to a third party, a change in the Company's fiscal year, and other extraordinary transactions that are outside the ordinary course of business. In no event shall the option become exercisable for any Option Shares not vested at the time of Optionee's cessation of Service.

1. GRANT OF OPTION. Gentner Communications Corporation, a Utah corporation (the "Corporation") hereby grants to the Optionee named above, as of the Grant Date, an option to purchase up to the total number of Option Shares specified above. This grant includes the terms of the Stock Option Exercise Notice and Purchase Agreement attached hereto as Exhibit A, is made subject to all of the terms and conditions of this Grant and the Corporation's 1998 Stock Option Plan, a copy of which is attached hereto as Exhibit B. All capitalized terms not defined herein have the meaning set for the in the Appendix to the Plan.

2. OPTION TERM. The option term shall be measured from the Grant Date and shall accordingly expire at the close of business on the Expiration Date specified above, unless sooner terminated in accordance with paragraph 5 below.

3. LIMITED TRANSFERABILITY. This option shall be neither transferable nor assignable, in whole or in part, by Optionee other than by will or by the laws of descent and distribution following Optionee's death and may be exercised, during Optionee's lifetime, only by Optionee. However, if this option is designated a Non-Statutory Option above, then this option may also, in connection with Optionee's estate plan, be assigned in whole or in part during Optionee's lifetime to one or more members of Optionee's immediate family (spouse or children) or to a trust established exclusively for the benefit of one or more such immediate family members. Optionee shall give written notice of any such assignment during Optionee's lifetime to the Corporation within 20 days of assignment. The assigned portion may only be exercised by the person or persons who acquire a proprietary interest in the option pursuant to the assignment. The terms applicable to the assigned portion shall be the

same as those in effect for this option immediately prior to such assignment and shall be set forth in such documents issued to the assignee as the Plan Administrator may deem appropriate.

4. EXERCISABILITY. This option shall become exercisable for the Option Shares in one or more installments as provided in the Exercise Schedule specified above. As the option becomes exercisable for such installments, those installments shall accumulate and the option shall remain exercisable for the accumulated installments until the Expiration Date or sooner termination of the option term under paragraph 5 below.

5. CESSATION OF SERVICE. The option term specified in paragraph 2 above shall terminate, and this option shall cease to be outstanding prior to the Expiration Date, upon Optionee's ceasing to be in the Service of the Corporation. In such event, the following provisions shall apply:

a. Should Optionee cease to remain in Service for any reason (other than death, Permanent Disability or Misconduct) while this option is outstanding, then Optionee shall have a period of three (3) months (commencing with the date of such cessation of Service) during which to exercise this option as to vested Option Shares.

b. Should Optionee die while this option is outstanding, then the personal representative of Optionee's estate (or the person or persons to whom the option is transferred pursuant to Optionee's will or in accordance with the laws of descent and distribution) shall have a period of twelve (12) months (commencing with the date of such cessation of Service) during which to exercise this option as to vested Option Shares.

c. Should Optionee cease Service by reason of Permanent Disability while this option is outstanding, then Optionee shall have a period of twelve (12) months (commencing with the date of such cessation of Service) during which to exercise this option as to vested Option Shares.

d. Should Optionee's Service be terminated for Misconduct, then this option shall terminate immediately and cease to remain outstanding.

e. During the limited post-Service exercise period, this option may not be exercised in the aggregate for more than the number of vested Option Shares for which the option is exercisable on the date of the Optionee's cessation of Service. Upon the expiration of such limited post-Service exercise period or upon the Expiration Date (if earlier), this option shall terminate and cease to be outstanding for any vested Option Shares for which the option has not been exercised. In no event shall this option be exercisable at any time after the Expiration Date. To the extent this option is not otherwise exercisable for vested Option Shares at the time of Optionee's cessation of Service, this option shall immediately terminate and cease to be outstanding with respect to those shares.

6. ADJUSTMENT IN OPTION SHARES. Should any change be made to the Common Stock by reason of any split, stock dividend, recapitalization, combination of shares, exchange of shares or other change affecting the outstanding Common Stock as a class without the Corporation's receipt of consideration, appropriate adjustments shall be made to (i) the total number and/or class of securities subject to this option, and (ii) the Exercise Price, in order to reflect such change and thereby preclude a dilution or enlargement of benefits hereunder.

7. STOCKHOLDER RIGHTS. The holder of this option shall not have any stockholder rights with respect to the Option Shares until such person shall have exercised the option, paid the Exercise Price, and become a holder of record of the Purchased Shares.

## 8. MANNER OF EXERCISING OPTIONS

a. In order to exercise this option with respect to all or any part of the Option Shares for which this option is at the time exercisable, Optionee (or any other person or persons exercising this option) must take the following actions:

(1) Execute and deliver to the Corporation a Stock Option Exercise Notice and Purchase Agreement for the Option Shares for which the option is exercised.

(2) Pay the aggregate Exercise Price for the Purchased Shares in one or more of the following forms:

(a) Cash or check made payable to the Corporation; or

(b) A promissory note payable to the Corporation, but only to the extent authorized by the Plan Administrator in accordance with paragraph 12.

Upon prior written approval of the Plan Administrator, the Exercise Price may also be paid as follows:

(c) In shares of Common Stock held by Optionee (or any other person or persons exercising the option) for the requisite period necessary to avoid a charge to the Corporation's earnings for financial reporting purposes and valued at Fair Market Value on the Exercise Date; or

(d) Through a special sale and remittance procedure pursuant to which Optionee (or any other person or persons exercising the option) shall concurrently provide irrevocable written instructions (1) to a Corporation-designated brokerage firm to effect the immediate sale of the Purchased Shares and remit to the Corporation, out of the sale proceeds available on the settlement date, sufficient funds to cover the aggregate Exercise Price payable for the Purchased Shares plus all applicable federal, state and local income and employment taxes required to be withheld by the Corporation by reason of such exercise and (2) to the Corporation to deliver the certificates for the Purchased Shares directly to such brokerage firm in order to complete the sale.

Except to the extent the sale and remittance procedure is utilized in connection with the option exercise, payment of the Exercise Price must accompany the Stock Option Exercise Notice and Purchase Agreement delivered to the Corporation in connection with the option exercise.

(3) Furnish to the Corporation appropriate documentation that the person or persons exercising the option (if other than Optionee) have the right to exercise this option.

(4) Execute and deliver to the Corporation such written representations as may be requested by the Corporation in order for it to comply with the applicable requirements of federal and state securities laws.

(5) Make appropriate arrangements with the Corporation (or Parent or Subsidiary employing or retaining Optionee) for the satisfaction of all federal, state and local income and employment tax withholding requirements applicable to the option exercise.

a. As soon as practical after the Exercise Date, the Corporation shall issue to, or, on behalf of Optionee (or any other person or persons

exercising this option), a share certificate for the Purchased Shares.

b. In no event may this option be exercised for any fractional shares.

#### 9. COMPLIANCE WITH LAWS AND REGULATIONS

a. The exercise of this option and the issuance of the Option Shares upon such exercise shall be subject to compliance by the Corporation and Optionee with all applicable requirements of law relating thereto and with all applicable regulations of any stock exchange (or Nasdaq, if applicable) on which the Common Stock may be listed for trading at the time of such exercise and issuance.

b. The inability of the Corporation to obtain approval from any regulatory body having authority deemed by the Corporation to be necessary to the lawful issuance and sale of any Common Stock pursuant to this option shall relieve the Corporation of any liability with respect to the non-issuance or sale of the Common Stock as to which such approval shall not have been obtained. The Corporation, however, shall use its best efforts to obtain all such approvals.

10. SUCCESSIONS AND ASSIGNS. Except to the extent otherwise provided in paragraph 3, the provisions of this Agreement shall inure to the benefit of, and be binding upon, the Corporation and its successors and assigns and Optionee, Optionee's permitted assigns and the legal representatives, heirs and legatees of Optionee's estate.

11. NOTICES. Any notice required to be given or delivered to the Corporation under the terms of this Agreement shall be in writing and addressed to the Corporation at its principal corporate offices. Any notice required to be given or delivered to Optionee shall be in writing and addressed to Optionee at the address indicated on the Stock Option Grant. All notices shall be deemed effective upon personal delivery or upon deposit in the U.S. mail, postage prepaid and properly addressed to the party to be notified.

12. FINANCING. The Plan Administrator may, in its absolute discretion and without any obligation to do so, permit Optionee to pay the Exercise Price for the purchase Option Shares by delivering a full-recourse promissory note payable to the Corporation. The terms of any such promissory note (including the interest rate, the requirements for collateral and the terms of repayment) shall be established by the Plan Administrator in its sole discretion.

13. CONSTRUCTION. This Agreement and the option evidenced hereby are made and granted pursuant to the Plan and are in all respects limited by and subject to the terms of the Plan and the Stock Option Exercise Notice and Purchase Agreement. All decisions of the Plan Administrator with respect to any question or issue arising under the Plan or this Agreement shall be conclusive and binding on all persons having an interest in this option.

14. GOVERNING LAW. The interpretation, performance and enforcement of this Agreement shall be governed by the laws of the State of Utah without resort to its conflict-of-laws rules.

15. ADDITIONAL TERMS APPLICABLE TO AN INCENTIVE OPTION. In the event this option is designated an Incentive Option above, the following terms and conditions shall also apply to the grant:

a. This option shall cease to qualify for favorable tax treatment as an Incentive Option if (and to the extent) this option is exercised for one or more Option Shares: (1) more than three (3) months after the date Optionee ceases to be an Employee or in the Service of the Corporation for any reason other than death or Permanent Disability or (2) more than twelve (12) months after the date Optionee ceases to be an Employee by reason of death or Permanent Disability.

b. No installment under this option shall qualify for favorable tax treatment as an Incentive Option if (and to the extent) the aggregate Fair Market Value (determined at the Grant Date) of the Common Stock for which such installment first becomes exercisable hereunder would, when added to the aggregate value (determined as of the respective date or dates of grant) of any earlier installments of the Common Stock and any other securities for which this option or any other Incentive Options granted to Optionee prior to the Grant Date (whether under the Plan or any other option plan of the Corporation or any Parent or Subsidiary) first become exercisable during the same calendar year, exceed One Hundred Thousand Dollars (\$100,000) in the aggregate. Should such One Hundred Thousand Dollar (\$100,000) limitation be exceeded in any calendar year, this option shall nevertheless become exercisable for the excess shares in such calendar year as a Non-Statutory Option.

c. Should the Board elect to accelerate the exercisability of this option upon a Corporate Transaction, then this option shall qualify as an Incentive Option only to the extent the aggregate Fair Market Value (determined at the Grant Date) of the Common Stock for which this option first becomes exercisable in the calendar year in which the Corporate Transaction occurs does not, when added to the aggregate value (determined as of the respective date or dates of grant) of the Common Stock or other securities for which this option or one or more other Incentive Options granted to Optionee prior to the Grant Date (whether under the Plan or any other option plan of the Corporation or any Parent or Subsidiary) first become exercisable during the same calendar year, exceed One Hundred Thousand Dollars (\$100,000) in the aggregate. Should the applicable One Hundred Thousand Dollar (\$100,000) limitation be exceeded in the calendar year of such Corporate Transaction, the option may nevertheless be exercised for the excess shares in such calendar year as a Non-Statutory Option.

d. Should Optionee hold, in addition to this option, one or more other options to purchase Common Stock which become exercisable for the first time in the same calendar year as this option, then the foregoing limitations on the exercisability of such options as Incentive Options shall be applied on the basis of the order in which such options are granted.

e. The grant of this option is subject to approval of the Plan by Corporation's stockholders within twelve (12) months after the adoption of the Plan by the Board. In the event that such stockholder approval is not obtained, then this option shall not qualify as an Incentive Option.

f. If the Option Shares covered by this Agreement exceed, as of the Grant Date, the number of shares of Common Stock which may without stockholder approval be issued under the Plan, then this option shall cease to qualify as an Incentive Option unless stockholder approval of an amendment sufficiently increasing the number of shares of Common Stock issuable under the Plan is obtained in accordance with the provisions of the Plan.

g. If Optionee is a 10% Stockholder, then the Exercise Price shall not be less than one hundred ten percent (110%) of the Fair Market Value per share of Common Stock on the Grant Date, and the option term shall not exceed five (5) years measured from the Grant Date.

h. Shares purchased pursuant to this option shall cease to qualify for favorable tax treatment as Incentive Option shares if and to the extent Optionee disposes of such shares within two (2) years from the Grant Date or within one (1) year of Optionee's purchase of said shares.

i. Optionee acknowledges that the rules regarding Incentive Options as contained in the Internal Revenue Code are subject to amendment in the future. Optionee should consult his or her tax advisor prior to taking any action with respect to this option or the shares purchased hereunder.

IN WITNESS WHEREOF, this Agreement is executed as of the Grant Date first noted above.

GENTNER COMMUNICATIONS  
CORPORATION

By\_\_\_\_\_

Title\_\_\_\_\_



## ACKNOWLEDGEMENT

Optionee understands and agrees that the option is granted subject to and in accordance with the terms of the Corporation's 1998 Stock Option Plan (the "Plan"). Optionee further agrees to be bound by the terms of the Plan and the terms of the option as set forth in this Agreement. Optionee understands that any Option Shares purchased under the option shall be subject to the terms set forth in the Stock Option Exercise Notice and Purchase Agreement attached hereto as Exhibit A.

Optionee hereby acknowledges receipt of a copy of the Plan in the form attached hereto as Exhibit B, and represents that Optionee has read and understands the Plan, and accepts this option subject to all terms and provisions of the Plan and the Plan documents. Optionee hereby agrees to accept as binding, conclusive and final, all decisions and interpretations of the Board of Directors upon any questions arising under the Plan. Optionee acknowledges that there may be adverse tax consequences upon exercise of this option and/or upon disposition of the Purchased Shares, and that Optionee should consult a tax advisor prior to such exercise or disposition.

OPTIONEE

-----  
OPTIONEE-----  
DATE

## SCHEDULE 1

-----  
Name of Optionee

-----  
Date of Grant

-----  
Number of Option Shares

This Schedule 1 sets forth the vesting of stock options granted pursuant to the Gentner Communications, Inc. Stock Option Grant referenced above.

Fiscal Year (June 30)	Annual Earnings Per Share(\$)		Percentage of the one-fifth installment that vests
	From	To	
1999	0.0000	0.1699	0%
	0.1700	0.1799	50%
	0.1800	0.1899	60%
	0.1900	0.1999	70%
	0.2000	0.2099	80%
	0.2100	0.2199	90%
	>0.2199		100%
2000	0.0000	0.2799	0%
	0.2800	0.2899	50%
	0.2900	0.2999	60%
	0.3000	0.3099	70%
	0.3100	0.3199	80%
	0.3200	0.3299	90%
	>0.3299		100%
2001	0.0000	0.4199	0%
	0.4200	0.4399	50%
	0.4400	0.4599	60%
	0.4600	0.4799	70%
	0.4800	0.4999	80%
	0.5000	0.5199	90%
	>0.5199		100%
2002	0.0000	0.6399	0%
	0.6400	0.6899	50%
	0.6900	0.7399	60%
	0.7400	0.7899	70%
	0.7900	0.8399	80%
	0.8400	0.8899	90%
	>0.8899		100%
2003	0.0000	1.0499	0%
	1.0500	1.1299	50%
	1.1300	1.2099	60%
	1.2100	1.2899	70%
	1.2900	1.3699	80%
	1.3700	1.4499	90%
	>1.4499		100%

## EXHIBIT A

GENTNER COMMUNICATIONS CORPORATION  
STOCK OPTION EXERCISE NOTICE  
AND PURCHASE AGREEMENT

This Stock Option Exercise Notice and Purchase Agreement ("Agreement") is made as of this \_\_\_\_ day of \_\_\_\_\_, 19\_\_\_\_, by and between Gentner Communications Corporation, a Utah corporation and \_\_\_\_\_, Optionee under the Corporation's 1998 Stock Option Plan (the "Plan").

All capitalized terms used in this Agreement and not defined herein shall have the meaning assigned to them in the Appendix to the Plan.

# 1. EXERCISE OF OPTION

a. EXERCISE. Optionee hereby elects to exercise Optionee's option to purchase \_\_\_\_\_ (\_\_\_\_\_) shares of Common Stock (the "Purchased Shares") of the Corporation, pursuant to that certain option (the "Option") granted Optionee on \_\_\_\_\_, 19\_\_\_\_ (the "Grant Date") to purchase \_\_\_\_\_ shares of Common Stock under the Plan at the exercise price of \$\_\_\_\_\_ per share (the "Exercise Price").

b. PAYMENT. Concurrent with the delivery of this Agreement to the Corporation, Optionee shall pay the Exercise Price for the Purchased Shares in accordance with the provisions of the Stock Option Grant and shall deliver whatever additional documents may be required by the Stock Option Grant as a condition for exercise with respect to the Purchased Shares.

# 2. MARKET STAND-OFF AGREEMENT

a. RESTRICTION ON TRANSFER. In connection with any underwritten public offering by the Corporation of its equity securities pursuant to an effective registration statement filed under the 1933 Act, including the Corporation's initial public offering, Owner shall not sell, make any short sale of, loan, hypothecate, pledge, grant any option for the purchase of, or otherwise dispose or transfer for value or otherwise agree to engage in any of the foregoing transactions with respect to, any Purchased Shares without the prior written consent of the Corporation or its underwriters. Such restrictions (the "Market Stand-Off") shall be in effect for such period of time from and after the effective date of the final prospectus for the offering as may be requested by the Corporation or such underwriters. In no event, however, shall such period exceed one hundred eighty (180) days and the Market Stand-Off shall in all events terminate two (2) years after the effective date of the Corporation's initial public offering.

b. OFFICERS AND DIRECTORS. Owner shall be subject to the Market Stand-Off provided and only if the officers and directors of the Corporation are also subject to similar restrictions.

c. ADDITIONAL SHARES. Any new, substituted or additional securities which are, by reason of any Recapitalization or Reorganization, distributed with respect to the Purchased Shares shall be immediately subject to the Market Stand-Off, to the same extent the Purchased Shares are at such time covered by such provisions.

d. STOP TRANSFER. In order to enforce the Market Stand-Off, the Corporation may impose stop-transfer instructions with respect to the Purchased Shares until the end of the applicable stand-off period.

# 3. MISCELLANEOUS PROVISIONS

a. NO EMPLOYMENT OR SERVICE CONTRACT. Nothing in this Agreement or in the Plan shall confer upon Optionee any right to continue in Service for any period of specific duration or interfere with or otherwise restrict in any way the rights of the Corporation (or any Parent or Subsidiary employing or retaining Optionee) or of Optionee, which rights are hereby expressly reserved by each, to terminate Optionee's Service at any time for any reason with or without cause.

b. NOTICES. Any notice required to be given under this Agreement shall be in writing and shall be deemed effective upon personal delivery or upon deposit in the U.S. mail, registered or certified, postage prepaid and properly addressed to the party entitled to such notice at the address indicated below such party's signature line on this Agreement or at such other address as such party may designate by ten (10) days' advance written notice under this paragraph to all other parties to this Agreement.

c. AMENDMENTS AND WAIVERS. No waiver or amendment of this Agreement shall be effective unless agreed to in writing by the parties hereto. No waiver of any breach or condition of this Agreement shall be deemed to be a waiver of any other or subsequent breach or condition, whether of like or different nature.

d. OPTIONEE UNDERTAKING. Optionee hereby agrees to take whatever additional action and execute whatever additional documents the Corporation may deem necessary or advisable in order to carry out or effect one or more of the obligations or restrictions imposed on either Optionee or the Purchased Shares pursuant to the provisions of this Agreement.

e. GOVERNING LAW. This Agreement shall be governed by, and construed in accordance with, the laws of the State of Utah without resort to that State's conflict-of-laws rules.



f. SUCCESSORS AND ASSIGNS. The provisions of this Agreement shall inure to the benefit of, and be binding upon, the Corporation and its successors and assigns and upon Optionee, Optionee's permitted assigns and the legal representatives, heirs and legatees of Optionee's estate, whether or not any such person shall have become a party to this Agreement and have agreed in writing to join herein and be bound by the terms hereof.

IN WITNESS WHEREOF, the parties have executed this Agreement on the day and year first indicated above.

GENTNER COMMUNICATIONS CORPORATION

By:\_\_\_\_\_

Title:\_\_\_\_\_

\_\_\_\_\_  
OPTIONEE

Address:\_\_\_\_\_

\_\_\_\_\_

EXHIBIT B  
1998 STOCK OPTION PLAN  
ARTICLE 1.  
GENERAL PROVISIONS

1.1. PURPOSE OF THE PLAN

This 1998 Stock Option Plan (the "Plan") is intended to promote the interests of Gentner Communications Corporation, a Utah corporation, (the "Corporation") by providing eligible persons with the opportunity to acquire or increase their proprietary interest in the Corporation as an incentive for them to remain in the Service of the Corporation.

Capitalized terms shall have the meanings assigned to such terms in the attached Appendix.

1.2. ADMINISTRATION OF THE PLAN

a. The Plan shall be administered by the Board or, to the extent required under applicable Stock Exchange requirements or if desired by the Board, a committee of the Board. If administered by committee, the Primary Committee shall have sole and exclusive authority to administer the Plan with respect to Section 16 Insiders; committee authority to administer the Plan with respect to all other persons may be vested in either the Primary Committee or a Secondary Committee, as determined by the Board.

b. Members of the Primary Committee or any Secondary Committee shall serve for such period of time as the Board may determine and may be removed by the Board at any time. The Board may terminate the functions of any Secondary Committee at any time and delegate all powers and authority previously delegated to such committee to the Primary Committee. To the extent committee administration is no longer required by applicable law, regulation or Stock Exchange requirement, the Board may also terminate the functions of any committee at any time and reassume all powers and authority previously delegated to such committee.

c. Each Plan Administrator shall, within the scope of its administrative functions under the Plan, have full power and authority to establish such rules and regulations as it may deem appropriate for proper administration of the Plan and to make such determinations under, and issue such interpretations of, the provisions of the Plan and any outstanding options thereunder as it may deem necessary or advisable. Decisions of the Plan Administrator within the scope of its administrative functions under the Plan shall be final and binding on all parties who have an interest in the Plan under its jurisdiction or any option thereunder.

d. Service on the Primary Committee or the Secondary Committee shall constitute service as a Board member, and members of each such committee shall accordingly be entitled to full indemnification and reimbursement as Board members for their service on such committee. No member of the Primary Committee or the Secondary Committee shall be liable for any act or omission made in good faith with respect to the Plan or any option grants under the Plan.

e. Each Plan Administrator shall, within the scope of its administrative jurisdiction under the Plan, have full authority (subject to the provisions of the Plan) to determine which eligible persons are to receive option grants, the time or times when such option grants are to be made, the number of shares to be covered by each such grant, the status of the granted option as either an Incentive Option or a Non-Statutory Option, the time or times at which each option is to become exercisable, the vesting schedule (if any) applicable to the option shares, the acceleration of such vesting schedule, and all other terms and conditions of the option grants.

1.3. ELIGIBILITY



The following persons shall be eligible to participate in the Plan:

a. Employees,

b. non-employee members of the Board or the board of directors of any Parent or Subsidiary, and

c. consultants and other independent advisors who provide Services to the Corporation or any Parent or Subsidiary.

#### 1.4. STOCK SUBJECT TO THE PLAN

a. The stock issuable under the Plan shall be shares of authorized but unissued Common Stock, including shares repurchased by the Corporation on the open market. The maximum number of shares of Common Stock which may be issued over the term of the Plan shall not exceed 1,700,000 shares, which number of shares may be changed from time to time in accordance with Article 3.4 below.

b. Shares of Common Stock subject to outstanding options shall be available for subsequent issuance under the Plan to the extent (i) the options expire or terminate for any reason prior to exercise in full or (ii) the options are cancelled in accordance with the cancellation-regrant provisions of Article 2.4. However, should the Exercise Price be paid with shares of Common Stock or should shares of Common Stock otherwise issuable under the Plan be withheld by the Corporation in satisfaction of the withholding taxes incurred in connection with the exercise of an option under the Plan, then the number of shares of Common Stock available for issuance under the Plan shall be reduced by the gross number of shares for which the option is exercised, and not by the net number of shares of Common Stock issued to the holder of such option.

c. Should any change be made to the Common Stock by reason of any stock split, stock dividend, recapitalization, combination of shares, exchange of shares or other change affecting the outstanding Common Stock as a class without the Corporation's receipt of consideration, appropriate adjustments shall be made to (i) the maximum number and/or class of securities issuable under the Plan, (ii) the number and/or class of securities for which any one person may be granted options per calendar year, and (iii) the number and/or class of securities and the Exercise Price in effect under each outstanding option in order to prevent the dilution or enlargement of benefits thereunder. The adjustments determined by the Plan Administrator shall be final, binding and conclusive.

### ARTICLE 2. OPTION GRANT PROGRAM

#### 2.1. OPTION TERMS

Each option shall be evidenced by one or more documents in the form approved by the Plan Administrator; provided, however, that each such document shall comply with the terms specified below. Each document evidencing an Incentive Option shall, in addition, be subject to the provisions of Article 2.2 of the Plan, below.

##### a. Exercise Price

(1) The Exercise Price shall be fixed by the Plan Administrator but shall not be less than one hundred percent (100%) of the Fair Market Value per share of Common Stock on the Grant Date.

(2) The Exercise Price shall become immediately due upon exercise of the option and shall, subject to the provisions of Article 3.1, and the documents evidencing the option, be payable in one or more of the forms specified below:

(a) cash or check made payable to the Corporation,

(b) a promissory note payable to the Corporation, but only to the extent authorized by the Administrator pursuant to Section 12 of the Plan,

(c) shares of Common Stock held for the requisite period necessary to avoid a charge to the Corporation's earnings for financial reporting purposes and valued at Fair Market Value on the Exercise Date, but only upon prior written approval of the Plan Administrator, or

(d) upon the prior written approval of the Plan Administrator, and to the extent the option is exercised for vested shares, through a special sale and remittance procedure pursuant to which the Optionee shall concurrently provide irrevocable written instructions to (a) a Corporation-designated brokerage firm to effect the immediate sale of the Purchased Shares and remit to the Corporation, out of the sale proceeds available on the settlement date, sufficient funds to cover the aggregate Exercise Price payable for the Purchased Shares plus all applicable federal, state and local income and employment taxes required to be withheld by the Corporation by reason of such exercise and (b) the Corporation to deliver the certificates for the Purchased Shares directly to such brokerage firm in order to complete the sale.

Except to the extent such sale and remittance procedure is utilized, payment of the Exercise Price for the Purchased Shares must be made on the Exercise Date.

b. Exercise and Term of Options. Each option shall be exercisable at such time or times, during such period and for such number of shares as shall be determined by the Plan Administrator and set forth in the documents evidencing the option. However, no option shall have a term in excess of ten (10) years measured from the Grant Date.

c. Effect of Termination of Service

(1) The following provisions shall govern the exercise of any options held by the Optionee at the time of cessation of Service:

(a) Any option outstanding at the time of the Optionee's cessation of Service for any reason except death, Permanent Disability or Misconduct shall remain exercisable for a three (3) month period thereafter, provided no option shall be exercisable after the Expiration Date.

(b) Any option outstanding at the time of the Optionee's cessation of Service due to death or Permanent Disability shall remain exercisable for a twelve (12) month period thereafter, provided no option shall be exercisable after the Expiration Date. Subject to the foregoing, any option exercisable in whole or in part by the Optionee at the time of death may be exercised subsequently by the personal representative of the Optionee's estate or by the person or persons to whom the option is transferred pursuant to the Optionee's will or in accordance with the laws of descent and distribution.

(c) Should the Optionee's Service be terminated for Misconduct, then all outstanding options held by the Optionee shall terminate immediately and cease to be outstanding.

(d) During the applicable post-Service exercise period, the option may not be exercised in the aggregate for more than the number of shares for which the option is exercisable on the date of the Optionee's cessation of Service; the option shall, immediately upon the Optionee's cessation of Service, terminate and cease to be outstanding to the extent the option is not otherwise at that time exercisable. Upon the expiration of the applicable exercise period or (if earlier) upon the Expiration Date, the option shall terminate and cease to be outstanding for any shares for which the option has not been exercised.

(2) The Plan Administrator shall have the discretion, exercisable either at the time an option is granted or at any time while the option remains outstanding, to:

(a) extend the period of time for which the option is to remain exercisable following the Optionee's cessation of Service from the period otherwise in effect for that option to such greater

period of time as the Plan Administrator shall deem appropriate, but in no event beyond the Expiration Date, and/or

(b) permit the option to be exercised, during the applicable post-Service exercise period, not only with respect to the number of shares of Common Stock for which such option is exercisable at the time of the Optionee's cessation of Service but also with respect to one or more additional shares that would have vested under the option had the Optionee continued in Service.

d. Stockholder Rights. The holder of an option shall have no stockholder rights with respect to the shares subject to the option until such person shall have exercised the option, paid the Exercise Price, and become a holder of record of the Purchased Shares.

e. Limited Transferability of Options. During the lifetime of the Optionee, Incentive Options may be exercised only by the Optionee, and shall not be assignable or transferable except by will or the laws of descent and distribution following the Optionee's death. Non-Statutory Options may be assigned or transferred in whole or in part only (i) during the Optionee's lifetime if in connection with the Optionee's estate plan to one or more members of the Optionee's immediate family (spouse and children) or to a trust established exclusively for the benefit of one or more such immediate family members, or (ii) by will or the laws of descent and distribution following the Optionee's death. The assigned portion may only be exercised by the person or persons who acquire a proprietary interest in the option pursuant to the assignment. The terms applicable to the assigned portion shall be the same as those in effect for the option immediately prior to such assignment and shall be set forth in such documents issued to the assignee as the Plan Administrator may deem appropriate.

## 2.2. INCENTIVE OPTIONS

The terms specified below shall apply to all Incentive Options. Except as modified by the provisions of this Article 2.2, all the provisions of this Plan shall apply to Incentive Options. Options specifically designated as Non-Statutory Options when issued under the Plan shall not be subject to the terms of this Article 2.2.

a. Eligibility. Incentive Options may only be granted to Employees.

b. Exercise Price. The Exercise Price shall not be less than one hundred percent (100%) of the Fair Market Value per share of Common Stock on the Grant Date.

c. Dollar Limitation. The aggregate Fair Market Value of the shares of Common Stock (determined as of the respective date or dates of grant) for which one or more options granted to any Employee under the Plan (or any other option plan of the Corporation or any Parent or Subsidiary) may for the first time become exercisable as Incentive Options during any one (1) calendar year shall not exceed the sum of One Hundred Thousand Dollars (\$100,000). To the extent the Employee holds two (2) or more such options which become exercisable for the first time in the same calendar year, the foregoing limitation on the exercisability of such options as Incentive Options shall be applied in the order in which such options are granted.

d. 10% Stockholder. If an Employee to whom an Incentive Option is granted is a 10% Stockholder, then the Exercise Price shall not be less than one hundred ten percent (110%) of the Fair Market Value per share of Common Stock on the Grant Date, and the option term shall not exceed five (5) years measured from the Grant Date.

e. Holding Period. Shares purchased pursuant to an option shall cease to qualify for favorable tax treatment as Incentive Option Shares if and to the extent Optionee disposes of such shares within two (2) years of the Grant Date or within one (1) year of Optionee's purchase of said shares.

## 2.3. CORPORATE TRANSACTION/CHANGE IN CONTROL

a. In the event of any Corporate Transaction, the Board of Directors shall have the sole discretion to elect that each outstanding option shall automatically accelerate so that each such option shall, immediately prior to the effective date of the Corporate Transaction, become fully exercisable for all of the shares of Common Stock at the time

subject to such option and may be exercised for any or all of those shares as fully-vested shares of Common Stock. The Board may exercise its discretion to accelerate the vesting of options whether or not (i) such option is, in connection with the Corporate Transaction, either to be assumed by the successor corporation or parent thereof or to be replaced with a comparable option to purchase shares of the capital stock of the successor corporation or parent thereof, (ii) such option is to be replaced with a cash incentive program of the successor corporation which preserves the spread existing on the unvested option shares at the time of the Corporate Transaction and provides for subsequent payout in accordance with the same vesting schedule applicable to such option, except to the extent that the acceleration of such option is subject to other limitations imposed by the Plan Administrator at the time of the option grant.

b. The Plan Administrator's discretion under Article 2.3.a. above shall be exercisable either at the time the option is granted or at any time while the option remains outstanding, whether or not those options are to be assumed or replaced in the Corporate Transaction. The Plan Administrator shall also have the discretion to grant options which do not accelerate whether or not such options are assumed in connection with a Corporate Transaction.

c. If the Board of Directors elects the automatic acceleration of some or all of the outstanding options upon the occurrence of a Corporate Transaction, all such outstanding options shall terminate and cease to be outstanding, except to the extent assumed by the successor corporation (or parent thereof) immediately following the consummation of the Corporate Transaction.

d. Each option which is assumed in connection with a Corporate Transaction shall be appropriately adjusted, immediately after such Corporate Transaction, to apply to the number and class of securities that would have been issuable to the Optionee in consummation of such Corporate Transaction had the option been exercised immediately prior to such Corporate Transaction. Appropriate adjustments shall also be made to (i) the number and class of securities available for issuance under the Plan following the consummation of such Corporate Transaction, (ii) the exercise price payable per share under each outstanding option, provided the aggregate exercise price payable for such securities shall remain the same and (iii) the maximum number of securities and/or class of securities for which any one person may be granted stock options.

e. The Plan Administrator shall have the discretion, exercisable at the time the option is granted or at any time while the option remains outstanding, to provide for the automatic acceleration of any options assumed or replaced in a Corporate Transaction that do not otherwise accelerate at that time in the event the Optionee's Service should subsequently terminate by reason of an Involuntary Termination within eighteen (18) months following the effective date of such Corporate Transaction. Any options so accelerated shall remain exercisable for shares until the earlier of (i) the expiration of the option term or (ii) the expiration of the one (1)-year period measured from the effective date of the Involuntary Termination.

f. The Plan Administrator shall have the discretion, exercisable either at the time the option is granted or at any time while the option remains outstanding, to (i) provide for the automatic acceleration of one or more outstanding options upon the occurrence of a Change in Control or (ii) condition any such option acceleration upon the subsequent Involuntary Termination of the Optionee's Service within a specified period (not to exceed eighteen (18) months) following the effective date of such Change in Control. Any options accelerated in connection with a Change in Control shall remain fully exercisable until the Expiration Date or sooner termination of the option term.

g. The portion of any Incentive Option accelerated in connection with a Corporate Transaction or Change in Control shall remain exercisable as an Incentive Option only to the extent the applicable One Hundred Thousand Dollar (\$100,000) limitation is not exceeded. To the extent such dollar limitation is exceeded, the accelerated portion of such option shall be exercisable as a Non-Statutory Option under the federal tax laws.

h. The grant of options under the Plan shall in no way affect the right of the Corporation to adjust, reclassify, reorganize or otherwise change its capital or business structure or to merge, consolidate, dissolve, liquidate or sell or transfer all or any part of its business or assets.

ARTICLE 3.  
MISCELLANEOUS

3.1. FINANCING

a. The Plan Administrator may permit any Optionee to pay the option Exercise Price by delivering a promissory note payable in one or more installments. The terms of any such promissory note (including the interest rate and the terms of repayment) shall be established by the Plan Administrator in its sole discretion. Promissory notes may be authorized with or without security or collateral. In all events, the maximum credit available to the Optionee may not exceed the sum of (i) the aggregate option Exercise Price payable for the Purchased Shares plus (ii) the amount of any federal, state and local income and employment tax liability incurred by the Optionee in connection with the option exercise.

b. The Plan Administrator may, in its discretion, determine that one or more such promissory notes shall be subject to forgiveness by the Corporation in whole or in part upon such terms as the Plan Administrator may deem appropriate.

3.2. TAX WITHHOLDING

a. The Corporation's obligation to deliver shares of Common Stock upon the exercise of options under the Plan shall be subject to the satisfaction of all applicable federal, state and local income and employment tax withholding requirements.

b. The Plan Administrator may, in its discretion, provide any or all holders of Non-Statutory Options under the Plan with the right to use shares of Common Stock in satisfaction of all or part of the Taxes incurred by such holders in connection with the exercise of their options. Such right may be provided to any such holder in either or both of the following formats:

(1) Stock Withholding: The election to have the Corporation withhold, from the shares of Common Stock otherwise issuable upon the exercise of such Non-Statutory Option, a portion of those shares with an aggregate Fair Market Value equal to the percentage of the Taxes (not to exceed one hundred percent (100%)) designated by the holder.

(2) Stock Delivery: The election to deliver to the Corporation, at the time the Non-Statutory Option is exercised, one or more shares of Common Stock previously acquired by such holder (other than in connection with the option exercise triggering the Taxes) with an aggregate Fair Market Value equal to the percentage of the Taxes (not to exceed one hundred percent (100%)) designated by the holder.

3.3. EFFECTIVE DATE AND TERM OF THE PLAN

a. The Plan shall become effective on the Plan Effective Date. However, no shares shall be issued under the Plan pursuant to Incentive Options until the Plan is approved by the Corporation's stockholders. If such stockholder approval is not obtained within twelve (12) months after the Plan Effective Date, then all Incentive Options previously granted under this Plan shall automatically convert into Non-Statutory Options.

b. The Plan shall terminate upon the earliest of (i) June 10, 2008, (ii) the date on which all shares available for issuance under the Plan shall have been issued, or (iii) the termination of all outstanding options in connection with a Corporate Transaction. Upon such Plan termination, all outstanding options shall continue to have force and effect in accordance with the provisions of the documents evidencing such options.

#### 3.4. AMENDMENT OF THE PLAN

a. The Board shall have complete and exclusive power and authority to amend or modify the Plan in any or all respects, or to cancel any grants made thereunder; provided, however, that no such amendment, modification, or cancellation shall adversely affect any rights and obligations with respect to options at the time outstanding under the Plan unless each affected Optionee consents to such amendment, modification, or cancellation. In addition, amendments to the Plan shall be subject to approval of the Corporation's stockholders to the extent required by applicable laws, regulations, or Nasdaq or Stock Exchange requirements.

b. Options to purchase shares of Common Stock may be granted under the Plan that are in each instance in excess of the number of shares then available for issuance under the Plan, provided any excess shares actually issued are held in escrow until there is obtained Board approval (and shareholder approval if required by applicable laws, regulations, or Stock Exchange requirements) of an amendment sufficiently increasing the number of shares of Common Stock available for issuance under the Plan.

#### 3.5. USE OF PROCEEDS

Any cash proceeds received by the Corporation from the sale of shares of Common Stock under the Plan shall be used for general corporate purposes.

#### 3.6. REGULATORY APPROVALS

a. The implementation of the Plan, the granting of any option under the Plan, and the issuance of any shares of Common Stock upon the exercise of any option shall be subject to the Corporation's obtaining all approvals and permits required by regulatory authorities having jurisdiction over the Plan and the options granted under it, and the shares of Common Stock issued pursuant to the Plan.

b. No shares of Common Stock shall be issued or delivered under the Plan unless and until there shall have been compliance with all applicable requirements of federal and state securities laws and all applicable listing requirements of any stock exchange (or the Nasdaq market, if applicable) on which Common Stock is then listed for trading.

#### 3.7. NO EMPLOYMENT/SERVICE RIGHTS

Nothing in the Plan shall confer upon the Optionee any right to continue in Service for any period of specific duration or interfere with or otherwise restrict in any way the rights of the Corporation (or any Parent or Subsidiary employing or retaining such person) or of the Optionee, which rights are hereby expressly reserved by each, to terminate such person's Service at any time for any reason, with or without cause.

## APPENDIX

The following definitions shall be in effect under the Plan and the Plan Documents:

0.1. BOARD shall mean the Corporation's Board of Directors.

2. CHANGE IN CONTROL shall mean a change in ownership or control of the Corporation effected through either of the following transactions:

(i) the acquisition, directly or indirectly, by any person or related group of persons (other than the Corporation or a person that directly or indirectly controls, is controlled by, or is under common control with, the Corporation), of beneficial ownership (within the meaning of Rule 13d-3 of the 1934 Act) of securities possessing more than fifty percent (50%) of the total combined voting power of the Corporation's outstanding securities pursuant to a tender or exchange offer made directly to the Corporation's stockholders, which the Board does not recommend such stockholders to accept, or

(ii) a change in the composition of the Board over a period of thirty-six (36) consecutive months or less such that a majority of the Board members ceases, by reason of one or more contested elections for Board membership, to be comprised of individuals who either (A) have been Board members continuously since the beginning of such period or (B) have been elected or nominated for election as Board members during such period by at least a majority of the Board members described in clause (A) who were still in office at the time the Board approved such election or nomination.

3. CODE shall mean the Internal Revenue Code of 1986, as amended.

4. COMMON STOCK shall mean the Corporation's common stock.

5. CORPORATE TRANSACTION shall mean either of the following stockholder-approved transactions to which the Corporation is a party:

(i) a merger or consolidation in which securities possessing more than fifty percent (50%) of the total combined voting power of the Corporation's outstanding securities are transferred to a person or persons different from the persons holding those securities immediately prior to such transaction; or

(ii) the sale, transfer or other disposition of all or substantially all of the Corporation's assets in complete liquidation or dissolution of the Corporation.

6. ELIGIBLE DIRECTOR shall mean a non-employee Board member eligible to participate in the Plan.

7. EMPLOYEE shall mean an individual who is in the employ of the Corporation (or any Parent or Subsidiary), subject to the control and direction of the employer entity as to both the work to be performed and the manner and method of performance.

8. EXERCISE DATE shall mean the date on which the Corporation shall have received written notice of the option exercise.

9. EXERCISE PRICE shall mean the exercise price per share as specified in the Stock Option Grant.

10. EXPIRATION DATE shall mean the date on which the option expires as specified in the Stock Option Grant.

11. FAIR MARKET VALUE per share of Common Stock on any relevant date shall be determined in accordance with the following provisions:

(i) If the Common Stock is traded at the time on the Nasdaq National Market, then the Fair Market Value shall be the closing selling price per share of Common Stock on the date in question, as such price is reported by the National Association of Securities Dealers on the Nasdaq National Market or any successor system. If there is no closing selling price for the Common Stock on the date in question, then the Fair Market Value shall be the closing selling price on the last preceding date for which such quotation exists.

(ii) If the Common Stock is at the time listed on any Stock Exchange, then the Fair Market Value shall be the closing selling price per share of Common Stock on the date in question on the Stock Exchange determined by the Plan Administrator to be the primary market for the Common Stock, as such price is officially quoted in the composite tape of transactions on such exchange. If there is no closing selling price for the Common Stock on the date in question, then the Fair Market Value shall be the closing selling price on the last preceding date for which such quotation exists.

(iii) If the Common Stock is not listed on any Stock Exchange nor traded on the Nasdaq National Market, then the Fair Market Value shall be determined by the Plan Administrator after taking into account such factors as the Plan Administrator shall deem appropriate.

(iv) For purposes of any option grants made on the Underwriting Date, the Fair Market Value shall be deemed to be equal to the price per share at which the Common Stock is sold in the initial public offering pursuant to the Underwriting Agreement.

12. GRANT DATE shall mean the date on which the option is granted to Optionee as specified in the Stock Option Grant.

13. INCENTIVE OPTION shall mean an option which satisfies the requirements of Code Section 422.

14. INVOLUNTARY TERMINATION shall mean the termination of the Service of any individual which occurs by reason of:

(i) such individual's involuntary dismissal or discharge by the Corporation for reasons other than Misconduct, or

(ii) such individual's voluntary resignation following (A) a change in his or her position with the Corporation which materially reduces his or her level of responsibility, (B) a reduction in his or her level of compensation (including base salary, fringe benefits and participation in corporate-performance based bonus or incentive programs) by more than fifteen percent (15%) or (C) a relocation of such individual's place of employment by more than fifty (50) miles, provided and only if such change, reduction or relocation is effected by the Corporation without the individual's consent.

15. MARKET STAND OFF shall mean the market stand off restriction on disposition of the Purchased Shares as identified under such title in the Stock Option Exercise Notice and Purchase Agreement.

16. MISCONDUCT shall mean the commission of any act of fraud, embezzlement or dishonesty by the Optionee, any unauthorized use or disclosure by such person of confidential information or trade secrets of the Corporation (or any Parent or Subsidiary), or any other intentional misconduct by such person adversely affecting the business or affairs of the Corporation (or any Parent or Subsidiary) in a material manner. The foregoing definition shall not be deemed to be inclusive of all the acts or omissions which the Corporation (or any Parent or Subsidiary) may consider as grounds for the dismissal or discharge of any Optionee or other person in the Service of the Corporation (or any Parent or Subsidiary).

17. 1933 ACT shall mean the Securities Act of 1933, as amended.

18. 1934 ACT shall mean the Securities Exchange Act of 1934, as amended.



19. NON-STATUTORY OPTION shall mean an option not intended to satisfy the requirements of Code Section 422.

20. OPTIONEE shall mean any person to whom an option is granted under Plan.

21. OPTION SHARES shall mean the number of shares of Common Stock subject to the option as specified in the Stock Option Grant.

22. OWNER shall mean Optionee and all subsequent holders of the Purchased Shares who derive their claim of ownership through a Permitted Transfer from Optionee.

23. PARENT shall mean any corporation (other than the Corporation) in an unbroken chain of corporations ending with the Corporation, provided each corporation in the unbroken chain (other than the Corporation) owns, at the time of the determination, stock possessing fifty percent (50%) or more of the total combined voting power of all classes of stock in one or the other corporations in such chain.

24. PERMANENT DISABILITY OR PERMANENTLY DISABLED shall mean the inability of the Optionee to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment expected to result in death or to be of continuous duration of twelve (12) months or more.

25. PERMITTED TRANSFER shall mean (i) a gratuitous transfer of the Purchased Shares, provided and only if Optionee obtains the Corporation's prior written consent to such transfer, (ii) a transfer of title to the Purchased Shares effected pursuant to Optionee's will or the laws of intestate succession following Optionee's death, or (iii) a transfer to the Corporation in pledge as security for any purchase-money indebtedness incurred by Optionee in connection with the acquisition of the Purchased Shares.

26. PLAN ADMINISTRATOR shall mean the particular entity, whether the Board or a committee of the Board, which is authorized to administer the Plan with respect to one or more classes of eligible persons, to the extent such entity is carrying out its administrative functions under the Plan with respect to the persons under its jurisdiction.

27. PLAN DOCUMENTS shall mean the Plan, the Stock Option Grant, and Stock Option Exercise Notice and Purchase Agreement, collectively.

28. PLAN EFFECTIVE DATE shall mean \_\_\_\_\_, the date on which the Plan was adopted by the Board.

29. PRIMARY COMMITTEE shall mean the committee of two (2) or more non-employee Board members (as defined in the regulations to Section 16 of the 1934 Act) appointed by the Board to administer the Plan with respect to Section 16 Insiders.

30. PURCHASED SHARES shall mean the shares purchased upon exercise of the Option.

31. RECAPITALIZATION shall mean any stock split, stock dividend, recapitalization, combination of shares, exchange of shares or other charge affecting the Corporation's outstanding Common Stock as a class without the Corporation's receipt of consideration.

32. REORGANIZATION shall mean any of the following transactions:

(i) a merger or consolidation in which the Corporation is not the surviving entity;

(ii) a sale, transfer or other disposition of all or substantially all of the Corporation's assets;

(iii) a reverse merger in which the Corporation is the surviving entity but in which the Corporation's outstanding voting securities are transferred in whole or in part to a person or persons different from the persons holding those securities immediately prior to the merger; or

(iv) any transaction effected primarily to change the state in which the Corporation is incorporated or to create a holding company structure.

33. SEC shall mean the Securities Exchange Commission.

34. SECONDARY COMMITTEE shall mean a committee of two (2) or more Board members appointed by the Board to administer the Plan with respect to eligible persons other than Section 16 Insiders.

35. SECTION 16 INSIDER shall mean an officer or director of the Corporation subject to the short-swing profit liabilities of Section 16 of the 1934 Act.

36. SERVICE shall mean the performance of services to the Corporation (or any Parent or Subsidiary) by a person in the capacity of an Employee, a non-employee member of the board of directors or a consultant or independent advisor, except to the extent otherwise specifically provided in the documents evidencing the option grant.

37. STOCK EXCHANGE shall mean either the American Stock Exchange, the New York Stock Exchange, another regional stock exchange, or the Nasdaq market as established by the National Association of Securities Dealers.

38. STOCK OPTION EXERCISE NOTICE AND PURCHASE AGREEMENT shall mean the agreement of said title in substantially the form of Exhibit A to the Stock Option Grant, pursuant to which Optionee gives notice of his intent to exercise the option and purchase Shares.

39. STOCK OPTION GRANT shall mean the Stock Option Grant document, pursuant to which Optionee has been informed of the basic terms of the option granted under the Plan.

40. SUBSIDIARY shall mean any corporation (other than the Corporation) in an unbroken chain of corporations beginning with the Corporation, provided each corporation (other than the last corporation) in the unbroken chain owns, at the time of the determination, stock possessing fifty percent (50%) or more of the total combined voting power of all classes of stock in one of the other corporations in such chain.

41. TAXES shall mean the Federal, state and local income and employment tax liabilities incurred by the holder of Non-Statutory Options in connection with the exercise of those options.

42. 10% STOCKHOLDER shall mean the owner of stock (as determined under Code Section 424(d)) possessing more than ten percent (10%) of the total combined voting power of all classes of stock of the Corporation (or any Parent or Subsidiary).

FIRST  
SECURITY  
BANK

## MODIFICATION AGREEMENT

PRINCIPAL	LOAN DATE	MATURITY	LOAN NO	CALL	COLLATERAL	ACCOUNT	OFFICER	INITIALS
\$2,000,000.00		12-24-1997	9001			0023791	68073	

References in the shaded area are for Lender's use only and do not limit the applicability of this document to any particular loan or item.

Borrower: Gentner Communications Corporation  
1825 Research Way  
Salt Lake City, UT 84119

Lender: First Security Bank, N.A.  
Commercial Banking  
15 East 100 South  
2nd Floor  
Salt Lake City, UT 84111

\*FMODA\*

First Security Bank, N.A. ("Lender") has extended credit (the "Loan") to Gentner Communications Corporation (individually and collectively "Borrower") pursuant to a promissory note dated October 24, 1996 (the "Note") in the stated principal amount of \$2,000,000.00. The Loan is secured by security agreements, trust deeds, mortgages, lien instruments, and/or other collateral documents (the "Collateral Documents").

The Note and any loan agreements, guaranties, subordinations, Collateral Documents, and other instruments and documents executed in connection therewith, together with any previous modifications and any of these instruments or documents, shall be referred to as the "Loan Documents."

Borrower has requested certain modifications to the Loan Documents and Lender is willing to grant such modifications on the following terms and conditions:

1. Provided that all conditions stated herein are satisfied, the terms of the Loan Documents are hereby modified as follows:

MODIFICATIONS TO THE TERMS OF THE NOTE:

The maturity date of the Note is extended to December 24, 1998.

This Agreement does not constitute a repayment of extinguishment of the Note, but only a modification thereof.

2. As preconditions to the terms of this agreement, Borrower shall complete or provide the following:

Borrower shall pay or shall have paid all reasonable fees, costs and expenses, of whatever kind or nature, incurred by Lender in connection with this Agreement, including but not limited to attorney's fees, lien search fees, title reports and policies, and recording and filing fees.

Borrower shall pay a loan fee of 0.25% of the commitment amount (\$5,000.00) upon execution of this Modification Agreement.

3. It is the intention and agreement of Borrower and Lender that: (i) all collateral security in which Lender has acquired a security interest or other lien pursuant to the Loan Documents shall continue to serve as collateral security for payment and performance of all the obligations of the Borrower under the Loan Documents, and (ii) all agreements, representations, warranties, and covenants contained in the Loan Documents are hereby reaffirmed in full by Borrower except as specifically modified by this Agreement.
4. Borrower hereby acknowledges that: (i) the Loan Documents are in full force and effect, as modified by this Agreement, and (ii) by entering into this Agreement, Lender does not waive any existing default or any default hereafter occurring or become obligated to waive any condition or obligation under the Loan Documents.
5. Borrower hereby acknowledges that Borrower has no claim, demand, lawsuit, cause of action, claim for relief, remedy, or defense against enforcement of the Loan Documents that could be asserted against Lender, its affiliates, directors, officers, employees, or agents, whether known or unknown, for acts, failures to act (whether such act or failure to act is

intentional or negligent), representations, commitments, statements or warranties, including without limitation any such conduct arising out of or in any way connected with the Loan Documents. Notwithstanding the foregoing, Borrower hereby waives, releases, and relinquishes any and all claims, demands, lawsuits, causes of action, claims for relief, remedies, or defenses against enforcement of the Loan Documents that could be asserted against Lender, its affiliates, directors, officers, employees, or agents, whether known or unknown.

6. In addition to this Agreement, the Loan Documents, and any additional documents that this Agreement requires, this finance transaction may include other written closing documentation such as resolutions, waivers, certificates, financing statements, filings, statements, closing or escrow instructions, loan purpose statements, and other documents that Lender may customarily use in such transactions. Such documents are incorporated herein by this reference. All the documents to which this paragraph makes reference express, embody, and supersede any previous understandings, agreements, or promises (whether oral or written) with respect to this finance transaction, and represent the final expression of the agreement between Lender and Borrower, the terms and conditions of which cannot hereafter be contradicted by any oral understand (if any) not reduced to writing and identified above.

FINAL AGREEMENT. Borrower understands that the loan documents signed in connection with this loan are the final expression of the agreement between Lender and Borrower and may not be contradicted by evidence of any alleged oral agreement.

Effective as of December 24, 1997.

LENDER:

First Security Bank, N.A.

By:

Authorized Officer

BORROWER:

Gentner Communications Corporation

By: /s/ Susie Strohm

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SUSIE STROHM, SECRETARY

## Consent of Independent Auditors

We consent to the incorporation by reference in this Annual Report (Form 10-KSB) of Gentner Communications Corporation of our report dated July 31, 1998, included in the 1998 Annual Report to Shareholders of Gentner Communications Corporation.

/s/ Ernst & Young, LLP

Salt Lake City, Utah  
September 28, 1998

YEAR	
	JUN-30-1998
	JUN-30-1998
	\$715,325
	0
	\$1,989,390
	(246,000)
	\$3,154,983
	\$5,828,365
	\$5,831,816
	(3,511,480)
	\$8,311,740
\$1,919,422	
	0
	0
	0
	\$7,699
	\$5,229,307
\$8,311,740	
	\$17,267,886
	\$17,294,550
	\$8,347,300
	\$15,610,730
	0
	0
	\$240,371
	\$1,443,449
	\$39,000
\$1,404,449	
	0
	0
	0
	\$1,404,449
	\$0.18
	\$0.18