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

FORM 10-Q

(Mark One)
[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2016

[ ] 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 [X] No [ ]

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes [X] 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	[X]
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 [X]

The number of shares of common stock, with $0.01 par value, outstanding on August 9, 2016 was 94,546,555.

IMAGEWARE SYSTEMS, INC.
INDEX

PART I

ITEM 1. FINANCIAL STATEMENTS

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

	June 30, 2016	December 31, 2015
ASSETS	(Unaudited)	
Current Assets:		
Cash and cash equivalents	$ 327	$ 3,352
Accounts receivable, net of allowance for doubtful accounts of $3 at June 30, 2016 and December 31, 2015	274	349
Inventory, net	74	46
Other current assets	185	69
Total Current Assets	860	3,816
Property and equipment, net	141	162
Other assets	31	98
Intangible assets, net of accumulated amortization	112	117
Goodwill	3,416	3,416
Total Assets	**$ 4,560**	**$ 7,609**
LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)		
Current Liabilities:		
Accounts payable	$ 198	$ 198
Deferred revenue	625	1,059
Accrued expense	822	1,149
Lines of credit payable to related parties, net of discount	1,391	—
Total Current Liabilities	3,036	2,406
Pension obligation	1,592	1,511
Total Liabilities	4,628	3,917
Shareholders' Equity (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 June 30, 2016 and December 31, 2015; liquidation preference $607 at June 30, 2016 and at December 31, 2015.	2	2
Series E Convertible Redeemable Preferred Stock, $0.01 par value; designated 12,000 shares, 12,000 shares issued and outstanding at June 30, 2016 and December 31, 2015; liquidation preference $12,000 and $12,240 at June 30, 2016 and December 31, 2015, respectively.	—	—
Common Stock, $0.01 par value, 150,000,000 shares authorized; 94,553,259 and 94,077,599 shares issued at June 30, 2016 and December 31, 2015, respectively, and 94,546,555 and 94,070,895 shares outstanding at June 30, 2016 and December 31, 2015, respectively.	944	940
Additional paid-in capital	151,215	149,902
Treasury stock, at cost 6,704 shares	(64)	(64)
Accumulated other comprehensive loss	(1,226)	(1,195)
Accumulated deficit	(150,939)	(145,893)
Total Shareholders' Equity (Deficit)	(68)	3,692
Total Liabilities and Shareholders' Equity (Deficit)	**$ 4,560**	**$ 7,609**

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 June 30,		Six Months Ended June 30,	
	2016	**2015**	**2016**	**2015**
Revenue:				
Product	$ 356	$ 1,022	$ 759	$ 1,400
Maintenance	640	673	1,280	1,287
	996	1,695	2,039	2,687
Cost of revenue:				
Product	56	589	130	663
Maintenance	219	209	424	420
Gross profit	721	897	1,485	1,604
Operating expense:				
General and administrative	899	788	1,905	1,704
Sales and marketing	743	717	1,416	1,368
Research and development	1,318	1,114	2,631	2,148
Depreciation and amortization	35	41	70	83
	2,995	2,660	6,022	5,303
Loss from operations	(2,274)	(1,763)	(4,537)	(3,699)
Interest expense (income), net	36	(2)	46	435
Other income, net	(200)	—	(200)	(46)
Loss before income taxes	(2,110)	(1,761)	(4,383)	(4,088)
Income tax expense	4	6	6	8
Net loss	(2,114)	(1,767)	(4,389)	(4,096)
Preferred dividends	(309)	(302)	(657)	(506)
Net loss available to common shareholders	$ (2,423)	$ (2,069)	$ (5,046)	$ (4,602)
Basic and diluted loss per common share - see Note 3:				
Net loss	$ (0.02)	$ (0.02)	$ (0.05)	$ (0.04)
Preferred dividends	(0.01)	(0.00)	(0.00)	(0.01)
Basic and diluted loss per share available to common shareholders	$ (0.03)	$ (0.02)	$ (0.05)	$ (0.05)
Basic and diluted weighted-average shares outstanding	94,298,567	93,674,349	94,185,967	93,595,433

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 June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Net loss	$ (2,114)	$ (1,767)	$ (4,389)	$ (4,096)
Other comprehensive income (loss):				
Foreign currency translation adjustment	23	34	(31)	(46)
Comprehensive loss	$ (2,091)	$ (1,733)	$ (4,420)	$ (4,142)

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)

	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015
Cash flows from operating activities		
Net loss	$ (4,389)	$ (4,096)
Adjustments to reconcile net loss to net cash used by operating activities:		
Depreciation and amortization	70	83
Amortization of debt issuance costs and beneficial conversion feature	37	426
Reduction in accrued expense from the expiration of statute of limitations	(200)	—
Warrants issued in lieu of cash paid for services	—	80
Stock-based compensation	565	376
Change in assets and liabilities		
Accounts receivable	75	(47)
Inventory	(28)	443
Other assets	(73)	9
Accounts payable	—	(326)
Deferred revenue	(434)	(1,177)
Accrued expense	(129)	83
Pension obligation	81	10
Total adjustments	(36)	(40)
Net cash used in operating activities	(4,425)	(4,136)
Cash flows from investing activities		
Purchase of property and equipment	(44)	(43)
Net cash used in investing activities	(44)	(43)
Cash flows from financing activities		
Proceeds from exercised stock options	—	33
Proceeds from issuance of preferred stock, net of issuance costs	—	9,955
Proceeds from lines of credit	1,500	750
Repayment of line of credit borrowings	—	(350)
Dividends paid	(25)	(25)
Net cash provided by financing activities	1,475	10,363
Effect of exchange rate changes on cash	(31)	46
Net increase (decrease) in cash and cash equivalents	(3,025)	6,230
Cash and cash equivalents at beginning of period	3,352	218
Cash and cash equivalents at end of period	$ 327	$ 6,448
Supplemental disclosure of cash flow information:		
Cash paid for interest	$ 1	$ 1
Cash paid for income taxes	$ —	$ —
Summary of non-cash investing and financing activities:		
Beneficial conversion feature of convertible debt	$ 121	$ 146
Conversion of related party notes into Series E Preferred	$ —	$ 1,978
Stock dividend on Series E Preferred	$ 631	$ 480

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 market for biometrically enabled software-based identity management solutions. The Company develops mobile and cloud-based identity management solutions providing biometric, secure credential and law enforcement technologies. Our patented biometric product line includes our flagship product, the Biometric Engine®, a hardware and algorithm independent multi-biometric engine that enables the enrollment and management of unlimited population sizes. Our identification products are used to create, issue and manage secure credentials, including national IDs, passports, driver's licenses, smart cards and access control credentials. Our digital booking products provide law enforcement with integrated mug shots, fingerprint live scans, and investigative capabilities. The Company is headquartered in San Diego, CA, with offices in Portland, OR, Washington, D.C., Mexico, and Ottawa, Ontario.

Recent Developments

On March 9, 2016, the Company and Neal I. Goldman, a director of the Company ("*Goldman*"), entered into the fourth amendment (the "*Fourth Amendment*") to the convertible promissory note and line of credit previously issued by the Company to Goldman on March 27, 2013 (the "*Goldman LOC*"). The Fourth Amendment (i) provides the Company with the ability to borrow up to $5.0 million under the terms of the Goldman LOC; (ii) permits Goldman to convert the outstanding principal, plus any accrued but unpaid interest due under the Goldman LOC (the "*Outstanding Balance*"), into shares of the Company's common stock, par value $0.001 per share ("*Common Stock*"), for $1.25 per share; and (iii) extends the maturity date of the Goldman LOC to June 30, 2017.

In addition, on March 9, 2016, the Company and Charles Crocker, also a director of the Company ("*Crocker*"), entered into a new line of credit and promissory note (the "*New Crocker LOC*"), in the principal amount of $500,000. The New Crocker LOC shall accrue interest at a rate of 8% per annum, and matures on the earlier to occur of June 30, 2017 or such date that the Company consummates a debt and/or equity financing resulting in net proceeds to the Company of at least $3.5 million. All outstanding amounts due under the terms of the New Crocker LOC shall be convertible into the Company's Common Stock at $1.25 per share.

As of June 30, 2016, $1,250,000 was outstanding under the terms of the Goldman LOC and $250,000 was outstanding under the terms of the New Crocker LOC (together, the "*Lines of Credit*"). Subsequent to June 30, 2016, we borrowed an additional $500,000 under the Lines of Credit. As a result, approximately $3,500,000 remains available under the Lines of Credit for additional borrowings.

Liquidity, Capital Resources

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, including our Lines of Credit. 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 Software-as-a-Service ("*SaaS*") capabilities for existing products as well as general working capital and capital expenditure requirements. We expect that, as our revenue grows, our sales and marketing and research and development expense will continue to grow, albeit at a slower rate and, as a result, we will need to generate significant net revenue to achieve and sustain income from operations.

Reliance on Lines of Credit

During the three months ended June 30, 2016, we incurred borrowings under our existing Lines of Credit of approximately $1,500,000, due and payable on June 30, 2017, and an additional $500,000 subsequent to June 30, 2016. We anticipate needing to increase our borrowings under the Lines of Credit to continue to fund our working capital needs, thereby increasing the aggregate indebtedness due and payable on or before June 30, 2017.

We currently do not anticipate generating sufficient revenue and profit to repay these borrowings in full when due. Therefore, unless the holders of the notes issued under the Lines of Credit convert any outstanding balance into shares of common stock, we will need to seek an extension of the maturity date of the Lines of Credit on or before June 30, 2017. If remaining available borrowings under our Lines of Credit are insufficient or we are unable to extend the maturity date of the Lines of Credit, we will be required to raise additional capital through debt and/or equity financing to continue operations. No assurances can be given that any such financing will be available to us on favorable terms, if at all. At this time, we do not have any commitments for alternative financing or for an extension of the maturity date of the Lines of Credit.

Going Concern

As reflected in the accompanying consolidated financial statements, the Company has continuing losses, negative working capital and negative cash flows from operations. Available borrowings under our existing Lines of Credit may be insufficient to provide for our working capital needs for the next twelve months. As a result, we may need to raise additional capital through debt and/or equity financing to execute our business plan. In addition, in the event we are unable to raise additional capital, we may be required to sell certain of the Company’s assets or license the Company’s technologies to others. These uncertainties raise substantial doubt about the Company’s ability to continue as a going concern.

In view of the matters described in the preceding paragraph, recoverability of a major portion of the recorded asset amounts shown in the accompanying consolidated balance sheet is dependent upon continued operations of the Company, which, in turn, is dependent upon the Company’s ability to continue to raise capital and generate positive cash flows from operations. However, the Company operates in markets that are emerging and highly competitive. There is no assurance that the Company will operate at a profit or generate positive cash flows in the future.

The consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts and classifications of liabilities that might be necessary should the Company be unable to continue as a going concern.

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES AND BASIS OF PRESENTATION

Basis of Presentation

The accompanying condensed consolidated balance sheet as of December 31, 2015, 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 accounting principles generally accepted in the United States of America (“*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, 2015, which are included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2015 that was filed with the SEC on March 15, 2016.

Operating results for the three and six months ended June 30, 2016 are not necessarily indicative of the results that may be expected for the year ended December 31, 2016, or any other future periods.

Significant Accounting Policies

Principles of Consolidation

The condensed consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All significant intercompany transactions and balances have been eliminated.

Operating Cycle

Assets and liabilities related to long-term contracts are included in current assets and current liabilities in the accompanying condensed consolidated balance sheets, although they will be recognized in the consolidated statement of operations in the normal course of contract completion which may take more than one operating cycle.

Use of Estimates

The preparation of the condensed consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements, and the reported amounts of revenue and expense during the reporting period. Significant estimates include the allowance for doubtful accounts receivable, inventory carrying values, 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, and assumptions used in the application of fair value methodologies to calculate the fair value of pension assets and obligations. Actual results could differ from estimates.

Cash and Cash Equivalents

The Company defines cash equivalents as highly liquid investments with original maturities of less than 90 days that are not held for sale in the ordinary course of business.

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 an 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.

Inventories

Finished goods inventories are stated at the lower of cost, determined using the average cost method, or market. See Note 4, "*Inventory*", below.

Fair Value of Financial Instruments

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

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
- Post-contract customer support ("*PCS*")

The Company's revenue recognition policies are consistent with GAAP including the Financial Accounting Standards Board ("*FASB*"), Accounting Standards Codification ("*ASC*") 985-605, *Software Revenue Recognition*, ASC 605-35, *Revenue Recognition, Construction-Type and Production-Type Contracts*, SEC 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: (i) persuasive evidence that an arrangement exists, (ii) delivery has occurred or services have been rendered, (iii) the fee is fixed or determinable and (iv) collectability is reasonably assured.

The Company recognizes revenue and profit as work progresses on long-term, fixed-price contracts involving significant amounts of hardware and software customization using the percentage of completion method based on costs incurred to date, compared to total estimated costs upon completion. The primary components of costs incurred are third party software and direct labor cost including fringe benefits. Revenue 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 revenue 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. For contracts that require significant amounts of customization that the Company accounts for under the completed contract method of revenue recognition, the Company defers revenue recognition until customer acceptance is received. For contracts containing either extended or dependent payment terms, revenue recognition is deferred until such time as payment has been received by the Company. 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. Amounts collected in advance for maintenance services are included in current liabilities under "Deferred revenue". Sales tax collected from customers is excluded from revenue.

Customer Concentration

For the three months ended June 30, 2016, two customers accounted for approximately 31% or $313,000 of our total revenue and had trade receivables at June 30, 2016 of $0. For the six months ended June 30, 2016, two customers accounted for approximately 32% or $644,000 of our total revenue and had trade receivables at June 30, 2016 of $53,000.

For the three months ended June 30, 2015, three customers accounted for approximately 56% or $953,000 of our total revenue and had trade receivables at June 30, 2015 of $0. For the six months ended June 30, 2015, three customers accounted for approximately 42% or $1,126,000 of our total revenue and had trade receivables at June 30, 2015 of $0.

Recently Issued Accounting Standards

From time to time, new accounting pronouncements are issued by the Financial Accounting Standards Board (the "*FASB*"), or other standard setting bodies, which are adopted by us as of the specified effective date.

FASB ASU 2014-09. In May 2014, FASB issued Accounting Standards Update ("*ASU*") No. 2014-09, *Revenue from Contracts with Customers*, which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. ASU No. 2014-09 will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. In July 2015, the FASB finalized a one-year deferral of the effective date of the new standard. For public entities, the deferral results in the new revenue standard being effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017. Calendar year-end public companies are therefore required to apply the revenue guidance beginning in their 2018 interim and annual financial statements. The standard permits the use of either the retrospective or cumulative effect transition method. We are currently evaluating the effect that ASU No. 2014-09 will have on our consolidated financial statements and related disclosures.

FASB ASU No. 2014-15. In August 2014, the FASB issued ASU No. 2014-15, *Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern*, which provides guidance on management's responsibility in evaluating whether there is substantial doubt about a company's ability to continue as a going concern and to provide related footnote disclosures. ASU 2014-15 will be effective in the fourth quarter of 2016, with early adoption permitted. The Company is currently evaluating the impact of its pending adoption of ASU 2014-15 on its consolidated financial statements.

FASB ASU No. 2015-11. In July 2015, the FASB issued ASU 2015-11, "*Simplifying the Measurement of Inventory (Topic 330): Simplifying the Measurement of Inventory"*. The amendments in ASU 2015-11 require an entity of measure inventory at the lower of cost or market. Market could be replacement cost, net realizable value, or net realizable value less an approximately normal profit margin. The amendments do not apply to inventory that is measured using last-in, first out (LIFO) or the retail inventory method. The amendments apply to all other inventory, which includes inventory that is measured using first-in, first-out (FIFO) or average cost. For public business entities, the amendments in ASU 2015-11 are effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. The amendments should be applied prospectively with earlier application permitted as of the beginning of an interim or annual reporting period. We do not expect adoption of ASU No. 2015-11 to have a significant impact on our consolidated financial statements.

FASB ASU No. 2016-01. In January 2016, the FASB issued ASU 2016-01, *"Financial Instruments—Overall - Recognition and Measurement of Financial Assets and Financial Liabilities"*. The amendments in this ASU address certain aspects of recognition, measurement, presentation, and disclosure of financial instruments and apply to all entities that hold financial assets or owe financial liabilities. The amendments in this ASU also simplify the impairment assessment of equity investments without readily determinable fair values by requiring assessment for impairment qualitatively at each reporting period. That impairment assessment is similar to the qualitative assessment for long-lived assets, goodwill, and indefinite-lived intangible assets. This ASU is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years, with earlier application permitted for financial statements that have not been issued. An entity should apply the amendments by means of a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption. We plan to adopt the provisions of this ASU for our fiscal year beginning January 1, 2018 and are currently evaluating the impact the adoption of this new accounting standard will have on our consolidated financial statements.

FASB ASU No. 2016-02. In February 2016, the FASB issued ASU No. 2016-02, "*Leases"*. This guidance will result in key changes to lease accounting and will aim to bring leases onto balance sheets to give investors, lenders, and other financial statement users a more comprehensive view of a company's long-term financial obligations as well as the assets it owns versus leases. The new leasing standard will be effective for fiscal years beginning after December 15, 2018, and for interim periods within those fiscal years. The Company is currently evaluating the impact this guidance will have on our consolidated financial statements as well as the expected adoption method.

FASB ASU No. 2016-06. In March 2016, the FASB issued Accounting Standards Update No. 2016-06, *Derivatives and Hedging (Topic 815) – Contingent Put and Call Options in Debt Instruments* ("ASU 2016-06"), which will reduce diversity of practice in identifying embedded derivatives in debt instruments. ASU 2016-06 clarifies that the nature of an exercise contingency is not subject to the "clearly and closely" criteria for purposes of assessing whether the call or put option must be separated from the debt instrument and accounted for separately as a derivative. This guidance is effective for fiscal years beginning after December 15, 2016 and interim periods within those fiscal years. The Company is currently assessing the impact that adopting this new accounting standard will have on its consolidated financial statements and footnote disclosures.

FASB ASU No. 2016-08. In March 2016, the FASB issued Accounting Standards Update No. 2016-08, *Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net)* ("ASU 2016-08"). ASU 2016-08 clarifies the implementation guidance on principal versus agent considerations. The guidance includes indicators to assist an entity in determining whether it controls a specified good or service before it is transferred to the customers. This guidance is effective for fiscal years beginning after December 15, 2017 including interim periods within those fiscal years. The Company is currently assessing the impact that adopting this new accounting standard will have on its consolidated financial statements and footnote disclosures.

FASB ASU No. 2016-09. In March 2016, the FASB issued Accounting Standards Update No. 2016-09, *Compensation – Stock Compensation (Topic 718)* (“ASU 2016-09”). ASU 2016-09 identifies areas for simplification involving several aspects of accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, an option to recognize gross stock compensation expense with actual forfeitures recognized as they occur, as well as certain classifications on the statement of cash flows. This ASU is effective for fiscal years beginning after December 15, 2016 and interim periods within those annual periods. The Company is currently assessing the impact that adopting this new accounting standard will have on its consolidated financial statements and footnote disclosures.

FASB ASU No. 2016-10. In April 2016, the FASB issued Accounting Standards Update No. 2016-10, *Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing* (“ASU 2016-10”). ASU 2016-10 provides further implementation guidance on identifying performance obligations and also improves the operability and understandability of the licensing implementation guidance. This guidance is effective for fiscal years beginning after December 15, 2017 including interim periods within those fiscal years. The Company is currently assessing the impact that adopting this new accounting standard will have on its consolidated financial statements and footnote disclosures.

FASB ASU No. 2016-13. In June 2016, the FASB issued Accounting Standard Update No. 2016-13, F*inancial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments.* ASU 2016-13 changes the impairment model for most financial assets and certain other instruments. For trade and other receivables, held-to-maturity debt securities, loans and other instruments, entities will be required to use a new forward-looking “expected loss” model that will replace today’s “incurred loss” model and generally will result in the earlier recognition of allowances for losses. For available-for-sale debt securities with unrealized losses, entities will measure credit losses in a manner similar to current practice, except that the losses will be recognized as an allowance. This guidance is effective for fiscal years beginning after December 15, 2019 including interim periods within those fiscal years. The Company is currently evaluating the potential impact of adoption of this standard on its 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 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, 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 and if-converted methods. For diluted loss per share calculation purposes, the net loss available to common 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 June 30,**		**Six Months Ended June 30,**	
	2016	**2015**	**2016**	**2015**
Numerator for basic and diluted loss per share:				
Net loss	$ (2,114)	$ (1,767)	$ (4,389)	$ (4,096)
Preferred dividends	(309)	(302)	(657)	(506)
Net loss available to common shareholders	$ (2,423)	$ (2,069)	$ (5,046)	$ (4,602)
Denominator for basic and dilutive loss per share – weighted-average shares outstanding	94,298,567	93,674,349	94,185,967	93,595,433
Net loss	$ (0.02)	$ (0.02)	$ (0.05)	$ (0.04)
Preferred dividends	(0.01)	(0.00)	(0.00)	(0.01)
Basic and diluted loss per share available to common shareholders	$ (0.03)	$ (0.02)	$ (0.05)	$ (0.05)

The following potential dilutive securities have been excluded from the computations of diluted weighted-average shares outstanding as their effect would have been antidilutive:

Potential Dilutive Securities	For the Three and Six Months Ended June 30, 2016	2015
Convertible notes payable	1,209,635	—
Convertible preferred stock	6,361,818	6,361,818
Stock options	5,582,136	4,041,635
Warrants	450,000	661,666
Total potential dilutive securities	13,603,589	11,065,119

NOTE 4. SELECT BALANCE SHEET DETAILS

Inventory

Inventories of $74,000 as of June 30, 2016 were comprised of work in process of $63,000 representing direct labor costs on in-process projects and finished goods of $11,000 net of reserves for obsolete and slow-moving items of $3,000.

Inventories of $46,000 as of December 31, 2015 were comprised of work in process of $42,000 representing direct labor costs on in-process projects and finished goods of $4,000 net of reserves for obsolete and slow-moving items of $3,000.

Intangible Assets

The Company has intangible assets in the form of trademarks, trade names and patents. The carrying amounts of the Company's acquired trademark and trade name intangible assets were $0 as of June 30, 2016 and December 31, 2015, respectively, which include accumulated amortization of $347,000 as of June 30, 2016 and December 31, 2015. Amortization expense for the intangible assets was $0 for the three and six months ended June 30, 2016 and $4,000 and $7,000 for the three and six months ended June 30, 2015, respectively. All intangible assets were 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 No. 350, *Intangibles – Goodwill and Other*, for proper treatment.

The carrying amounts of the Company's patent assets were $112,000 and $117,000 as of June 30, 2016 and December 31, 2015, respectively, which include accumulated amortization of $547,000 and $542,000 as of June 30, 2016 and December 31, 2015, respectively. Amortization expense for patent assets was $3,000 and $5,000 for the three and six months ended June 30, 2016 and 2015, respectively. Patent assets are being amortized on a straight-line basis over their weighted-average remaining life of approximately 10 years.

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)
2016 (6 months)	$ 6
2017	12
2018	12
2019	12
2020	12
Thereafter	58
Totals	$ 112

Goodwill

The Company annually, or more frequently if events or circumstances indicate a need, tests the carrying amount of goodwill for impairment. A two-step impairment test is used to first identify potential goodwill impairment and then measure the amount of goodwill impairment loss, if any. The first step was conducted by determining and comparing the fair value, employing the market approach, of the Company's reporting unit to the carrying value of the reporting unit. The Company continues to have only one reporting unit, Identity Management. Based on the results of this impairment test, the Company determined that its goodwill was not impaired as of June 30, 2016 and December 31, 2015.

NOTE 5. LINES OF CREDIT

Outstanding lines of credit consists of the following:

($ in thousands)	**June 30, 2016**	**December 31, 2015**
Lines of Credit to related parties		
8% convertible lines of credit. Face value of advances under lines of credit $1,500 at June 30, 2016 and $0 at December 31, 2015. Discount on advances under lines of credit is $109 at June 30, 2016 and $0 at December 31, 2015. Maturity date is June 30, 2017.	$ 1,391	$ —
Total lines of credit to related parties	1,391	—
Less current portion	(1,391)	—
Long-term lines of credit to related parties	$ —	$ —

In March 2013, the Company entered into the Goldman LOC with available borrowings of up to $2.5 million. In March 2014, borrowings under the Goldman LOC were increased to an aggregate total of $3.5 million (the "*Amendment*"). Pursuant to the terms and conditions of the Amendment, Goldman had the right to convert up to $2.5 million of the outstanding balance of the Goldman LOC into shares of the Company's Common Stock for $0.95 per share. Any remaining outstanding balance was convertible into shares of the Company's Common Stock for $2.25 per share.

As consideration for the initial Goldman LOC, the Company issued a warrant to Goldman, exercisable for 1,052,632 shares of the Company's Common Stock (the "*LOC Warrant*"). The LOC Warrant had a term of two years from the date of issuance and an exercise price of $0.95 per share. As consideration for entering into the Amendment, the Company issued a second warrant to Goldman, exercisable for 177,778 shares of the Company's Common Stock (the "*Amendment Warrant*"). The Amendment Warrant expired on March 27, 2015 and had an exercise price of $2.25 per share.

The Company estimated the fair value of the LOC Warrant using the Black-Scholes option pricing model using the following assumptions: term of two years, a risk free interest rate of 2.58%, a dividend yield of 0%, and volatility of 79%. The Company recorded the fair value of the LOC Warrant as a deferred financing fee of approximately $580,000 to be amortized over the life of the Goldman LOC. The Company estimated the fair value of the Amendment Warrant using the Black-Scholes option pricing model using the following assumptions: term on one year, a risk free interest rate of 2.58%, a dividend yield of 0% and volatility of 74%. The Company recorded the fair value of the Amendment Warrant as an additional deferred financing fee of approximately $127,000 to be amortized over the life of the Goldman LOC.

During the six months ended June 30, 2016 and 2015, the Company recorded an aggregate of approximately $24,000 and $41,000, respectively in deferred financing fee amortization expense which is recorded as a component of interest expense in the Company's condensed consolidated statements of operations.

In April 2014, the Company and Goldman entered into a further amendment to the Goldman LOC to decrease the available borrowings to $3.0 million (the "*Second Amendment*"). Contemporaneous with the execution of the Second Amendment, the Company entered into a new unsecured line of credit with available borrowings of up to $500,000 (the "*Crocker LOC*") with Crocker, which amount was convertible into shares of the Company's Common Stock for $2.25 per share. As a result of these amendments, total available borrowings under aggregate lines of credit available to the Company remained unchanged at a total of $3.5 million. In connection with the Second Amendment, Goldman assigned and transferred to Crocker one-half of the Amendment Warrant.

In December 2014, the Company and Goldman entered into a further amendment to the Goldman LOC to increase the available borrowing to $5.0 million and extended the maturity date of the Goldman LOC to March 27, 2017 (the "*Third Amendment*"). Also, as a result of the Third Amendment, Goldman had the right to convert up to $2.5 million of the Outstanding Balance into shares of the Company's Common Stock for $0.95 per share, the next $500,000 Outstanding Balance into shares of Common Stock for $2.25 per share and any remaining Outstanding Balance thereafter into shares of Common Stock for $2.30 per share. The Third Amendment also modified the definition of a "*Qualified Financing*" to mean a debt or equity financing resulting in gross proceeds to the Company of at least $5.0 million.

In February 2015, as a result of the Series E Financing discussed under Note 6, "*Equity*", below, the Company issued 1,978 shares of Series E Convertible Redeemable Preferred Stock ("*Series E Preferred*") to Goldman to satisfy $1.95 million in principal borrowings under the Goldman LOC plus approximately $28,000 in accrued interest. As a result of the Series E Financing, the Company's borrowing capacity under the Goldman LOC was reduced to $3.05 million with the maturity date unchanged and the Crocker LOC was terminated in accordance with its terms.

On March 9, 2016, the Company and Goldman entered into the Fourth Amendment, that (i) provides the Company with the ability to borrow up to $5.0 million under the terms of the Goldman LOC; (ii) permits Goldman to convert the Outstanding Balance into shares of the Company's Common Stock for $1.25 per share; and (iii) extends the maturity date of the Goldman LOC to June 30, 2017.

In addition, on March 9, 2016, the Company and Crocker entered into the New Crocker LOC in the principal amount of $500,000. The New Crocker LOC shall accrue interest at a rate of 8% per annum, and matures on the earlier to occur of June 30, 2017 or such date that the Company consummates a debt and/or equity financing resulting in net proceeds to the Company of at least $3.5 million. All outstanding amounts due under the terms of the New Crocker LOC shall be convertible into the Company's Common Stock at $1.25 per share.

As of June 30, 2016, $1,500,000 was outstanding under the terms of the Lines of Credit. Subsequent to June 30, 2016, we borrowed an additional $500,000 under the Lines of Credit. As a result, approximately $3,500,000 remains available under the Lines of Credit for additional borrowings.

The Company evaluated the Lines of Credit and determined that the instruments contain a contingent beneficial conversion feature, i.e. an embedded conversion right that enables the holder to obtain the underlying Common Stock at a price below market value. The beneficial conversion feature is contingent as the terms of the conversion do not permit the Company to compute the number of shares that the holder would receive if the contingent event occurs (i.e. future borrowings under the Line of Credit). The Company has considered the accounting for this contingent beneficial conversion feature using the guidance in ASC 470, Debt. The guidance in ASC 470 states that a contingent beneficial conversion feature in an instrument shall not be recognized in earnings until the contingency is resolved. The beneficial conversion features of future borrowings under the Line of Credit will be measured using the intrinsic value calculated at the date the contingency is resolved using the conversion price and trading value of the Company's Common Stock at the date the Lines of Credit were issued (commitment date). Pursuant to borrowings made during the 2015 year, the Company recognized approximately $146,000 in beneficial conversion feature as debt discount. As a result of the retirement of all amounts outstanding under the Lines of Credit in 2015, the Company recognized all remaining unamortized debt discount of approximately $385,000 as a component of interest expense during the three months ended March 31, 2015. As there was $1,500,000 in borrowings under the Lines of Credit during the six months ended June 30, 2016, the Company recorded approximately $121,000 in debt discount attributable to the beneficial conversion feature during the six months ended June 30, 2016. During the three and six months ended June 30, 2016, the Company accreted approximately $12,000 of the note discount as a component of interest expense.

NOTE 6. EQUITY

The Company's Certificate of Incorporation, as amended, authorized 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.

Series B Convertible Redeemable Preferred Stock

The Company had 239,400 shares of Series B Convertible Redeemable Preferred ("*Series B Preferred*") redeemable at the option of the Company, outstanding as of June 30, 2016 and December 31, 2015. At June 30, 2016 and December 31, 2015, the Company had cumulative undeclared dividends of approximately $8,000. There were no conversions of Series B Preferred into Common Stock during the six months ended June 30, 2016 or 2015.

Series E Convertible Redeemable Preferred Stock

On January 29, 2015, the Company filed the Certificate of Designations, Preferences, and Rights of the Series E Convertible Redeemable Preferred Stock ("*Series E Preferred*") with the Delaware Secretary of State, designating 12,000 shares of the Company's preferred stock, par value $0.01 per share, as Series E Preferred. Shares of Series E Preferred accrue dividends at a rate of 8% per annum if the Company chooses to pay accrued dividends in cash, and 10% per annum if the Company chooses to pay accrued dividends in shares of Common Stock. Each share of Series E Preferred has a liquidation preference of $1,000 per share and is convertible, at the option of the holder, into that number of shares of the Company's Common Stock equal to the Liquidation Preference, divided by $1.90. Each holder of the Series E Preferred is entitled to vote on all matters, together with the holders of Common Stock, on an as converted basis.

Any time after the six-month period following the issuance date, the Company may redeem all or a portion of the Series E Preferred outstanding upon thirty (30) calendar days prior written notice in cash at a price per share of Series E Preferred equal to 110% of the Liquidation Preference Amount plus all accrued and unpaid dividends. Also, simultaneous with the occurrence of a Change of Control transaction, the Company, at its option, shall have the right to redeem all or a portion of the outstanding Series E Preferred in cash at a price per share of Series E Preferred equal to 110% of the Liquidation Preference Amount plus all accrued and unpaid dividends.

In February 2015 the Company consummated a registered direct offering conducted without an underwriter or placement agent. In connection therewith, the Company issued 12,000 shares of Series E Preferred to certain investors at a price of $1,000 per share, with each share convertible into 526.32 shares of the Company's Common Stock at $1.90 per share (the "*Series E Financing*").

The Company had 12,000 shares of Series E Preferred outstanding as of June 30, 2016 and December 31, 2015. At June 30, 2016 and December 31, 2015, the Company had cumulative undeclared dividends of $0 and $240,000, respectively. There were no conversions of Series E Preferred into Common Stock during the six months ended June 30, 2016. The Company issued the holders of Series E Preferred 250,743 shares of Common Stock on June 30, 2016 as payment of dividends due on this date. For the six month period ended June 30, 2016, the Company has issued the holders of Series E Preferred 475,660 shares of common Stock as payment of dividends due.

Common Stock

The following table summarizes Common Stock activity for the six months ended June 30, 2016:

	Common Stock
Shares outstanding at December 31, 2015	94,070,895
Shares issued pursuant to payment of stock dividend on Series E Preferred	475,660
Shares outstanding at June 30, 2016	94,546,555

During the six months ended June 30, 2016, the Company issued 475,660 shares of Common Stock in payment of the accumulated Series E Preferred dividends due and payable as of June 30, 2016.

Warrants

The following table summarizes warrant activity for the following periods:

	Warrants	Weighted-Average Exercise Price
Balance at December 31, 2015	450,000	$ 0.67
Granted	—	—
Expired / Canceled	—	—
Exercised	—	—
Balance at June 30, 2016	450,000	$ 0.67

As of June 30, 2016, warrants to purchase 450,000 shares of Common Stock at prices ranging from $0.50 to $1.10 were outstanding. All warrants are exercisable as of June 30, 2016, and expire at various dates through December 2017, with the exception of an aggregate of 150,000 warrants, which become exercisable only upon the attainment of specified events. The intrinsic value of warrants outstanding at June 30, 2016 was approximately $231,000.

Stock-Based Compensation

As of June 30, 2016, the Company had one active stock-based compensation plan for employees and nonemployee directors, which authorizes the granting of various equity-based incentives including stock options and restricted stock. On July 1, 2014, the Company began soliciting written consents from its shareholders to approve an amendment to the Company's 1999 Stock Option Plan to increase the number of shares authorized for issuance thereunder from approximately 4.0 million to approximately 7.0 million (the "*Plan Amendment*"). As of July 21, 2014, the Company had received written consents approving the Plan Amendment from over 50% of the Company's stockholders. As such, the Plan Amendment was approved.

The Company estimates the fair value of its stock options using a Black-Scholes option-valuation 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 is reported in general and administrative, sales and marketing, engineering and customer service expense 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 $233,000 and $475,000 for the three and six months ended June 30, 2016, respectively. Stock-based compensation expense related to equity options was approximately $141,000 and $269,000 for the three and six months ended June 30, 2015, respectively.

ASC No. 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-valuation 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-valuation 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 six months ended June 30, 2016 and 2015 ranged from 65% to 121%. 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 six months ended June 30, 2016 and 2015 was 5.17 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 six months ended June 30, 2016 and 2015 was 2.6%. Dividend yield is zero, as the Company does not expect to declare any dividends on the Company's Common Stock 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, 4.1% for members of the Board of Directors and 6.0% for all other employees. The Company reviews the expected forfeiture rate annually to determine if that percent is still reasonable based on historical experience.

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

	Options	Weighted-Average Exercise Price
Balance at December 31, 2015	5,376,969	$ 1.17
Granted	236,000	1.24
Expired/Cancelled	(30,833)	1.33
Exercised	—	-
Balance at June 30, 2016	5,582,136	1.18

The intrinsic value of options exercisable at June 30, 2016 was approximately $1,201,000. The aggregate intrinsic value for all options outstanding as of June 30, 2016 was approximately $1,230,000. The weighted-average grant-date per share fair value of options granted during the six months ended June 30, 2016 was $0.78. At June 30, 2016, the total remaining unrecognized compensation cost related to unvested stock options amounted to approximately $1,556,000 which will be recognized over a weighted-average period of 2.1 years.

In September 2015, the Company issued an aggregate of 144,000 options to purchase shares of the Company's stock to certain members of the Company's Board of Directors in return for their service from January 1, 2016 through December 31, 2016. Such options will vest at the rate of 12,000 options per month on the last day of each month during the 2016 year. The options have an exercise price of $1.73 per share and a term of 10 years. Pursuant to this issuance, the Company recorded compensation expense of approximately $44,000 and $90,000 for the three and six months ended June 30, 2016, respectively, based on the grant-date fair value of the options determined using the Black-Scholes option-valuation model.

In May 2015, the Company issued an aggregate of 16,000 options to purchase shares of the Company's stock to a new member of the Company's Board of Directors in return for their service from May, 2016 through December 31, 2016. Such options will vest at the rate of 2,000 options per month on the last day of each month during the 2016 year. The options have an exercise price of $1.29 per share and a term of 10 years. Pursuant to this issuance, the Company recorded compensation expense of approximately $3,000 during the six months ended June 30, 2016 based on the grant-date fair value of the options determined using the Black-Scholes option-valuation model.

In December 2014, the Company issued 94,116 shares of its Common Stock to certain members of the Company's Board of Directors as compensation to be rendered through December 2015. Such shares are forfeitable should the Board members' services be terminated. Pursuant to this issuance, the Company recorded approximately $54,000 as compensation expense for the six months ended June 30, 2015.

Stock-based compensation related to equity options and restricted stock grants has been classified as follows in the accompanying condensed consolidated statements of operations (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Cost of revenue	$ 5	$ 3	$ 10	$ 5
General and administrative	172	130	346	253
Sales and marketing	54	32	109	62
Research and development	49	30	100	56
Total	$ 280	$ 195	$ 565	$ 376

NOTE 7. FAIR VALUE ACCOUNTING

The Company accounts for fair value measurements in accordance with ASC 820, *Fair Value Measurements and Disclosures*, which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements.

ASC 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 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 820, assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

	Fair Value at June 30, 2016			
($ in thousands)	**Total**	**Level 1**	**Level 2**	**Level 3**
Assets:				
Pension assets	$ 1,590	1,590	—	—
Totals	$ 1,590	1,590	—	—

	Fair Value at December 31, 2015			
($ in thousands)	**Total**	**Level 1**	**Level 2**	**Level 3**
Assets:				
Pension assets	$ 1,557	$ 1,557	$ —	$ —
Totals	$ 1,557	$ 1,557	$ —	$ —

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.

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 8. RELATED PARTY TRANSACTIONS

The Company has certain Lines of Credit extended by certain members of the Company's Board of Directors. For a more detailed discussion of the Company's Lines of Credit, see Note 5 - Lines of Credit. During the quarter ended June 30, 2016, the Company borrowed $1,250,000 under the terms of the Goldman LOC and $250,000 under the terms of the New Crocker LOC. Subsequent to June 30, 2016, we borrowed an additional $250,000 under the Goldman LOC and $250,000 under the New Crocker LOC.

Each of Messrs. Goldman and Crocker are members of the Board of Directors of the Company.

NOTE 9. CONTINGENT LIABILITIES

Employment Agreements

The Company has employment agreements with its Chief Executive Officer, Senior Vice President of Administration and Chief Financial Officer and Chief Technical 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.

Under the terms of the agreement, the Chief Executive Officer will be entitled to the following severance benefits if we terminate his employment without cause or in the event of an involuntary termination: (i) a lump sum cash payment equal to twenty-four months base salary; (ii) continuation of fringe benefits and medical insurance for a period of three years; and (iii) immediate vesting of 50% of outstanding stock options and restricted stock awards. In the event that the Chief Executive Officer's employment is terminated within nine months prior to or thirteen months following a change of control, the Chief Executive Officer is entitled to the severance benefits described above, except that 100% of the Chief Executive Officer's outstanding stock options and restricted stock awards will immediately vest.

Under the terms of the employment agreements with our Senior Vice President of Administration and Chief Financial Officer and Chief Technical Officer, these executives will be entitled to the following severance benefits if we terminate their employment without cause or in the event of an involuntary termination: (i) a lump sum cash payment equal to six months of base salary; (ii) continuation of their medical and health benefits for a period of six months; (iii) immediate vesting of 50% of their outstanding stock options and restricted stock awards. In the event that their employment is terminated within nine months prior to or thirteen months following a change of control (defined below), they are entitled to the severance benefits described above, except that 100% of their outstanding stock options and restricted stock awards will immediately vest.

Leases

Our corporate headquarters are located in San Diego, California where we occupy 9,927 square feet of office space. This facility is leased through October 2017 at a cost of approximately $18,000 per month. In addition to our corporate headquarters, we also occupied the following spaces at June 30, 2016:

- 1,508 square feet in Ottawa, Province of Ontario, Canada, at a cost of approximately $3,000 per month until the expiration of the lease on March 31, 2021. This lease was renewed in April 2016 for a five-year period ending on March 31, 2021. Renewal terms were substantially unchanged from the existing lease;

- 8,045 square feet in Portland, Oregon, at a cost of approximately $16,000 per month until the expiration of the lease on October 31, 2018; and

- 425 square feet of office space in Mexico City, Mexico, at a cost of approximately $3,000 per month until terminated by either party.

At June 30, 2016, future minimum lease payments are as follows:

($ in thousands)	
2016 (6 months)	$ 229
2017	$ 421
2018	$ 202
2019	$ 35
2020 and thereafter	$ 44
	$ 931

Rental expense incurred under operating leases for the six months ended June 30, 2016 and 2015 was approximately $242,000 and $227,000, respectively.

NOTE 10. SUBSEQUENT EVENTS

Subsequent to June 30, 2016, we borrowed an additional $250,000 under the terms of the Goldman LOC and $250,000 under the New Crocker LOC. As a result, the total principal amount due and payable under the Lines of Credit are $2,000,000, and approximately $3,500,000 remains available under the Lines of Credit for additional borrowings.

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

Forward-Looking Statements

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 under "Risk Factors" in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2015, 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

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, including the Company's "flagship" product – the patented IWS Biometric Engine®. Our products are used to manage and issue secure credentials including national IDs, passports, driver's licenses and access control credentials. Our products also provide law enforcement with integrated mug shot, LiveScan fingerprint and investigative capabilities. We also provide comprehensive authentication security software using biometrics to secure physical and logistical access to facilities, computer networks and Internet sites. Biometric technology is now an integral part of all markets we address, and all of our products are integrated into the IWS Biometric Engine.

Recent Developments

On March 9, 2016, the Company and Neal I. Goldman, a director of the Company ("*Goldman*"), entered into the fourth amendment (the "*Fourth Amendment*") to the convertible promissory note and line of credit previously issued by the Company to Goldman on March 27, 2013 (the "*Goldman LOC*"). The Fourth Amendment (i) provides the Company with the ability to borrow up to $5.0 million under the terms of the Goldman LOC; (ii) permits Goldman to convert the outstanding principal, plus any accrued but unpaid interest due under the Goldman LOC (the "*Outstanding Balance*"), into shares of the Company's common stock, par value $0.001 per share ("*Common Stock*"), for $1.25 per share; and (iii) extends the maturity date of the Goldman LOC to June 30, 2017.

In addition, on March 9, 2016, the Company and Charles Crocker, also a director of the Company ("*Crocker*"), entered into a new line of credit and promissory note (the "*New Crocker LOC*"), in the principal amount of $500,000. The New Crocker LOC shall accrue interest at a rate of 8% per annum, and matures on the earlier to occur of June 30, 2017 or such date that the Company consummates a debt and/or equity financing resulting in net proceeds to the Company of at least $3.5 million. All outstanding amounts due under the terms of the New Crocker LOC shall be convertible into the Company's Common Stock at $1.25 per share.

As of June 30, 2016, $1,250,000 was outstanding under the terms of the Goldman LOC and $250,000 was outstanding under the terms of the New Crocker LOC (together, the "*Lines of Credit*"). Subsequent to June 30, 2016, we borrowed an additional $500,000 under the Lines of Credit. As a result, approximately $3,500,000 remain available under the Lines of Credit for additional borrowings.

Critical Accounting Policies and Estimates

The discussion and analysis of our condensed consolidated financial condition and results of operations are based on our condensed consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America ("*GAAP*"). The preparation of these condensed consolidated financial statements in accordance with 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 condensed consolidated financial statements and the reported amounts of revenue and expense 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, inventory carrying values, 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, revenue and cost of revenue recognized under the percentage of completion method and assumptions used in the application of fair value methodologies to calculate the fair value of pension assets and obligations.

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 June 30, 2016 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, 2015.

Results of Operations

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

Comparison of the Three Months Ended June 30, 2016 to the Three Months Ended June 30, 2015

Product Revenue

Net Product Revenue (dollars in thousands)	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	$ Change	% Change
Software and royalties	$ 284	$ 671	$ (387)	(58)%
Percentage of total net product revenue	80%	66%		
Hardware and consumables	$ 23	$ 20	$ 3	15%
Percentage of total net product revenue	6%	2%		
Services	$ 49	$ 331	$ (282)	(85)%
Percentage of total net product revenue	14%	32%		
Total net product revenue	$ 356	$ 1,022	$ (666)	(65)%

Software and royalty revenue decreased 58% or approximately $387,000 during the three months ended June 30, 2016 as compared to the corresponding period in 2015. This decrease is attributable to lower identification project related revenue of approximately $361,000, lower sales of boxed identity management software sold through our distribution channel of approximately $18,000, lower sales of law enforcement project related revenue of approximately $12,000, offset by an increase in royalty revenue of approximately $4,000.

Revenue from the sale of hardware and consumables increased approximately $3,000 during the three months ended June 30, 2016 as compared to the corresponding period in 2015. This increase resulted from higher sales of hardware and consumables in project solutions.

Services revenue is comprised primarily of software integration services, system installation services and customer training. Such revenue decreased approximately $282,000 during the three months ended June 30, 2016 as compared to the corresponding period in 2015, due primarily to the completion of the service element in certain identity management project solutions in the 2015 period.

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 an increase in government procurement and implementations with respect to identity management initiatives; however, we cannot predict the timing of such initiatives. During the quarter ended June 30, 2016, we continued to accelerate our efforts to move the Biometric Engine into cloud and mobile markets and expanding our end-user market into non-government sectors including commercial, consumer and healthcare applications. We anticipate that we will see positive developments from these efforts in the second-half of 2016, which should help us to begin to smooth out our period-to-period fluctuations in revenue and enable us to provide better visibility into the timing of future revenue.

Maintenance Revenue

Maintenance Revenue (dollars in thousands)	Three Months Ended June 30, 2016	2015	$ Change	% Change
Total maintenance revenue	$ 640	$ 673	$ (33)	(5)%

Maintenance revenue was approximately $640,000 for the three months ended June 30, 2016, as compared to approximately $673,000 for the corresponding period in 2015. Identity management maintenance revenue generated from identification software solutions was approximately $294,000 for the three months ended June 30, 2016 as compared to approximately $303,000 during the comparable period in 2015. Law enforcement maintenance revenue was approximately $346,000 for the three months ended June 30, 2016 as compared to approximately $370,000 during the comparable period in 2015. The decrease of $9,000 in identification software solutions for the three months ended June 30, 2016 as compared to the corresponding period of 2015 reflects the 2015 period containing a one-time recognition of approximately $49,000 based on certain revenue recognition criteria. The decrease of approximately $24,000 related to law enforcement solutions results from 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 June 30, 2016	2015	$ Change	% Change
Software and royalties	$ 26	$ 27	$ (1)	(4)%
Percentage of software and royalty product revenue	9%	4%		
Hardware and consumables	$ 22	$ 15	$ 7	47%
Percentage of hardware and consumables product revenue	96%	75%		
Services	$ 8	$ 547	$ (539)	(99)%
Percentage of services product revenue	16%	165%		
Total product cost of revenue	$ 56	$ 589	$ (533)	(90)%
Percentage of total product revenue	16%	58%		

The cost of software and royalty product revenue decreased approximately $1,000 for the three months ended June 30, 2016 and 2015 despite lower software and royalty product revenue during the three months ended June 30, 2015 of approximately $387,000 due to the 2015 period containing significant levels of software licenses with no third-party software content resulting in uncharacteristically low cost of software and royalty product revenue for this component. In addition to changes in costs of software and royalty product revenue caused by revenue level fluctuations, costs of products can vary as a percentage of product revenue from period to period depending upon level of software customization and third party software license content included in product sales during a given period.

The increase in the cost of product revenue for our hardware and consumable sales of approximately $7,000 for the three months ended June 30, 2016 as compared to the corresponding period in 2015 reflects higher hardware and consumables product revenue.

The cost of services revenue decreased approximately $539,000 during the three months ended June 30, 2016 as compared to the corresponding period in 2015 due to lower services revenue of approximately $282,000 in the 2016 period. This decrease reflects higher professional cost of service revenue for the three months ended June 30, 2015 due to more costly engineering resources utilized in the generation of non-recurring revenue from one customer in the 2015 period as compared to the corresponding period in 2016. In addition to changes in costs of services product revenue caused by revenue level fluctuations, costs of services can vary as a percentage of service revenue from period to period depending upon both the level and complexity of professional service resources utilized in the completion of the service element.

Cost of Maintenance Revenue

	Three Months Ended June 30,			
Maintenance cost of revenue (dollars in thousands)	**2016**	**2015**	**$ Change**	**% Change**
Total maintenance cost of revenue	$ 219	$ 209	$ 10	5%
Percentage of total maintenance revenue	34%	31%		

Cost of maintenance revenue increased 5% or approximately $10,000 during the three months ended June 30, 2016 as compared to the corresponding period in 2015. This increase results from higher departmental expense for the three months ended June 30, 2016 as compared to the corresponding period in 2015.

Product Gross Profit

	Three Months Ended June 30,			
Product gross profit (dollars in thousands)	**2016**	**2015**	**$ Change**	**% Change**
Software and royalties	$ 258	$ 644	$ (386)	(60) %
Percentage of software and royalty product revenue	91%	96%		
Hardware and consumables	$ 1	$ 5	$ (4)	(80)%
Percentage of hardware and consumables product revenue	4%	25%		
Services	$ 41	$ (216)	$ 257	119%
Percentage of services product revenue	84%	(65)%		
Total product gross profit	$ 300	$ 433	$ (133)	(31) %
Percentage of total product revenue	84%	42%		

Software and royalty gross profit decreased 60% or approximately $386,000 for the three months ended June 30, 2016 from the corresponding period in 2015 due primarily to lower software and royalty revenue of approximately $387,000. In addition to changes in costs of software and royalty product revenue caused by revenue level fluctuations, costs of products can vary as a percentage of product revenue from period to period depending upon level of software customization and third party software license content included in product sales during a given period.

Services gross profit increased approximately $257,000 for the three months ended June 30, 2016 as compared to the corresponding period in 2015 due to lower service revenue of approximately $282,000 combined with lower cost of service revenue of approximately $539,000 for the three months ended June 30, 2016 as compared to the corresponding period in 2015. The decrease in service revenue and uncharacteristically high cost of service revenue in the 2015 period reflect the impact of non-recurring revenue received from one customer combined with significant costs incurred from implementation challenges. The Company's contract with this one customer in the 2015 period also included software product revenue of approximately $440,000, offset by minimal costs.

Maintenance Gross Profit

Maintenance gross profit (dollars in thousands)	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	$ Change	% Change
Total maintenance gross profit	$ 421	$ 464	$ (43)	(9)%
Percentage of total maintenance revenue	66%	69%		

Gross profit related to maintenance revenue decreased 9% or approximately $43,000 for the three months ended June 30, 2016 as compared to the same period ended June 30, 2015. This decrease is due to lower maintenance revenue of approximately $33,000 combined with higher cost of maintenance revenue of approximately $10,000. This inverse relationship is caused by the three month period ending March 31, 2015 containing approximately $49,000 of maintenance revenue resulting from a one-time recognition combined with the 2016 period containing approximately $10,000 in higher departmental costs.

Operating Expense

Operating expense (dollars in thousands)	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	$ Change	% Change
General and administrative	$ 899	$ 788	$ 111	14%
Percentage of total net revenue	90%	47%		
Sales and marketing	$ 743	$ 717	$ 26	4%
Percentage of total net revenue	75%	42%		
Research and development	$ 1,318	$ 1,114	$ 204	18%
Percentage of total net revenue	132%	66%		
Depreciation and amortization	$ 35	$ 41	$ (6)	(15)%
Percentage of total net revenue	4%	2%		

General and Administrative Expense

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 dollar increase of approximately $111,000 during the three months ended June 30, 2016 as compared to the corresponding period in 2015 is comprised of the following major components:

- Increase in personnel related expense of approximately $81,000 due to increased salaries from headcount increases of approximately $84,000, higher 401(k) plan employer contributions of approximately $6,000 offset by lower pension expense of our foreign sales office of approximately $9,000.

- Increase in stock-based compensation expense of approximately $50,000.

- Decreases in professional services of approximately $14,000 which includes Board of Director fees of approximately $8,000, lower contractor fees of approximately $28,000, lower legal and patent-related expense of approximately $5,000 offset by higher auditing fees of approximately $14,000, higher investor relations fees of approximately $9,000 and higher corporate expense of approximately $4,000.

- Decrease in travel, insurances, licenses, dues, rent, and office related costs of approximately $7,000.

We continue to focus our efforts on achieving additional future operating efficiencies by reviewing and improving upon existing business processes and evaluating our cost structure. We believe these efforts will allow us to continue to gradually decrease our level of general and administrative expense expressed as a percentage of total revenue.

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, and business development functions. The dollar increase of approximately $26,000 during the three months ended June 30, 2016 as compared to the corresponding period in 2015 is primarily comprised of the following major components:

- Decrease in personnel related expense of approximately $33,000 due to the three month period ending June 30, 2015 containing approximately $100,000 in severance payments.

- Increase in contractor services of approximately $66,000 resulting from increased utilization of certain sales consultants.

- Increase in contract services, travel and trade show expense and office related expense of approximately $2,000.

- Increase in stock-based compensation expense of approximately $21,000.

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 approximately $204,000 for the three months ended June 30, 2016 as compared to the corresponding period in 2015 due primarily to the following major components:

- Increase in personnel related expense of approximately $213,000 due to headcount increases needed for the accelerated development of the Company’s mobile identity management solutions.

- Decrease in contractor fees and contract services of approximately $9,000.

- Increase in stock-based compensation of approximately $19,000.

- Decrease in office related expense and travel of approximately $19,000.

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 development as well as continue to enhance existing products.

Depreciation and Amortization

During the three months ended June 30, 2016 and 2015, depreciation and amortization expense was approximately $35,000 and $41,000, respectively. The relatively small amount of depreciation and amortization is a reflection of the relatively small property and equipment carrying value.

Interest Expense, Net

For the three months ended June 30, 2016, we recognized interest expense of approximately $36,000 and interest income of approximately $0. For the three months ended June 30, 2015, we recognized interest expense of approximately $0 and interest income of approximately $2,000. Interest expense for the three months ended June 30, 2016 is comprised of approximately $12,000 of amortization expense of deferred financing fees related to the Goldman LOC, interest expense of approximately $12,000 of coupon interest on debt outstanding under the Lines of Credit, and approximately $12,000 related to the recognition of beneficial conversion feature related to the Lines of Credit.

Other Income

For the three months ended June 30, 2016, we recognized other income of approximately $200,000. For the three months ended June 30, 2015, we recognized other income of approximately $0. Other income for the three months ended June 30, 2016 is comprised of approximately $200,000 from the write off of certain accrued expense due to the expiration of the legal statute of limitations on such liabilities.

Comparison of the Six Months Ended June 30, 2016 to the Six Months Ended June 30, 2015

Product Revenue

Net Product Revenue (dollars in thousands)	**Six Months Ended June 30, 2016**	**2015**	**$ Change**	**% Change**
Software and royalties	$ 502	$ 974	$ (472)	(48)%
Percentage of total net product revenue	66%	70%		
Hardware and consumables	$ 54	$ 23	$ 31	135%
Percentage of total net product revenue	7%	1%		
Services	$ 203	$ 403	$ (200)	(50)%
Percentage of total net product revenue	27%	29%		
Total net product revenue	$ 759	$ 1,400	$ (641)	(46)%

Software and royalty revenue decreased 48% or approximately $472,000 during the six months ended June 30, 2016 as compared to the corresponding period in 2015. This decrease is attributable to lower identification project related revenue of approximately $433,000, lower sales of boxed identity management software sold through our distribution channel of approximately $40,000, lower sales of law enforcement project related revenue of approximately $3,000 offset by higher royalty revenue of approximately $4,000.

Revenue from the sale of hardware and consumables increased approximately $31,000 during the six months ended June 30, 2016 as compared to the corresponding period in 2015. This increase resulted from higher sales of hardware and consumables in project solutions.

Services revenue is comprised primarily of software integration services, system installation services and customer training. Such revenue decreased approximately $200,000 during the six months ended June 30, 2016 as compared to the corresponding period in 2015, due primarily to the completion of the service element in certain identity management project solutions in the 2015 period.

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 an increase in government procurement and implementations with respect to identity management initiatives; however, we cannot predict the timing of such initiatives. During the quarter ended June 30, 2016, we continued to accelerate our efforts to move the Biometric Engine into cloud and mobile markets and expanding our end-user market into non-government sectors including commercial, consumer and healthcare applications. We anticipate that we will see positive developments from these efforts in the second-half of 2016, which should help us to begin to smooth out our period-to-period fluctuations in revenue and enable us to provide better visibility into the timing of future revenue.

Maintenance Revenue

Maintenance Revenue (dollars in thousands)	Six Months Ended June 30, 2016	2015	$ Change	% Change
Total maintenance revenue	$ 1,280	$ 1,287	$ (7)	(1)%

Maintenance revenue was approximately $1,280,000 for the six months ended June 30, 2016, as compared to approximately $1,287,000 for the corresponding period in 2015. Identity management maintenance revenue generated from identification software solutions was approximately $583,000 for the six months ended June 30, 2016 as compared to approximately $545,000 during the comparable period in 2015. Law enforcement maintenance revenue was approximately $697,000 for the six months ended June 30, 2016 as compared to approximately $742,000 during the comparable period in 2015. The increase of $38,000 in identification software solutions reflects the completion of certain projects and an increase to our installed base. The decrease of approximately $45,000 related to law enforcement solutions results from 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)	Six Months Ended June 30, 2016	2015	$ Change	% Change
Software and royalties	$ 51	$ 48	$ 3	6%
Percentage of software and royalty product revenue	10%	5%		
Hardware and consumables	$ 29	$ 15	$ 14	93%
Percentage of hardware and consumables product revenue	54%	65%		
Services	$ 50	$ 600	$ (550)	92%
Percentage of services product revenue	25%	149%		
Total product cost of revenue	$ 130	$ 663	$ (533)	80%
Percentage of total product revenue	17%	47%		

The cost of software and royalty product revenue increased approximately $3,000 for the six months ended June 30, 2016 and 2015 despite lower software and royalty product revenue during the six months ended June 30, 2015 of approximately $472,000 due to the 2015 period containing significant levels of software licenses with no third-party software content resulting in uncharacteristically low cost of software and royalty product revenue for this component. In addition to changes in costs of software and royalty product revenue caused by revenue level fluctuations, costs of products can vary as a percentage of product revenue from period to period depending upon level of software customization and third party software license content included in product sales during a given period.

The increase in the cost of product revenue for our hardware and consumable sales of approximately $14,000 for the six months ended June 30, 2016 as compared to the corresponding period in 2015 reflects higher hardware and consumables product revenue of approximately $31,000 for the six months ended June 30, 2016 as compared to the corresponding period in 2015.

The cost of services revenue decreased approximately $550,000 during the six months ended June 30, 2016 as compared to the corresponding period in 2015 due to lower services revenue of approximately $200,000 in the 2016 period. This decrease reflects higher professional cost of service revenue for the six months ended June 30, 2015 due more costly engineering resources utilized in the generation of non-recurring revenue from one customer in the 2015 period as compared to the corresponding period in 2016. In addition to changes in costs of services product revenue caused by revenue level fluctuations, costs of services can vary as a percentage of service revenue from period to period depending upon both the level and complexity of professional service resources utilized in the completion of the service element.

Cost of Maintenance Revenue

Maintenance cost of revenue (dollars in thousands)	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015	$ Change	% Change
Total maintenance cost of revenue	$ 424	$ 420	$ 4	1%
Percentage of total maintenance revenue	33%	33%		

Cost of maintenance revenue increased 1% or approximately $4,000 during the six months ended June 30, 2015 as compared to the corresponding period in 2014. This increase results from higher departmental expense for the six months ended June 30, 2016 as compared to the corresponding period in 2015.

Product Gross Profit

Product gross profit (dollars in thousands)	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015	$ Change	% Change
Software and royalties	$ 451	$ 926	$ (475)	(51) %
Percentage of software and royalty product revenue	90%	95%		
Hardware and consumables	$ 25	$ 8	$ 17	213%
Percentage of hardware and consumables product revenue	46%	35%		
Services	$ 153	$ (197)	$ 350	178%
Percentage of services product revenue	75%	(49) %		
Total product gross profit	$ 629	$ 737	$ (108)	(15) %
Percentage of total product revenue	83%	53%		

Software and royalty gross profit decreased 51% or approximately $475,000 for the six months ended June 30, 2016 from the corresponding period in 2015 due primarily to lower software and royalty revenue of approximately $472,000. In addition to changes in costs of software and royalty product revenue caused by revenue level fluctuations, costs of products can vary as a percentage of product revenue from period to period depending upon level of software customization and third party software license content included in product sales during a given period.

Services gross profit increased approximately $350,000 for the six months ended June 30, 2016 as compared to the corresponding period in 2015 due to lower service revenue of approximately $200,000 combined with lower cost of service revenue of approximately $550,000 for the six months ended June 30, 2016 as compared to the corresponding period in 2015. The decrease in service revenue and uncharacteristically high cost of service revenue in the 2015 period reflect the impact of non-recurring revenue received from one customer combined with significant costs incurred from implementation challenges. The Company's contract with this same customer in the 2015 period also included software product revenue of approximately $440,000, offset by minimal costs

Maintenance Gross Profit

Maintenance gross profit (dollars in thousands)	Six Months Ended June 30, 2016	2015	$ Change	% Change
Total maintenance gross profit	$ 856	$ 867	$ (11)	(1)%
Percentage of total maintenance revenue	67%	67%		

Gross profit related to maintenance revenue decreased 1% or approximately $11,000 for the six months ended June 30, 2016 as compared to the same period ended June 30, 2015. This decrease is due to lower maintenance revenue of approximately $7,000 combined with higher cost of maintenance revenue of approximately $4,000.

Operating Expense

Operating expense (dollars in thousands)	Six Months Ended June 30, 2016	2015	$ Change	% Change
General and administrative	$ 1,905	$ 1,704	$ 201	12%
Percentage of total net revenue	93%	63%		
Sales and marketing	$ 1,416	$ 1,368	$ 48	4%
Percentage of total net revenue	69%	51%		
Research and development	$ 2,631	$ 2,148	$ 483	23%
Percentage of total net revenue	129%	80%		
Depreciation and amortization	$ 70	$ 83	$ (13)	(16)%
Percentage of total net revenue	3%	3%		

General and Administrative Expense

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 dollar increase of approximately $201,000 during six months ended June 30, 2016 as compared to the corresponding period in 2015 is comprised of the following major components:

- Increase in personnel related expense of approximately $157,000 due to increased salaries from headcount increases of approximately $106,000, higher 401(k) plan employer contributions of approximately $20,000 and higher pension expense of our foreign sales office of approximately $31,000.

- Increase in stock-based compensation expense of approximately $111,000.

- Decreases in professional services of approximately $66,000 which includes decreases in Board of Director fees of approximately $17,000, lower contractor fees of approximately $40,000, lower corporate-related expense of approximately $8,000, lower legal and patent-related expense of approximately $37,000 offset by higher auditing fees of approximately $20,000 and higher investor relations fees of approximately $16,000.

- Decrease in travel, insurances, licenses, dues, rent, and office related costs of approximately $1,000.

We continue to focus our efforts on achieving additional future operating efficiencies by reviewing and improving upon existing business processes and evaluating our cost structure. We believe these efforts will allow us to continue to gradually decrease our level of general and administrative expense expressed as a percentage of total revenue.

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, and business development functions. The dollar increase of approximately $48,000 during the six months ended June 30, 2016 as compared to the corresponding period in 2015 is primarily comprised of the following major components:

- Increase in personnel related expense of approximately $31,000 due to headcount increases.
- Decrease in professional services of approximately $8,000 resulting from lower utilization of certain consultants.
- Decrease in contract services, travel and trade show expense and office related expense of approximately $22,000.
- Increase in stock-based compensation expense of approximately $47,000.

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 approximately $483,000 for the six months ended June 30, 2016 as compared to the corresponding period in 2015 due primarily to the following major components:

- Increase in personnel related expense of approximately $491,000 due to headcount increases.
- Decrease in contractor fees and contract services of approximately $31,000.
- Increase in stock-based compensation of approximately $43,000.
- Decrease in office related expense and travel of approximately $20,000.

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 development as well as continue to enhance existing products.

Depreciation and Amortization

During the six months ended June 30, 2016 and 2015, depreciation and amortization expense was approximately $70,000 and $83,000, respectively. The relatively small amount of depreciation and amortization is a reflection of the relatively small property and equipment carrying value.

Interest Expense, Net

For the six months ended June 30, 2016, we recognized interest expense of approximately $48,000 and interest income of approximately $2,000. For the six months ended June 30, 2015, we recognized interest expense of approximately $438,000 and interest income of approximately $3,000. Interest expense for the six months ended June 30, 2016 is comprised of approximately $24,000 of amortization expense of deferred financing fees related to the Lines of Credit, interest expense of approximately $12,000 of coupon interest on debt outstanding under the Lines of Credit, and approximately $12,000 related to the recognition of beneficial conversion feature related to the Lines of Credit. Interest expense for the six months ended June 30, 2015 is comprised of approximately $12,000 of coupon interest on debt outstanding under our Line of Credit, approximately $41,000 in deferred financing fee amortization related to our Line of Credit and approximately $385,000 related to the recognition of beneficial conversion feature related to our Line of Credit.

Other Income

For the six months ended June 30, 2016, we recognized other income of approximately $200,000. For the six months ended June 30, 2015, we recognized other income of approximately $46,000. Other income for the six months ended June 30, 2016 is comprised of approximately $200,000 related to the write-off of certain accrued liabilities due to the expiration of the legal statute of limitations on such liabilities.

LIQUIDITY AND CAPITAL RESOURCES

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, including our Lines of Credit. 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 Software-as-a-Service ("*SaaS*") capabilities for existing products as well as general working capital and capital expenditure requirements. We expect that, as our revenue grows, our sales and marketing and research and development expense will continue to grow, albeit at a slower rate and, as a result, we will need to generate significant net revenue to achieve and sustain income from operations.

At June 30, 2016, our principal sources of liquidity consisted of cash and cash equivalents of $327,000, accounts receivable, net of $274,000, and available borrowings under the Lines of Credit of $3,500,000. As of June 30, 2016, we had negative working capital of $2,176,000. We have a history of recurring losses, and as of June 30, 2016, we have incurred a cumulative net loss of approximately $150,939,000.

Lines of Credit

On March 9, 2016, the Company and Goldman entered into the Fourth Amendment, that (i) provides the Company with the ability to borrow up to $5.0 million under the terms of the Goldman LOC; (ii) permits Goldman to convert the Outstanding Balance into shares of the Company's Common Stock for $1.25 per share; and (iii) extends the maturity date of the Goldman LOC to June 30, 2017.

In addition, on March 9, 2016, the Company and Crocker entered into the New Crocker LOC, in the principal amount of $500,000. The New Crocker LOC shall accrue interest at a rate of 8% per annum, and matures on the earlier to occur of June 30, 2017 or such date that the Company consummates the Qualified Financing. All outstanding amounts due under the terms of the New Crocker LOC shall be convertible into the Company's Common Stock at $1.25 per share.

During the three months ended June 30, 2016, we incurred borrowings under our existing Lines of Credit of approximately $1,500,000, due and payable on June 30, 2017, and an additional $500,000 subsequent to June 30, 2016. We anticipate needing to increase our borrowings under the Lines of Credit to continue to fund our working capital needs, thereby increasing the aggregate indebtedness due and payable on or before June 30, 2017.

We currently do not anticipate generating sufficient revenue and profit to repay these borrowings in full when due. Therefore, unless the holders of the notes issued under the Lines of Credit convert any outstanding balance into shares of common stock, we will need to seek an extension of the maturity date of the Lines of Credit on or before June 30, 2017. If remaining available borrowings under our Lines of Credit are insufficient or we are unable to extend the maturity date of the Lines of Credit, we will be required to raise additional capital through debt and/or equity financing to continue operations. No assurances can be given that any such financing will be available to us on favorable terms, if at all. At this time, we do not have any commitments for alternative financing or for an extension of the maturity date of the Lines of Credit.

Going Concern

As reflected in the accompanying consolidated financial statements, the Company has continuing losses, negative working capital and negative cash flows from operations. Available borrowings under our existing Lines of Credit may be insufficient to provide for our working capital needs for the next twelve months. As a result, we may need to raise additional capital through debt and/or equity financing to execute our business plan. In addition, in the event we are unable to raise additional capital, we may be required to sell certain of the Company's assets or license the Company's technologies to others. These uncertainties raise substantial doubt about the Company's ability to continue as a going concern.

In view of the matters described in the preceding paragraph, recoverability of a major portion of the recorded asset amounts shown in the accompanying consolidated balance sheet is dependent upon continued operations of the Company, which, in turn, is dependent upon the Company's ability to continue to raise capital and generate positive cash flows from operations. However, the Company operates in markets that are emerging and highly competitive. There is no assurance that the Company will operate at a profit or generate positive cash flows in the future.

The consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts and classifications of liabilities that might be necessary should the Company be unable to continue as a going concern.

Operating Activities

We used net cash of $4,425,000 in operating activities for the six months ended June 30, 2016 as compared to net cash used of $4,136,000 during the comparable period in 2015. During the six months ended June 30, 2016, net cash used in operating activities consisted of net loss of $4,389,000 and a decrease in working capital and other assets and liabilities of $508,000. Those amounts were offset by $472,000 of non-cash costs including $565,000 in stock based compensation, $37,000 in debt issuance cost amortization and beneficial conversion feature amortization, $70,000 in depreciation and amortization, offset by $200,000 from the write off of accrued expense due to the expiration of the legal statute of limitations on such liabilities. During the six months ended June 30, 2016, we used cash of $26,000 to fund increases in current assets and used cash of $482,000 through reductions in current liabilities and deferred revenue, excluding debt.

We used net cash of $4,136,000 in operating activities for the six months ended June 30, 2015. During the six months ended June 30, 2015, net cash used in operating activities consisted of net loss of $4,096,000 and a decrease in working capital and other assets and liabilities of $1,005,000. Those amounts were offset by $965,000 of non-cash costs including $376,000 in stock based compensation, $426,000 in debt issuance cost and beneficial conversion feature amortization, $80,000 in warrant compensation expense and $83,000 in depreciation and amortization. During the six months ended June 30, 2015, we generated cash of $405,000 through decreases in current assets and used cash of $1,410,000 through reductions in current liabilities and deferred revenue, excluding debt.

Investing Activities

Net cash used in investing activities was $44,000 for the six months ended June 30, 2016 as compared to $43,000 used in the six months ended June 30, 2015. For the six months ended June 30, 2016, we used cash to fund capital expenditures of computer equipment, software and furniture and fixtures of approximately $44,000. This level of equipment purchases resulted primarily from the replacement of older equipment. For the six months ended June 30, 2015, we used cash to fund capital expenditures of computer equipment, software and furniture and fixtures of approximately $43,000.

Financing Activities

During the six months ended June 30, 2016, the Company received $1,500,000 in borrowings under the Lines of Credit. We used cash of $25,000 for the payment of dividends on our Series B Preferred. We generated cash of $10,363,000 from financing activities for the six months ended June 30, 2015. During the six months ended June 30, 2015, we generated cash of $10,022,000 from the Series E Financing offset by $67,000 in offering costs, $33,000 from the exercise of 38,039 Common Stock options and $750,000 from borrowings under the Line of Credit offset by the repayment of $350,000 under the Line of Credit. During the six months ended June 30, 2015, we also used cash of $25,000 for the payment of dividends on our Series B Preferred.

Debt

At June 30, 2016, the Company had $1,512,000 outstanding under the terms of the Lines of Credit, which amount included $12,000 in accrued but unpaid interest. Subsequent to June 30, 2016, we borrowed an additional $500,000 under the Lines of Credit. As a result, the total principal amount under the Lines of Credit totaled $2,000,000 at July 31, 2016.

Contractual Obligations

Total contractual obligations and commercial commitments as of June 30, 2016 are summarized in the following table (in thousands):

	Payment Due by Year				
	Total	Less than 1 Year	1-3 Years	3-5 Years	More than 5 Years
Operating lease obligations	1,039	337	658	44	—
Notes payable to related parties	1,512	—	1,512	—	—
Total	$ 2,551	337	2,170	44	—

Real Property Leases

Our corporate headquarters are located in San Diego, California where we occupy 9,927 square feet of office space. This facility is leased through October 2017 at a cost of approximately $18,000 per month. In addition to our corporate headquarters, we also occupied the following spaces at June 30, 2016:

- 1,508 square feet in Ottawa, Province of Ontario, Canada, at a cost of approximately $3,000 per month until the expiration of the lease on March 31, 2021. This lease was renewed in April 2016 for a five-year period ending on March 31, 2021. Renewal terms were substantially unchanged from the existing lease;

- 8,045 square feet in Portland, Oregon, at a cost of approximately $16,000 per month until the expiration of the lease on October 31, 2018; and

- 425 square feet of office space in Mexico City, Mexico, at a cost of approximately $3,000 per month, on a month-to-month basis until terminated by either party.

At June 30, 2016, future minimum lease payments are as follows:

($ in thousands)	
2016 (6 months)	$ 229
2017	$ 421
2018	$ 202
2019	$ 35
2020 and thereafter	$ 44
	$ 931

Off-Balance Sheet Arrangements

At June 30, 2016, we did not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance, special purpose or variable interest entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. In addition, we did not engage in trading activities involving non-exchange traded contracts. As a result, we are not exposed to any financing, liquidity, market or credit risk that could arise if we had engaged in such relationships. We do not have relationships and transactions with persons or entities that derive benefits from their non-independent relationship with us or our related parties except as disclosed elsewhere in this Quarterly Report.

Recently Issued Accounting Standards

Please refer to the section “Recently Issued Accounting Standards” in Note 2 of our Notes to the Condensed Consolidated Financial Statements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Each of our contracts requires 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 affected by factors such as changes in foreign currency exchange rates**.**

ITEM 4. CONTROLS AND PROCEDURES

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 June 30, 2016. 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.

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

ITEM 1. LEGAL PROCEEDINGS

None.

ITEM 1A. RISK FACTORS

We have identified the following risk factor in addition to 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, 2015:

Available borrowings under our Lines of Credit may be insufficient to provide for our working capital needs for the next twelve months. In the event such Lines of Credit are insufficient to provide for our working capital requirements, we will need to raise additional capital to continue as a going concern.

During the quarter ended June 30, 2016, we incurred borrowings under the Lines of Credit of approximately $1,500,000, due and payable on June 30, 2017, and an additional $500,000 subsequent to June 30, 2016. As a result, available borrowings under our Lines of Credit are $3,500,000. We anticipate needing to increase our borrowings under the Line of Credits to continue to fund our working capital needs, thereby increasing the aggregate amount of indebtedness due and payable on or before June 30, 2017.

We currently do not anticipate generating sufficient revenue and profit to repay these borrowings in full when due. Therefore, unless the holders of the notes issued under the Lines of Credit convert any outstanding balance into shares of common stock, we will need to seek an extension of the maturity date of the Lines of Credit on or before June 30, 2017. If we are unable to extend the maturity date of the Lines of Credit, we will be required to raise additional capital through debt and/or equity financing to continue as a going concern. No assurances can be given that any such financing will be available to us on favorable terms, if at all. At this time, we do not have any commitments for alternative financing or for an extension of the maturity date of the Lines of Credit. The inability to obtain debt or equity financing in a timely manner and in amounts sufficient to fund our operations, if necessary, would have an immediate and substantial adverse impact on our business, financial condition or results of operations.

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

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

(a)	EXHIBITS
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

SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: August 9, 2016	IMAGEWARE SYTEMS, INC
	By: /s/ S. James Miller S. James Miller Chief Executive Officer, Chairman and Director (Principal Executive Officer)
Date: August 9, 2016	By: /s/ Wayne Wetherell Wayne Wetherell Chief Financial Officer (Principal Financial and Accounting Officer)

Exhibit 31.1

Certification pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 and pursuant to Rule 13a-14(a) and Rule 15d-14 under the Securities Exchange Act of 1934

I, S. James Miller, Jr., Chief Executive Officer of the Company, 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 financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in 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 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 evaluations: 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 that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

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

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

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

Date: August 9, 2016

ImageWare Systems, Inc.

By: /s/ S. James Miller, Jr.
S. James Miller, Jr.
Chief Executive Officer
(Principal Executive Officer)

Exhibit 31.2

Certification pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 and pursuant to Rule 13a-14(a) and Rule 15d-14 under the Securities Exchange Act of 1934

I, Wayne Wetherell, Chief Financial Officer of the Company, 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 financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in 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 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 evaluations: 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 that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

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

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

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

Date: August 9, 2016

ImageWare Systems, Inc.

By: /s/ Wayne Wetherell
Wayne Wetherell
Chief Financial Officer (Principal Financial Officer)

Exhibit 32.1

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 June 30, 2016 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 June 30, 2016 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 9th day of August, 2016.

/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.