Zoom Telephonics, Inc.
Form 10-Q
May 14, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

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FORM 10-Q

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(Mark One)

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

For the quarterly period ended March 31, 2010

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 0-53722

ZOOM TELEPHONICS, INC.

(Exact Name of Registrant as Specified in its Charter)

Delaware	**04-2621506**
(State or Other Jurisdiction of Incorporation or Organization)	*(I.R.S. Employer Identification No.)*

207 South Street, Boston, Massachusetts	**02111**
(Address of Principal Executive Offices)	*(Zip Code)*

Registrant s Telephone Number, Including Area Code: **(617) 423-1072**

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

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

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

Large accelerated filer ¨	Accelerated filer ¨
Non-accelerated filer ¨ (do not check if a smaller reporting company)	Smaller Reporting Company þ

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES ¨ NO þ

The number of shares outstanding of the registrant s Common Stock, $.01 par value, as of May 3, 2010, was 1,980,978 shares.

ZOOM TELEPHONICS, INC.

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Part I. - Financial Information

Part II. Other Information

INFORMATION PRESENTED IN THIS QUARTERLY REPORT

On January 28, 2009, Zoom Technologies, Inc. entered into a Share Exchange Agreement (the Agreement) with Tianjin Tong Guang Group Digital Communication Co., Ltd (TCB Digital), TCB Digital s majority shareholder, Gold Lion Holding Limited (Gold Lion) and Lei Gu (Gu), a shareholder of Gold Lion. On May 12, 2009, the parties amended the Agreement to, among other actions, add Songtao Du (Du), a shareholder of Gold Lion, as a party to the Agreement. On September 22, 2009, pursuant to the Agreement, Zoom Technologies acquired all the outstanding shares of Gold Lion. In addition, as part of the transaction, Zoom Technologies spun off its then-current business, which consisted of its ownership of Zoom Telephonics, to its stockholders, by distributing and transferring its assets and liabilities to Zoom Telephonics and issuing a dividend of the Zoom Telephonics shares to its stockholders.

Upon the completion of the spin-off, Zoom Telephonics became a separate publicly traded company. Zoom Telephonics produces, markets, sells, and supports broadband and dial-up modems, Voice over Internet Protocol or VoIP products and services, Bluetooth® wireless products, and other communication-related products (the Communications Business) which had been formerly owned and operated by Zoom Technologies.

As used in Quarterly Report on Form 10-Q, the terms we, us, our, and the Company mean Zoom Telephonics, (unless the context indicates a different meaning).

We describe in this Quarterly Report on Form 10-Q the Communications Business transferred to Zoom Telephonics by Zoom Technologies in connection with the spin-off as though the Communications Business were our business for all historical periods described. References in this Quarterly Report to the historical assets, liabilities, products, business or activities of our business are intended to refer to the historical assets, liabilities, products, business or activities of the Communications Business as those were conducted as part of Zoom Technologies prior to the date of the spin-off.

PART I - FINANCIAL INFORMATION

ITEM 1.

FINANCIAL STATEMENTS

ZOOM TELEPHONICS, INC.

Condensed Balance Sheets (Unaudited)

		March 31, 2010		December 31, 2009
ASSETS				
Current assets				
Cash and cash equivalents	$	1,202,082	$	1,223,507
Accounts receivable, net of allowances of $434,886 at March 31, 2010 and $466,595 at December 31, 2009		959,766		1,199,581
Inventories		1,714,734		1,586,079
Prepaid expenses and other current assets		196,746		223,891
Total current assets		4,073,327		4,233,058
Equipment, net		50,471		57,787
Deferred other receivable		160,763		166,144
Total assets	$	4,284,561	$	4,456,989
LIABILITIES AND STOCKHOLDERS' EQUITY				
Current liabilities				
Accounts payable	$	1,114,179	$	1,014,979
Accrued expenses		379,655		375,414
Total current liabilities		1,493,834		1,390,393
Total liabilities		1,493,834		1,390,393
Stockholders' equity				
Common stock, $0.01 par value:				
Authorized - 25,000,000 shares; issued 1,980,978 shares at March 31, 2010 and December 31, 2009		19,810		19,810
Additional paid-in capital		32,553,627		32,520,464
Accumulated deficit		(30,134,655)		(29,836,577)
		351,945		362,899

Accumulated other comprehensive income currency translation adjustment				
Total stockholders' equity		2,790,727		3,066,596
Total liabilities and stockholders' equity	$	4,284,561	$	4,456,989

See accompanying notes.

ZOOM TELEPHONICS, INC.

Condensed Statement of Operations
(Unaudited)

	Three Months Ended March 31, 2010	Three Months Ended March 31, 2009
Net sales	$ 2,493,592	$ 2,348,414
Cost of goods sold	1,730,332	1,891,869
Gross profit	763,260	456,545
Operating expenses:		
Selling	447,784	486,897
General and administrative	372,666	598,361
Research and development	305,347	362,994
	1,125,797	1,448,252
Operating profit (loss)	(362,537)	(991,707)
Other :		
Interest income	183	2,128
Other, net	64,537	44,359
Total other income (expense), net	64,720	46,487
Income (loss) before income taxes	(297,817)	(945,220)
Income taxes (benefit)	261	
Net income (loss)	$ (298,078)	$ (945,220)
Basic and diluted net income (loss) per share	$ (0.15)	$ (0.49)
Weighted average common and common equivalent shares:		
Basic and diluted	1,980,978	1,931,378

Zoom Telephonics common stock was not publicly traded prior to the September 22, 2009 Spin-Off of Zoom

Telephonics from its then parent Zoom Technologies. For comparability purposes, the calculation of weighted average common shares outstanding shown above for the quarter ended March 31, 2009 includes the common shares of Zoom Technologies outstanding for such period prior to September 22, 2009.

See accompanying notes.

ZOOM TELEPHONICS, INC.

Condensed Statements of Cash Flows
(Unaudited)

	Three Months Ended March 31, 2010	Three Months Ended March 31, 2009
Operating activities:		
Net income (loss)	$ (298,078)	$ (945,220)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	7,902	13,954
Stock based compensation	33,163	22,783
Changes in operating assets and liabilities:		
Accounts receivable, net	234,400	161,637
Inventories	(129,629)	378,986
Prepaid expenses and other assets	26,321	21,538
Accounts payable and accrued expenses	100,396	123,744
Net cash provided by (used in) operating activities	(25,525)	(222,578)
Investing activities:		
Proceeds from sale of Unity investment	5,381	
Additions to property, plant and equipment		(737)
Net cash provided by (used in) investing activities	5,381	(737)
Effect of exchange rate changes on cash	(1,281)	(446)
Net change in cash	(21,425)	(223,761)
Cash and cash equivalents at beginning of period	1,223,507	1,204,984
Cash and cash equivalents at end of period	$ 1,202,082	$ 981,223

Supplemental disclosures of cash flow information:

Cash paid during the period for:				
Interest	$		$	
Income taxes	$	261	$	

See accompanying notes.

ZOOM TELEPHONICS, INC.

Notes to Condensed Financial Statements
(Unaudited)

(1) Summary of Significant Accounting Policies

On January 28, 2009, Zoom Technologies, Inc. entered into a Share Exchange Agreement (the Agreement) with Tianjin Tong Guang Group Digital Communication Co., Ltd (TCB Digital), TCB Digital s majority shareholder, Gold Lion Holding Limited (Gold Lion) and Lei Gu (Gu), a shareholder of Gold Lion. On May 12, 2009, the parties amended the Agreement to, among other actions, add Songtao Du (Du), a shareholder of Gold Lion, as a party to the Agreement. On September 22, 2009, pursuant to the Agreement, Zoom Technologies acquired all the outstanding shares of Gold Lion. In addition, as part of the transaction, Zoom Technologies spun off its then-current business, which consisted of its ownership of Zoom Telephonics, to its stockholders, by distributing and transferring its assets and liabilities to Zoom Telephonics and issuing a dividend of the Zoom Telephonics shares to its stockholders.

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The condensed financial statements of Zoom Telephonics, Inc. (the "Company") presented herein have been prepared pursuant to the rules of the Securities and Exchange Commission for quarterly reports on Form 10-Q and do not include all of the information and disclosures required by accounting principles generally accepted in the United States of America. These financial statements should be read in conjunction with the audited financial statements and notes thereto for the year ended December 31, 2009 included in the Company's 2009 Annual Report on Form 10-K.

The accompanying financial statements are unaudited. However, the condensed balance sheet as of December 31, 2009 was derived from audited financial statements. In the opinion of management, the accompanying financial statements include all adjustments, normal recurring adjustments, necessary for a fair presentation.

The accompanying financial statements include the accounts of the Company.

The results of operations for the periods presented are not necessarily indicative of the results to be expected for the entire year.

(a)

Recently Issued or Proposed Accounting Pronouncements

In January 2010, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. 2010-06, Improving Disclosures about Fair Value Measurements (ASU 2010-06). ASU 2010-06 amends ASC 820 to require a number of additional disclosures regarding fair value measurements. The amended guidance requires entities to disclose the amounts of significant transfers between Level 1 and Level 2 of the fair value hierarchy and the reasons for these transfers, the reasons for any transfers in or out of Level 3, and information in the reconciliation of recurring Level 3 measurements about purchases, sales, issuances and settlements on a gross basis. The ASU also clarifies the requirement for entities to disclose information about both the valuation techniques and inputs used in estimating Level 2 and Level 3 fair value measurements. The amended guidance was effective for financial periods beginning after December 15, 2009, except the requirement to disclose Level 3 transactions on a gross basis, which becomes effective for financial periods beginning after December 15, 2010. ASU 2010-06 did not have a significant effect on the Company s financial position or results of operations.

(2) Liquidity

On March 31, 2010 we had working capital of $2.6 million including $1.2 million in cash and cash equivalents. On December 31, 2009 we had working capital of $2.8 million including $1.2 million in cash and cash equivalents. Our current ratio at March 31, 2010 was 2.7 compared to 3.0 at December 31, 2009. A significant portion of the reduction of the current ratio was due to the decline in accounts receivable and the increase in accounts payable.

In the first quarter of 2010 the Company s operating activities used $25 thousand in cash. The Company s net loss in the first quarter of 2010 was $0.3 million. Sources of cash from operations included a decrease in accounts receivable of $0.2 million, and an increase in accounts payable and accrued expense of $0.1 million. Use of cash from operations was an increase in inventory of $0.1 million.

In the first quarter of 2010 the Company incurred an operating loss of $0.4 million and a net loss of $0.3 million. Ongoing losses and other conditions raise substantial doubt about the Company's ability to continue as a going concern. Management does not believe that the Company has sufficient resources to fund its normal operations over the next 12 months unless sales improve significantly or the Company can raise capital. Additional financing may not be available on terms favorable to the Company, or at all. If these funds are not available the Company may not be able to execute its business plan or take advantage of business opportunities. The ability of the Company to obtain such additional financing and to achieve its operating goals is uncertain. In the event that the Company does not obtain additional capital or is not able to increase cash flow through the increase of sales, there is substantial doubt as to its ability to continue as a going concern. Risk Factors set forth in our Annual Report on Form 10-K for the year ended December 31, 2009, filed with the Securities and Exchange Commission (SEC) on March 31, 2010 and in our other filings with the SEC for further information with respect to events and uncertainties that could harm our business, operating results, and financial condition.

(3) Inventories

		March 31,		**December 31,**
Inventories consist of :		**2010**		**2009**
Raw materials	$	891,075	$	742,253
Work in process		32,437		1,135
Finished goods		791,222		842,691
Total Inventories	$	1,714,734	$	1,586,079

(4) Comprehensive Income (Loss)

Comprehensive income (loss) follows:

		Three Months Ended March 31,		
		2010		**2009**
Net income (loss)	$	(298,078)	$	(945,220)
Foreign currency translation adjustment		(10,954)		(7,735)

Comprehensive income (loss)	$	(309,032)	$	(952,955)

(5) Contingencies

The Company is party to various lawsuits and administrative proceedings arising in the ordinary course of business. The Company evaluates such lawsuits and proceedings on a case-by-case basis, and its policy is to vigorously contest any such claims that it believes are without merit. The Company's management believes that the ultimate resolution of such pending matters will not have a material adverse affect the Company's business, financial position, results of operations or cash flows.

(6) Segment and Geographic Information

The Company s operations are classified as one reportable segment. The Company s net sales by geographic region follow:

	Three Months Ended March 31, 2010	% of Total	Three Months Ended March 31, 2009	% of Total
North America	$ 2,181,055	87 %	$ 1,977,204	84 %
UK	194,828	8 %	141,624	6 %
All Other	117,709	5 %	229,586	10 %
Total	$ 2,493,592	100 %	$ 2,348,414	100 %

(7) Customer Concentrations

Relatively few customers account for a substantial portion of the Company's net sales. In the first quarter of 2010 the Company's net sales to its top three customers accounted for 52% of its total net sales. In the first quarter of 2009 the Company's net sales to its top three customers accounted for 49% of its total net sales. The Company's customers generally do not enter into long-term agreements obligating them to purchase the Company s products. The Company may not continue to receive significant revenues from any of these or from other large customers. A reduction or delay in orders from any of the Company's significant customers, or a delay or default in payment by any significant customer could materially harm the Company's business and prospects. Because of the Company's significant customer concentration, its net sales and operating income could fluctuate significantly due to changes in political or economic conditions, or the loss, reduction of business, or less favorable terms for any of our significant customers.

(8) Investments

During the quarter ended September 30, 2007 the Company purchased all the Series A Preferred Shares (the Series A Shares) of Unity Business Networks, LLC (Unity) for cash of $1.2 million, including transaction costs. The Series A Shares were convertible at any time at our option into 15% of Unity s common stock on a fully-diluted basis. In addition, we had an option to purchase all the outstanding common stock of Unity based on a specified multiple of Unity s 2008 revenues, as defined.

On September 30, 2009 the Company received a cash payment of $766,950 in connection with Telesphere Networks purchase of the VoIP services business of Unity, including Zoom s preferred stock investment described above. The transaction calls for additional periodic payments totaling $43,050 over the following 24 months beginning in October 2009 and a final payment of $150,000 on September 30, 2011, or $960,000 in total. Additional payments have been received and the balances of expected payments recorded on the March 31, 2010 balance sheet are a current receivable of $21,525 and a long-term asset of $160,763. The Company s basis in this investment was originally recorded in 2007 as $1,178,709, which included the Company s attorney fees involved in closing the investment. The investment was written down to $960,000 as of December 31, 2008. As of December 31, 2009 and March 31, 2010 the investment is no longer reflected on the balance sheet.

ITEM 2.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis should be read in conjunction with the safe harbor statement and the risk factors contained in Item IA of Part II of this Quarterly Report on Form 10-Q, in our Annual Report on Form 10-K for the year ended December 31, 2009, filed with the SEC on March 31, 2010 and in our other filings with the SEC. Readers should also be cautioned that results of any reported period are often not indicative of results for any future period.

Overview

We derive our net sales primarily from sales of Internet-related communication products, principally broadband and dial-up modems and other communication products, to retailers, distributors, Internet Service Providers and Original Equipment Manufacturers. We sell our products through a direct sales force and through independent sales agents. Our employees are primarily located at our headquarters in Boston, Massachusetts and our sales office in the United

Kingdom. We are experienced in electronics hardware, firmware, and software design and test, regulatory approvals, product documentation, and packaging; and we use that experience in developing each product in-house or in partnership with suppliers who are typically based in Asia. Electronic assembly and testing of the Company s products in accordance with our specifications is typically done in China.

For many years we performed most of the final assembly, test, packaging, warehousing and distribution at a production and warehouse facility on Summer Street in Boston, Massachusetts, which had also engaged in firmware programming for some products. On June 30, 2006 we announced our plans to move most of our Summer Street operations to a dedicated facility in Tijuana, Mexico commencing approximately September 1, 2006, and we have since implemented that plan. In August 2006 we signed a lease for a 35,575 square foot manufacturing and warehousing facility in Tijuana, Mexico with an initial lease term from October 2006 to May 2007, with five two-year options thereafter. In February, 2007 we renegotiated the first renewal term and signed a one-year extension starting in May 2007, with five two-year options thereafter. We signed a one-year extension starting in May 2008. In March 2009 we signed a one-year lease with one one-year option for a smaller facility for lower cost. We received verbal approval from the landlord and expect to sign another extension ending April 30, 2011.

Since 1983 our headquarters has been near South Station in downtown Boston. Zoom historically owned two adjacent buildings which connect on most floors, and which house our entire Boston staff. In December 2006 we sold our headquarters buildings to a third party, with a two-year lease-back of approximately 25,000 square feet of the 62,000 square foot facility. Our net sale proceeds were approximately $7.7 million of which approximately $3.6 million was repaid to our mortgage holder, eliminating the mortgage debt from our balance sheet. Our lease expired in December 2008, and we signed a lease extension in January 2009 that commits us for at least 2 years. On January 1, 2009 we reduced our leased Boston space from 25,000 square feet to 14,400 square feet with an increase in rent per square foot, resulting in a savings in 2009 of $54,000. The January 2009 lease can be cancelled as of December 2011 with 6 months notice. We are currently in discussion with our landlord for a reduction in our current rent.

For many years we derived a majority of our net sales from the retail after-market sale of dial-up modems to customers seeking to add or upgrade a modem for their personal computers. In recent years the size of this market and our sales to this market have declined, as personal computer manufacturers have incorporated a modem as a built-in component in most consumer personal computers and as increasing numbers of consumers world-wide have switched to broadband Internet access. The consensus of communications industry analysts is that after-market sales of dial-up modems will probably continue to decline. There is also consensus among industry analysts that the installed base for broadband Internet connection devices, such as cable modems and DSL modems, will grow rapidly during the decade. In response to increased and forecasted worldwide demand for faster connection speeds and increased modem functionality, we have invested and continue to invest resources to advance our product line of broadband modems, both DSL modems and cable modems.

We continually seek to improve our product designs and manufacturing approach in order to improve product performance and reduce our costs. We pursue a strategy of outsourcing rather than internally developing our modem chipsets, which are application-specific integrated circuits that form the technology base for our modems. By outsourcing the chipset technology, we are able to concentrate our research and development resources on modem system design, leverage the extensive research and development capabilities of our chipset suppliers, and reduce our development time and associated costs and risks. As a result of this approach, we are able to quickly develop new products while maintaining a relatively low level of research and development expense as a percentage of net sales. We also outsource aspects of our manufacturing to contract manufacturers as a means of reducing our costs of production, and to provide us with greater flexibility in our production capacity.

Generally our gross margin for a given product depends on a number of factors including the type of customer to whom we are selling. The gross margin for retailers tends to be higher than for some of our other customers; but the sales, support, returns, and overhead costs associated with retailers also tend to be higher. Zoom s sales to certain countries are currently handled by a single master distributor for each country who handles the support and marketing costs within the country. Gross margin for sales to these master distributors tends to be low, since lower pricing to these distributors helps them to cover the support and marketing costs for their country.

Over the past several years our net sales have declined. In response to declining sales volume, we have cut costs by reducing staffing and some overhead costs. Our total headcount was reduced from 47 on March 31, 2009 to 40 on March 31, 2010. As of May 1, 2010 Zoom had 39 full-time and part-time employees and 1 agency contractor. Of the

40 included in our headcount on May 1, 2010 8 were engaged in research and development, 10 were involved in manufacturing oversight, purchasing, assembly, packaging, shipping and quality control, 14 were engaged in sales, marketing and technical support, and the remaining 8 performed accounting, administrative, management information systems, and executive functions. Zoom has implemented cost cutting measures including reducing our headcount and reducing the number of days that certain employees work. As a result, Zoom currently has 35 full-time employees and 5 employees working less than 5 days per week. Our dedicated manufacturing personnel in Mexico are employees of our Mexican manufacturing service provider and not included in our headcount.

On March 31, 2010 we had working capital of $2.6 million including $1.2 million in cash and cash equivalents. On December 31, 2009 we had working capital of $2.8 million including $1.2 million in cash and cash equivalents. Our current ratio at March 31, 2010 was 2.7 compared to 3.0 at December 31, 2009. A significant portion of the reduction of the current ratio was due to the decline in accounts receivable and the increase in accounts payable.

In the first quarter of 2010 the Company s operating activities used $25 thousand in cash. The Company s net loss in the first quarter of 2010 was $0.3 million. Sources of cash from operations included a decrease in accounts receivable of $0.2 million, and an increase in accounts payable and accrued expense of $0.1 million. Use of cash from operations was an increase in inventory of $0.1 million.

Critical Accounting Policies and Estimates

Following is a discussion of what we view as our more significant accounting policies and estimates. As described below, management judgments and estimates must be made and used in connection with the preparation of our financial statements. We have identified areas where material differences could result in the amount and timing of our net sales, costs, and expenses for any period if we had made different judgments or used different estimates.

Revenue (Net Sales) Recognition. We primarily sell hardware products to our customers. The hardware products include dial-up modems, DSL modems, cable modems, voice over IP products, and wireless and wired networking equipment. We earn a small amount of royalty revenue that is included in our net sales, primarily from internet service providers. We generally do not sell software. We began selling services in 2004. We introduced our Global Village VoIP service in late 2004, but sales of those services to date have not been material.

We derive our net sales primarily from the sales of hardware products to four types of customers:

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computer peripherals retailers,

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computer product distributors,

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Internet service providers, and

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original equipment manufacturers (OEMs)

We recognize hardware net sales for our customers at the point when the customers take legal ownership of the delivered products. Legal ownership passes from Zoom to the customer based on the contractual FOB point specified in signed contracts and purchase orders, which are both used extensively. Many of our customer contracts or purchase orders specify FOB destination. We verify the delivery date on all significant FOB destination shipments made during the last 10 business days of each quarter.

Our net sales of hardware include reductions resulting from certain events which are characteristic of the sales of hardware to retailers of computer peripherals. These events are product returns, certain sales and marketing incentives, price protection refunds, and consumer mail-in and in-store rebates. Each of these is accounted for as a reduction of net sales based on detailed management estimates, which are reconciled to actual customer or end-consumer credits on a monthly or quarterly basis.

Product Returns. Products are returned by retail stores and distributors for inventory balancing, contractual stock rotation privileges, and warranty repair or replacements. We estimate the sales and cost value of expected future product returns of previously sold products. Our estimates for product returns are based on recent historical trends plus estimates for returns prompted by, among other things, announced stock rotations and announced customer store closings. Management reviews historical returns, current economic trends, and changes in customer demand and acceptance of our products when estimating sales return allowances. The estimate for future returns is recorded as a reserve against accounts receivable, a reduction in our net sales, and the corresponding change to inventory reserves and cost of sales. Product returns as a percentage of total shipments were 5.7% and 13.7%, respectively, for the first quarter of 2010 and 2009, respectively.

Price Protection Refunds. We have a policy of offering price protection to certain of our retailer and distributor customers for some or all their inventory. Under the price protection policies, when we reduce our prices for a product, the customer receives a credit for the difference between the original purchase price and our reduced price for their unsold inventory of that product. Our estimates for price protection refunds are based on a detailed understanding and tracking by customer and by sales program. Estimated price protection refunds are recorded in the same period as the announcement of a pricing change. Information from customer inventory-on-hand reports or from direct communications with the customers is used to estimate the refund, which is recorded as a reduction of net sales and a reserve against accounts receivable. Reductions in our net sales due to price protection were negligible in both the first quarter of 2010 and the first quarter of 2009.

Sales and Marketing Incentives. Many of our retailer customers require sales and marketing support funding, usually set as a percentage of our sales in their stores. The incentives were reported as reductions in our net sales and were $0.2 million in the first quarter of 2010 and $0.1 million in the first quarter of 2009.

Consumer Mail-In and In-Store Rebates. Our estimates for consumer mail-in and in-store rebates are based on a detailed understanding and tracking by customer and sales program, supported by actual rebate claims processed by the rebate redemption centers plus an accrual for an estimated lag in processing at the redemption centers. The estimate for mail-in and in-store rebates is recorded as a reserve against accounts receivable and a reduction of net sales in the same period that the rebate obligation was triggered. Reductions in our net sales due to the consumer rebates were negligible in both the first quarter of 2010 and the first quarter of 2009.

To ensure that the sales, discounts, and marketing incentives are recorded in the proper period, we perform extensive tracking and documenting by customer, by period, and by type of marketing event. This tracking includes reconciliation to the accounts receivable records for deductions taken by our customers for these discounts and incentives.

Accounts Receivable Valuation. We establish accounts receivable valuation allowances equal to the above-discussed net sales adjustments for estimates of product returns, price protection refunds, consumer rebates, and general bad debt reserves. These allowances are reduced as actual credits are issued to the customer's accounts. Our bad-debt write-offs were negligible in the first quarter of 2010 and 2009, respectively.

Inventory Valuation and Cost of Goods Sold. Inventory is valued at the lower of cost, determined by the first-in, first-out method, or market. We review inventories for obsolete slow moving products each quarter and make provisions based on our estimate of the probability that the material will not be consumed or that it will be sold below cost. In the first quarter of 2010 we recorded an additional charge of $0.01 million and a negligible value in the first quarter of 2009, for inventory reserves related to obsolete and slow-moving products.

Valuation and Impairment of Deferred Tax Assets. As part of the process of preparing our financial statements we estimate our income tax expense and deferred income tax position. This process involves the estimation of our actual current tax exposure together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included in our balance sheet. We then assess the likelihood that our deferred tax assets will be recovered from future taxable income. To the extent we believe that recovery is not likely, we establish a valuation allowance. Changes in the valuation allowance are reflected in the statement of operations.

Significant management judgment is required in determining our provision for income taxes and any valuation allowances. We have recorded a 100% valuation allowance against our deferred income tax assets. It is management's estimate that, after considering all the available objective evidence, historical and prospective, with greater weight given to historical evidence, it is more likely than not that these assets will not be realized. If we establish a record of continuing profitability, at some point we will be required to reduce the valuation allowance and recognize an equal income tax benefit which will increase net income in that period(s).

As of December 31, 2009 we had federal net operating loss carry forwards of approximately $45,693,000. These federal net operating losses are available to offset future taxable income, and are due to expire in years ranging from 2018 to 2029. We also had state net operating loss carry forwards of approximately $16,680,000. These state net operating losses are available to offset future taxable income, and are primarily due to expire in years ranging from 2010 to 2014.

Valuation of Investments. During the quarter ended September 30, 2007 we purchased all the Series A Preferred Shares (the Series A Shares) of Unity Business Networks, LLC (Unity) for cash of $1.2 million, including transaction costs. The Series A Shares were convertible at any time at our option into 15% of Unity s common stock on a fully-diluted basis. In addition, we had an option to purchase all the outstanding common stock of Unity based on a specified multiple of Unity s 2008 revenues, as defined.

On September 30, 2009 the Company received a cash payment of $766,950 in connection with Telesphere Networks purchase of the VoIP services business of Unity, including Zoom s preferred stock investment described above. The transaction calls for additional periodic payments totaling $43,050 over the following 24 months beginning in October 2009 and a final payment of $150,000 on September 30, 2011, or $960,000 in total. Additional payments have been received and the balances of expected payments recorded on the March 31, 2010 balance sheet are a current receivable of $21,525 and a long-term asset of $160,763. The Company s basis in this investment was originally recorded in 2007 as $1,178,709, which included the Company s attorney fees involved in closing the investment. The investment was written down to $960,000 as of December 31, 2008. As of December 31, 2009 and March 31, 2010 the investment is no longer reflected on the balance sheet.

Results of Operations

Summary. Net sales were $2.5 million for our first quarter ended March 31, 2010, up 6.2% from $2.3 million in the first quarter of 2009. We had a net loss of $0.3 million for the first quarter of 2010, compared to a net loss of $0.9 million in the first quarter of 2009. Loss per diluted share was $0.15 in the first quarter of 2010 compared to $0.49 for the first quarter of 2009.

Net Sales. Our total net sales for the first quarter of 2010 increased $0.15 million or 6.2% from the first quarter of 2009, primarily due to increases in dial-up modem sales. The increase in dial-up modem sales was primarily due to the success of our retail placements and to the leveling off of the decline of the dial-up modem after-market. Dial-up modem net sales increased from $1.1 million in the first quarter of 2009 to $1.5 million in the first quarter of 2010, primarily in our U.S. retail channel. DSL modem net sales decreased from $0.6 million in the first quarter of 2009 to $0.4 million in the first quarter of 2010.

Our net sales in North America increased by $0.2 million from $2.0 million in the first quarter of 2009 to $2.2 million in the first quarter of 2010. Our net sales outside North America were relatively constant at $0.3 million in the first quarter of 2009 compared to the first quarter of 2010.

In the quarter ended March 31, 2010 three customers accounted for 53% of total net sales. Because of our significant customer concentration, our net sales and operating income has fluctuated and could in the future fluctuate significantly due to changes in political or economic conditions or the loss, reduction of business, or less favorable terms for any of our significant customers.

Gross Profit. Our total gross profit was $0.8 million in the first quarter of 2010, an increase from $0.5 million in the first quarter of 2009. Our gross margin percent of net sales was 30.6% in the first quarter of 2010 compared to 19.4% in the first quarter of 2009. The gross margin percentage increased in the first quarter of 2010 primarily due to a shift in our product mix toward higher margin products and a reduction in manufacturing expense.

Selling Expense. Selling expense was $0.4 million or 18.0% of net sales in the first quarter of 2010 compared to $0.5 million or 20.7% of net sales in the first quarter of 2009. Selling expense decreased primarily as a result of lower personnel cost.

General and Administrative Expense. General and administrative expense was $0.4 million or 14.9% of net sales in the first quarter of 2010 and $0.6 million or 25.4% of net sales in the first quarter of 2009. General and administrative expense decreased in the first quarter of 2010 compared to the first quarter of 2009 primarily as a result of lower personnel costs in the first quarter of 2010 and costs in the first quarter of 2009 associated with our September, 2009 share exchange transaction.

Research and Development Expense. Research and development expense was $0.3 million or 12.2% of net sales in the first quarter of 2010 and $0.4 million or 15.5% of net sales in the first quarter of 2009. Development and support continues on all of our major product lines.

Other Income. Other income was $0.07 million in the first quarter of 2010 and $0.05 million in the first quarter of 2009. The income increase in the first quarter of 2010 was primarily due to our share of a DRAM semi-conductor class action refund settlement.

Liquidity and Capital Resources

On March 31, 2010 we had working capital of $2.6 million including $1.2 million in cash and cash equivalents. On December 31, 2009 we had working capital of $2.8 million including $1.2 million in cash and cash equivalents. Our current ratio at March 31, 2010 was 2.7 compared to 3.0 at December 31, 2009. A significant portion of the reduction of the current ratio was due to the decline in accounts receivable and increase in accounts payable.

In the first quarter of 2010 our operating activities used $25 thousand in cash. Our net loss in the first quarter of 2010 was $0.3 million. Sources of cash from operations included a decrease in accounts receivable of $0.2 million, and an increase in accounts payable and accrued expense of $0.1 million. Use of cash from operations was an increase in inventory of $0.1 million.

To conserve cash and manage our liquidity, we have implemented cost-cutting initiatives including the reduction of employee headcount and overhead costs. As of March 31, 2010 we had 40 employees compared to 47 as of March 31, 2009. We plan to continue to assess our cost structure as it relates to our revenues and cash position, and we may make further reductions if the actions are deemed necessary.

In the first quarter of 2010 the Company incurred an operating loss of $0.4 million and a net loss of $0.3 million. The continuing loss condition and other conditions raise substantial doubt about the Company's ability to continue as a going concern. Management does not believe we have sufficient resources to fund our normal operations over the next 12 months unless sales improve significantly or we raise capital. Additional financing may not be available on terms favorable to the Company, or at all. If these funds are not available the Company may not be able to execute its business plan or take advantage of business opportunities. The ability of the Company to obtain such additional financing and to achieve its operating goals is uncertain. In the event that the Company does not obtain additional capital or is not able to increase cash flow through the increase of sales, there is substantial doubt as to its ability to continue as a going concern. See the risk factors contained in Item IA of Part II of this Quarterly Report on Form 10-Q, in our Annual Report on Form 10-K for the year ended December 31, 2009, filed with the SEC on March 31, 2010 and in our other filings with the SEC, for further information with respect to events and uncertainties that could harm our business, operating results, and financial condition.

Commitments

During the three months ended March 31, 2010, there were no material changes to our capital commitments and contractual obligations from those disclosed in our Form 10-K for the year ended December 31, 2009.

"Safe Harbor" Statement under the Private Securities Litigation Reform Act of 1995.

Some of the statements contained in this report are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These statements involve known and unknown risks, uncertainties and other factors which may cause our or our industry's actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. Forward-looking statements include, but are not limited to statements regarding: Zoom's plans, expectations and intentions, including statements relating to Zoom's prospects and plans relating to sales of and markets for its products; Zoom s expected benefits and cost savings resulting from the move of its manufacturing facilities to Mexico; and Zoom's financial condition or results of operations.

In some cases, you can identify forward-looking statements by terms such as "may," "will, " "should," "could," "would," "expects," "plans," "anticipates," "believes," "estimates," "projects," "predicts," "potential" and similar expressions intended to identify forward-looking statements. These statements are only predictions and involve known and unknown risks, uncertainties, and other factors that may cause our actual results, levels of activity, performance, or achievements to be materially different from any future results, levels of activity, performance, or achievements expressed or implied by such forward-looking statements. Given these uncertainties you should not place undue reliance on these forward-looking statements. Also, these forward-looking statements represent our estimates and assumptions only as of the date of this report. We expressly disclaim any obligation or undertaking to release publicly any updates or revisions to any forward-looking statement contained in this report to reflect any change in our expectations or any change in events, conditions or circumstances on which any of our forward-looking statements are based. Factors that could cause or contribute to differences in our future financial results include those discussed in the risk factors set forth in Item 1A of Part II below as well as those discussed elsewhere *in this report, in our Annual Report on Form 10-K for the year ended December 31, 2009, filed with the SEC on March 31, 2010 and in our other filings with the SEC.*

ITEM 3.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not Required.

ITEM 4.

CONTROLS AND PROCEDURES

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Securities Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, as ours are designed to do, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

As of March 31, 2010 we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective in enabling us to record, process, summarize and report information required to be included in our periodic filings with the Securities and Exchange Commission within the required time period.

There have been no changes in our internal control over financial reporting that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION

ITEM 1A.

RISK FACTORS

This report contains forward-looking statements that involve risks and uncertainties, such as statements of our objectives, expectations and intentions. The cautionary statements made in this report are applicable to all forward-looking statements wherever they appear in this report. Our actual results could differ materially from those discussed herein. Factors that could cause or contribute to such differences include the risk factors contained in our Annual Report on Form 10-K for the year ended December 31, 2009, filed with the SEC on March 31, 2010, as well as those discussed in this report and in our other filings with the SEC.

ITEM 6.

EXHIBITS

Exhibit No.	Exhibit Description
10.1	Severance Agreement between Zoom Telephonics, Inc. and Frank B. Manning
10.2	Severance Agreement between Zoom Telephonics, Inc. and Robert Crist
10.3	Severance Agreement between Zoom Telephonics, Inc. and Deena Randall
10.4	Severance Agreement between Zoom Telephonics, Inc. and Terry Manning
31.1	CEO Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	CFO Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	CEO Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	CFO Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

ZOOM TELEPHONICS, INC.

SIGNATURES

Pursuant to the requirements of the Securities and Exchange Act of 1934, the Company has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

ZOOM TELEPHONICS, INC.

(Registrant)

Date: May 14, 2010	By:	/s/ FRANK B. MANNING Frank B. Manning, President (Principal Executive Officer)
Date: May 14, 2010	By:	/s/ ROBERT CRIST Robert Crist, Vice President of Finance and Chief Financial Officer (Principal Financial and Accounting Officer)

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