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

FORM 10-Q

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

For the quarterly period ended March 31, 2012

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE EXCHANGE ACT**

For the transition period from to

Commission file number 001-15757

IMAGEWARE SYSTEMS, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**33-0224167**
(State or Other Jurisdiction of Incorporation or Organization)	(IRS Employer Identification No.)

10815 Rancho Bernardo Rd., Suite 310
San Diego, CA 92127
(Address of Principal Executive Offices)

(858) 673-8600
(Registrant's Telephone Number, Including Area Code)

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

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-12 of the Exchange Act). Yes ☐ No ☐

The number of shares of Common Stock, with $0.01 par value, outstanding on May 11, 2012 was 68,612,106.

IMAGEWARE SYSTEMS, INC.
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PART I

ITEM 1. FINANCIAL STATEMENTS

IMAGEWARE SYSTEMS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In Thousands, except share and per share data)

	March 31, 2012 (Unaudited)	December 31, 2011
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 5,223	$ 6,773
Accounts receivable, net of allowance for doubtful accounts of $4 at March 31, 2012 and December 31, 2011	376	348
Inventory, net	83	45
Other current assets	125	66
Total Current Assets	5,807	7,232
Property and equipment, net	87	18
Other assets	58	58
Intangible assets, net of accumulated amortization	59	63
Goodwill	3,416	3,416
Total Assets	**$ 9,427**	**$ 10,787**
LIABILITIES AND SHAREHOLDERS' DEFICIT		
Current Liabilities:		
Accounts payable	$ 735	$ 1,103
Deferred revenue	1,445	1,066
Accrued expenses	1,782	2,005
Notes payable to related parties	65	110
Total Current Liabilities	4,027	4,284
Derivative liabilities	5,772	11,824
Pension obligation	404	391
Total Liabilities	10,203	16,499
Shareholders' deficit:		
Preferred stock, authorized 4,000,000 shares:		
Series B convertible redeemable preferred stock, $0.01 par value; designated 750,000 shares, 389,400 shares issued, and 239,400 shares outstanding at March 31, 2012 and December 31, 2011, respectively; liquidation preference $620 and $786 at March 31, 2012 and December 31, 2011, respectively	2	2
Common stock, $0.01 par value, 150,000,000 shares authorized; 67,995,620 and 67,988,916 shares issued and outstanding at March 31, 2012 and December 31, 2011, respectively	679	679
Additional paid-in capital	115,458	101,720
Treasury stock, at cost - 6,704 shares	(64)	(64)
Accumulated other comprehensive loss	(99)	(65)
Accumulated deficit	(116,752)	(107,984)
Total Shareholders' deficit	(776)	(5,712)
Total Liabilities and Shareholders' Deficit	**$ 9,427**	**$ 10,787**

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

IMAGEWARE SYSTEMS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In Thousands, except share and per share amounts)
(Unaudited)

	Three Months Ended March 31, 2012	Three Months Ended March 31, 2011
Revenues:		
Product	$ 388	$ 1,257
Maintenance	733	664
	1,121	1,921
Cost of revenues:		
Product	83	131
Maintenance	239	238
Gross profit	799	1,552
Operating expenses:		
General and administrative	944	507
Sales and marketing	394	371
Research and development	734	627
Depreciation and amortization	12	7
	2,084	1,512
Income (loss) from operations	(1,285)	40
Interest expense, net	4	628
Change in fair value of derivative liabilities	7,536	7,273
Other income, net	(235)	(5)
Loss before income taxes	(8,590)	(7,856)
Income tax expense	-	2
Net loss	(8,590)	(7,858)
Preferred dividends	(13)	(103)
Net loss available to common shareholders	$ (8,603)	$ (7,961)
Basic loss per common share:		
Net loss	$ (0.13)	$ (0.31)
Preferred dividends	(0.00)	(0.00)
Basic loss per share available to common shareholders	$ (0.13)	$ (0.31)
Basic weighted-average shares	67,988,916	25,317,525

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

IMAGEWARE SYSTEMS, INC
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(In Thousands)
(Unaudited)

	Three Months Ended March 31, 2012	Three Months Ended March 31, 2011
Net loss	$ (8,590)	$ (7,858)
Foreign currency translation adjustment	(34)	(57)
Comprehensive loss	$ (8,624)	$ (7,915)

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

IMAGEWARE SYSTEMS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In Thousands)
(Unaudited)

	Three Months Ended March 31, 2012	Three Months Ended March 31, 2011
Cash flows from operating activities		
Net loss	$ (8,590)	$ (7,858)
Adjustments to reconcile net loss to net cash used in operating activities		
Depreciation and amortization	12	7
Amortization of debt discount and debt issuance costs	-	540
Reduction in accounts payable from expiration of statute of limitations	(230)	-
Change in fair value of derivative liabilities	7,536	7,273
Stock issued in lieu of cash	-	13
Stock-based compensation	150	77
Change in assets and liabilities		
Accounts receivable, net	(28)	(41)
Inventory, net	(38)	(15)
Other assets	(59)	(13)
Accounts payable	(138)	(18)
Accrued expenses	(223)	4
Deferred revenue	379	65
Billings in excess of costs and estimated earnings on uncompleted contracts	-	(139)
Pension obligation	13	24
Total adjustments	7,374	7,777
Net cash used in operating activities	(1,216)	(81)
Cash flows from investing activities		
Purchase of property and equipment	(77)	(1)
Net cash used in investing activities	(77)	(1)
Cash flows from financing activities		
Proceeds from exercised stock options	-	4
Proceeds from exercised stock purchase warrants	-	655
Repayment of notes payable	(45)	-
Dividends paid	(178)	-
Net cash (used in) provided by financing activities	(223)	659
Effect of exchange rate changes on cash	(34)	(57)
Net increase (decrease) in cash and cash equivalents	(1,550)	520
Cash and cash equivalents at beginning of period	6,773	103
Cash and cash equivalents at end of period	$ 5,223	$ 623
Supplemental disclosure of cash flow information:		
Cash paid for interest	$ -	$ -
Cash paid for income taxes	$ -	$ -
Summary of non-cash investing and financing activities:		-
Reclassification of warrants previously classified as derivative liabilities to additional paid-in capital	$ 13,588	$ -
Issuance of common stock pursuant to cashless warrant exercises	$ -	$ 8

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

IMAGEWARE SYSTEMS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 1. ORGANIZATION AND DESCRIPTION OF BUSINESS

Overview

ImageWare Systems, Inc. (the "Company") is incorporated in the state of Delaware. The Company is a pioneer and leader in the emerging market for biometrically enabled software-based identity management solutions. Using those human characteristics that are unique to us all, the Company creates software that provides a highly reliable indication of a person's identity. The Company's "flagship" product is the patented IWS Biometric Engine®. The Company's products are used to manage and issue secure credentials, including national IDs, passports, driver licenses and access control credentials. The Company's products also provide law enforcement with integrated mug shot, fingerprint LiveScan and investigative capabilities. The Company also provides comprehensive authentication security software using biometrics to secure physical and logical access to facilities or computer networks or Internet sites. Biometric technology is now an integral part of all markets the Company addresses and all of the products are integrated into the IWS Biometric Engine.

Recent Developments

In March 2012, the Company entered into agreements with the holders of certain warrants acquired in connection with a financing consummated by the Company on December 21, 2011 (the "Qualified Financing"), which warrants are currently exercisable for 12,252,500 shares of the Company's common stock at an exercise price of $0.50 per share. The warrants contained certain settlement provisions that required, under specific circumstances, a net cash settlement upon the occurrence of a "Fundamental Transaction" as defined in the warrants. These provisions effectively resulted in the characterization of the warrants as derivative liabilities. The agreements amended the warrants to revise, among other provisions, the definition of "Fundamental Transaction". As a result of the amendments, the warrants no longer qualify as derivative liabilities. The Company determined the change in fair value from the date of previous measurement (December 31, 2011) to the date of the amendment (March 21, 2012) for these warrants and recorded approximately $5,110,000 in expense. Such expense is included in the Company's condensed consolidated statement of operations for the three months ended March 31, 2012 under the caption "Change in fair value of derivative liabilities".

Additionally, as a result of the agreements to amend the warrants and the warrants no longer qualifying for derivative liability treatment, the Company reclassified approximately $13,588,000 in derivative liability into a component of additional paid-in capital in the Company's financial statements for the period ended March 31, 2012.

During the three months ended March 31, 2012, the Company paid approximately $178,000 in accumulated dividends to the holders of its Series B convertible preferred stock.

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES AND BASIS OF PRESENTATION

Basis of Presentation

The accompanying condensed consolidated balance sheet as of December 31, 2011, which has been derived from audited financial statements, and the unaudited interim condensed consolidated financial statements have been prepared by the Company in accordance with U.S. generally accepted accounting principles ("GAAP") and the rules and regulations of the Securities and Exchange Commission ("SEC") related to a quarterly report on Form 10-Q. Certain information and note disclosures normally included in annual financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to those rules and regulations, although the Company believes that the disclosures made are adequate to make the information not misleading. The interim financial statements reflect all adjustments which, in the opinion of management, are necessary for a fair statement of the results for the periods presented. All such adjustments are of a normal and recurring nature. These unaudited condensed consolidated financial statements should be read in conjunction with the Company's audited financial statements for the year ended December 31, 2011, which are included in the Company's Annual Report on Form 10-K for the year ended December 31, 2011 that was filed with the SEC on April 4, 2012.

Operating results for the three months ended March 31, 2012 are not necessarily indicative of the results that may be expected for the year ended December 31, 2012, or any other future periods.

Significant Accounting Policies

Cash and cash equivalents

Cash and cash equivalents consist primarily of cash on deposit and money market accounts that are readily convertible into cash. The Company considers all highly-liquid investments with original maturities of three months or less to be cash equivalents.

Accounts Receivable

In the normal course of business, the Company extends credit without collateral requirements to its customers that satisfy pre-defined credit criteria. Accounts receivable are recorded net of an allowance for doubtful accounts. The Company records its allowance for doubtful accounts based upon its assessment of various factors. The Company considers historical experience, the age of the accounts receivable balances, the credit quality of its customers, current economic conditions and other factors that may affect customers' ability to pay to determine the level of allowance required. Accounts receivable are written off against the allowance for doubtful accounts when all collection efforts by the Company have been unsuccessful.

Fair Value of Financial Instruments

For certain of the Company's financial instruments, including accounts receivable, accounts payable, accrued expenses, deferred revenues and notes payable to related parties, the carrying amounts approximate fair value due to their relatively short maturities.

Derivative Financial Instruments

The Company does not use derivative instruments to hedge exposures to cash flow, market or foreign currency risks.

The Company reviews the terms of the common and preferred stock, warrants and convertible debt it issues to determine whether there are embedded derivative instruments, including embedded conversion options, which are required to be bifurcated and accounted for separately as derivative financial instruments. In circumstances where the host instrument contains more than one embedded derivative instrument, including the conversion option, that is required to be bifurcated, the bifurcated derivative instruments are accounted for as a single, compound derivative instrument.

Bifurcated embedded derivatives are initially recorded at fair value and are then revalued at each reporting date with changes in the fair value reported as non-operating income or expense. When the equity or convertible debt instruments contain embedded derivative instruments that are to be bifurcated and accounted for as liabilities, the total proceeds received are first allocated to the fair value of all the bifurcated derivative instruments. The remaining proceeds, if any, are then allocated to the host instruments themselves, usually resulting in those instruments being recorded at a discount from their face value.

The discount from the face value of the convertible debt, together with the stated interest on the instrument, is amortized over the life of the instrument through periodic charges to interest expense, using the effective interest method.

Revenue Recognition

The Company recognizes revenue from the following major revenue sources:

- Long-term fixed-price contracts involving significant customization
- Fixed-price contracts involving minimal customization
- Software licensing
- Sales of computer hardware and identification media
- Postcontract customer support (PCS)

The Company’s revenue recognition policies are consistent with U.S. GAAP including ASC 985-605, “Software Revenue Recognition”, ASC 605-35 “Revenue Recognition, Construction-Type and Production-Type Contracts”, “Securities and Exchange Commission Staff Accounting Bulletin 104”, and ASC 605-25 “Revenue Recognition , Multiple Element Arrangements”. Accordingly, the Company recognizes revenue when all of the following criteria are met: persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the fee is fixed or determinable, and collectability is reasonably assured.

The Company recognizes revenue and profit as work progresses on long-term, fixed-price contracts involving significant amount of hardware and software customization using the percentage of completion method based on costs incurred to date compared to total estimated costs at completion. The primary components of costs incurred are third party software and direct labor cost including fringe benefits. Revenues recognized in excess of amounts billed are classified as current assets under “Costs and estimated earnings in excess of billings on uncompleted contracts”. Amounts billed to customers in excess of revenues recognized are classified as current liabilities under “Billings in excess of costs and estimated earnings on uncompleted contracts”. Revenue from contracts for which the Company cannot reliably estimate total costs or there are not significant amounts of customization are recognized upon completion. The Company also generates non-recurring revenue from the licensing of its software. Software license revenue is recognized upon the execution of a license agreement, upon deliverance, when fees are fixed and determinable, when collectability is probable and when all other significant obligations have been fulfilled. The Company also generates revenue from the sale of computer hardware and identification media. Revenue for these items is recognized upon delivery of these products to the customer. The Company’s revenue from periodic maintenance agreements is generally recognized ratably over the respective maintenance periods provided no significant obligations remain and collectability of the related receivable is probable. Pricing of maintenance contracts is consistent period to period and calculated as a percentage of the software or hardware revenue which is approximately 15% annually. Amounts collected in advance for maintenance services are included in current liabilities under "Deferred revenues". Sales tax collected from customers is excluded from revenue.

Customer Concentration

For the three months ended March 31, 2012, one customer accounted for approximately 14% or $153,000 of total revenues and had trade receivables at March 31, 2012 of $0. For the three months ended March 31, 2011, one customer accounted for approximately 55% or $1,048,000 of total revenues and had trade receivables at March 31, 2011 of $0.

Recently Issued Accounting Standards

From time to time, new accounting pronouncements are issued by the Financial Accounting Standards Board, or FASB, or other standard setting bodies, which are adopted by us as of the specified effective date. Unless otherwise discussed, the Company’s management believes that the impact of recently issued standards that are not yet effective will not have a material impact on the Company’s consolidated financial statements upon adoption.

FASB ASU 2011-05. In June 2011 the FASB issued ASU No. 2011-05, *Comprehensive Income (Topic 220): Presentation of Comprehensive Income*, (“ASU 2011-05”). This new accounting standard: (1) eliminates the option to present the components of other comprehensive income as part of the statement of changes in stockholders’ equity; (2) requires the consecutive presentation of the statement of net income and other comprehensive income; and (3) requires an entity to present reclassification adjustments on the face of the financial statements from other comprehensive income to net income. This new standard does not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income, nor does it affect how earnings per share is calculated or presented. ASU 2011-05 is required to be applied retrospectively and is effective for fiscal years and interim periods within those years beginning after December 15, 2011, with early adoption permitted. As this new standard only requires enhanced disclosure, the adoption of ASU 2011-05 did not impact the Company’s financial position or results of operations.

FASB ASU 2011-08. In September 2011 the FASB issued ASU No. 2011-08, *Goodwill and Other (Topic 350): Testing Goodwill for Impairment*, ("ASU 2011-08"). This new accounting standard simplifies goodwill impairment tests and states that a qualitative assessment may be performed to determine whether further impairment testing is necessary. ASU 2011-08 is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. The adoption of ASU 2011-08 did not have a material impact on the Company's condensed consolidated financial statements.

FASB ASU 2011-09. The FASB has issued Accounting Standards Update (ASU) No. 2011-09, Compensation-Retirement Benefits-Multiemployer Plans (Subtopic 715-80): Disclosures about an Employer's Participation in a Multiemployer Plan. ASU 2011-09 is intended to address concerns from various users of financial statements on the lack of transparency about an employer's participation in a multiemployer pension plan. Users of financial statements have requested additional disclosure to increase awareness of the commitments and risks involved with participating in multiemployer pension plans. The amendments in this ASU will require additional disclosures about an employer's participation in a multiemployer pension plan. Previously, disclosures were limited primarily to the historical contributions made to the plans. ASU 2011-09 applies to nongovernmental entities that participate in multiemployer plans. For public entities, ASU 2011-09 is effective for annual periods for fiscal years ending after December 15, 2011. For nonpublic entities, ASU 2011-09 is effective for annual periods for fiscal years ending after December 15, 2012. Early adoption is permissible for both public and nonpublic entities. ASU 2011-09 should be applied retrospectively for all prior periods presented. The adoption of ASU 2011-09 did not have a material impact on the Company's consolidated financial statements.

FASB ASU 2011-11. The FASB has issued ASU 2011-11, "Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities". The amendments in this ASU require an entity to disclose information about offsetting and related arrangements to enable users of its financial statements to understand the effect of those arrangements on its financial position. Coinciding with the release of ASU No. 2011-11, the International Accounting Standards Board (IASB) has issued Disclosures - Offsetting Financial Assets and Financial Liabilities (Amendments to International Financial Reporting Standards 7). This amendment requires disclosures about the offsetting of financial assets and financial liabilities common to those in ASU 2011-11. An entity is required to apply the amendments for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. An entity should provide the disclosures required by those amendments retrospectively for all comparative periods presented. The Company does not expect the adoption of this pronouncement to have a material impact on its consolidated financial statements.

FASB ASU 2011-12. The FASB has issued ASU 2011-12, "Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05". The amendments to the Codification in ASU 2011-12 are effective at the same time as the amendments in ASU 2011-05, "Comprehensive Income (Topic 220): Presentation of Comprehensive Income", so that entities will not be required to comply with the presentation requirements in ASU 2011-05 that ASU 2011-12 is deferring. In order to defer only those changes in ASU 2011-05 that relate to the presentation of reclassification adjustments, the paragraphs in ASU 2011-12 supersede certain pending paragraphs in ASU 2011-05. The amendments are being made to allow the FASB time to redeliberate whether to present on the face of the financial statements the effects of reclassifications out of accumulated other comprehensive income on the components of net income and other comprehensive income for all periods presented. While the FASB is considering the operational concerns about the presentation requirements for reclassification adjustments and the needs of financial statement users for additional information about reclassification adjustments, entities should continue to report reclassifications out of accumulated other comprehensive income consistent with the presentation requirements in effect before ASU 2011-05. All other requirements in ASU 2011-05 are not affected by ASU 2011-12, including the requirement to report comprehensive income either in a single continuous financial statement or in two separate but consecutive financial statements. Public entities should apply these requirements for fiscal years, and interim periods within those years, beginning after December 15, 2011. The adoption of ASU 2011-12 did not have a material impact on the Company's consolidated financial statements.

NOTE 3. NET LOSS PER COMMON SHARE

Basic loss per common share is calculated by dividing net loss available to common shareholders for the period by the weighted-average number of common shares outstanding during the period. Diluted earnings per common share is calculated by dividing net income available to common shareholders for the period by the weighted-average number of common shares outstanding during the period, adjusted to include, if dilutive, potential dilutive shares consisting of convertible preferred stock, convertible notes payable, stock options and warrants, calculated using the treasury stock method. For diluted earnings per share calculation purposes, the net income available to commons shareholders is adjusted to add back any preferred stock dividends and any interest on convertible debt reflected in the condensed consolidated statement of operations for the respective periods.

The table below presents the computation of basic and diluted loss per share:

(Amounts in thousands except share and per share amounts)	**Three Months Ended March 31, 2012**	**Three Months Ended March 31, 2011**
Numerator for basic loss per share:		
Net loss	$ (8,590)	$ (7,858)
Preferred dividends	(13)	(103)
Net loss available to common shareholders	$ (8,603)	$ (7,961)
Denominator for basic and diluted loss per share — weighted-average shares outstanding	67,988,916	25,317,525
Net loss	$ (0.13)	$ (0.31)
Preferred dividends	(0.00)	(0.00)
Net loss available to common shareholders	$ (0.13)	$ (0.31)

The Company has excluded the following securities from the calculation of diluted loss per share, as their effect would have been antidilutive:

Dilutive securities	**Three Months Ended March 31, 2012**	**Three Months Ended March 31, 2011**
Restricted stock grants	360,000	360,000
Convertible notes payable	164,950	11,488,871
Convertible preferred stock	46,896	11,328,318
Stock options	3,007,713	1,731,907
Warrants	28,453,760	17,114,374
Total dilutive securities	32,033,319	42,023,470

NOTE 4. SELECT BALANCE SHEET DETAILS

Inventory

Inventories of $83,000 at March 31, 2012 were comprised of work in process of $72,000 representing direct labor costs on in-process projects and finished goods of $11,000 net of reserves for obsolete and slow-moving items of $2,000. Inventories of $45,000 at December 31, 2011 were comprised of work in process of $29,000 representing direct labor costs on in-process projects and finished goods of $16,000 net of reserves for obsolete and slow-moving items of $2,000. Appropriate consideration is given to obsolescence, excessive levels, deterioration, and other factors in evaluating net realizable value and required reserve levels.

Intangible Assets

The Company has intangible assets in the form of trademarks and trade names. The carrying amounts of the Company's acquired intangible assets were $59,000 and $63,000 as of March 31, 2012 and December 31, 2011, respectively, which include accumulated amortization of $276,000 and $272,000 as of March 31, 2012 and December 31, 2011, respectively. Amortization expense for the intangible assets was $4,000 for the three months ended March 31, 2012 and 2011. All intangible assets are being amortized over their estimated useful lives with no estimated residual values. Any costs incurred by the Company to renew or extend the life of intangible assets will be evaluated under ASC 350 "*Intangibles – Goodwill and Other*" for proper treatment.

The estimated acquired intangible amortization expense for the next five fiscal years is as follows:

Fiscal Year Ended December 31,	**Estimated Amortization Expense ($ in thousands)**
2012 (9 months)	12
2013	16
2014	16
2015	15
2016	—
Thereafter	—
Total	$ 59

Goodwill

The Company annually, or more frequently if events or circumstances indicate a need, tests the carrying amount of goodwill for impairment. The Company performs its annual impairment test in the fourth quarter of each year. A two-step impairment test is used to first identify potential goodwill impairment and then measure the amount of goodwill impairment loss, if any. These tests were conducted by determining and comparing the fair value, employing the market approach, of the Company's reporting units to the carrying value of the reporting unit. The Company has determined that its only reporting unit is Identity Management. Based on the results of these impairment tests, the Company determined that its goodwill assets were not impaired as of December 31, 2011 and there have been no indications of impairment during the three months ended March 31, 2012 or 2011.

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NOTE 5. NOTES PAYABLE

Notes payable consist of the following:

($ in thousands)	March 31, 2012	December 31, 2011
Notes payable to related parties:		
7% convertible promissory notes. Face value of notes $65 at March 31, 2012 and $110 at December 31, 2011. Discount on notes is $0 at March 31, 2012 and $0 at December 30, 2011. Notes were due January 2010. The Company is currently seeking a waiver of default.	65	110
Total notes payable to related parties	65	110
Total notes payable	65	110
Less current portion	(65)	(110)
Long-term notes payable	$ -	$ -

7% Convertible Promissory Notes to Related Parties

On November 14, 2008, the Company entered into a series of convertible promissory notes (the "Related-Party Convertible Notes"), aggregating $110,000 with certain officers and members of the Company's Board of Directors. The Related-Party Convertible Notes bear interest at 7.0% per annum and were due February 14, 2009. The principal amount of the Related-Party Convertible Notes plus accrued but unpaid interest is convertible at the option of the holder into common stock of the Company. The number of shares into which the Related-Party Convertible Notes are convertible shall be calculated by dividing the outstanding principal and accrued but unpaid interest by $0.55 (the "Conversion Price").

In conjunction with the issuance of the Related-Party Convertible Notes, the Company issued an aggregate of 149,996 warrants to the note holders to purchase common stock of the Company. The warrants have an exercise price of $0.55 per share and may be exercised at any time from November 14, 2008 until November 14, 2013.

The Company, in 2008, initially recorded the convertible notes net of a discount equal to the fair value allocated to the warrants of approximately $13,000. The Company estimated the fair value of the warrants using the Black-Scholes option pricing model using the following assumptions: term of 5 years, a risk free interest rate of 2.53%, a dividend yield of 0%, and volatility of 96%. The convertible notes also contained a beneficial conversion feature, which resulted in an additional debt discount of $12,000. The beneficial conversion amount was measured using the accounting intrinsic value, i.e. the excess of the aggregate fair value of the common stock into which the debt is convertible over the proceeds allocated to the security. The Company has accreted the beneficial conversion feature over the life of the note.

The Company did not repay the Related-Party Convertible Notes on the due date. In August 2009, the Company received from the Related-Party Convertible Note holders a waiver of default and extension to January 31, 2010 of the maturity date of the Related-Party Convertible Notes. As consideration for the waiver and note extension, the Company issued to the Related-Party Convertible Note holders an aggregate of 150,000 warrants to purchase shares of the Company's common stock. The warrants have an exercise price of $0.54 per share and expire on August 25, 2014.

The Company did not repay the notes on January 31, 2010. During the three months ended March 31, 2012, the Company repaid $45,000 in principal to certain holders of the Related-Party Convertible Notes. The Company is currently seeking an additional waiver of default from the holders of the Related-Party Convertible Notes.

NOTE 6. EQUITY

The Company's Articles of Incorporation, as amended, authorize the issuance of two classes of stock to be designated "Common Stock" and "Preferred Stock". The Preferred Stock may be divided into such number of series and with the rights, preferences, privileges and restrictions as the Board of Directors may determine.

On October 13, 2011, the Company filed with the Secretary of State of the State of Delaware a Certificate of Amendment to its Certificate of Incorporation increasing the authorized number of shares of its common stock to 150,000,000 from 50,000,000 shares ("Certificate of Amendment"). In addition, the Company filed with the Secretary of State of the State of Delaware Certificates of Amendment to its Certificate of Designation of Preferences, Rights and Limitations of Series C 8% Convertible Preferred Stock ("Series C Preferred"), and its Certificate of Designation of Preferences, Rights and Limitations of Series D 8% Convertible Preferred Stock ("Series D Preferred") of the Company (together, the "Preferred Amendments"), in each case to, among other things, provide for the automatic conversion of the Series C Preferred and Series D Preferred into shares of the Company's common stock in the event the Company consummates a qualified financing of at least $10.0 million on or before December 31, 2011 ("Qualified Financing").

The Certificate of Amendment and the Preferred Amendments were approved by shareholders acting by written consent, dated October 5, 2011, and were approved by shareholders holding in excess of 50% of the shares of common stock entitled to vote with respect to each matter.

Series B Convertible Redeemable Preferred Stock

The Company had 239,400 shares of Series B Preferred outstanding as of March 31, 2012 and December 31, 2011. At March 31, 2012 and December 31, 2011, the Company had cumulative undeclared dividends of approximately $21,000 and $187,000, respectively. There were no conversions of Series B Preferred into common stock during the three months ended March 31, 2012 or 2011.

Warrants

As of March 31, 2012, warrants to purchase 28,453,760 shares of common stock at prices ranging from $0.50 to $1.67 were outstanding. All warrants are exercisable as of March 31, 2012 and expire at various dates through October 2016. There were no warrants issued, exercised or expired/cancelled during the three months ended March 31, 2012.

Stock-Based Compensation

As of March 31, 2012, the Company had two active stock-based compensation plans for employees and nonemployee directors, which authorize the granting of various equity-based incentives including stock options and restricted stock.

The Company estimates the fair value of its stock options using a Black-Scholes option-pricing model, consistent with the provisions of ASC No. 718, *Compensation – Stock Compensation*. The fair value of stock options granted is recognized to expense over the requisite service period. Stock-based compensation expense for all share-based payment awards is recognized using the straight-line single-option method. Stock-based compensation expense is reported in operating expenses based upon the departments to which substantially all of the associated employees report and credited to Additional paid-in capital. Stock-based compensation expense related to equity options was approximately $141,000 and $67,000 for the three months ended March 31, 2012 and 2011, respectively.

ASC 718 requires the use of a valuation model to calculate the fair value of stock-based awards. The Company has elected to use the Black-Scholes option-pricing model, which incorporates various assumptions including volatility, expected life, and interest rates. The Company is required to make various assumptions in the application of the Black-Scholes option-pricing model. The Company has determined that the best measure of expected volatility is based on the historical weekly volatility of the Company's common stock. Historical volatility factors utilized in the Company's Black-Scholes computations for the three months ended March 31, 2012 and 2011 ranged from 135% to 144%. The Company has elected to estimate the expected life of an award based upon the SEC approved "simplified method" noted under the provisions of Staff Accounting Bulletin No. 110. The expected term used by the Company during the three months ended March 31, 2012 and 2011 was 5.9 years. The difference between the actual historical expected life and the simplified method was immaterial. The interest rate used is the risk free interest rate and is based upon U. S. Treasury rates appropriate for the expected term. Interest rates used in the Company's Black-Scholes calculations for the three months ended March 31, 2012 and 2011 was 2.6%. Dividend yield is zero as the Company does not expect to declare any dividends on the Company's common shares in the foreseeable future.

In addition to the key assumptions used in the Black-Scholes model, the estimated forfeiture rate at the time of valuation is a critical assumption. The Company has estimated an annualized forfeiture rate of approximately 0% for corporate officers, 4% for members of the Board of Directors and 6% for all other employees. The Company reviews the expected forfeiture rate annually to determine if that percent is still reasonable based on historical experience.

In January of 2010, the Company issued 847,258 shares of restricted stock to members of management and the Board. These shares will vest quarterly over a three-year period. The restricted shares were issued as compensation for the cancellation of 1,412,096 options held by members of management and the Board. The Company evaluated the exchange in accordance with ASC 718 and determined there was no incremental cost to be recorded in conjunction with the exchange as the fair value of the options surrendered at the modification date exceeded the fair value of the restricted shares issued at the modification date. Stock-based compensation expense related to these restricted stock grants was approximately $9,000 for the three months ended March 31, 2012 and $10,000 for the three months ended March 31, 2011.

During March 2011, the Company granted 880,000 performance units to certain key employees that grant the holder the right to receive compensation based on the appreciation in the Company's common stock in the event of transfer of control of the Company ("Performance Units"). As the vesting of the Performance Units is contingent upon the sale of the Company, the expense associated with the granting of the Performance Units was not material. The Performance Units issued to such key employees were terminated, and exchanged for options to purchase a total of 435,000 shares of common stock during the three months ended March 31, 2012.

A summary of the activity under the Company's stock option plans is as follows:

	Options	Weighted-Average Exercise Price
Balance at December 31, 2011	1,707,713	$ 1.65
Granted	1,300,000	$ 0.92
Expired/Cancelled	—	$ —
Exercised	—	$ —
Balance at March 31,2012	3,007,713	$ 0.83

The weighted-average grant date fair value of options granted during the three months ended March 31, 2012 was $0.74.

NOTE 7. DERIVATIVE LIABILITIES

The Company accounts for its derivative instruments under the provisions of ASC 815, "Derivatives and Hedging-Contracts in Entity's Own Equity-Scope and Scope Exceptions". Under the provisions of ASC 815, the anti-dilution and cash settlement provisions in certain warrants (collectively the "Derivative Liabilities") qualify as derivative instruments.

The Company is required to mark to market at the end of each reporting period the value of the derivative liabilities. The Company revalues these derivative liabilities at the end of each reporting period by using available market information and commonly accepted valuation methodologies. The periodic change in value of the derivative liabilities is recorded as either non-cash derivative income (if the value of the embedded derivative and warrants decrease) or as non-cash derivative expense (if the value of the embedded derivative and warrants increase). Although the values of the embedded derivative and warrants are affected by interest rates, the remaining contractual conversion period and the Company's stock volatility, the primary cause of the change in the values of the derivative liabilities will be the value of the Company's common stock. If the stock price goes up, the value of these derivatives will generally increase and if the stock price goes down the value of these derivatives will generally decrease.

The Company uses a Monte-Carlo simulation methodology and the Black Scholes option-pricing model in the determination of the fair value of the Derivative Liabilities. The Monte-Carlo simulation methodology is affected by the Company's stock price as well as assumptions regarding the expected stock price volatility over the term of the Derivative Liabilities and assumptions regarding future financings. The Company utilized the services of an independent valuation firm, Vantage Point Advisors, Inc. to perform the Monte-Carlo simulations.

The Black-Scholes option-pricing model is affected by the Company's stock prices as well as assumptions regarding the expected stock price volatility of the term of the derivative liabilities in addition to interest rates and dividend yields.

As of December 31, 2011, the Company had 18,547,293 outstanding warrants to purchase shares of the Company's common stock that qualified for derivative liability treatment. The recorded fair market value of those warrants at December 31, 2011 was approximately $11,824,000 which is reflected as a non-current liability in the consolidated balance sheet as of December 31, 2011. On March 21, 2012, the Company amended 12,252,500 warrants such that these warrants no longer qualify as derivative liabilities. The Company determined the change in fair value from date of previous measurement (December 31, 2011) to the date of amendment (March 21, 2012) for these warrants and recorded approximately $5,110,000 in expense. Such expense is included in Company's condensed consolidated statement of operations for the three months ended March 31, 2012 under the caption "Change in fair value of derivative liabilities".

Additionally, as a result of the agreements to amend the warrants and the warrants no longer qualifying for derivative liability treatment, the Company reclassified $13,588,000 of derivative liabilities into a component of additional paid-in capital in the Company's consolidated financial statements for the period ended March 31, 2012.

NOTE 8. FAIR VALUE ACCOUNTING

The Company accounts for fair value measurements in accordance with ASC Topic No. 820, "*Fair Value Measurements and Disclosures*," ("Topic No. 820") which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements.

ASC Topic 820 establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under ASC Topic 820 are described below:

Level 1 Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

Level 2 Applies to assets or liabilities for which there are inputs other than quoted prices included within Level 1 that are observable for the asset or liability such as quoted prices for similar assets or liabilities in active markets; quoted prices for identical assets or liabilities in markets with insufficient volume or infrequent transactions (less active markets); or model-derived valuations in which significant inputs are observable or can be derived principally from, or corroborated by, observable market data.

Level 3 Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (supported by little or no market activity).

The following table sets forth the Company's financial assets and liabilities measured at fair value by level within the fair value hierarchy. As required by ASC Topic 820, assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

($ in thousands)	Fair Value at March 31, 2012			
	Total	**Level 1**	**Level 2**	**Level 3**
Assets:				
Pension assets	$ 1,572	$ 1,572	$ —	$ —
Totals	$ 1,572	$ 1,572	$ —	$ —
Liabilities:				
Derivative liabilities	$ 5,772	$ —	$ —	$ 5,772
Totals	$ 5,772	$ —	$ —	$ 5,772

($ in thousands)	Fair Value at December 31, 2011			
	Total	**Level 1**	**Level 2**	**Level 3**
Assets:				
Pension assets	$ 1,455	$ 1,455	$ —	$ —
Totals	$ 1,455	$ 1,455	$ —	$ —
Liabilities:				
Derivative liabilities	$ 11,824	$ —	$ —	$ 11,824
Totals	$ 11,824	$ —	$ —	$ 11,824

The Company's pension assets are classified within Level 1 of the fair value hierarchy because they are valued using market prices. The pension assets are primarily comprised of the cash surrender value of insurance contracts. All plan assets are managed in a policyholder pool in Germany by outside investment managers. The investment objectives for the plan are the preservation of capital, current income and long-term growth of capital.

As of March 31, 2012, the Company had 6,294,793 outstanding warrants to purchase shares of the Company's common stock that qualified for derivative liability treatment. The recorded fair market value of those warrants at March 31, 2012 was approximately $5,772,000 which is reflected as a non-current liability in the consolidated balance sheet as of March 31, 2012. The fair value of the Company's derivative liabilities are classified within Level 3 of the fair value hierarchy because they are valued using pricing models that incorporate management assumptions that cannot be corroborated with observable market data. The Company uses Black Scholes or Monte-Carlo simulation methodologies in the determination of the fair value of the derivative liabilities.

The Monte-Carlo simulation methodology is affected by the Company's stock price as well as assumptions regarding the expected stock price volatility over the term of the derivative liabilities in addition to the probability of future financings. The Black Scholes valuation model is affected by the Company's stock price as well as assumptions regarding the expected stock price volatility over the term of the derivative liabilities in addition to expected dividend yield and risk free interest rates appropriate for the expected term.

The Company monitors the activity within each level and any changes with the underlying valuation techniques or inputs utilized to recognize if any transfers between levels are necessary. That determination is made, in part, by working with outside valuation experts for Level 3 instruments and monitoring market related data and other valuation inputs for Level 1 and Level 2 instruments.

A reconciliation of the Company's liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) is as follows:

($ in thousands)	**Derivative Liabilities**
Balance at December 31, 2011	$ 11,824
Total unrealized gains	—
Included in earnings	7,536
Settlements	(13,588)
Issuances	—
Transfers in and/or out of Level 3	—
Balance at March 31, 2012	$ 5,772

All unrealized gains or losses resulting from changes in value of any Level 3 instruments are reflected as a separate line in the condensed consolidated statement of operations in arriving at net loss. The Company is not a party to any hedge arrangements, commodity swap agreement or any other derivative financial instruments.

Certain assets are measured at fair value on a non-recurring basis and are subject to fair value adjustments only in certain circumstances. Included in this category is goodwill written down to fair value when determined to be impaired. The valuation methods for goodwill involve assumptions based on management's judgment using internal and external data, and which are classified in Level 3 of the valuation hierarchy.

NOTE 9. RELATED PARTY TRANSACTIONS

As more fully described in Note 5 to these consolidated financial statements, on November 14, 2008, the Company entered into a series of convertible promissory notes (the "Related Party Convertible Notes"), aggregating $110,000, with certain officers and members of the Company's Board of Directors. The Related Party Convertible Notes bear interest at 7.0% per annum and were originally due February 14, 2009. The Company continues to seek a waiver from the holders of the Related Party Convertible Notes.

In conjunction with the issuance of the Related Party Convertible Notes, the Company issued an aggregate of 149,996 warrants to the note holders to purchase Common Stock of the Company. The warrants have an exercise price $0.55 per share and may be exercised at any time from November 14, 2008 until November 14, 2013. All warrants were outstanding and exercisable as of March 31, 2012 and December 31, 2011.

During the three months ended March 31, 2012, the Company repaid $45,000 in principal to certain holders of the Related Party Convertible Notes.

In January 2012, the Company entered into a professional services contract with an entity that a member of the Company's Board of directors has an ownership interest in. The contract value was $50,000 and the Company paid the professional services firm $25,000 during the three months ended March 31, 2012.

NOTE 10. CONTINGENT LIABILITIES

During the three months ended March 31, 2012, the Company wrote off certain accounts payable totaling approximately $230,000, which is included in "Other income, net" in the accompanying condensed consolidated statements of operations. Such accounts payable represented amounts that could not be paid in full at the time, or were, in the view of management, unenforceable. While management believes that such amounts no longer represent recognized liabilities of the Company, such creditors may subsequently assert a claim against the Company.

Employment Agreements

The Company has employment agreements with its Chief Executive Officer and Senior Vice President of Administration and Chief Financial Officer. The Company may terminate the agreements with or without cause. Subject to the conditions and other limitations set forth in each respective employment agreement, each executive will be entitled to the following severance benefits if the Company terminates the executive's employment without cause or in the event of an involuntary termination (as defined in the employment agreements) by the Company or by the executive: (i) a lump sum cash payment equal to between six months and twenty-four months of base salary, based upon specific agreements; (ii) continuation of the executive's fringe benefits and medical insurance for a period of three years; and (iii) immediate vesting of 50% of each executive's outstanding restricted stock awards and stock options. In the event that the executive's employment is terminated within the six months prior to or the thirteen months following a change of control (as defined in the employment agreements), the executive is entitled to the severance benefits described above, except that 100% of each executive's restricted stock awards outstanding and stock options will immediately vest. Each executive's eligibility to receive any severance payments or other benefits upon his termination is conditioned upon him executing a general release of liability.

The Company also has a Change of Control and Severance Benefits Agreement with its Chief Technical Officer and Vice President of Business Development. Subject to the conditions and other limitations set forth in each respective employment agreement, each executive will be entitled to the following severance benefits if the Company terminates his employment without cause prior to the closing of any change of control transaction: (i) a lump sum cash payment equal to six months of base salary; and (ii) continuation of the executive's health insurance benefits until the earlier of six (6) months following the date of termination, the date on which he is no longer entitled to continuation coverage pursuant to COBRA or the date that he obtains comparable health insurance coverage. In the event that the executive's employment is terminated within the twelve months following a change of control, he is entitled to the severance benefits described above, plus his stock options will immediately vest and become exercisable. The executive's eligibility to receive severance payments or other benefits upon his termination is conditioned upon him executing a general release of liability.

Registration Rights

As part of the Qualified Financing discussed in Note 1 and elsewhere in this Form 10-Q, the Company entered into a registration rights agreement for the benefit of the Qualified Financing investor participants. That agreement requires that the Company pay the participants certain liquidating damages should specific deadlines regarding the preparation and filing of a registration statement or similar document in compliance with the 1933 Act be missed. Specifically, a registration statement must be filed no later than 60 days after the consummation of the Qualified Financing and that statement must be "effective" no later than 150 days after the consummation of the Qualified Financing. The liquidating damages are calculated as a percentage of the aggregate amount invested by each participant. Such payments, which are required to be made in cash, increase on a daily basis until the registration statement is filed; however, the liquidating damages in aggregate are not to exceed 10% of the total investment by each participant. The Company filed the required registration statement on Form S-1 on February 10, 2012 and it became effective on May 10, 2012, which is within the required timeframe.

In accordance with ASC 825, “Financial Instruments”, the Company has determined that it is not probable, as defined under ASC 450, “Contingencies”, that the registration statement will either not be declared “effective” or be declared effective at a date requiring payment of any liquidating damages. Therefore, the Company has not recorded any loss contingencies related to these registration rights.

NOTE 11. SUBSEQUENT EVENTS

In April and May 2012, the Company issued 623,190 shares of its common stock pursuant to the cashless exercise of 1,039,000 warrants.

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

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. All forward-looking statements included in this report are based on information available to us as of the date hereof and we assume no obligation to update any forward-looking statements. Forward-looking statements involve known or unknown risks, uncertainties and other factors, which may cause our actual results, performance or achievements, or industry results to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include but are not limited to those items discussed in our Annual Report on Form 10-K for the year ended December 31, 2011, under “Risk Factors” and in Item 1A of Part II of this Quarterly Report on Form 10-Q.

The following discussion of the financial condition and results of operations should be read in conjunction with the condensed consolidated financial statements included elsewhere within this Quarterly Report. Fluctuations in annual and quarterly results may occur as a result of factors affecting demand for our products such as the timing of new product introductions by us and by our competitors and our customers’ political and budgetary constraints. Due to such fluctuations, historical results and percentage relationships are not necessarily indicative of the operating results for any future period.

OVERVIEW

ImageWare Systems, Inc. (the “Company”) is incorporated in the state of Delaware. The Company is a pioneer and leader in the emerging market for biometrically enabled software-based identity management solutions. Using those human characteristics that are unique to us all, the Company creates software that provides a highly reliable indication of a person’s identity. The Company’s “flagship” product is the patented IWS Biometric Engine®. The Company’s products are used to manage and issue secure credentials, including national IDs, passports, driver licenses and access control credentials. The Company’s products also provide law enforcement with integrated mug shot, fingerprint LiveScan and investigative capabilities. The Company also provides comprehensive authentication security software using biometrics to secure physical and logical access to facilities or computer networks or Internet sites. Biometric technology is now an integral part of all markets the Company addresses and all of the products are integrated into the IWS Biometric Engine.

Recent Developments

In March 2012, the Company entered into agreements with the holders of certain warrants acquired in connection with a financing consummated by the Company on December 21, 2011 (the “Qualified Financing”), which warrants are currently exercisable for 12,252,500 shares of the Company’s common stock at an exercise price of $0.50 per share. The warrants contained certain settlement provisions that required, under specific circumstances, a net cash settlement upon the occurrence of a “Fundamental Transaction” as defined in the warrants. These provisions effectively resulted in the characterization of the warrants as derivative liabilities. The agreements amended the warrants to revise, among other provisions, the definition of “Fundamental Transaction”. As a result of the amendments, the warrants no longer qualify as derivative liabilities. The Company determined the change in fair value from the date of previous measurement (December 31, 2011) to the date of the amendment (March 21, 2012) for these warrants and recorded approximately $5,110,000 in expense. Such expense is included in the Company’s condensed consolidated statement of operations for the three months ended March 31, 2012 under the caption “Change in fair value of derivative liabilities”.

Additionally, as a result of the agreements to amend the warrants and the warrants no longer qualifying for derivative liability treatment, the Company reclassified approximately $13,588,000 in derivative liability into a component of additional paid-in capital in the Company's financial statements for the period ended March 31, 2012.

During the three months ended March 31, 2012, the Company paid approximately $178,000 in accumulated dividends to the holders of its Series B convertible preferred stock.

Critical Accounting Policies and Estimates

The discussion and analysis of our consolidated financial condition and results of operations are based on our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America, or U.S. GAAP. The preparation of these consolidated financial statements in accordance with U.S. GAAP requires us to utilize accounting policies and make certain estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingencies as of the date of the consolidated financial statements and the reported amounts of revenue and expenses during a fiscal period. The SEC considers an accounting policy to be critical if it is important to a company’s financial condition and results of operations, and if it requires significant judgment and estimates on the part of management in its application.

Significant estimates include the allowance for doubtful accounts receivable, calculation of the Company’s tax provision, inventory obsolescence reserve, deferred tax asset valuation allowances, accounting for loss contingencies, recoverability of goodwill and acquired intangible assets and amortization periods, assumptions used in the Black-Scholes model to calculate the fair value of share based payments, assumptions used in the application of fair value methodologies to calculate the fair value of derivative liabilities and revenue and cost of revenues recognized under the percentage of completion method.

Critical accounting policies are those that, in management’s view, are most important in the portrayal of our financial condition and results of operations. Management believes there have been no material changes during the three months ended March 31, 2012 to the critical accounting policies discussed in the Management’s Discussion and Analysis of Financial Condition and Results of Operations section of our Annual Report on Form 10-K for the year ended December 31, 2011.

This management’s discussion and analysis of financial condition and results of operations should be read in conjunction with the consolidated financial statements and related notes contained elsewhere in this Annual Report.

RESULTS OF OPERATIONS

Three Months Ended March 31, 2012 Compared to the Three Months Ended March 31, 2011.

Product Revenue

Net Product Revenue (dollars in thousands)	Three Months Ended March 31, 2012	Three Months Ended March 31, 2011	$ Change	% Change
Software and royalties	$ 280	$ 1,076	$ (796)	(74)%
Percentage of total net product revenue	72%	86%		
Hardware and consumables	$ 85	$ 17	$ 68	400%
Percentage of total net product revenue	22%	1%		
Services	$ 23	$ 164	$ (141)	(86)%
Percentage of total net product revenue	6%	13%		
Total net product revenue	$ 388	$ 1,257	$ (869)	(69)%

Software and royalty revenue decreased 74% or approximately $796,000 during the three months ended March 31, 2012 as compared to the corresponding period in 2011. This decrease is due to lower project-oriented revenue of our identity management software solutions of approximately $888,000 offset by higher revenue from our sales of boxed identity management software through our distribution channel of approximately $26,000, higher revenue from identification software royalties and license revenue of approximately $3,000 and higher revenue from Law Enforcement software solutions of approximately $63,000.

During the quarter we delivered and received payment for software licenses for Los Angeles World Airports valued at approximately $440,000, however we will not recognize revenue on the sale until all services have been completed and accepted.

Revenue from the sale of hardware and consumables increased approximately $68,000 due to higher purchases of replacement equipment by certain Law Enforcement customers during the three months ended March 31, 2012 as compared to the corresponding period in 2011.

Services revenue is comprised primarily of software integration services, system installation services and customer training. Such revenue decreased 86% or approximately $141,000 during the three months ended March 31, 2012 as compared to the corresponding period in 2011, due primarily to the completion of the service element in certain contracts and decreases in identity management solutions requiring significant amounts of customization, integration or installation.

We believe our first quarter product revenue was negatively impacted by the later than expected release of our newest version of the Biometric Engine which was released in late April 2012, approximately six months later than originally planned. A number of sales initiatives were dependent upon the release of this newest version. Additionally, several significant international projects which were forecast to begin in the first quarter of 2012 were delayed into the second and third quarters of 2012.

We believe that the period-to-period fluctuations of identity management software revenue in project-oriented solutions are largely due to the timing of government procurement with respect to the various programs we are pursuing. Based on management's current visibility into the timing of potential government procurements, we believe that we will see a significant increase in government procurement and implementations with respect to identity management initiatives; however we cannot predict the timing of such initiatives.

Maintenance Revenue

Maintenance Revenue (dollars in thousands)	**Three Months Ended March 31, 2012**	**2011**	**$ Change**	**% Change**
Maintenance revenue	$ 733	$ 664	$ 69	10%

Maintenance revenue was $733,000 for the three months ended March 31, 2012 as compared to $664,000 for the corresponding period in 2011 representing a 10% or $69,000 increase. Identity management maintenance revenue generated from identification software solutions was $238,000 for the three months ended March 31, 2012 as compared to $171,000 during the comparable period in 2011. The increase of $67,000 is due to higher maintenance revenues generated from our biometric engine. Law enforcement maintenance revenues increased $2,000 for the three month period ended March 31, 2012 as compared to the corresponding period in 2011 due to our the expiration of certain maintenance contracts.

We anticipate growth of our maintenance revenue through the retention of existing customers combined with the expansion of our installed base resulting from the completion of project-oriented work, however we cannot predict the timing of this anticipated growth.

Cost of Product Revenue

Cost of Product Revenue: (dollars in thousands)	Three Months Ended March 31, 2012	2011	$ Change	% Change
Software and royalties	$ 41	$ 32	$ 9	28%
Percentage of software and royalty product revenue	15%	3%		
Hardware and consumables	$ 26	$ 16	$ 10	63%
Percentage of hardware and consumables product revenue	31%	94%		
Services	$ 16	$ 83	$ (67)	(81)%
Percentage of services product revenue	70%	51%		
Total product cost of revenue	$ 83	$ 131	$ (48)	(37)%
Percentage of total product revenue	21%	10%		

The cost of software and royalty product revenue increased approximately $9,000 despite lower software and royalties sales of approximately $796,000 due to the three month ended March 31, 2011 containing significant amounts of software only sales which typically have an extremely low cost of product revenue as compared to the comparable period in 2012.

The increase in the cost of product revenue for our hardware and consumable sales of 63% or approximately $10,000 for the three months ended March 31, 2012 as compared to the corresponding period in 2011, reflects higher hardware and consumable revenues during the three months ended March 31, 2012, as compared to the comparable period of 2011.

The 81% or $67,000 decrease in the cost of services product revenue for the three months ended March 31, 2012 as compared to the corresponding period of 2011, reflects lower software integration services and system installation service revenue generated from project work during the three month period ended March 31, 2012.

Cost of Maintenance Revenue

Cost of Maintenance Revenue (dollars in thousands)	Three Months Ended March 31, 2012	2011	$ Change	% Change
Total maintenance cost of revenue	$ 239	$ 238	$ 1	0%
Percentage of total maintenance revenue	33%	36%		

Cost of maintenance revenue did not change significantly for the three months ended March 31, 2012 as compared to the corresponding period in 2011. See the gross profit section below for a discussion regarding the decrease in cost of maintenance revenue as a percentage of maintenance revenue.

Product Gross Profit

Product gross profit (dollars in thousands)	Three Months Ended March 31, 2012	Three Months Ended March 31, 2011	$ Change	% Change
Software and royalties	$ 239	$ 1,044	$ (805)	(77)%
Percentage of software and royalty product revenue	85%	97%		
Hardware and consumables	$ 59	$ 1	$ 58	5800%
Percentage of hardware and consumables product revenue	69%	6%		
Services	$ 7	$ 81	$ (74)	(91)%
Percentage of services product revenue	30%	49%		
Total product gross profit	$ 305	$ 1,126	$ (821)	(73)%
Percentage of total product revenue	79%	90%		

Software and royalty gross profit decreased by 77% or approximately $805,000 for the three months ended March 31, 2012 from the corresponding period in 2011, due to lower software and royalty product revenue of approximately $796,000 combined with higher costs of software and royalty revenue of $9,000. The increase in cost of software and royalty product revenues despite lower software and royalty sales is reflective of the three month period ended March 31, 2011 containing extremely high levels of software license revenues with minimal cost of sales as compared to the corresponding period in 2012. Costs of software products can also vary as a percentage of product revenue from quarter to quarter depending upon product mix and third party software licenses included in software solutions.

Hardware gross profit increased by approximately $58,000 due to higher hardware and consumable revenues of approximately $68,000 combined with lower costs of hardware and consumable revenue of approximately $10,000. The increase in hardware and consumable revenues resulted from higher purchases of replacement equipment by certain Law Enforcement customers during the three months ended March 31, 2012 as compared to the corresponding period of 2011.

Services gross profit decreased approximately $74,000 or 91% due to lower services revenue of approximately $141,000 generated through project sales for the three month period ending March 31, 2012 as compared to the corresponding period in 2011.

Maintenance Gross Profit

Maintenance gross profit (dollars in thousands)	Three Months Ended March 31, 2012	Three Months Ended March 31, 2011	$ Change	% Change
Total maintenance gross profit	$ 494	$ 426	$ 68	16%
Percentage of total maintenance revenue	67%	64%		

Gross margins related to maintenance revenue increased $68,000 or 16% due to higher maintenance revenues of approximately $69,000 offset by a $1,000 increase in maintenance cost of revenue for the three months ended March 31, 2012 as compared to the corresponding period in 2011. The increase in gross profit percentage from 64% for the three months ended March 31, 2011 to 67% for the corresponding period of 2012 reflects a higher revenue base to absorb fixed maintenance costs.

Operating Expense

Operating expense (dollars in thousands)	Three Months Ended March 31, 2012	2011	$ Change	% Change
General and administrative	$ 944	$ 507	$ 437	86%
Percentage of total net revenue	84%	26%		
Sales and marketing	$ 394	$ 371	$ 23	6%
Percentage of total net revenue	35%	19%		
Research and development	$ 734	$ 627	$ 107	17%
Percentage of total net revenue	65%	33%		
Depreciation and amortization	$ 12	$ 7	$ 5	71%
Percentage of total net revenue	1%	0%		

General and Administrative Expenses

General and administrative expense is comprised primarily of salaries and other employee-related costs for executive, financial, and other infrastructure personnel. General legal, accounting and consulting services, insurance, occupancy and communication costs are also included with general and administrative expense. The $437,000 increase in such expense is primarily comprised of the following major components:

- Increase in professional services, consulting and contract services expense of $379,000, related primarily to bringing the Company's financial reporting current with the Securities and Exchange Commission.
- Increase in personnel related expense of approximately $19,000.
- Increase in stock based compensation of approximately $61,000.
- Decrease in financing expense of approximately $25,000.

Sales and Marketing

Sales and marketing expense consists primarily of the salaries, commissions, other incentive compensation, employee benefits and travel expense of our sales, marketing, business development and product management functions. The dollar increase of $23,000 during the three months ended March 31, 2012 as compared to the corresponding period in 2011 is comprised of the following major components:

- Increase in personnel related expense of approximately $18,000 due to sales commissions earned.
- Increase in sales contractor fees of approximately $15,000.
- Decrease in rent, office related and other expense of approximately $16,000.

Research and Development

Research and development expense consists primarily of salaries, employee benefits and outside contractors for new product development, product enhancements, custom integration work and related facility costs. Such expense increased $107,000 for the three months ended March 31, 2012 as compared to the corresponding period in 2011. The increase is comprised of the following major components:

- Increase in personnel expenditures of approximately $96,000.
- Decrease in rent and office related costs of approximately $5,000.
- Increase in stock-based compensation of approximately $16,000.

Our level of expenditures in research and development reflects our belief that to maintain our competitive position in markets characterized by rapid rates of technological advancement, we must continue to invest significant resources in new systems and software as well as continue to enhance existing products.

Depreciation and Amortization

During the three months ended March 31, 2012, depreciation and amortization expense increased $5,000 as compared to the corresponding period in 2011. The increase in depreciation and amortization expense reflects the acquisition of computer equipment of approximately $77,000 during the three months ended March 31, 2012. The Company's amortization expense consisted solely of amortization expense incurred on the Company's EPI trademark and trade name intangible asset.

Interest Expense (Income), Net

For the three months ended March 31, 2012, we recognized interest income of $2,000 and interest expense of $6,000. For the three months ended March 31, 2011, we recognized interest income of $0 and interest expense of $628,000. Interest expense for the three months ended March 31, 2012 contains the following components:

- Coupon interest of approximately $2,000 related to our 7% convertible notes
- Other interest expense of approximately $4,000

Interest expense for the three months March 31, 2011 contains the following components:

- Coupon interest of approximately $82,000 related to our 7% convertible notes and 9% secured notes payable
- Note discount and beneficial conversion feature amortizations classified as interest expense of $540,000
- Other interest expense of approximately $6,000

Change in Fair Value of Derivative Liabilities

For the three months ended March 31, 2012, we recognized non-cash expense of $7,536,000 compared to $7,273,000 for the corresponding period of 2011. This expense is related to the change in fair value of the Company's derivative liabilities associated with the anti-dilution provisions and cash settlement provisions in certain warrants to purchase shares of our common stock. The derivative liabilities were revalued using available market information and commonly accepted valuation methodologies.

Other Income

For the three months ended March 31, 2012, we recognized other income of $235,000. For the three months ended March 31, 2011, we recognized other income of $5,000. Other income for the three months ended March 31, 2012 is comprised of approximately $230,000 from the write off of certain accounts payable due to the expiration of the legal statute of limitation on such payables and $5,000 in miscellaneous other income. Other income for the three months ended March 31, 2011 contains approximately $5,000 from collections on previously derecognized receivables.

LIQUIDITY AND CAPITAL RESOURCES

On December 20, 2011, we consummated an equity financing resulting in gross proceeds of $10.0 million (“Qualified Financing”), including the $750,000 of promissory notes converted into the Qualified Financing. In connection with the Qualified Financing, we issued 20,000,000 shares of our common stock (the “Shares”), and warrants to purchase 12,207,500 shares of common stock exercisable for $0.50 per share (“Warrants”), which number includes 2,207,500 shares issuable upon exchange of warrants issued to MDB Capital Group in consideration for acting as placement agent in connection with the Qualified Financing. We also issued 90,000 shares of common stock and a warrant exercisable for 45,000 shares of common stock in lieu of cash in payment for legal fees related to the Qualified Financing. We also issued a warrant to purchase 250,000 shares of the Company’s common stock at an exercise price of $0.50, which expires two years from the date of grant, to a significant investor to cover certain expenses related to and in anticipation of the Qualified Financing. The net proceeds from the Qualified Financing were approximately $8,544,000, of which, $1,500,000 was then used to repay certain convertible notes payable. As of March 31, 2012, all debt other than the $65,000 in related party notes payable had been converted to common stock or repaid. In addition, in connection with the Qualified Financing, (i) the anti-dilution provision contained in certain of our existing warrants were amended resulting in such warrants no longer qualifying as derivative liabilities; and (ii) a significant investor ("Investor") exchanged $4.5 million principal amount of convertible promissory notes of the Company ("Exchanged Notes"), and accrued but unpaid interest on the Exchanged Notes and on an additional $2.25 million in promissory notes, into 9,774,559 shares of our common stock ("Exchange Shares"). The Investor also agreed to convert $750,000 principal amount of additional promissory notes held by the Investor and invest the proceeds into the Qualified Financing.

At March 31, 2012, our principal sources of liquidity consisted of cash and cash equivalents of $5,223,000 and accounts receivable, net of $376,000. As of March 31, 2012, we had positive working capital of $1,780,000 which included $1,445,000 of deferred revenue. This compares to negative working capital of $3,321,000 during the corresponding period in 2011. Historically, our principal sources of cash have included customer payments from the sale of our products, proceeds from the issuance of common and preferred stock and proceeds from the issuance of debt. Our principal uses of cash have included cash used in operations, payments relating to purchases of property and equipment and repayments of borrowings. We expect that our principal uses of cash in the future will be for product development including customization of identity management products for enterprise and consumer applications, further development of intellectual property, development of SaaS capabilities for existing products as well as general working capital and capital expenditure requirements. We expect that, as our revenues grow, our sales and marketing and research and development expenses will continue to grow and, as a result, we will need to generate significant net revenues to achieve and sustain income from operations.

Management believes that the Company’s current cash and cash equivalents will be sufficient to meet working capital and capital expenditure requirements for at least the next 12 months from the date of this filing and that we will have sufficient liquidity to fund its business and meet its contractual obligations over a period beyond the next 12 months.

Operating Activities

We used net cash of $1,216,000 in operating activities for the three months ended March 31, 2012 compared to net cash use of $81,000 during the same period in the prior year. During the three months ended March 31, 2012, net cash used in operating activities primarily consisted of net loss of $8,590,000 and a net decrease in working capital and other assets and liabilities of $94,000. Those amounts were offset by $7,468,000, net of non-cash costs including a $7,536,000 unrealized loss related to the change in value of our derivative liabilities, $150,000 in stock based compensation and $12,000 in depreciation and amortization offset by $230,000 of non-cash income from the write off of certain accounts payable due to the expiration of the statute of limitations. During the three months ended March 31, 2012, we used cash of $125,000 to fund increases in current assets and generated cash of $31,000 through increases in current liabilities and deferred revenues, excluding debt. For the three months ended March 31, 2011, we used cash of $69,000 to fund increases in current assets and used cash of $64,000 from decreases in current liabilities and deferred revenues, excluding debt.

Investing Activities

Net cash used in investing activities was $77,000 and $1,000 for the three months ended March 31, 2012 and 2011, respectively. For the three months ended March 31, 2012, we used cash to fund capital expenditures of computer equipment and software of approximately $77,000. This level of equipment and software purchases resulted primarily from the replacement of older equipment and software.

Financing Activities

We used cash of $223,000 in financing activities for the three months ended March 31, 2012 compared to the generation of $659,000 for the same period in the prior year. For the three months ended March 31, 2012, we used cash of $45,000 to partially repay certain related party convertible note holders and used cash of $178,000 to pay dividends on our Series B Preferred Stock. For the three months ended March 31, 2011, we generated cash of $655,000 from the exercise of common stock purchase warrants and generated cash of $4,000 from the exercise of common stock options.

Debt

At March 31, 2012, we had approximately $65,000 in outstanding debt, exclusive of any debt discounts, and another $26,000 in related accrued interest.

7% Convertible Promissory Notes to Related Parties

On November 14, 2008, the Company entered into a series of convertible promissory notes (the "Related-Party Convertible Notes"), aggregating $110,000 with certain officers and members of the Company’s Board of Directors. The Related-Party Convertible Notes bear interest at 7.0% per annum and were due February 14, 2009. The principal amount of the Related-Party Convertible Notes plus accrued but unpaid interest is convertible at the option of the holder into common stock of the Company. The number of shares into which the Related-Party Convertible Notes are convertible shall be calculated by dividing the outstanding principal and accrued but unpaid interest by $0.55 (the “Conversion Price”).

In conjunction with the issuance of the Related-Party Convertible Notes, the Company issued an aggregate of 149,996 warrants to the note holders to purchase common stock of the Company. The warrants have an exercise price of $0.55 per share and may be exercised at any time from November 14, 2008 until November 14, 2013.

The Company, in 2008, initially recorded the convertible notes net of a discount equal to the fair value allocated to the warrants of approximately $13,000. The Company estimated the fair value of the warrants using the Black-Scholes option pricing model using the following assumptions: term of 5 years, a risk free interest rate of 2.53%, a dividend yield of 0%, and volatility of 96%. The convertible notes also contained a beneficial conversion feature, which resulted in an additional debt discount of $12,000. The beneficial conversion amount was measured using the accounting intrinsic value, i.e. the excess of the aggregate fair value of the common stock into which the debt is convertible over the proceeds allocated to the security. The Company has accreted the beneficial conversion feature over the life of the note.

The Company did not repay the Related-Party Convertible Notes on the due date. In August 2009, the Company received from the Related-Party Convertible Note holders a waiver of default and extension to January 31, 2010 of the maturity date of the Related-Party Convertible Notes. As consideration for the waiver and note extension, the Company issued to the Related-Party Convertible Note holders an aggregate of 150,000 warrants to purchase shares of the Company’s common stock. The warrants have an exercise price of $0.54 per share and expire on August 25, 2014.

The Company did not repay the notes on January 31, 2010 and is currently seeking an additional waiver of default from the holders of the Related-Party Convertible Notes. During the three months ended March 31, 2012 the Company repaid $45,000 to certain holders of the Related-Party Convertible Notes.

Contractual Obligations

Total contractual obligations and commercial commitments as of March 31, 2012 are summarized in the following table (in thousands):

	Payment Due by Year						
	Total	2012 (9 months)	2013	2014	2015	2016	Thereafter
7% related party promissory notes*	$ 65	$ 65	$	$ —	$ —	$ —	$ —
Operating lease obligations	576	338	238	—	—	—	—
Total	$ 641	$ 403	$ 238	$ —	$ —	$ —	$ —

* Notes had a maturity date of January, 2010. We did not repay the notes on January 31, 2010 and we are currently seeking an additional waiver of default from the holders of the Related-Party Convertible Notes.

Real Property Leases

In December 2010, we entered into a new lease agreement and relocated our corporate headquarters to Rancho Bernardo Road in San Diego, California. The lease term commenced in December 2010 and ends on December 31, 2013. We are obligated under the lease to pay base rent and certain operating costs and taxes for the building. In addition to the corporate headquarters lease in San Diego, California, we also lease space in Ottawa, Province of Ontario, Canada; Portland, Oregon and Mexico City, Mexico. Those contractual lease obligations, as well as the San Diego lease, are included in the "contractual obligations" summary table above.

Stock-based Compensation

Stock-based compensation has been classified as follows in the accompanying condensed consolidated statements of operations (in thousands, except per share data):

	Three Months Ended March 31,	
	2012	2011
Cost of revenues	$ 3	$ 2
General and administrative	82	44
Sales and marketing	34	16
Research and development	31	15
Total	$ 150	$ 77

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Each of our contracts require payment in U.S. dollars. We therefore do not engage in hedging transactions to reduce our exposure to changes in currency exchange rates, although in the event any future contracts are denominated in a foreign currency, we may do so in the future. As a result, our financial results are not significantly affected by factors such as changes in foreign currency exchange rates.

ITEM 4. CONTROLS AND PROCEDURES

(a) Evaluation of disclosure controls and procedures.

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of the design and operations of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as of March 31, 2012. Based on this evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective to ensure that information required to be disclosed in the reports submitted under the Securities and Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, including to ensure that information required to be disclosed by the Company is accumulated and communicated to management, including the principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

(b) Changes in internal controls over financial reporting.

The Company's Chief Executive Officer and Chief Financial Officer have determined that there have been no changes, in the Company's internal control over financial reporting during the period covered by this report identified in connection with the evaluation described in the above paragraph that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II

OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are from time to time involved in various legal proceedings incidental to the conduct of our business. We do not have any ongoing legal proceedings at this time.

ITEM 1A. RISK FACTORS

There were no material changes from the risk factors previously disclosed in Part I, Item 1A "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2011.

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

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

(a)	EXHIBITS
23.1	Consent of Independent Valuation Firm
31.1	Certification of the Principal Executive Officer pursuant to Rule 13a-14(a) and 15d-14(a)
31.2	Certification of the Principal Financial and Accounting Officer pursuant to Rule 13a-14(a) and 15d-14(a)
32.1	Certification by the Principal Executive Officer and Principal Financial and Accounting Officer pursuant to 18 U.S.C. 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase
101.DEF*	XBRL Taxonomy Extension Definition Linkbase
101.LAB*	XBRL Taxonomy Extension Label Linkbase
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase

** Pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933 or Section 18 of the Securities Exchange Act of 1934 and otherwise are not subject to liability.*

SIGNATURES

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

Date: May 15, 2012	IMAGEWARE SYTEMS, INC
	By: /s/ S. James Miller S. James Miller Chief Executive Officer, Chairman and Director (Principal Executive Officer)
Date: May 15, 2012	By /s/ Wayne Wetherell Wayne Wetherell Chief Financial Officer (Principal Financial and Accounting Officer)

Exhibit 23.1

CONSENT OF INDEPENDENT VALUATION FIRM

As independent valuation consultants, Vantage Point Advisors, Inc. hereby consents to the use of the name Vantage Point Advisors, Inc. and to references to our report entitled "Valuation Analysis of ImageWare Systems, Inc." prepared for ImageWare Systems, Inc., or information contained therein, for inclusion in the Quarterly Report on Form 10-Q of ImageWare Systems, Inc. for the three-month period ended March 31, 2012.

Vantage Point Advisors, Inc.
San Diego, California
May 1, 2012

EX 31.1

CERTIFICATION OF CHIEF EXECUTIVE OFFICER
Pursuant to Rule 13a-14(a) adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, S. James Miller, certify that:

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

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the consolidated financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: May 15, 2012

/s/ S. James Miller
S. James Miller
Chief Executive Officer

EX 31.2

CERTIFICATION OF CHIEF FINANCIAL OFFICER
Pursuant to Rule 13a-14(a) adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Wayne G. Wetherell, certify that:

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

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the consolidated financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: May 15, 2012

/s/ Wayne G. Wetherell
Wayne G. Wetherell
Chief Financial Officer

CERTIFICATION

S. James Miller, Chief Executive Officer of ImageWare Systems, Inc. (the "Company"), and Wayne Wetherell, Chief Financial Officer of the Company, each hereby certifies pursuant to the requirement set forth in Rule 13a-14(b) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. Section 1350) that, to the best of his knowledge:

1. The Quarterly Report on Form 10-Q of the Company for the period ended March 31, 2012 fully complies with the requirements of Section 13(a) or 15(d) of the Exchange Act; and

2. The information contained in the Quarterly Report on Form 10-Q of the Company for the quarter ended March 31, 2012 fairly presents, in all material respects, the financial condition of the Company at the end of the period covered by the Quarterly Report and the results of operations of the Company for the period covered by the Quarterly Report.

IN WITNESS WHEREOF, the undersigned have set their hands hereto as of the 15th day of May, 2012.

/s/ S. James Miller

S. James Miller
Chief Executive Officer

/s/ Wayne Wetherell

Wayne Wetherell
Chief Financial Officer
(Principal Financial and Accounting Officer)

A signed original of this written statement required by Section 906 has been provided to ImageWare Systems, Inc. and will be retained by ImageWare Systems, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.