

Edgar Filing: VIEW SYSTEMS INC - Form 10QSB

VIEW SYSTEMS INC
Form 10QSB
August 14, 2006

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

FORM 10-QSB

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

For the quarterly period ended June 30, 2006

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

Commission File Number 0-30178

VIEW SYSTEMS, INC.

(Exact name of small business issuer as specified in its charter)

Nevada

59-2928366

(State of incorporation)

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

1550 Caton Center Drive, Suite E, Baltimore, Maryland 21227

(Address of principal executive offices)

(410) 242-8439

(Issuer's telephone number)

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

Yes No

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

Yes No

As of July 17, 2006, View Systems, Inc. had 90,702,422 shares of common stock
outstanding.

Transitional small business disclosure format: Yes No

TABLE OF CONTENTS

PART I: FINANCIAL INFORMATION

Item 1. Financial Statements.....2
Item 2. Management's Discussion and Analysis or Plan of Operation.....9

Edgar Filing: VIEW SYSTEMS INC - Form 10QSB

Item 3. Controls and Procedures.....15

PART II: OTHER INFORMATION

Item 4. Other Information.....16

Item 6. Exhibits.....16

Signatures.....17

PART I: FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

The financial information set forth below with respect to our statements of operations for the three and six month periods ended June 30, 2006 and 2005 is unaudited. This financial information, in the opinion of management, includes all adjustments consisting of normal recurring entries necessary for the fair presentation of such data. The results of operations for the six month period ended June 30, 2006 are not necessarily indicative of results to be expected for any subsequent period.

View Systems, Inc. and Subsidiaries
Consolidated Balance Sheets

ASSETS

	June 30, 2006	December 31, 2005
	-----	-----
Current Assets		
Cash	\$ 67,434	\$ 8,708
Accounts Receivable (Net of Allowance of \$9,369 and \$64,486 as of June 30, 2006 and December 31, 2005)	84,302	280,001
Inventory	156,843	72,012
	-----	-----
Total Current Assets	308,579	360,721
	-----	-----
Property & Equipment (Net)	28,542	18,043
	-----	-----
Other Assets		
Licenses	1,676,854	1,626,854
Due from Affiliates	116,875	95,575
Deposits	9,646	7,291

Edgar Filing: VIEW SYSTEMS INC - Form 10QSB

	-----	-----
Total Other Assets	1,803,375	1,729,720
	-----	-----
Total Assets	\$ 2,140,496	\$ 2,108,484
	=====	=====
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities		
Accounts Payable	\$ 483,361	\$ 343,430
Accrued Expenses	44,679	43,229
Accrued Interest	90,467	77,000
Accrued Royalties	37,500	75,000
Loans from Shareholder	64,000	64,000
Notes Payable	440,000	110,000
	-----	-----
Total Current Liabilities	1,160,007	712,659
	-----	-----
Stockholders' Equity		
Preferred Stock, Authorized 10,000,000 Shares, \$.01 Par Value, Issued and outstanding 7,171,725	71,717	71,717
Common Stock, Authorized 100,000,000 Shares, \$.001 Par Value, Issued and Outstanding 91,837,422	91,838	-
Issued and Outstanding 90,775,752	-	90,776
Additional Paid in Capital	19,413,609	19,293,804
Retained Earnings (Deficit)	(18,596,675)	(18,060,472)
	-----	-----
Total Stockholders' Equity	980,489	1,395,825
	-----	-----
Total Liabilities and Stockholders' Equity	\$ 2,140,496	\$ 2,108,484
	=====	=====

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

3

View Systems, Inc. and Subsidiaries
Consolidated Statements of Operations

	For the		For the	
	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
	-----	-----	-----	-----
Revenues, Net	\$ 222,403	\$ 195,914	\$ 624,978	\$ 481,556

Edgar Filing: VIEW SYSTEMS INC - Form 10QSB

Cost of Sales	111,457	125,180	318,739	229,508
Gross Profit (Loss)	110,946	70,734	306,239	252,048
Operating Expenses				
Business Development	73,700	17,617	113,377	32,646
General & Administrative	81,835	25,238	194,747	94,020
Professional Fees	52,137	31,341	103,432	69,856
Salaries & Benefits	211,665	148,812	416,871	234,365
Total Operating Expenses	419,337	223,008	828,427	430,887
Net Operating Income (Loss)	(308,391)	(152,274)	(522,188)	(178,839)
Other Income (Expense)				
Interest Expense	(8,669)	(5,538)	(14,015)	(5,538)
Total Other Income (Expense)	(8,669)	(5,538)	(14,015)	(5,538)
Net Income (Loss)	\$ (317,060)	\$ (157,812)	\$ (536,203)	\$ (184,377)
Net Income (Loss) Per Share	\$ (0.00)	\$ (0.00)	\$ (0.01)	\$ (0.00)
Weighted Average Shares Outstanding	91,106,170	76,866,047	91,106,170	76,866,047

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

4

View Systems, Inc. and Subsidiaries
Consolidated Statements of Stockholders' Equity (Deficit)

	Preferred Shares	Preferred Amount	Common Shares	Common Amount	Additional Paid-in Capital	Retained Earnings (Deficit)
Balance, December 31, 2004	-	\$ -	76,533,922	\$ 76,534	\$ 17,119,596	\$ (15,000,000)
January - March 2005 - shares issued for cash	-	-	155,000	155	15,345	
January - March 2005 - shares issued in payment of accounts payable	-	-	128,000	128	18,872	

Edgar Filing: VIEW SYSTEMS INC - Form 10QSB

January - March 2005 - shares issued for services	-	-	1,805,000	1,805	191,335	
April - June 2005 - shares issued for cash	-	-	2,287,500	2,288	114,713	
April - June 2005 - shares issued for services	-	-	1,242,000	1,242	77,004	
July - September 2005 - shares issued for cash	-	-	612,000	612	55,588	
July - September 2005 - shares issued for services	-	-	150,000	150	37,998	
July - September 2005 - shares issued	7,171,725	71,717	-	-	-	
October - December 2005 - shares issued for cash	-	-	953,330	953	122,880	
October - December 2005 - shares issued for services	-	-	6,909,000	6,909	1,540,473	
Net loss for the year ended December 31, 2005	-	-	-	-	-	(2)
Balance, December 31, 2005	7,171,725	71,717	90,775,752	90,776	19,293,804	(18)
January - March 2006 - shares issued for cash	-	-	100,000	100	9,900	
January - March 2006 - shares issued for services	-	-	160,000	160	15,840	
April - June 2006 - shares issued for cash	-	-	60,000	60	5,940	
April - June 2006 - shares issued for services	-	-	1,075,000	1,075	121,125	
Reclassification of a receipt of proceeds from a loan which was previously reflected as a payment for stock	-	-	(333,330)	(333)	(33,000)	
Net loss for the period ended June 20, 2006	-	-	-	-	-	
Balance, June 30, 2006	7,171,725	\$ 71,717	91,837,422	\$ 91,838	\$ 19,413,609	\$(18)

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

Edgar Filing: VIEW SYSTEMS INC - Form 10QSB

View Systems, Inc. and Subsidiaries
Consolidated Statements of Cash Flows

	For the Six Months Ended June 30,	
	2006	2005
Cash Flows from Operating Activities:		
Net Income (Loss)	\$ (536,203)	\$ (184,377)
Adjustments to Reconcile Net Loss to Net Cash Provided by Operations:		
Depreciation & Amortization	6,000	6,400
Adjustment to allowance for doubtful accounts	(55,117)	-
Stock issued for services	138,200	71,150
Change in Operating Assets and Liabilities:		
(Increase) Decrease in:		
Accounts Receivable	250,816	94,370
Inventories	(84,831)	35,000
Deposits	(2,355)	-
Increase (Decrease) in:		
Accounts Payable	139,931	(164,898)
Accrued Expenses	1,450	(64,346)
Accrued Interest	13,467	-
Accrued Royalties	(37,500)	-
Net Cash Provided (Used) by Operating Activities	(166,142)	(206,701)
Cash Flows from Investing Activities:		
Purchases of equipment	(16,499)	(1,115)
Purchase of licenses	(50,000)	-
Funds advanced (to) from affiliated entities	(21,300)	(4,901)
Net Cash Used In Investing Activities	(87,799)	(6,016)
Cash Flows from Financing Activities:		
Fund provided by issuance of notes payable	296,667	-
Proceeds from stock issuance	16,000	132,500
Net Cash Provided by Financing Activities	312,667	132,500
Increase (Decrease) in Cash	58,726	(80,217)
Cash and Cash Equivalents at Beginning of Period	8,708	173,486
Cash and Cash Equivalents at End of Period	\$ 67,434	\$ 93,269

Edgar Filing: VIEW SYSTEMS INC - Form 10QSB

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

6

View Systems, Inc. and Subsidiaries
Consolidated Statements of Cash Flows (Continued)

	For the Six Months Ended June 30,	
	2006	2005
Cash Paid For:		
Interest	\$ -	\$ 138
Income Taxes	\$ -	\$ -
Non-Cash Investing and Financing Activities:		
Stock issued in payment of accounts payable	\$ -	\$ 19,000

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

7

View Systems, Inc.
Notes to the Consolidated Financial Statements
June 30, 2006

GENERAL

View Systems, Inc. (the Company) has elected to omit substantially all footnotes to the financial statements for the six months ended June 30, 2006 since there have been no material changes (other than indicated in other footnotes) to the information previously reported by the Company in their Annual Report filed on the Form 10-KSB for the twelve months ended December 31, 2005.

UNAUDITED INFORMATION

Edgar Filing: VIEW SYSTEMS INC - Form 10QSB

The information furnished herein was taken from the books and records of the Company without audit. However, such information reflects all adjustments which are, in the opinion of management, necessary to properly reflect the results of the interim period presented. The information presented is not necessarily indicative of the results from operations expected for the full fiscal year.

8

In this report references to "View Systems," "we," "us," and "our" refer to View Systems, Inc. and its subsidiaries.

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

The Securities and Exchange Commission ("SEC") encourages companies to disclose forward-looking information so that investors can better understand future prospects and make informed investment decisions. This report contains these types of statements. Words such as "may," "will," "expect," "believe," "anticipate," "estimate," "project," or "continue" or comparable terminology used in connection with any discussion of future operating results or financial performance identify forward-looking statements. You are cautioned not to place undue reliance on the forward-looking statements, which speak only as of the date of this report. All forward-looking statements reflect our present expectation of future events and are subject to a number of important factors and uncertainties that could cause actual results to differ materially from those described in the forward-looking statements.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

EXECUTIVE OVERVIEW

Our product lines are related to visual surveillance, intrusion detection and physical security. Our principal products include:

- .. SecureScan Concealed Weapons Detection System - a walk-through concealed weapons detector which uses passive magnetic sensing technology and location algorithms to accurately pinpoint the location, size and number of threat objects. The control unit for this patented product combines the magnetic and video information in a manner that allows it to be stored and displayed for easy recognition and auditory warning. The software system's architecture allows for easy integration of biometrics and access control devices.
- .. Fingerprint biometric verification systems, magnetic door locks and central monitoring or video command centers which can be combined with our principal products.
- .. Passport and driver's license verification system for positive identification in correctional facilities, large government and commercial office buildings combined with our concealed weapons detection SecureScan.
- .. RADView - a patented integrated neutron and gamma-ray radiation sub-system which are being integrated into other detection systems.
- .. ViewMaxx Digital Video products - a high-resolution, digital video recording and real-time monitoring system.
- .. Visual First Responder - a lightweight, wireless camera system housed in a tough, waterproof flashlight body. The camera systems sends

Edgar Filing: VIEW SYSTEMS INC - Form 10QSB

real-time images back to a video monitor at a command post located outside the exclusion zone or containment area. The Visual First Responder is able to transmit high quality video in the most difficult environments. It uses a triple-diversity antenna system that minimizes signal distortion in urban environments.

Management believes that heightened attention to personal threats, potential large scale destruction and theft of property in the United States along with spending by the United States government on Homeland Security will continue to drive growth in the market for security products.

In June 2006 we previewed our Biometric SecureScan III which includes positive identification and biometric verification capabilities. The SecureScan III includes a fingerprint identification and verification system, state-issued identification scanning device for driver's licenses and passports, and a visitor badge printing system.

We intend to integrate technology to sense enriched nuclear material into our SecureScan and our Visual First Responder products. This technology will allow our products to detect enriched nuclear material that may be used to build nuclear based explosive devices or for creating radiological disasters. In addition, this technology will be used in stand alone handheld portable detectors. This technology is based on existing patents owned by the United States government and is licensed exclusively to View Systems for the purpose of commercializing it.

9

For the next twelve months our primary challenge will be to develop our sales and distribution network into additional regions and markets in the United States and abroad. We intend to increase sales by offering demonstrations of our products in specific geographical areas to potential customers or at region specific trade shows, such as sheriff's conventions, court administrators' meetings, civil support team, state police shows and dealers shows. When a demonstration results in a sale of one of our products, then we attempt to expand that market by contacting other potential customers in the area, such as, correctional facilities, courthouses and other municipal buildings. After several sales in a particular geographic area management will decide whether it is appropriate to open a sales and service office.

LIQUIDITY AND CAPITAL RESOURCES

We have incurred losses for the past two fiscal years and had a net loss of \$317,060 at June 30, 2006. Our revenues from product sales have been increasing but are not sufficient to cover our operating expenses. Our auditors have expressed substantial doubt that we can continue as a going concern unless we obtain financing.

Historically, we have relied on revenues, debt financing and sales of our common stock to satisfy our cash requirements for working capital. For the six month period ended June 30, 2006 (the "2006 six month period") we received cash from revenues of \$624,978, proceeds of \$296,667 from debt financing and \$16,000 from sales of our common stock. For the six month period ended June 30, 2005 (the "2005 six month period"), we received cash from revenues of \$481,556 and received proceeds of \$132,500 from the sale of our common stock.

Edgar Filing: VIEW SYSTEMS INC - Form 10QSB

Management intends to finance our operations with revenue from product sales and any cash short falls will be addressed through equity or debt financing.

In December 2005 we completed debt financing to fund operations in the short term. We entered into a subscription agreement, discussed below in "Commitments and Contingent Liabilities", that provides for the purchase of convertible promissory notes through \$100,000 installments over a five month period. As of June 30, 2006, we have received funds of \$296,667 from this subscription agreement and we expect to receive an additional approximate \$170,000 under this agreement. We will use this cash for marketing, working capital, and to enhance our presence in other geographical regions.

At our current revenue levels we will require an additional \$500,000 during the next six months to cover our operating costs of approximately \$100,000 per month. These operating costs include cost of sales, general and administrative expenses, salaries and benefits and professional fees related to contracting engineers. We may rely on equity financing to raise additional funds; however, as of the date of this filing we have approximately 9,000,000 authorized common shares of common stock remaining. Management is taking steps to increase our authorized common stock within the next 60 days to provide shares for additional financing.

Management believes revenues will continue to increase but not to the point of profitability in the short term. We will need to continue to raise additional capital, both internally and externally, to cover cash shortfalls and to compete in our markets. We cannot assure you that we will be able to obtain financing on favorable terms and if we cannot obtain financing, then we may be required to reduce our expenses and scale back our operations.

COMMITMENTS AND CONTINGENT LIABILITIES

Our base rent for operating leases related to our principal office and manufacturing facility is approximately \$2,870 per month, with an annual rent escalator of 3%. At December 31, 2005, future minimum payments for operating leases related to our office and manufacturing facility were \$97,646 through December 31, 2008. We also lease two additional offices. We lease a 1,299 square foot sales, engineering and manufacturing office in the East Point Business Center in Jacksonville, Florida. This lease has a base rent of approximately \$1,500 with a 4% annual escalator and expires on January 1, 2008. The second sales and engineering office is located in Office World Plaza in Lomita, California, near Los Angeles. We lease this office for \$850 per month and this lease expires February 28, 2007.

10

Our total current liabilities increased to \$1,160,007 at June 30, 2006 compared to \$712,659 at December 31, 2005. The increase was primarily the result of notes payable related to the subscription agreement discussed below.

At June 30, 2006, we are in default on a \$110,000 note payable to a former stockholder of Xyros Technology which was due in 1999. We negotiated to repay the loan as cash flows permit and this debt remains outstanding. We are in doubt about the intentions, will or ability of the note holder to attempt collection of this debt.

Subscription Agreement

Edgar Filing: VIEW SYSTEMS INC - Form 10QSB

We entered into a Subscription Agreement, dated December 23, 2005, with three accredited investors; Starr Consulting, Inc., Active Stealth, LLC, and KCS Referral Service LLC (the "Subscribers"). We agreed to sale and the Subscribers agreed to purchase convertible promissory notes and warrants. However, on January 6, 2006, the Subscribers consented to the removal of the warrants from the subscription agreement, with the understanding that the warrants would be reinstated after we increased our authorized common stock and the shares underlying the warrants would be registered at a later date. The Subscribers did not receive any other additional consideration for the removal of the warrants. The Subscribers agreed to purchase up to an aggregate of \$500,000 of 8% promissory notes convertible into shares of our common stock at a per share conversion price of \$0.10. The notes are due and payable by December 31, 2006. The Subscribers agreed to purchase the promissory notes over a 5 month period in \$100,000 per month installments; however, other than the contractual agreement there is no guarantee that the Subscribers will purchase the promissory notes. In March 2006 we terminated this agreement with KCS Referral Service LLC.

Starr Consulting, Inc. agreed to purchase convertible promissory notes in the aggregate amount of \$166,667, which may be converted into 1,666,667 shares of our common stock. Active Stealth, LLC and KCS Referral Service LLC each agreed to purchase convertible promissory notes in the aggregate amount of \$166,666, convertible into 1,666,666 common shares. As of June 30, 2006, Starr Consulting purchased promissory notes valued at \$148,334, Active Stealth purchased promissory notes of \$115,000, KCS Referral Service LLC purchased promissory notes valued at \$33,333 and Elite Equity Marketing purchased promissory notes valued at \$66,000 that were originally designated for KCS Referral Service LLC.

The agreement provides for piggy back registration rights for the shares underlying the convertible promissory notes. The agreement provides that we must file a registration statement within 60 days of a request by any Subscriber and cause the registration statement to become effective within 120 days of that request. We are obligated to maintain the effectiveness of the registration statement until all the underlying shares have been sold by the Subscribers. If we fail to obtain or maintain effectiveness of the registration statement, then we are required to pay liquidated damages in an amount equal to 2% of the purchase price of the convertible promissory notes remaining unconverted and the purchase price of the shares issued upon conversion of the notes owned of record by the holder of the notes for each 30 day period that the registration statement is not effective. We filed a registration statement on Form SB-2 on February 2, 2006 to register the underlying shares, but as of the date of this filing, the registration statement has not been declared effective.

If we fail to issue shares within 10 business days after a request by a Subscriber, then the Subscriber is entitled to a sum of money, whichever is greater of either (i) multiplying the outstanding principal amount of the note designated by the Subscriber by 130%, or (ii) multiplying the number of shares deliverable upon conversion of the amount of the note's principal and/or interest at the conversion price that would be in effect on the deemed conversion date by the highest closing price of the common stock on the principal market for the period commencing on the deemed conversion date until the day prior to the receipt of the payment.

OFF-BALANCE SHEET ARRANGEMENTS

None.

CRITICAL ACCOUNTING POLICIES

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Estimates of particular significance in our financial statements include annual tests for impairment of our licenses. These estimates could likely be materially different if events beyond our control, such as changes in government regulations that affect the usefulness of our licenses or the introduction of new technologies that compete directly with our licensed technologies affect the value of our licenses.

We first determine the value of the license using a projected cash-flow analysis to determine the present value of cash flows. The test is done using assumptions as to various scenarios of increases and decreases in the revenue stream and applying a discount rate of 6%. If the value achieved under these various methods is less than the carrying value of the assets then it is considered that an impairment has occurred and the asset's carrying value is adjusted to reflect the impairment.

Management also makes estimates on the useful life of our licenses based on the following criteria:

- .. Whether other assets or group of assets are related to the useful life of the licenses,
- .. Whether any legal, regulatory or contractual provisions will limit the use of the assets,
- .. We evaluate the cost of maintaining the license,
- .. We consider the possible effects of obsolescence, and
- .. Whether there is maintenance or any other costs associated with the license.

RESULTS OF OPERATIONS

The following discussions are based on the consolidated financial statements of View Systems and its subsidiaries. These charts and discussions summarize our financial statements for the three and six month periods ended June 30, 2006 and 2005 and should be read in conjunction with the financial statements, and notes thereto, included with this report at Part I, Item 1, above.

Summary Comparison of 2006 and 2005 Period Operations

	Three month period ended		Six month period ended	
	June 30, 2006	June 30, 2005	June 30, 2006	June 30, 2005
Revenues, net	\$ 222,403	\$ 195,914	\$ 624,978	\$ 481,556
Cost of sales	111,457	125,180	318,739	229,508
Gross profit (loss)	110,946	70,734	306,239	252,048
Total operating expenses	419,337	223,008	828,427	430,887

Edgar Filing: VIEW SYSTEMS INC - Form 10QSB

Net operating loss	(308,391)	(152,274)	(522,188)	(178,839)
Total other income (expense)	(8,669)	(5,538)	(14,015)	(5,538)
Net income (loss)	(317,060)	(157,812)	(536,203)	(184,377)
Net earnings (loss) per share	\$ (0.00)	\$ (0.00)	\$ (0.01)	\$ (0.00)

Revenue is considered earned when the product is shipped to the customer. The concealed weapons system and the digital video system each require installation and training. Training is a revenue source separate and apart from the

12

sale of the product. In those cases revenue is recognized at the completion of the installation and training. The following chart provides a breakdown of our sales for the 2006 and 2005 six month periods.

	June 30, 2006	June 30, 2005
	-----	-----
Secure Scan	\$ 291,721	\$ 221,970
Digital Video	6,870	38,017
Visual First Responder	302,120	219,691
Service, installation and training	\$ 24,267	\$ 1,878

Our marketing efforts have increased sales of our SecureScan and Visual First Responder, while sales of our ViewMaxx digital video decreased in the 2006 six month period when compared to the 2005 comparable period. We had strong sales of this product in the 2005 six month period, but that level of sales did not continue in 2006. Service, installation and training revenues increased due to the sales of our SecureScan and Visual First Responder sales.

Management anticipates that increases in revenues will continue as we develop our sales and marketing channels and establish local sales and service offices in geographic areas where we have already completed sales. In addition, the introduction of our new products that have biometric identification capabilities and new products that have the capability to sense enriched nuclear material may also increase our sales.

Our backlog at June 30, 2006, was approximately \$382,000 compared to \$160,000 at March 31, 2006. Our back log is carried in part by our third party manufacturers because purchase orders are placed with the manufacturers and they receive payment when we receive payment from the customer. However, the delay between the time of the purchase order and shipping of the product results in a delay of recognition of the revenue from the sale. This delay in recognition of revenues will continue as part of our results of operations.

Cost of sales includes costs of products sold and shipping costs. Cost of sales was approximately 47% to 50% of net revenues for the 2006 six month

Edgar Filing: VIEW SYSTEMS INC - Form 10QSB

period and the three month period ended June 30, 2006 (the "2006 second quarter") and the three month period ended June 30, 2005 (the "2005 second quarter"). However, cost of sales was 63.9% of net revenues for the 2005 second quarter due to lower economy of scale factors. Management anticipates that the relative margins for product sales for each product line, assuming similar quantities sold and similar sourcing of components, should remain relatively the same during the remainder of 2006.

Total operating expense increased in the 2006 periods compared to the 2005 periods due to increases in all aspects of our operation expenses. Business development increased as a result of our active efforts to increase business. General and administrative expenses increased primarily due to increases in rent from the addition of office space in California and Florida.

Professional fees increased in the 2006 six month period due to an increase in engineering fees and recognition of the issuance of shares for services in the 2006 periods. We rely on independent contractors to provide services rather than hiring employees and we issued shares of our common stock for services under these contracts rather than deplete our cash. Salaries and benefits expenses increased due to the addition of three employees to our Florida office. We anticipate total operating expense will continue to increase as we continue business development, expand our sales channels, and possibly open regional sales and engineering offices with employees.

Total other expense for the 2006 six month period was related to interest on loans. Management anticipates interest expense to increase as a result of the subscription agreement with the Subscribers, described above, and our need to seek further private financing in the future to cover cash shortfalls.

Management believes net losses will continue in the short term as we expand our sales channels.

13

FACTORS AFFECTING FUTURE PERFORMANCE

Our independent auditors have expressed substantial doubt whether we can continue as a going concern.

We have incurred ongoing operating losses and do not currently have financing commitments in place to meet expected cash requirements for the next twelve months. We recorded a net loss of \$536,203 for the six month period ended June 30, 2006 and have negative working capital of \$851,428. We are unable to fund our day-to-day operations through revenues alone and management believes we will incur operating losses for the near future while we expand our sales channels. While we have expanded our product line and expect to establish new sales channels, we may be unable to increase revenues to the point that we attain and are able to maintain profitability. As a result we rely on private financing to cover cash shortfalls.

We need additional external capital and may be unable to raise it.

Based on our current growth plan we believe we may require approximately \$500,000 in additional financing within the next twelve months to develop our

Edgar Filing: VIEW SYSTEMS INC - Form 10QSB

sales channels. Our success will depend upon our ability to access equity capital markets and borrow on terms that are financially advantageous to us. However, we may not be able to obtain additional funds on acceptable terms. If we fail to obtain funds on acceptable terms, then we might be forced to delay or abandon some or all of our business plans or may not have sufficient working capital to develop products, finance acquisitions, or pursue business opportunities. If we borrow funds, then we could be forced to use a large portion of our cash, if any, to repay principal and interest on those loans. If we issue our securities for capital, then the interests of investors and stockholders will be diluted.

We are currently dependent on the efforts of resellers for our continued growth and must expand our sales channels to increase our revenues and further develop our business plans.

We are in the process of developing and expanding our sales channels, but we expect overall sales to remain down as we develop these sales channels. We are actively recruiting additional resellers and dealers and have hired in-house sales personnel for regional and national sales. We must continue to find other methods of distribution to increase our sales. If we are unsuccessful in developing sales channels we may have to delay further development of our business plan.

We may not be able to compete successfully in our market because we have a small market share and compete with large national and international companies.

We estimate that we have less than a 1% market share of the surveillance and weapons detection market. We compete with many companies that have greater brand name recognition and significantly greater financial, technical, marketing, and managerial resources. The position of these competitors in the market may prevent us from capturing more market share. We intend to remain competitive by increasing our existing business through marketing efforts, selectively acquiring complementary technologies or businesses and services, increasing our efficiency, and reducing costs.

Our revenues are dependent in part upon our relationships and alliances with government agencies and partners.

While we own exclusive licenses for the SecureScan technology, we are dependent upon the continuation of the ongoing contract between the Department of Energy and National Institute of Justice for continuations and improvements to the concealed weapons detection technology. We are also reliant upon the Department of Energy and National Institute of Justice for continuations and improvements to the Visual First Responder. If either of these entities should discontinue its operations or research and development in these areas we may lose our competitive edge in our market.

We must successfully introduce new or enhanced products and manage the costs associated with producing several product lines to be successful.

Our future success depends on our ability to continue to improve our existing products and to develop new products using the latest technology that can satisfy customer needs. For example, our short term success will depend on the continued acceptance of the SecureScan portal and Visual First Responder product lines. We cannot be certain that we will be successful at producing

Edgar Filing: VIEW SYSTEMS INC - Form 10QSB

multiple product lines and we may find that the cost of production of multiple product lines inhibits our ability to maintain or improve our gross profit margins. In addition, the failure of our products to gain or maintain market acceptance or our failure to successfully manage our cost of production could adversely affect our financial condition.

Our directors and officers are able to exercise significant influence over matters requiring stockholder approval.

Currently, our directors and executive officers collectively hold approximately 58.1% of the voting power of our common and preferred stock entitled to vote on any matter brought to a vote of the stockholders. Specifically, Gunther Than, our CEO, holds approximately 56.5 % of the total voting power as of the date of this report. Pursuant to Nevada law and our bylaws, the holders of a majority of our voting stock may authorize or take corporate action with only a notice provided to our stockholders. A stockholder vote may not be made available to our minority stockholders, and in any event, a stockholder vote would be controlled by the majority stockholders. As a result, our minority stockholders may not have the opportunity to approve or consent to corporate actions or other transactions. This concentration of ownership may also have the effect of delaying or preventing a change in control.

Failure to achieve and maintain effective internal controls in accordance with Section 404 of the Sarbanes-Oxley Act could lead to loss of investor confidence in our reported financial information.

Pursuant to proposals related to Section 404 of the Sarbanes-Oxley Act of 2002, beginning with our Annual Report on Form 10-KSB for the fiscal year ending December 31, 2008, we will be required to furnish a report by our management on our internal control over financial reporting. If we cannot provide reliable financial reports or prevent fraud, then our business and operating results could be harmed, investors could lose confidence in our reported financial information, and the trading price of our stock could drop significantly.

In order to achieve compliance with Section 404 of the Act within the prescribed period, we will need to engage in a process to document and evaluate our internal control over financial reporting, which will be both costly and challenging. In this regard, management will need to dedicate internal resources, engage outside consultants and adopt a detailed work plan.

During the course of our testing we may identify deficiencies which we may not be able to remedy in time to meet the deadline imposed by the Sarbanes-Oxley Act for compliance with the requirements of Section 404. In addition, if we fail to achieve and maintain the adequacy of our internal controls, as such standards are modified, supplemented or amended from time to time, we may not be able to ensure that we can conclude on an ongoing basis that we have effective internal controls over financial reporting in accordance with Section 404 of the Sarbanes-Oxley Act. Moreover, effective internal controls, particularly those related to revenue recognition, are necessary for us to produce reliable financial reports and are important to helping prevent financial fraud.

ITEM 3. CONTROLS AND PROCEDURES

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our filings under the Exchange Act is recorded, processed, summarized and reported within the periods specified in the rules and forms of the SEC. This information is accumulated and communicated to our executive officers to allow timely decisions regarding required disclosure. Our Chief Executive Officer, who also acts in the

Edgar Filing: VIEW SYSTEMS INC - Form 10QSB

capacity of principal financial officer, evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based on that evaluation, he concluded that our disclosure controls and procedures were effective.

15

Also, our Chief Executive Officer determined that there were no changes made in our internal controls over financial reporting during the second quarter of 2006 that have materially affected, or are reasonably likely to materially affect our internal control over financial reporting.

PART II: OTHER INFORMATION

ITEM 5. OTHER INFORMATION

We filed a preliminary Schedule 14C information statement on May 2, 2006, related to increasing our authorized common stock to 250,000,000, ratifying prior corporate actions and seeking new acquisitions and business opportunities. Due to SEC regulatory review, we intend to revise the preliminary Schedule 14C and file a definitive Schedule 14C within the next 30 days.

ITEM 6. EXHIBITS

Part I Exhibits

- 31.1 Chief Executive Officer Certification
- 31.2 Principal Financial Officer Certification
- 32.1 Section 1350 Certification

Part II Exhibits

- 3.1 Articles of Incorporation of View Systems, as amended (Incorporated by reference to exhibit 3.1 to Form 10-QSB, filed November 14, 2003)
- 3.2 By-Laws of View Systems (Incorporated by reference to exhibit 3.2 to Form 10-QSB, filed November 14, 2003)
- 4.1 View Systems, Inc. 2005(b) Professional/Consultant Compensation Plan, dated November 7, 2005 (Incorporated by reference to exhibit 4.1 to Form S-8 filed November 8, 2005)
- 4.2 Subscription Agreement between View Systems, Inc. and Starr Consulting, Inc., Active Stealth, LLC, and KCS Referral Service LLC, dated December 23, 2005 (Incorporated by reference to exhibit 4.1 of Form 8-K, filed January 6, 2006)
- 10.1 View Systems, Inc. 1999 Stock Option Plan (Incorporated by reference to exhibit 10.16 to Form SB-2 filed January 11, 2000)
- 10.2 Employment agreement between View Systems and Gunther Than, dated January 1, 2003 (Incorporated by reference to exhibit 10.3 for Form 10-KSB, filed April 14, 2004)
- 10.3 Lease agreement between View Systems and MIE Properties, Inc., dated August 3, 2005 (Incorporated by reference to exhibit 10.2 to Form 10-QSB, filed November 10, 2005)
- 10.4 Consulting Agreement between View Systems and Business Development

