U.S. SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

(Mark One)

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

For the fiscal year ended June 30, 2015

☐ **TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from to

Commission File No. 001-14949

Implant Sciences Corporation

(Exact name of registrant as specified in its charter)

Massachusetts (State or other jurisdiction of incorporation or organization)	**04-2837126** (I.R.S. Employer Identification No.)
500 Research Drive, Unit 3, Wilmington, MA (Address of principal executive offices)	**01887** (Zip Code)

Registrant's telephone number **(978) 752-1700**

Securities registered pursuant to Section 12(b) of the Exchange Act: **None**

Securities registered pursuant to Section 12(g) of the Act: **Common Stock, $0.001 par value per share**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐ No ☒

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ☐ No ☒

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

Indicate by check mark whether the registrant 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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☐

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

☐ Large Accelerated Filer ☒ Accelerated Filer

☐ Non-accelerated Filer (do not check if a smaller reporting company) ☐ Smaller reporting company

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 September 15, 2015, 75,166,120 shares of the registrant's Common Stock were outstanding. As of December 31, 2014, the last business day of the registrant's most recent completed second quarter, the aggregate market value of the registrant's Common Stock held by non-affiliates of the registrant (without admitting that any person whose shares are not included in such calculation is an affiliate) was $75,525,000 based on the last sale price as reported by the Over-The-Counter-Bulletin-Board on such date.

IMPLANT SCIENCES CORPORATION
FORM 10-K
FOR THE YEAR ENDED JUNE 30, 2015

INDEX

PART I		
Item 1.	Business	3
Item 1A.	Risk Factors	12
Item 1B.	Unresolved Staff Comments	21
Item 2.	Properties	21
Item 3.	Legal Proceedings	21
Item 4.	Mine Safety Disclosures	21
PART II		
Item 5.	Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	22
Item 6.	Selected Financial Data	23
Item 7.	Management's Discussion and Analysis of Financial Condition and Results of Operations	24
Item 7A.	Quantitative and Qualitative Disclosures About Market Risk	32
Item 8.	Financial Statements and Supplementary Data	32
Item 9.	Changes In and Disagreements With Accountants on Accounting and Financial Disclosure	32
Item 9A.	Controls and Procedures	32
Item 9B.	Other Information	35
PART III		
Item 10.	Directors, Executive Officers and Corporate Governance	36
Item 11.	Executive Compensation	36
Item 12.	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	36
Item 13.	Certain Relationships and Related Transactions, and Director Independence	36
Item 14.	Principal Accounting Fees and Services	36
PART IV		
Item 15.	Exhibits, Financial Statement Schedules	37

PART I

Item 1. Business

Cautionary Note Regarding Forward Looking Statements

This Annual Report on Form 10-K contains certain statements that are "forward-looking" within the meaning of the federal securities laws. These forward looking statements and other information are based on our beliefs as well as assumptions made by us using information currently available.

The words "anticipate," "believe," "estimate," "expect," "intend," "will," "should" and similar expressions, as they relate to us, are intended to identify forward-looking statements. Such statements reflect our current views with respect to future events and are subject to certain risks, uncertainties and assumptions, and are not guaranties of future performance. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those described herein as anticipated, believed, estimated, expected, intended or using other similar expressions.

We are making investors aware that such forward-looking statements, because they relate to future events, are by their very nature subject to many important factors that could cause actual results to differ materially from those contemplated by the forward-looking statements contained in this Annual Report on Form 10-K. Important factors that could cause actual results to differ from our predictions include those discussed under "Risk Factors," "Management's Discussion and Analysis" and "Business." Although we have sought to identify the most significant risks to our business, we cannot predict whether, or to what extent, any of such risks may be realized, nor can there be any assurance that we have identified all possible issues which we might face. In addition, assumptions relating to budgeting, marketing, product development and other management decisions are subjective in many respects and thus susceptible to interpretations and periodic revisions based on actual experience and business developments, the impact of which may cause us to alter our marketing, capital expenditure or other budgets, which may in turn affect our financial position and results of operations. For all of these reasons, the reader is cautioned not to place undue reliance on forward-looking statements contained herein, which speak only as of the date hereof. We assume no responsibility to update any forward-looking statements as a result of new information, future events, or otherwise except as required by law. We urge readers to review carefully the risk factors described in this Annual Report and in the other documents that we file with the Securities and Exchange Commission. You can read these documents at *www.sec.gov*.

Where we say "we," "us," "our," "Company" or "Implant Sciences," we mean Implant Sciences Corporation and its subsidiaries.

General

Overview and Recent Developments

We develop, manufacture and sell sophisticated sensors and systems for the security, safety and defense industries. A variety of technologies are currently used worldwide in security and inspection applications. In broad terms, the technologies focus on detection in two major categories: (i) the detection of "bulk" contraband, which includes materials that would be visible to the eye, such as weapons, explosives, narcotics and chemical agents; and (ii) the detection of "trace" amounts of contraband, which includes trace particles or vapors of explosives, narcotics and chemical agents. Technologies used in the detection of "bulk" materials include computed tomography, transmission and backscatter x-ray, metal detection, trace detection and x-ray, gamma-ray, passive millimeter wave, and neutron analysis. Trace detection techniques used include mass spectrometry, gas chromatography, chemical luminescence, and ion mobility spectrometry.

We have developed proprietary technologies used in explosives and narcotics trace detection ("ETD" and "NTD", respectively) applications and market and sell handheld ETD and desktop ETD and NTD systems that use our proprietary technologies. Our products are marketed and sold to a growing number of locations domestically and internationally. These systems are used by private companies and government agencies to screen baggage, cargo, other objects and people for the detection of trace amounts of explosives and narcotics.

On September 30, 2013, the Service Technique de l'Aviation Civile in France certified our QS-B220 Desktop Explosives and Narcotics Detector for use in passenger and air cargo screening at airports throughout France, French territories and several European Union member nations. The QS-B220 received regulatory approval from the German Federal Ministry of the Interior for aviation security applications at German airports on March 25, 2014 for use at all non-passenger airport checkpoints for screening of deliveries, food service, and other airport service functions.

On October 18, 2013, the QS-B220 was accepted into the "Qualified" section of the Air Cargo Screening Technology List published by the United States Transportation Security Administration (the "TSA"). With this acceptance, which follows the "Approved" status granted by the TSA in January 2013, the QS-B220 joined the list of products from which regulated parties, such as air carriers, independent cargo screening facilities and shippers, are encouraged to purchase security solutions.

On May 13, 2014, we achieved registration status to ISO 9001:2008 and ISO 14001:2004 quality standards. ISO 9001 is currently the most rigorous international standard for Quality Management and Assurance and ISO 14001 is an Environmental Management System. ISO standards were developed by the International Organization for Standardization in Geneva, Switzerland to promote and facilitate international trade. More than 150 countries, including European Union members, the United States and Japan, recognize ISO standards.

Our QS-B220 desktop ETD system successfully completed and passed testing requirements for the TSA's qualification test for aviation checkpoint and checked baggage and has been placed on the TSA's Qualified Product List ("QPL") on August 28, 2014. The QS-B220 is the first ETD with a non-radioactive source to be approved by the TSA for use in U.S. airports for passenger and baggage screening. We are now able to participate in TSA tenders for ETD procurements for aviation checkpoint and checked baggage screening.

On October 6, 2014, the QS-B220 successfully passed the European Civil Aviation Conference's ("ECAC") Common Evaluation Process of Security Equipment ("CEP") for airport checkpoint screening of passengers and baggage. The CEP was established to provide standards for security equipment performance across ECAC's 44 member nations.

On October 16, 2014, the U.S. Department of Homeland Security ("DHS") selected our proposal to develop next generation explosives trace detection screening systems for funding. The project, pending successful negotiations, is potentially worth up to approximately $2 million. Subject to successful conclusion of negotiations with the DHS, we expect the project to commence in the second quarter of fiscal 2016.

On November 10, 2014, we entered into an Indefinite Delivery / Indefinite Quantity ("IDIQ") contract with the United States Transportation Security Administration ("TSA") for our QS-B220 desktop explosives trace detectors. The IDIQ is a necessary prerequisite for competing for TSA's annual trace detection procurements and establishes contract terms under which the TSA could purchase up to $162 million of equipment and services.

On November 10, 2014, we received an initial delivery order from the TSA for 1,170 QS-B220 desktop explosives trace detectors.

On November 25, 2014, we received notification from the TSA that a bid protest had been filed with the General Accountability Office ("GAO") regarding our receipt of a delivery order from the TSA, which protest was denied by the GAO on March 3, 2015.

History

Since our incorporation in 1984, we have operated as a multi-faceted company engaged in the development of ion-based technologies and providing commercial services and products to the semiconductor, medical device and security industries. In 2007, we made the strategic decision to focus exclusively on our security business and in 2007 and 2008 we divested our non-core semiconductor and medical businesses.

At present, we have developed portable systems, which have been marketed and sold both domestically and internationally since 2004, and a desktop system which we began shipping commercially in the third quarter of fiscal 2012. In order to reduce manufacturing costs and be responsive to large quantity orders, we use a contract manufacturer to manufacture our handheld ETD systems. We are presently manufacturing our desktop systems at our facility in Wilmington, Massachusetts. As we continue to sell and deliver our security products, we work both independently and in conjunction with various government agencies to develop the next generation of trace explosives detectors and to identify new applications for our proprietary technology.

In April 2008, we acquired all of the capital stock of Ion Metrics, Inc., located in San Diego, California. Ion Metrics develops mass sensor systems to detect and analyze chemical compounds such as explosives, chemical warfare agents, narcotics, and toxic industrial chemicals for the homeland defense, forensic, environmental, and safety/security markets. Ion Metrics miniaturized quadrupole mass spectrometry ("QMS") detector technology provides high performance and reliability in combination with low manufacturing costs. We are currently developing interfaces for integrating the QMS detector into our future products.

Industry Overview

We believe that the market for security and inspection products will continue to be affected by the threat of terrorist incidents and by new government mandates and appropriations for security and inspection products in the United States and internationally.

The September 11, 2001 terrorist attacks on the World Trade Center and the Pentagon using hijacked airliners led to nationwide shifts in transportation and facilities security policies. Shortly following these attacks, the U.S. Congress passed the Aviation and Transportation Security Act and integrated many U.S. security-related agencies, including the Federal Aviation Administration, into the U.S. Department of Homeland Security ("DHS"). Under its directive from Congress, the DHS has undertaken numerous initiatives to prevent terrorists from entering the country, hijacking airliners, and obtaining and trafficking in weapons of mass destruction and their components, to secure sensitive U.S. technologies and to identify and screen high-risk cargo containers before they are loaded onto vessels destined for the U.S., among others. These initiatives, more fully described in the Strategic Border Initiative, the Customs-Trade Partnership Against Terrorism and the U.S. Customs and Border Protection Container Security Initiative, have resulted in an increased demand for security and inspection products both in the United States and other nations.

These government-sponsored initiatives have also stimulated security programs in other areas of the world as the U.S initiatives call on other nations to bolster their port security strategies, including acquiring or improving their security and inspection equipment. As a result, the international market for non-intrusive inspection equipment continues to expand as countries that ship goods directly to the United States are required to improve their security infrastructure.

In 2007, the U.S. Congress passed legislation that mandated the inspection of international maritime cargo destined for the United States, domestic civil aviation cargo, and for radiological and nuclear threats in cargo entering the United States. In May 2012, the Transportation Security Administration announced that beginning December 3, 2012, air carriers were required to conduct 100% screening for explosives on international flights bound for the United States for all cargo shipments loaded on passenger aircraft fulfilling a requirement of the Implementing Recommendations of the 9/11 Commission Act. In addition, following recommendations outlined in the "9/11 Commission Report," issued by the National Commission on Terrorist Attacks Upon the United States, federal law has required the screening of all cargo carried on passenger aircraft for flights originating in the United States since August 2010.

Furthermore, DHS's Science and Technology Directorate has supported the development of new security inspection technologies and products. We participate in a number of such research and development efforts, including projects to develop new technologies for improving the accuracy of detection of trace amounts of explosives, narcotics and chemical agents; and improved sampling techniques for the application of trace detection to aviation and cargo screening. The Science and Technology Directorate has also initiated programs for the development of technologies capable of protecting highways, railways and waterways from terrorist attack.

In addition, the U.S. Department of Defense has also begun to invest more heavily in technologies and services that screen would-be attackers before they are able to harm U.S. and allied forces.

Similar initiatives by international organizations such as the European Union have also resulted in a growing worldwide demand for airline, cargo, port and border inspection technologies. For example, the European Union has tasked a working group to establish uniform performance standards for people, cargo, mail & parcel and hold baggage ETD screening systems, just as it has with X-Ray and liquid explosives detection systems which resulted in the European Civil Aviation Conference's ("ECAC") Common Evaluation Process of Security Equipment ("CEP") for airport checkpoint screening of passengers and baggage. The CEP was established to provide standards for security equipment performance across ECAC's 44 member nations. The promulgation of these new standards has established performance baselines against which we have directed certain of our research and development spending and the marketing our products to customers located in the European Union. As a result of these and other changes, sales of our security products have improved. Major projects recently installed or currently underway include system installations at airports, ports and border crossings, government and military facilities and other locations, primarily in the international marketplace. We anticipate that there may be growing demand from governments and commercial enterprises for increasingly sophisticated screening solutions in the future.

Technology

Since 1999, we have performed research and development in the area of explosives trace detection ("ETD"). We have developed several proprietary technologies in key areas of ETD which we believe improve the harvesting, collection and detection of trace particles and vapors of explosives substances. More recently, we have adapted this technology for the detection of narcotics ("NTD"). Our intellectual property portfolio contains 25 security-related patents and patents pending: nineteen issued and active United States patents, six United States patents pending, and

two licensed patents. We believe that our portfolio of patents and patents pending provides extensive protection in sample harvesting, sample detection and collection. A key to our past and future success is our ability to innovate and offer differentiation in these areas.

We compartmentalize ETD and NTD into four major areas: (i) harvest, (ii) transport, (iii) analysis, and (iv) reporting. These technologies are discussed in detail in the following sections.

Harvest - Aerosol Particle Release

Tiny particles of explosives and narcotics are "sticky" and may adhere to surfaces. Particles can be transferred if an object, such as a person's fingers or clothing, comes in contact with a particle. We have demonstrated that a person touching an explosives and narcotics material can transfer particles to numerous other objects, leaving a trail of particles behind.

Our competitors commonly swipe a surface to be interrogated for explosives or narcotics particles with cloth or paper. We believe that this "contact" methodology provides an effective but inconsistent method of harvesting a trace sample as compared to an automated, non-contact collection of the sample. We have developed a method, which we believe to be more efficient, using an aerosol of fine dry ice particles. This technique, which is surprisingly inexpensive to use, could increase collection sensitivity substantially and eliminate direct contact with a surface. Our aerosol technology functions as a very gentle version of "sandblasting" and is safe for almost all surfaces. Since dry ice sublimes into gas, no residue is left behind, and the aerosol may be used indoors. We have five patents issued on this methodology.

Transport

Vortex Sampling

Once the trace particle has been released from a surface, it must be transported to a collection point. Vortex sampling was the first of our sampling innovations. Our vortex is similar to a miniature tornado. A hollow spinning cylinder of air flowing outward surrounds and protects an inner vacuum flowing inward. It is this vortex sampling technology that enables particles released within the vortex, or blown into it, to be transported with high efficiency to a collection filter. We have three patents issued in the area of vortex sampling methodology.

Long-Life Sample Trap

Once particles have been liberated from the surface being interrogated for the presence of trace amounts of explosives or narcotics, the particles are transported to our innovative trapping filter, which is an ultra-fine stainless steel woven mesh. The trapping filter has a long usable life, which can span several years, requiring inexpensive, routine maintenance. We believe the trapping filter provides an innovative solution to the more costly consumables used by several of our competitors engaged in ETD and NTD using contact methodology for sampling and detection.

Analysis

Flash Desorption

Flash desorption is an optical method for converting the chemistry of a particle, such as the chemicals composing explosives or narcotics, into a vapor that can be subjected to analyses for the discrimination of chemical properties. In conventional trace chemical detectors, a sample is slowly warmed in an oven, producing diluted vapor with low chemical concentrations. Optical flash vaporization heats a sample within microseconds, producing a high sample concentration for detection.

This method is not appropriate with conventional sample collection methods, such as paper wipes, because the paper is white, and the light from the bright flash reflects off the paper, producing little heating. However, by using our trapping filter, a very fast detection response can be achieved without loss in sensitivity. We have three patents issued in the area of flash desorption methodology.

Photonic Ionization

The conventional method of ionizing vapors for analysis uses a radioactive beta source. While equipment using radioactive sources are simple, effective, and need no electricity in the ionization process, there are important issues involving safety, licensing, regular verification of source integrity, and disposal. Some markets, such as the European Union, Japan and Australia, are known to reject instruments with radioactive sources. We believe that most markets would prefer not to have to address the issues surrounding ETD and NTD equipment with radioactive sources.

We have developed two types of electronic ionization utilizing photonic methods and high voltage non-

radioactive spark sources for our instruments for applications requiring either the ionization of positive ions or negative ions. These ion sources may be found individually or in combination within our products, depending on the application for which the equipment is to be used. We have four patents issued and one patent pending in the area of photonic ionization.

Reporting

Reporting is that portion of the cycle that displays and stores information generated during the analysis phase. It is this information a system operator sees and indicates if an alarm condition exists or if the test is negative. Information can be displayed in both graphical and tabular formats. The reporting also indicates when the instrument is ready for the next sample as well as displaying built-in system diagnostics.

Other Intellectual Property

We have received patents for: 1) a general explosive detection system; and, 2) long-life calibrant and have a patent pending for a self-regenerating air dryer and purifier.

Intellectual Property

It is our policy to protect our proprietary position by, among other methods, filing United States patent applications. Our intellectual portfolio contains 25 security-related patents and patents pending: nineteen patents have been issued and are active, six patents are pending and we license two patents. The nineteen issued patents expire in the years 2022 through 2035.

We believe our patent portfolio provides extensive protection. We also rely on unpatented proprietary technology, trade secrets and know-how.

Manufacturing

We manufacture our handheld security products primarily through a sole source contract manufacturer located locally in Massachusetts. We also maintain an internal production group at our corporate headquarters in Wilmington, Massachusetts, which is responsible for pre-production logistics, oversight of contract manufacturing, quality control and inventory management. We believe our strategy to outsource manufacturing of our handheld products reduces manufacturing costs, improves scheduling flexibility, and allows us to focus our internal resources and management on product development, marketing, sales and distribution.

Our desktop explosives and narcotics detection systems are manufactured at our facility in Wilmington, Massachusetts. We anticipate that, in the future, we will manufacture more of our products ourselves, including our enhanced handheld detector currently under development. Although we have various "sole-source" suppliers who supply key components for our products, we are not dependent on sole-source suppliers for any of the raw materials used in our products and do not anticipate material interruptions in the supplies of these raw materials.

Products

We have developed several explosives detection systems designed for use in aviation and transportation security, high threat facilities and infrastructure, military installations, customs and border protection, and mail and cargo screening. The systems use our proprietary Quantum Sniffer™ technologies, including a photon-based, non-radioactive ion source in combination with ion mobility spectrometry ("IMS"), a classic detection tool sensitive to the unique speeds with which ions of various substances move through the air to electronically detect minute quantities of explosives vapor and particles.

Current Products

Quantum Sniffer™ QS-H150 Portable Explosives Detector

The Quantum Sniffer QS-H150 Portable Explosives Detector employs a patented vortex collector for the simultaneous detection of explosives particulates and vapors with or without physical contact and in real-time. We believe that our advanced QS-H150 is more sensitive than other handheld detection devices. The QS-H150 can detect vapors and nanogram quantities of explosives particulates for most explosives substances considered to be threats. Such substances include, but are not limited to, military and commercial explosives, improvised and homemade explosives, propellants and taggants.

The QS-H150 has automatic and continuous self-calibration. It monitors its environment, senses changes that would affect its accuracy, and re-calibrates accordingly. The system requires no user intervention and no calibration consumables. The detection process begins with the collection of a sample with our patented vortex collector. After collection, the sample is ionized photonically and analyzed using IMS technology. The presence of a threat

substance is indicated by visible and audible alarms. The threat substance is then identified and displayed on the integrated LCD screen.

When detecting a threat substance, the QS-H150 rapidly alarms and discontinues the collection of a sample. This real-time detection limits equipment contamination and allows for fast clear-down. Operation and maintenance are cost-effective. Since there is no requirement for dopants, calibration consumables or verification consumables, the overall cost of consumables are minimized. Routine maintenance consists only of care and cleaning using common supplies, and desiccant replacement as required. No radioactive material is used in the QS-H150, so there are no associated certifications, licenses, inspections, or end-of-life disposal issues. In early 2010, the QS-H150 was "Designated" as Qualified Anti-Terrorism Technology by DHS under the Support Anti-terrorism by Fostering Effective Technology Act of 2002 (the "SAFETY Act"). The SAFETY Act creates certain liability limitations for claims arising out of, relating to, or resulting from an Act of Terrorism (as defined in §442(2) of the SAFETY Act) where qualified anti-terrorism technologies have been deployed.

Quantum Sniffer™ QS-B220 Desktop Explosives and Narcotics Detector

Our QS-B220 Desktop Explosives and Narcotics Detector uses dual IMS with non-radioactive ionization for the detection and identification of a wide range of military, commercial, and improvised explosives as well as narcotics. The QS-B220 uses a sample trap which is wiped on the surface to be interrogated for explosives or narcotics particles.

The QS-B220 has automatic and continuous self-calibration. It monitors its environment, senses changes that would affect its accuracy, and re-calibrates accordingly. For detection, the sample is collected with a standard trap, ionized, and analyzed using IMS technology. The presence of a threat is indicated by visible and audible alarms, and the substance is identified and displayed on the integrated touch screen display. Users may save data locally or send data through standard interfaces such as USB and LAN. Multi-level password-protected data security is standard. We believe that the operation and maintenance of the QS-B220 are extremely cost-effective. Routine maintenance consists only of care and cleaning using common supplies, and desiccant replacement as required. No radioactive material is used in the QS-B220, so there are no associated certifications, licenses, inspections, or end-of-life disposal issues.

We introduced the QS-B220 at the Force Protection Equipment Demonstration, sponsored by the Department of Defense and Department of Energy, in May 2011. In October 2013, the QS-B220 was "Designated" as Qualified Anti-Terrorism Technology by DHS under the Support Anti-terrorism by Fostering Effective Technology Act of 2002 (the "SAFETY Act"). The SAFETY Act creates certain liability limitations for claims arising out of, relating to, or resulting from an Act of Terrorism (as defined in §442(2) of the SAFETY Act) where qualified anti-terrorism technologies have been deployed. We began commercial shipments of the QS-B220 in the third quarter of fiscal 2012.

On September 30, 2013, the Service Technique de l'Aviation Civile in France certified the QS-B220 for use in passenger and air cargo screening at airports throughout France, French territories and several European Union member nations.

The QS-B220 received regulatory approval from the German Federal Ministry of the Interior for aviation security applications at German airports on March 25, 2014 for use at all non-passenger airport checkpoints for screening of deliveries, food service, and other airport service functions.

On October 18, 2013, the QS-B220 was accepted into the "Qualified" section of the Air Cargo Screening Technology List published by the United States Transportation Security Administration (the "TSA"). With this acceptance, which follows the "Approved" status granted by the TSA in January 2013, the QS-B220 joined the list of products from which regulated parties, such as air carriers, independent cargo screening facilities and shippers, are encouraged to purchase security solutions. In July 2013, the QS-B220 successfully completed Independent Testing and Evaluation with the Transportation Security Laboratory, the TSA's testing body, and, in January 2014, the QS-B220 passed all requirements of the Qualification Testing and Evaluation portion of the checkpoint and checked baggage qualification tests at the TSA's Systems Integration Facility.

Our QS-B220 desktop ETD system successfully completed and passed testing requirements for the TSA's qualification test for aviation checkpoint and checked baggage and has been placed on the TSA's Qualified Product List ("QPL") on August 28, 2014. The QS-B220 is the first ETD with a non-radioactive source to be approved by the TSA for use in U.S. airports for passenger and baggage screening. We are now able to participate in TSA tenders for ETD procurements for aviation checkpoint and checked baggage screening.

On October 6, 2014, the QS-B220 successfully passed the European Civil Aviation Conference's ("ECAC") Common Evaluation Process of Security Equipment ("CEP") for airport checkpoint screening of passengers and

baggage. The CEP was established to provide standards for security equipment performance across ECAC's 44 member nations.

In December 2014, the Civil Aviation Administration of China ("CAAC") approved our QS-B220 desktop ETD system for airport screening of passengers and baggage.

Products Under Development

Quantum Sniffer ™ QS-H150E Portable Explosives and Narcotics Detector

We are developing a next-generation handheld detector that will use dual IMS non-radioactive ionization for the detection and identification of a wide range of military, commercial and improvised explosives, as well as narcotics. The QS-H150E will have automatic and continuous self-calibration, multi-level password-protected data security and will include a data management interface with data export to a network for recordkeeping, providing a link with the central command centers and logistics systems used by major carriers. We expect to begin shipment of the QS-H150E in the fourth quarter of fiscal 2016.

Miniature Mass Spectrometer

We initially developed our own proprietary IMS technology. We believe, however, that as market demand grows for greater precision of substance identification and the list of substances to be detected increases, more advanced detectors will be required.

Our acquisition of Ion Metrics enabled us to obtain miniaturized quadrupole mass spectrometry ("QMS") detector technology. The QMS detector is roughly the size of an AA battery and has low manufacturing costs. When used in conjunction with an IMS, the QMS detector senses the molecular weight of the chemical species resulting in an "orthogonal" detection method in which a more fundamental characteristic of a substance is measured. We believe that, because it is unlikely that two substances would share the same mass and the same ion mobility in air, QMS detector technology improves the accuracy of detection and minimizes false alarms. We are currently developing interfaces for integrating the QMS detector into our future products. We have one patent pending in the area of miniature sensor structures for ion mobility spectrometers.

Hyphenated Detectors

Depending on the application and the number of "interfering" background chemicals, it may be necessary to incorporate additional "orthogonal" detection methods into our product line. The combination of multiple sensors in series in which all sensors must agree that a threat is present before a valid alarm is declared is commonly known as a "hyphenated" system. By measuring different properties of the same sample, interferents are separated from the target for detection and identification with minimum rates of false alarms.

We are currently developing hyphenated systems employing conventional ion mobility, differential mobility and quadrupole mass spectrometry. We have two patent issued in real-time trace detection by IMS and QMS and three hyphenated system patents pending. These methods focus on real-time detection, identification and analysis of trace amounts of narcotics, explosives and chemical agents.

We believe detection systems incorporating hyphenated detection methods could accelerate the expansion of our product line to more effectively address the needs of the security, safety and defense sector, as well as accelerate our entry into the narcotics, chemical warfare, biological warfare and toxic industrial chemical detection marketplaces. Combining new technologies with our other innovative products could enhance our competitive position while improving sales volumes and product margins in the future. We expect hyphenated systems to appear in our future product offerings.

Growth Strategy

Our growth strategy is to focus on penetrating the U.S. market through TSA "qualification" and the retention of key industry advisors, to capitalize on our expanded sales and marketing capabilities to drive and support sales growth in our international markets, and to leverage our core intellectual property to extend our product offerings and through licensing or joint development agreements. Each of these initiatives is described below.

Focus on Penetrating the U.S. Market Through Transportation Security Administration Qualification.

Since we made the strategic decision to focus exclusively on our security business, foreign sales have represented a large majority of our revenue. We believe, however, that our long-term success will depend substantially on our ability to penetrate the U.S. market for explosives trace detection equipment. We are therefore focused on obtaining the necessary approvals from the TSA.

On October 18, 2013, our QS-B220 Desktop Explosives and Narcotics Detector was accepted into the "Qualified" section of the Air Cargo Screening Technology List published by the United States Transportation Security Administration (the "TSA"). With this acceptance, which follows the "Approved" status granted by the TSA in January 2013, the QS-B220 joined the list of products from which regulated parties, such as air carriers, independent cargo screening facilities and shippers, are encouraged to purchase security solutions. We believe the TSA's designation of the QS-B220 as "qualified" equipment on the Air Cargo Screening Technology List has allowed us to begin to address the U.S. market, both in domestic airports but also among freight-forwarders and originators of air cargo that are required to purchase "qualified" detection equipment.

On August 28, 2014, our QS-B220 desktop explosives trace detector successfully completed and passed testing requirements for the TSA's qualification test for aviation checkpoint and checked baggage and has been placed on the TSA's Qualified Product List ("QPL"). We are now able to participate in TSA tenders for ETD purchased for aviation checkpoint and checked baggage procurements.

On November 10, 2014, we entered into an Indefinite Delivery / Indefinite Quantity ("IDIQ") contract with the United States Transportation Security Administration ("TSA") for our QS-B220 desktop explosives trace detectors. The IDIQ, a necessary prerequisite for competing for TSA's annual trace detection procurements and establishes contract terms under which the TSA could purchase up to $162 million of equipment and services.

On November 10, 2014, we received an initial delivery order from the TSA for 1,170 QS-B220 desktop explosives trace detectors.

In addition, we believe that many state and local government agencies, unregulated businesses and foreign governments, which are not regulated by the TSA, also prefer to purchase "qualified" detection equipment. We believe, therefore, that achieving "qualified" designation may also accelerate our penetration of these markets.

Capitalize on Expanded Sales and Marketing Capabilities to Drive and Support Sales Growth in our International Markets.

Since 2011 we have expanded our sales and marketing staff as well as our global network of independent distributors. At June 30, 2015, we employed seven sales professionals, one of whom is focused solely on U.S. government opportunities, and two marketing professionals; and we were represented by more than 50 distributors. Our sales staff and distribution network has been instrumental in helping us to penetrate key vertical markets around the world, such as force protection and law enforcement, transportation security, aviation security, and critical infrastructure and "VIP" protection. To further support our sales growth, during fiscal 2014, we expanded our service and training capabilities. We intend to continue to increase our sales and marketing staff, to expand our distribution network and continue to expand our service and training capabilities. At the same time, we believe that our existing distributors, many of whom are new relationships, will increase their own sales of our products into these and other vertical markets.

Leverage our Intellectual Property to Introduce New Products and Through Licensing and Joint Development Agreements.

In addition to the QS-H150E Portable Explosives Detector and the hyphenated detector systems currently under development and described more fully under "Products – Products Under Development," we have developed proof of concepts of other solutions that leverage our patented non-contact detection technologies and intellectual property, including:

- An in-line ETD package scanner for use at security checkpoints;
- A "people portal" to screen individuals for the presence of trace particles of explosives; and
- A "vehicle portal" to identify trace particles of explosives on or in vehicles.

Although we will focus our sales efforts on our handheld and desktop systems for the foreseeable future, we will continue to explore the development of other solutions with the goal of introducing these or other trace detection products in the future.

We have also been in discussions with leading domestic and international security and defense companies concerning the implementation of our trace detection technology alongside existing third-party security systems. Future initiatives may include the joint development of security products with other companies, licenses of our intellectual property to other companies, and/or supplying our products on an "OEM" basis to other companies for inclusion within their own product offerings.

Marketing and Sales

We market and sell our products through direct sales and marketing staff located in the United States, in addition to a global network of independent and specialized sales representatives and distributors. Presently, our marketing and sales staff includes seven sales professionals, one of whom is focused solely on U.S. government opportunities, and two marketing professionals. During fiscal 2015, we expanded upon our global network of independent distributors and as of June 30, 2015 were represented by more than 50 distributors.

We have not experienced, and do not expect to experience, in any material respect, seasonality in sales of our products.

Competition

We believe that Morpho Detection, Inc., Smiths Detection, Inc. and NucTech Company Limited are our primary competitors in trace explosives and narcotics detection markets throughout the world. Companies in our industry compete on the basis of product performance, functionality, quality and features; quality of customer support services, documentation and training; and the capability of the technology to appeal to broader applications beyond the inspection of passengers, baggage and cargo carried on airlines. Each of our principal competitors uses IMS technologies; however, they use a radioactive ion source to ionize the explosive molecules. Our competitors have recently introduced ETD devices that do not use a radioactive ion source. We believe our technology differs from the competition in that we do not have a radioactive ion source; we have lower operating costs, and we can perform "real time" detection. We believe our patented technology provides our devices with greater operating advantages and fewer regulatory restrictions.

Research and Development

Our technical staff consists of 21 scientists and engineers, three of whom hold Ph.D. degrees, and four of whom hold Masters degrees. All of our existing and planned products rely on proprietary technologies developed in our research and development laboratories. Our research and development efforts are generally self-funded, but may also be funded by corporate partners or by awards under the Small Business Innovative Research and other programs of the U.S. government. Under the Small Business Innovative Research program, we retain the right to patent any technology developed pursuant to the program, subject to the retention by the U.S. government of a royalty-free license to use the technology. We have obtained over $20 million in U.S. government grants and research contracts over the past 20 years. However, we did not have any U.S. government grants or research contracts in fiscal 2014 or fiscal 2015.

We spent approximately $5,014,000, $4,787,000 and $4,754,000 on internally funded research and development in the fiscal years ended June 30, 2015, 2014 and 2013, respectively.

Government Regulation and Environmental Compliance

From time to time, legislation is drafted and introduced in Congress that could significantly change the statutory provisions governing the approval, manufacturing and marketing of security products.

Furthermore, our use, management, transportation, and disposal of certain chemicals and wastes are subject to regulation by several federal and state agencies depending on the nature of the chemical or waste material. Certain toxic chemicals and products containing toxic chemicals require special reporting to the U.S. Environmental Protection Agency and/or its state counterparts. Our costs to comply with these requirements have not been material. We are not aware of any specific environmental liabilities to which we are likely to be subject. Our future operations may require additional approvals from federal and/or state environmental agencies, the cost and effects of which cannot be determined at this time. On May 13, 2014, we achieved registration status to ISO 14001:2004 quality standards, the most rigorous international standard for an Environmental Management System.

Employees

As of June 30, 2015, we had 72 full-time employees at our Massachusetts facility, one full-time employee in California and two full-time employees in Shanghai, China. On March 25, 2015, our Board of Directors approved restructuring actions to better align costs with current and future geographic revenue sources and to improve efficiencies. Our Shanghai office closing will be completed in the second quarter of fiscal 2016.

None of these employees are covered by a collective bargaining agreement, and management considers its relations with its employees to be good.

Order Backlog

As of June 30, 2015, our order backlog was $44,782,000, largely due to the receipt, on November 10, 2014, of an initial delivery order from the TSA for 1,170 QS-B220 desktop explosives trace detectors and orders received as a result of the ECAC mandate to implement passenger checkpoint and checked baggage ETD screening at airports serving more than 500,000 passengers annually, by no later than September 1, 2015. Our order backlog as of June 30, 2014 was de minimis, as a substantial portion of our revenue in any quarter historically had been derived from orders booked and shipped in the same quarter.

We expect to ship a majority of the order backlog in our fiscal year ended June 30, 2016 and expect to ship the ECAC orders in the first quarter of fiscal 2016. However, our backlog does not necessarily represent actual future shipments since orders, including our delivery order with the TSA, may be delayed or cancelled by our customers without financial penalty. The rate of customer order cancellations can vary quarter to quarter and year to year. Customers may also reject nonconforming products.

Geographic Areas

Our revenues are derived from both domestic and international sales. During the fiscal years ended June 30, 2015, 2014 and 2013, international sales represented approximately 85%, 76% and 88%, respectively, of our revenue. For the fiscal year ended June 30, 2015, a customer from the Netherlands and a customer from Norway represented approximately 18% and 16% of our revenue, respectively. During the fiscal year ended June 30, 2014, a customer from Japan and a Taiwanese customer represented 18% and 11%, respectively, of our revenue. For the fiscal year ended June 30, 2013, a customer from India and a customer from France represented approximately 48% and 10% of our revenue, respectively.

Item 1A. Risk Factors

An investment in our common stock involves a high degree of risk. Investors should carefully consider the following risk factors, in addition to the risks, uncertainties and assumptions described elsewhere in this Annual Report, in evaluating our Company and our business. If any of these risks, or other risks not presently known to us or that we currently believe are not significant, develops into an actual event, then our business, financial condition and results of operations could be adversely affected. If that happens, the market price of our common stock could decline.

Risks Related to our Liquidity

We will require additional capital to fund operations and continue the development, commercialization and marketing of our product. Our failure to raise capital could have a material adverse effect on our business.

Management continually evaluates operating expenses and plans to increase sales and increase cash flow from operations. Despite our current sales, expense and cash flow projections and the cash available from our line of credit with DMRJ Group LLC ("DMRJ"), we will require additional capital in the third quarter of fiscal 2016 to fund operations and continue the development, commercialization and marketing of our products. Our failure to achieve our projections and/or obtain sufficient additional capital on acceptable terms would have a material adverse effect on our liquidity and operations and could require us to file for protection under bankruptcy laws.

We will be required to repay our secured borrowings on March 31, 2016.

We will be required to repay all of our borrowings from DMRJ, Montsant Partners LLC ("Montsant") and from a group of institutional investors for which BAM Administrative Services LLC ("BAM") acts as administrative agent, on March 31, 2016. Our obligations to BAM are secured by a security interest in substantially all of our assets. DMRJ and Montsant agreed to subordinate their security interest in all of our assets to the security interest held by BAM (See Note 13).

As of June 30, 2015, our obligations to DMRJ under each of the three promissory notes and a revolving line of credit approximated $12,000,000, $12,000,000, $1,000,000 and $16,662,000, respectively. Further, as of June 30, 2015, our obligation to DMRJ for accrued interest under these instruments approximated $11,350,000 and is included in current liabilities in the consolidated financial statements.

As of June 30, 2015, our obligations to Montsant under a promissory note approximated $3,184,000. Further, as of June 30, 2015, our obligation to Montsant for accrued interest under this instrument approximated $1,860,000 and is included in current liabilities in the consolidated financial statements.

As of June 30, 2015, our obligations under the senior secured promissory notes for which BAM is the agent were $20,000,000. Further, as of June 30, 2015, our obligation under such notes for accrued interest amounted to approximately $54,000 and is included in current liabilities in the consolidated financial statements.

As of September 15, 2015, our obligations to DMRJ under each of the three promissory notes and a revolving line of credit approximated $12,000,000, $12,000,000, $1,000,000 and $16,862,000, respectively. Further, as of September 15, 2015, our obligation to DMRJ for accrued interest under these instruments approximated $12,692,000.

As of September 15, 2015, our obligations to Montsant under a promissory note approximated $3,184,000. Further, as of September 15, 2015, our obligation to Montsant for accrued interest under this instrument approximated $1,963,000.

As of September 15, 2015, our obligations under the senior secured promissory notes for which BAM is the agent were $20,000,000. Further, as of September 15, 2015, our obligation under such notes for accrued interest amounted to approximately $738,000.

If we are unable to repay these amounts as required, refinance our obligations to DMRJ and/or the other institutional investors, or negotiate extensions of these obligations, DMRJ, Montsant and/or BAM may seize our assets and we may be forced to file for protection under bankruptcy laws and to curtail or discontinue operations entirely.

Independent auditor report includes cautionary language on our ability to continue as a going concern.

The audit report issued by our independent registered public accounting firm issued on our audited financial statements for the fiscal year ended June 30, 2015 contains an explanatory paragraph regarding our ability to continue as a going concern. This explanatory paragraph indicates there is substantial doubt as to our ability to continue as a going concern due to the risk that we may not have sufficient cash and liquid assets at June 30, 2015, to cover our operating capital requirements for the next twelve-month period and if sufficient cash cannot be obtained we would have to substantially alter our operations, or we may be forced to discontinue operations. Such an opinion from our independent registered public accounting firm may limit our ability to access certain types of financing, or may prevent us from obtaining financing on acceptable terms.

Risks Related to Our Business

We have incurred substantial operating losses and we may never be profitable. There can be no assurance that our revenue will be maintained at the current level or increase in the future.

During the fiscal years ended June 30, 2015, 2014 and 2013, we had revenues of approximately $12,991,000, $8,552,000 and $12,017,000, respectively. During the fiscal years ended June 30, 2015, 2014 and 2013, we had net losses of approximately $21,543,000, $21,010,000 and $27,354,000, respectively. There is a risk that we will never be profitable. We plan to further increase our expenditures to complete the development and commercialization of our new products, and to broaden our sales and marketing capabilities. As a result, we believe we will likely incur losses through fiscal 2016. Our accumulated deficit as of June 30, 2015 and 2014 was approximately $189,429,000 and $167,886,000, respectively. Our ability to generate sufficient revenues to achieve profits will depend on a variety of factors, many of which are outside our control, including:

- our ability to obtain necessary government approvals for our products;
- changes in governmental (including foreign governmental) initiatives and requirements;
- changes in domestic and foreign regulatory requirements;
- the size of the markets we address;
- the existence of competition and other solutions to the problems we address;
- the extent of patent and intellectual property protection afforded to our products;
- the costs associated with equipment development, repair and maintenance; and our ability to manufacture and deliver products at prices that exceed our costs; and
- the cost and availability of raw material and intermediate component supplies.

Our operating results have fluctuated in the past from quarter to quarter and are likely to fluctuate significantly in the future due to a variety of factors, many of which are beyond our control, including:

- changing demand for our products and services;
- the timing of actual customer orders, including significant one-time orders from a single customer in a given quarter, and requests for product shipment and the accuracy of our forecasts of future production requirements;
- the reduction, rescheduling or cancellation of product orders by customers;
- difficulties in forecasting demand for our products and the planning and managing of inventory levels;
- the introduction and market acceptance of our new products and changes in demand for our existing

products;

- changes in the relative portion of our revenue represented by our various products, services and customers, including the relative mix of our business across our target markets;
- changes in competitive or economic conditions generally or in our markets;
- competitive pressures on selling prices;
- the amount and timing of costs associated with product warranties and returns;
- changes in availability or costs of materials, components or supplies;
- changes in our product distribution channels and the timeliness of receipt of distributor resale information;
- the amount and timing of investments in research and development;
- difficulties in integrating acquired assets and businesses into our operations;
- charges to earnings resulting from the application of the purchase method of accounting following acquisitions; and
- non-cash charges to earnings resulting from recording stock-based compensation expense in our consolidated statement of income.

Historically, a substantial portion of our revenue in any quarter has been derived from orders booked and shipped in the same quarter, and backlog has not been a meaningful indicator of revenues for a particular period. As of June 30, 2015, our order backlog was $44,782,000, largely due to the receipt, on November 10, 2014, of an initial delivery order from the TSA for 1,170 QS-B220 desktop explosives trace detectors and orders received as a result of the ECAC mandate to implement passenger checkpoint and checked baggage ETD screening at airports serving more than 500,000 passengers annually, by no later than September 1, 2015. Accordingly, our sales expectations currently are based almost entirely on our backlog of customer orders and internal estimates of future demand. However, our backlog does not necessarily represent actual future shipments since orders, including our delivery order with the TSA, may be delayed or cancelled by our customers without financial penalty. The rate of customer order cancellations can vary quarter to quarter and year to year. Customers may also reject nonconforming products.

As a result of these factors, many of which are difficult to control or predict, as well as the other risk factors discussed in this Annual Report, we may experience material adverse fluctuations in our future operating results on a quarterly or annual basis.

Our markets are subject to technological change and our success will depend on our ability to develop and introduce new products.

The market for our security products is characterized by:

- changing technologies;
- changing customer needs;
- frequent new product introductions and enhancements;
- increased integration with other functions; and
- product obsolescence.

Our success will be dependent in part on the design and development of new products. To develop new products and designs for our security market, we must develop, gain access to and use leading technologies in a cost-effective and timely manner and continue to expand our technical and design expertise. The product development process is time-consuming and costly, and there can be no assurance that product development will be successfully completed, that necessary regulatory clearances or approvals will be granted on a timely basis, or at all, or that the potential products will achieve market acceptance. Our failure to develop, obtain necessary regulatory clearances or approvals for, or successfully market potential new products could have a material adverse effect on our business, financial condition and results of operations.

Economic, political and other risks associated with international sales and operations could adversely affect our sales.

Our revenues are derived from both domestic and international sales. During the fiscal years ended June 30, 2015, 2014 and 2013, international sales represented approximately 85%, 76% and 88%, respectively, of our revenue. For the year ended June 30, 2015 a customer from the Netherlands and a customer from Norway represented 18% and 16%, respectively, of our revenue. During the fiscal year ended June 30, 2014, a customer from Japan and a Taiwanese customer represented 18% and 11%, respectively, of our revenue. For the fiscal year ended June 30, 2013, a customer from India and a customer from France represented approximately 48% and 10% of our revenue, respectively.

Although we anticipate increased U.S. market penetration as a result of TSA qualification, the receipt of an Indefinite Delivery / Indefinite Quantity ("IDIQ") contract with the United States Transportation Security Administration ("TSA") for our QS-B220 desktop explosives trace detectors and the receipt an initial delivery order from the TSA for 1,170 QS-B220 desktop explosives trace detectors, we also expect that revenues from international operations will continue to represent a substantial portion of our total revenue. Accordingly, our future results could be impacted by a variety of factors, including:

- changes in foreign currency exchange rates;
- changes in a country's or region's political or economic conditions, particularly in developing or emerging markets;
- potentially longer payment cycles of foreign customers and difficulty of collecting receivables in foreign jurisdictions;
- trade protection measures and import or export licensing requirements;
- U.S. government sanctions which prohibit the issuance of export licenses and the export of our products;
- differing legal and court systems;
- differing tax laws and changes in those laws;
- differing protection of intellectual property and changes in that protection; and
- different regulatory requirements and changes in those requirements.

Our explosives detection products and technologies may not be accepted by government agencies or commercial consumers of security products, which could harm our future financial performance.

There can be no assurance that our explosives detection systems will generally achieve wide acceptance by government agencies, commercial consumers of security products, and market acceptance. The degree of market acceptance for our explosives detection products and services will also depend upon a number of factors, including the receipt and timing of regulatory approvals and the establishment and demonstration of the ability of our proposed device to detect trace explosives residues on personnel, baggage and other cargo. Our failure to develop a commercial product to compete successfully with respect to throughput, the ability to scan personnel, baggage and other cargo, and portability could delay, limit or prevent market acceptance. Moreover, the market for explosives detection systems, especially trace detection, is largely undeveloped, and we believe that the overall demand for explosives detection systems technology will depend significantly upon public perception of the risk of terrorist attacks. There can be no assurance that the public will perceive the threat of terrorist attacks to be substantial or that governmental agencies and private-industry will actively pursue explosives detection systems technology. Long-term market acceptance of our products and services will depend, in part, on the capabilities, operating features and price of our products and technologies as compared to those of other available products and services. As a result, there can be no assurance that currently available products, or products under development for commercialization, will be able to achieve market penetration, revenue growth or profitability.

If we cannot obtain the additional capital required to fund our operations on favorable terms, or at all, we may have to delay or reconsider our growth strategy.

Our growth strategy may require additional capital for, among other purposes, completing acquisitions of companies and customers' product lines and manufacturing assets, integrating acquired companies and assets, acquiring new equipment and maintaining the condition of existing equipment. If cash generated internally is insufficient to fund capital requirements, or if we desire to make additional acquisitions, we will require additional debt or equity financing. Adequate financing may not be available or, if available, may not be available on terms satisfactory to us. If we raise additional capital by issuing equity or convertible debt securities, the additional securities will dilute the share ownership of our existing investors. In addition, we may grant future investors rights that are superior to those of our existing investors. If we fail to obtain sufficient additional capital in the future, we could be forced to curtail our growth strategy by reducing or delaying capital expenditures and acquisitions, selling assets or restructuring or refinancing our indebtedness.

We depend on outside suppliers and subcontractors, and our production and reputation could be harmed if they are unable to meet our volume and quality requirements and alternative sources are not available.

We have various "sole-source" suppliers who supply key components for our products. Our outside suppliers may fail to develop and supply us with products and components on a timely basis, or may supply us with products and components that do not meet our quality, quantity or cost requirements. If any of these problems occur, we may be unable to obtain substitute sources of these products and components on a timely basis or on terms acceptable to us, which could harm our ability to manufacture our own products and components profitably or on time, and to ship products to customers on time and generate revenues. In addition, if the processes that our suppliers use to

manufacture products and components are proprietary, we may be unable to obtain comparable components from alternative suppliers.

We depend on a contract manufacturer, and our production and products could be harmed if it is unable or unwilling to meet our volume and quality requirements and alternative sources are not available.

We rely on a single contract manufacturer to provide manufacturing services for our handheld QS-H150 explosives detection products. If these services become unavailable, we would be required to identify and enter into an agreement with a new contract manufacturer or take the manufacturing in-house. From time to time in fiscal 2015, this manufacturer has limited the number of detectors it would manufacture due to our inability to pay for the detectors on a timely basis. In addition, this manufacturer has required that we prepay for materials and component parts in advance of procurement. The refusal to manufacture detectors for a substantial period, or the loss of our contract manufacturer altogether, could significantly disrupt production as well as increase the cost of production, thereby increasing the prices of our products. These changes could have a material adverse effect on our business and results of operations.

We may not be able to protect our intellectual property rights.

Our ability to compete is affected by our ability to protect our intellectual property rights. We rely on a combination of patents, trademarks, copyrights, trade secrets, confidentiality procedures and non-disclosure and licensing arrangements to protect our intellectual property rights. Despite these efforts, we cannot be certain that the steps we take to protect our intellectual property will be adequate to prevent misappropriation of our technology or protect that proprietary information. We cannot assure you that any pending or future patent applications will be approved, or that any issued patents will not be challenged by third parties. The validity and breadth of claims in technology patents involve complex legal and factual questions and, therefore, may be highly uncertain. Nor can we assure you that, if challenged, our patents will be found to be valid or enforceable, or that the patents of others will not have an adverse effect on our ability to do business. Although 85% of our revenue in fiscal 2015 was derived from international sales, we do not have any patents or patents pending outside of the United States. Moreover, the enforcement of laws protecting intellectual property in some of the countries in which we sell our products may be inadequate to protect our technology and proprietary information.

We may not have the resources to assert and protect our rights in our patents and other intellectual property. Any litigation or proceedings relating to our intellectual property rights, whether or not determined in our favor or settled by us, is costly and may divert the efforts and attention of our management and technical personnel.

We also rely on unpatented proprietary technology, trade secrets and know-how and no assurance can be given that others will not independently develop substantially equivalent proprietary information, techniques or processes, that such technology or know-how will not be disclosed or that we can meaningfully protect our rights to such unpatented proprietary technology, trade secrets, or know-how. Although we have entered into non-disclosure agreements with our employees, suppliers and consultants, there can be no assurance that such non-disclosure agreements will provide adequate protection for our trade secrets or other proprietary know-how.

Our success will depend on our ability to obtain new patents and to operate without infringing on the proprietary rights of others.

Although we have nineteen United States patents issued and six United States patent applications pending for our explosives detection technology and processes, our success will depend, in part, on our ability to obtain the patents applied for and maintain trade secret protection for our technology and operate without infringing on the proprietary rights of third parties. No assurance can be given that any pending or future patent applications will issue as patents, that the scope of any patent protection obtained will be sufficient to exclude competitors or provide competitive advantages to us, that any of our patents will be held valid if subsequently challenged or that others will not claim rights in or ownership of the patents and other proprietary rights held by us.

Furthermore, there can be no assurance that our competitors have not or will not independently develop technology, processes or products that are substantially similar or superior to ours, or that they will not duplicate any of our products or design around any patents issued or that may be issued in the future to us. In addition, whether or not patents are issued to us, others may hold or receive patents which contain claims having a scope that covers products or processes developed by us.

We may not have the resources to adequately defend any patent infringement litigation or proceedings. Any such litigation or proceedings, whether or not determined in our favor or settled by us, is costly and may divert the efforts and attention of our management and technical personnel. In addition, we may be required to obtain licenses to patents or proprietary rights from third parties. There can be no assurance that such licenses will be available on acceptable terms if at all. If we do not obtain required licenses, we could encounter delays in product development

or find that the development, manufacture or sale of products requiring such licenses could be foreclosed. Accordingly, challenges to our intellectual property, whether or not ultimately successful, could have a material adverse effect on our business and results of operations.

Our future success depends on the continued service of management, engineering and sales personnel and our ability to identify, hire and retain additional personnel.

Our success depends, to a significant extent, upon the efforts and abilities of members of senior management. The loss of the services of one or more of our senior management or other key employees could adversely affect our business. We do not maintain key person life insurance on any of our officers, employees or consultants.

There is intense competition for qualified employees in the security industry, particularly for highly skilled design, applications, engineering and sales people. We may not be able to continue to attract and retain technologists, managers, or other qualified personnel necessary for the development of our business or to replace qualified individuals who could leave us at any time in the future. Our anticipated growth is expected to place increased demands on our resources, and will likely require the addition of new management and engineering staff as well as the development of additional expertise by existing management employees. If we lose the services of or fail to recruit engineers or other technical and management personnel, our business could be harmed.

Periods of rapid growth and expansion could place a significant strain on our resources, including our employee base.

To manage any future growth effectively, we will be required to continue to improve our operational, financial and management systems. In doing so, we will periodically implement new software and other systems that will affect our internal operations regionally or globally.

Future growth would also require us to successfully hire, train, motivate and manage our employees. In addition, our continued growth and the evolution of our business plan will require significant additional management, technical and administrative resources. We may not be able to effectively manage the growth and evolution of our current business.

We are exposed to product liability claims that could place a substantial financial burden on us if we are sued.

The development and sale of explosives detection products entails an inherent risk of product liability. For example, if our products fail to adequately detect explosives, if we are unable to train technicians to properly use our products, or if the market determines or concludes that any of our products are not safe or effective for any reason, we may be exposed to product liability claims. We currently carry product liability insurance. No assurances can be given, however, that our product liability insurance will be adequate to pay any claims that might arise. A product liability claim, whether meritorious or not, could be time-consuming, distracting and expensive to defend, could be harmful to our reputation, could result in a diversion of management and financial resources away from our primary business and could result in product recalls. In any such case, there could be a material adverse effect on our business and results of operations and our business could fail.

Our QS-B220 and QS-H150 have both been "Designated" as Qualified Anti-Terrorism Technology by DHS under the Support Anti-terrorism by Fostering Effective Technology Act of 2002 (the "SAFETY Act"). The SAFETY Act creates certain liability limitations for claims arising out of, relating to, or resulting from an Act of Terrorism (as defined in §442(2) of the SAFETY Act) where qualified anti-terrorism technologies have been deployed.

We use hazardous materials in our research and manufacturing activities. Any liability resulting from the misuse of such hazardous materials could adversely affect our business.

Our research and manufacturing activities sometimes involve the use of various hazardous materials. Although we believe that our safety procedures for handling, manufacturing, distributing, transporting and disposing of such materials comply with the standards for protection of human health, safety, and the environment prescribed by local, state, federal and international regulations, the risk of accidental contamination or injury from these materials cannot be completely eliminated. Nor can we eliminate the risk that one or more of our hazardous material or hazardous waste handlers may cause contamination for which, under laws imposing strict liability, we could be held liable. While we currently maintain insurance in amounts which we believe are appropriate in light of the risk of accident, we could be held liable for any damages that might result from any such event. Any such liability could exceed our insurance and available resources and could have a material adverse effect on our business and results of operations.

We incur substantial costs to operate as a public reporting company.

We incur substantial legal, financial, accounting and other costs and expenses to operate as a public reporting company. We believe that these costs are a disproportionately larger percentage of our revenues than they are for many larger companies. In addition, the rules and regulations of the Securities and Exchange Commission impose significant requirements on public companies, including ongoing disclosure obligations and mandatory corporate governance practices. Our limited senior management and other personnel need to devote a substantial amount of time to ensure ongoing compliance with these requirements. Our common stock is currently quoted on the OTC Bulletin Board and on OTC Markets Group's OTCQB tier. Neither the OTC Bulletin Board nor OTC Markets Group's OTCQB tier impose any specific quotation requirements other than that issuers must be current in their reporting to the Securities and Exchange Commission and, in the case of the OTCQB, a minimum bid price of $0.01 per share. If we are successful in listing our stock for trading on a national securities exchange or having our stock quoted on the Nasdaq Stock Market, we will be subject to additional disclosure and governance obligations. There can be no assurance that we will continue to meet all of the public company requirements to which we are subject on a timely basis, or at all, or that our compliance costs will not continue to be material.

We have significant net operating loss carry forwards which may be impaired if we have a significant change in the stockholder base.

As of June 30, 2015, we had federal and state net operating loss carry forwards available to offset future taxable income of approximately $107,818,000 expiring between 2022 and 2035, and $74,878,000, expiring between 2016 and 2035, respectively. In the event that an "ownership change" occurs for purposes of Section 382 of the Internal Revenue Code, our ability to use these losses to offset future taxable income could be significantly limited. Any such limitation may result in the expiration of a portion of the carry forwards before we can use them. In general, an "ownership change" occurs if there is a change in ownership of more than 50% of our common stock during any cumulative three-year period. For this purpose, determinations of ownership changes are generally limited to shareholders deemed to own 5% or more of our common stock. Such a change in ownership may be triggered by regular trading activity in our common stock, which is generally beyond our control. We have not completed a study to assess whether one or more ownership changes have occurred since we became a loss corporation as defined in Section 382, but we believe that it is likely that an ownership change has occurred. If we are able to refinance our secured indebtedness or otherwise raise capital by issuing common stock or other securities that are convertible into common stock, a further "ownership change" may become more likely.

Risks Related to Competition

We may not be able to compete effectively against existing or new competitors.

We believe that our ability to compete in the explosive detection systems market is based upon such factors as: product performance, functionality, quality and features; quality of customer support services, documentation and training; and the capability of the technology to appeal to broader applications beyond the inspection of passengers, baggage, and cargo carried on airlines. Our competitors may have advantages over our existing technology with respect to these factors. There can be no assurance that we will be successful in convincing potential customers that our products will be superior to other systems given all of the necessary performance criteria, that new systems with comparable or greater performance, lower price and faster or equivalent throughput will not be introduced, or that, if such products are introduced, customers will not delay or cancel potential orders. Further, there can be no assurance that we will be able to bring to commercialization and further enhance our product to better compete on the basis of cost, throughput, accommodation of detection of passengers, baggage or other cargo carried onto airlines, or that we will otherwise be able to compete successfully with existing or new competitors.

Moreover, there can be no assurance that we will be able to price our products and services at or below the prices of competing products and technologies in order to facilitate market acceptance. Accordingly, our success will depend, in part, on our ability to respond quickly to technological changes through the development and introduction of new products and enhancements. Product development involves a high degree of risk, and there can be no assurance that our new product development efforts will result in any commercially successful products. Our failure to compete or respond to technological change in an effective manner would have a material adverse effect on our business and results of operations.

We may face pricing pressures that could prevent us from maintaining the prices of our products.

The sales process for our security products is typically a result of a request for quotations or tenders that are subjected to significant and time-consuming scrutiny prior to the determination of an award. In addition, we face aggressive cost-containment pressures from governmental agencies and the bidding process commonly involves several competitors, many of whom have greater financial and other resources that may enable them to submit bids at prices that might be significantly lower than the prices we may be able to offer. There can be no assurances that we will be able to maintain current prices in the face of continuing pricing pressures. Over time, the average price

for our products may decline as the markets for these products become more competitive. Any material reduction in product prices could negatively affect our gross margin, necessitating a corresponding increase in unit sales to maintain any given level of sales.

Risks Related to Our Securities

Because our common stock is not traded on a national securities exchange or quoted on the Nasdaq Stock Market, our stock has limited liquidity and our ability to raise capital is impaired.

Our common stock was delisted by the NYSE Amex LLC in June 2009. Our common stock has been quoted on the OTC Bulletin Board since May 2009 and is also quoted on the OTC Markets Group's OTCQB tier under the symbol "IMSC". We believe that trading "over the counter" has limited our stock's liquidity and has impaired our ability to raise capital.

Our stock price is volatile.

The market price of our common stock has fluctuated significantly to date. In the past fiscal year, our stock price ranged from $0.64 to $1.82. The market price of our common stock may also fluctuate significantly in the future due to:

- variations in our actual or expected quarterly operating results;
- our ability to obtain necessary government approvals for our products;
- announcements or introductions of new products by us or by our competitors;
- technological innovations by our competitors or development setbacks by us;
- the commencement or adverse outcome of litigation;
- changes in analysts' estimates of our performance or changes in analysts' forecasts regarding our industry, competitors or customers;
- announcements of acquisitions or acquisition transactions; or
- general economic and market conditions.

In addition, the stock market in recent years has experienced extreme price and volume fluctuations that have affected the market prices of many security product companies. These fluctuations have often been unrelated or disproportionate to the operating performance of companies in our industry, and could harm the market price of our common stock.

Additional authorized shares of our common stock and preferred stock available for issuance may adversely affect the market.

On July 1, 2015, at an Annual Meeting of Stockholders, our stockholders approved an amendment to the Company's Restated Articles of Organization to increase the number of authorized shares of common stock by 50,000,000 shares to 250,000,000 shares. We have intentionally delayed the filing of Articles of Amendment to our Restated Articles of Organization with the Commonwealth of Massachusetts to effect that increase. As a result of the stockholder approval, we are authorized to issue 250,000,000 shares of our common stock.

As of June 30, 2015, there were 75,113,665 and 75,103,120 shares of common stock issued and outstanding, respectively. However, the total number of shares of our common stock issued and outstanding does not include shares reserved in anticipation of the exercise of options, warrants, convertible debt instruments and convertible preferred stock.

As of June 30, 2015, we had outstanding stock options and warrants to purchase approximately 24,668,485 shares of our common stock, the exercise price of which range between $0.08 per share to $3.89 per share, and we have reserved shares of our common stock for issuance in connection with the potential exercise of these instruments. As of June 30, 2015, the outstanding balance due under the senior secured convertible promissory notes issued to DMRJ and accrued and unpaid interest was $34,841,000, of which $12,000,000 senior convertible promissory note and $5,145,000 of accrued and unpaid interest is convertible into shares of Series H Convertible Preferred Stock, which preferred stock is convertible into shares of our common stock at $1.09 per share; and a $12,000,000 senior secured promissory note and $3,698,000 of accrued and unpaid interest is convertible into shares of Series I Convertible Preferred Stock, which preferred stock is convertible into shares of our common stock at $1.18 per share. As of June 30, 2015, the outstanding balance due under the senior secured convertible promissory note issued to Montsant and accrued and unpaid interest was $5,044,000, of which a $3,184,000 senior secured promissory and $1,860,000 of accrued and unpaid interest are convertible into shares of our common stock at $0.08 per share. To the extent such options, warrants or convertible notes are exercised or converted, and to the extent that additional shares are issued under strategic advisory agreements, the holders of our common stock will experience

further dilution. Stockholders will also experience dilution upon the exercise of options that may be granted in the future under our stock option plans. In addition, in the event that any future financing or consideration for a future acquisition should be in the form of, be convertible into or exchangeable for, equity securities investors will experience additional dilution.

The exercise of our outstanding options and warrants, the conversion of convertible debt instruments and the issuance of shares of common stock under our advisory agreements will reduce the percentage of common stock held by our current stockholders. During the fiscal years ended June 30, 2015, 2014 and 2013, DMRJ converted senior secured convertible debt and accrued interest in the amounts of $799,000, $314,000 and $40,000, respectively, which resulted in the issuance of shares of our common stock of 9,987,500, 3,918,319 and 500,000, respectively. Further, the terms on which we could obtain additional capital during the life of the derivative securities may be adversely affected, and it should be expected that the holders of the derivative securities would exercise them at a time when we would be able to obtain equity capital on terms more favorable than those provided for by such derivative securities. As a result, any issuance of additional shares of common stock may cause our current stockholders to suffer significant dilution which may adversely affect the market.

In addition, we are authorized to issue 114,000 additional shares of preferred stock. During the fiscal years ended June 30, 2014 and 2013, DMRJ converted Series G preferred stock, which resulted in the issuance of shares of our common stock of 3,918,319 and 14,850,000, respectively. Although we have no present plans to issue any additional shares of preferred stock, our Board of Directors has the authority, without stockholder approval, to create and issue one or more series of such preferred stock and to determine the voting, dividend and other rights of holders of such preferred stock, including the ratio or ratios at which any such shares of preferred stock may be convertible into common stock. The issuance of any of such series of preferred stock may cause the holders of our common stock to experience substantial further dilution and other adverse effects and could make a takeover of our company more difficult.

Shares eligible for future sale may adversely affect the market.

From time to time, certain of our stockholders who acquired their shares directly from our company in privately negotiated transactions may be eligible to sell all or some of their shares of common stock by means of ordinary brokerage transactions in the open market pursuant to effective registration statements under the Securities Act of 1933 and under Rule 144, promulgated under the Securities Act. As of June 30, 2015, we are committed under two consulting agreements to issue and aggregate of 1,650,000 shares of our common stock over a 15 month term, commencing in September 2015. In general, pursuant to Rule 144, a stockholder (or stockholders whose shares are aggregated) who has satisfied a six-month holding period may, under certain circumstances, sell within any three-month period a number of securities which does not exceed the greater of 1% of the then outstanding shares of common stock or the average weekly trading volume of the class during the four calendar weeks prior to such sale. Rule 144 also permits, under certain circumstances, the sale of securities, without any limitation, by our stockholders that are non-affiliates that have satisfied a one-year holding period. Any substantial sale of our common stock pursuant to Rule 144 or pursuant to any resale registration statement may have material adverse effect on the market price of our securities.

There are limitations on director and officer liability which may limit our stockholders' rights to recover for breaches of fiduciary duty.

As permitted by Massachusetts law, our Restated Articles of Organization, as amended, limit the liability of our directors for monetary damages for breach of a director's fiduciary duties except in certain instances. As a result of these limitations and Massachusetts law, stockholders may have limited rights to recover against directors for breaches of their fiduciary duties. In addition, our bylaws provide that we will indemnify our directors, officers, employees and agents if such persons acted in good faith and reasoned that their conduct was in our best interest.

The anti-takeover provisions of our Restated Articles of Organization and Massachusetts law may delay, defer or prevent a change of control.

Our Board of Directors has the authority to issue up to 114,000 additional shares of preferred stock and to determine the price, rights, preferences and privileges and restrictions, including voting rights, of those shares without any further vote or action by our stockholders. The rights of the holders of common stock will be subject to, and may be harmed by, the rights of the holders of the various series of preferred stock that we have issued to date and which may be issued in the future. The issuance of preferred stock may delay, defer or prevent a change in control because the terms of any issued preferred stock could potentially prohibit our consummation of any acquisition, reorganization, sale of substantially all of our assets, liquidation or other extraordinary corporate transaction, without the approval of the holders of the outstanding shares of preferred stock.

Our stockholders must give substantial advance notice prior to the relevant meeting to nominate a candidate for director or present a proposal to our stockholders at a meeting. These notice requirements could inhibit a takeover by delaying stockholder action. Massachusetts law may also discourage, delay or prevent someone from acquiring or merging with us.

A secured lender and our directors and executive officers have the right to acquire a majority of our shares through the conversion or exercise of other securities, which may delay, defer or prevent a change of control and/or will limit the ability of other stockholders to influence corporate matters.

As of September 15, 2015, DMRJ and Montsant, two of our secured lenders, have the right to acquire up to 94,045,047 shares of our common stock upon the conversion of debt and interest. Our directors and executive officers own, or have the right to exercise options within 60 days to acquire, up to 8,633,113 shares of our common stock. If all of these shares of common stock are issued, DMRJ, Montsant and our directors and executive officers would own approximately 58.4% of our outstanding common stock, on a fully diluted basis. Accordingly, these stockholders could have a significant influence over, or have absolute control over, the outcome of any corporate transaction or other matter submitted to our stockholders for approval, including mergers, consolidations and the sale of all or substantially all of our assets and also could prevent or cause a change in control. The interests of these stockholders may differ from the interests of our other stockholders. Third parties may be discouraged from making a tender offer or bid to acquire us because of this concentration of ownership.

We have never paid dividends on our common stock and we do not anticipate paying any cash dividends in the foreseeable future.

We have paid no cash dividends on our common stock to date and we currently intend to retain our future earnings, if any, to fund the development and growth of our business. In addition, our agreements with our secured lenders prohibit the payment of cash dividends. As a result, capital appreciation, if any, of our common stock will be shareholders' sole source of gain for the foreseeable future.

Our management and our independent registered public accountants have identified internal control deficiencies, which our management and our independent registered public accountants determined to constitute material weaknesses.

In connection with the preparation of our financial statements for the years ended June 30, 2015, 2014 and 2013, our management and our independent registered public accountants identified certain deficiencies that, in the aggregate, represent material weaknesses, including the following. However, these weaknesses did not result in any material unadjusted differences when preparing the financial statements for the year ended June 30, 2015:

1. Insufficient segregation of duties, oversight of work performed and lack of compensating controls in our finance function due to limited personnel.
2. Lack of documentation to support occurrences and approval procedures.
3. Design deficiencies that do not meet stated objectives that elevate the level of risk of a material misstatement to the financial statements.
4. Policies and procedures with respect to the review, supervision and monitoring of the accounting operations were not designed effectively, due to insufficient segregation of duties.
5. The Company did not maintain an adequate risk oversight function to evaluate and report on risks to financial reporting throughout the Company, including completion of a comprehensive risk assessment to identify all potential risk areas and evaluate the adequacy of controls to mitigate identified risk.

Item 1B. Unresolved Staff Comments

Not Applicable.

Item 2. Properties

During the fiscal year ended June 30, 2015 we operated out of three locations. Our corporate offices are located in an approximately 58,000 square foot leased facility in Wilmington, Massachusetts. In addition to our corporate offices, this facility houses research and development, sales and marketing, and production. Our current lease expires in June 2020. On March 25, 2015, our Board of Directors approved restructuring actions to better align costs with current and future geographic revenue sources and to improve efficiencies. We have exited from previous lease commitments for 2,000 square feet of research and office space in San Diego, California and 300 square feet of office space in Shanghai, China. We believe that our current facility is suitable for our anticipated requirements.

Item 3. Legal Proceedings

On March 23, 2015, Bernard Miller ("Mr. Miller"), individually and on behalf of all others similarly situated shareholders of the company, filed a complaint against Dr. William J. McGann, Messrs. Glenn D. Bolduc, John H. Hassett, John A. Keating, Robert P. Liscouski, Howard Safir and Michael C. Turmelle and the Company in the Suffolk Superior Court of the Commonwealth of Massachusetts, seeking derivative action as a result of director breaches of fiduciary duty and unjust enrichment. Amongst other things, the plaintiff requested that the court compel the Company to hold an annual stockholders' meeting; subject the September 2012 Amendment to the 2004 Plan to a vote at the next annual stockholders' meeting; rescind the stock option awards granted under the September 2012 Amendment to 2004 Plan in the event that the amendment is not approved by a majority of our stockholders'; impose a trust, in favor of the Company, for any benefits improperly received; and award costs and expenses, including reasonable attorney fees.

On July 1, 2015 we held our 2015 Annual Meeting of Stockholders. Stockholders approved an amendment to the Company's 2004 Stock Option Plan to increase the aggregate number of shares of the Company's common stock, par value $0.001 per share available for issuance under the Plan by 16,000,000 shares to 20,000,000 shares and approved the Company's Amended and Restated 2014 Stock Option Plan.

We believe the case was without merit and that we had substantial defenses against the plaintiff's claims. We are contesting the matter vigorously; on May 22, 2015, a motion to dismiss the Complaint with prejudice was served on the plaintiff and subsequently filed with the Court. On July 21, 2015, the Court endorsed as an Order of Stipulation the parties entered into. The Stipulation provides, among other things, that the Complaint is dismissed with prejudice and the Motion to Dismiss is moot. The sole matter to be decided is whether the Plaintiff or we will recover their respective attorney's fees and expenses incurred as a result of this litigation. We believe that an unfavorable outcome on the case is possible, but not probable and the amount of the loss is estimated at $280,000. If, however, Mr. Miller is ultimately successful, it could have a material adverse effect on our business and financial condition.

In January 2011, Fulong Integrated Technique, Ltd. filed a complaint against us in the Middlesex Superior Court of the Commonwealth of Massachusetts, alleging non-payment of amounts owed for services provided to us in connection with the sale of handheld explosives detection equipment to a customer in China in the first quarter of fiscal 2009. Fulong sought general monetary damages, other statutory damages, attorneys' fees and costs.

In March 2013, we entered into a settlement agreement with Fulong, which provided for the payment of $200,000 and the transfer of ownership of five QS-H150 detectors to Fulong. We recognized a non-cash benefit of $295,000 in general and administrative expenses in the year ended June 30, 2013 as a result of the settlement.

We may, from time to time, be involved in actual or potential proceedings that we consider to be in the normal course of our business. We do not believe that any of these proceedings will have a material adverse effect on our business. We are not a party to any other legal proceedings, other than ordinary routine litigation incidental to our business, which we believe will not have a material effect on our business, assets or results of operations.

Item 4. Mine Safety Disclosures

Not Applicable.

PART II

Item 5. Market Information for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Our common has been quoted on the Over-The-Counter-Bulletin Board since May 2009 and is also quoted on the OTC Markets Group's OTCQB tier under the symbol "IMSC". The following table sets forth the high and low bid quotations for our common stock for each of the last two fiscal years, as reported on the OTCQB. Quotations from the OTCQB reflect inter-dealer prices, without retail mark-up, mark-down or commission and may not necessarily represent actual transactions.

	Fiscal Year 2015	
	High	Low
4th Quarter	$ 0.87	$ 0.64
3rd Quarter	1.10	0.71
2nd Quarter	1.54	0.86
1st Quarter	1.82	0.94

	Fiscal Year 2014	
	High	Low
4th Quarter	$ 1.16	$ 0.90
3rd Quarter	1.08	0.72
2nd Quarter	1.20	0.77
1st Quarter	1.30	1.03

As of September 15, 2015, we had approximately 110 stockholders of record. The last sale price as reported on the OTC Bulletin Board on September 15, 2015, was $0.74. We have never paid a cash dividend on our common stock and do not anticipate the payment of cash dividends in the foreseeable future. In addition, our agreements with our secured lenders prohibit the payment of cash dividends.

Securities Authorized for Issuance under Equity Compensation Plans as of the End of Fiscal 2015

Equity Compensation Plan Information

The table below sets forth certain information as of June 30, 2015 with respect to equity compensation plans under which our common stock is authorized for issuance:

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted average exercise price of outstanding options warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by stockholders (1)	22,513,485	$ 1.22	10,945,000
Equity compensation plans not approved by stockholders	-	$ -	-
	22,513,485	$ 1.22	10,945,000

(1) This total includes shares to be issued upon exercise of outstanding options under the equity compensation plans that have been approved by our stockholders (i.e., our 2000 Incentive and Non-Qualified Stock Option Plan and our 2004 Stock Option Plan). Our 2004 Stock Option Plan has been approved by our stockholders. An amendment to our September 2012 plan increasing the number of shares issuable under the plan from 4,000,000 shares to 20,000,000 shares, was approved by our stockholders on July 1, 2015.

Our 2000 Incentive and Non-Qualified Stock Option Plan expired in October 2010 and our 2004 Stock Option Plan expired in May 2014. In July 2014, we adopted our 2014 Stock Option Plan and reserved 15,000,000 shares of common stock for issuance thereunder. The 2014 Stock Option Plan was approved by our stockholders on July 1, 2015.

Recent Sales of Unregistered Securities

In June 2015, we issued 550,000 shares of common stock, having a value of $412,000, to two advisors, in consideration of services rendered to us under two advisory and consulting services agreements. The issuance of these shares was exempt from registration under the Securities Act pursuant to an exemption provided by Section 4(2) of the Securities Act.

Item 6. Selected Financial Data

You should read the following selected financial information together with our financial statements and related notes and "Management's Discussion and Analysis of Financial Condition and Results of Operations" also included in this Form 10-K. We have derived the statement of operations and comprehensive loss data for the years ended June 30, 2015, June 30, 2014 and June 30, 2013, and the balance sheet information at June 30, 2015 and June 30, 2014 from our audited financial statements included in this Form 10-K. We have derived the statements of operations and comprehensive loss data for the years ended June 30, 2012 and June 30, 2011, and the balance sheet data at June 30, 2013, June 30, 2012 and June 30, 2011, from our audited financial statements not included in this Form 10-K.

Statement of Operations Data

	For the Year Ended June 30,				
(In thousands, except share and per share amounts)	**2015**	**2014**	**2013**	**2012**	**2011**
Revenues	$ 12,991	$ 8,552	$ 12,017	$ 3,406	$ 6,652
Cost of revenues	8,472	6,498	8,588	2,407	4,011
Gross margin	4,519	2,054	3,429	999	2,641
Operating expenses	17,215	16,175	25,384	11,755	8,465
Loss from operations	(12,696)	(14,121)	(21,955)	(10,756)	(5,824)
Other expense, net	(8,847)	(6,889)	(5,399)	(3,880)	(9,731)
Net loss	$ (21,543)	$ (21,010)	$ (27,354)	$ (14,636)	$ (15,554)
Net loss per share, basic and diluted	$ (0.30)	$ (0.35)	$ (0.56)	$ (0.43)	$ (0.56)
Weighted average shares used in computing basic and diluted earnings per share	70,770,705	60,753,054	49,124,942	34,242,719	27,731,343
Other financial and operating data:					
Depreciation and amortization	$ 171	$ 154	$ 84	$ 72	$ 91
Capital expenditures	$ 433	$ 409	$ 151	$ 162	$ 59

Balance Sheet Data

	As of June 30,				
(In thousands)	**2015**	**2014**	**2013**	**2012**	**2011**
Cash and cash equivalents	$ 1,985	$ 391	$ 80	$ 84	$ 264
Total assets	$ 10,392	$ 5,479	$ 5,098	$ 6,236	$ 6,160
Borrowings under senior secured promissory notes, line of credit and current maturities under capital leases	$ 64,891	$ 51,224	$ 40,649	$ 30,479	$ 20,405
Long-term obligations	$ 289	$ 208	$ 89	$ 33	$ 58
Stockholders' deficit	$ (78,177)	$ (61,205)	$ (44,548)	$ (32,404)	$ (20,891)

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations Overview

Since our incorporation in 1984, we have operated as a multi-faceted company engaging in the development of ion-based technologies and providing commercial services and products to the semiconductor, medical device and security industries. In fiscal 2009, we completed the divestiture of our semiconductor and medical business activities in order to focus on our security business.

Since 1999, we have been performing research to improve explosives trace detection ("ETD") technology, and developing ETD products which can be used for detection of trace amounts of explosives. More recently, we have adapted this technology for the detection of narcotics ("NDT"). We now develop, manufacture and sell sophisticated sensors and systems for the security, safety and defense industries. We have developed handheld ETD systems, which have been marketed and sold both domestically and internationally, and a desktop ETD and NTD system which we began shipping commercially in the third quarter of fiscal 2012. These systems are used by private companies and government agencies to screen baggage, cargo, other objects and people, for the detection of trace amounts of explosives.

Critical Accounting Policies

Our significant accounting policies are described in Note 2 to the consolidated financial statements included in Item 8 of this Annual Report on Form 10-K for the fiscal year ended June 30, 2015. Our discussion and analysis of our financial condition and results of operations are based upon these financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, we evaluate our estimates, including those related to bad debts, product returns, inventories, investments, derivative liabilities, conversion features of our debt agreements and warranty obligations. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. In the past, actual results have not been materially different from our estimates. However, results may differ from these estimates under different assumptions or conditions.

We have identified the following as critical accounting policies, based on the significant judgments and estimates used in determining the amounts reported in our financial statements:

- *Revenue Recognition.* We recognize revenue when there is persuasive evidence of an arrangement with the customer that states a fixed or determinable price and terms, delivery of the product has occurred or the service performed is in accordance with the terms of the arrangement, and collectibility of the sale is reasonably assured. Revenues for which we have received payment, but are due to obligations under the sales agreement, are reflected on our balance sheet as deferred revenues. We allocate consideration for each deliverable as a separate unit of accounting based on its relative selling price. We determine selling price using vendor specific objective evidence ("VSOE"), if it exists, and otherwise third party evidence ("TPE"). If neither VSOE nor TPE of selling price exists for a unit of accounting, we use estimated selling price ("ESP"). We generally expect that we will not be able to determine TPE due to the nature of the markets in which we compete, and, as such, we typically determine selling price using VSOE or if not available, ESP. VSOE is the price charged when the same or similar product or service is sold separately. If a product or service is seldom sold separately, it is unlikely that we can determine VSOE for the product or service. TPE is determined based on prices charged by competitors of us for a similar deliverable when sold separately. Generally we are not able to use TPE, as we are usually not able to obtain sufficient information on competitor pricing to substantiate TPE. The objective of ESP is to determine the price at which we would transact if the product or service were sold on a standalone basis. We determine ESP for product or services based on the specific facts and circumstances of the arrangement. Maintenance or service revenues are recognized over the term of the contract.

- *Accounts Receivable and Allowance for Doubtful Accounts.* We maintain allowances for estimated losses resulting from the inability of our customers to make required payments. Judgments are used in determining the allowance for doubtful accounts and are based on a combination of factors. Such factors include historical collection experience, credit policy and specific customer collection issues. In circumstances where we are aware of a specific customer's inability to meet its financial obligations to us (e.g., due to a bankruptcy filing), we record a specific reserve for bad debts against amounts due to reduce the net recognized receivable to the amount we reasonably believe will be collected. We perform ongoing credit evaluations of our customers and continuously monitor collections and payments from our customers.

While actual bad debts have historically been within our expectations and the provisions established, we cannot guarantee that we will continue to experience the same bad debt rates that we have in the past. A significant change in the liquidity or financial position of any of our customers could result in the uncollectibility of the related accounts receivable and could adversely impact our operating cash flows in that period.

- *Inventories.* We value our inventories at lower of cost or market. Cost is determined by the first-in, first-out (FIFO) method, including material, labor and factory overhead. In assessing the ultimate realization of inventories, management judgment is required to determine the reserve for obsolete or excess inventory. Inventory on hand may exceed future demand either because the product is obsolete, or because the amount on hand is more than can be used to meet future needs. We provide for the total value of inventories that we determine to be obsolete or excess based on criteria such as customer demand and changing technologies. We historically have not experienced significant inaccuracies in computing our reserves for obsolete or excess inventory.

- *Warranties.* We provide for the estimated cost of product warranties at the time revenue is recognized. We record an estimate for warranty related costs at the time of sale based on our actual historical return rates and repair costs. While our warranty costs have historically been within our expectations and the provisions established, we cannot guarantee that we will continue to experience the same warranty return rates or repair costs that we have in the past. A significant increase in warranty return rates or costs to repair our products could have a material adverse impact on our operating results for the period or periods in which such returns or additional costs materialize.

- *Income Taxes.* Significant management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities and any valuation allowance recorded against deferred tax assets. We have recorded a full valuation allowance against our net deferred tax assets of $49,795,000 as of June 30, 2015, due to uncertainties related to our ability to utilize these assets. The valuation allowance is based on our estimates of taxable income and the period over which our deferred tax assets will be recoverable. In the event that actual results differ from these estimates or we adjust these estimates in future periods we may need to adjust our valuation allowance which could materially impact our financial position and results of operations.

- *Equity Transactions.* We evaluate the proper classification of our equity instruments that embody an unconditional obligation requiring the issuer to redeem it by transferring assets at a determinable date or that contain certain conditional obligations, typically classified as equity, be classified as a liability. We record financing costs associated with our capital raising efforts in our statements of operations. These include amortization of debt issue costs such as cash, warrants and other securities issued to finders and placement agents, and amortization of preferred stock discount created by in-the-money conversion features on convertible debt and allocates the proceeds amongst the securities based on relative fair values or based upon the residual method. We based our estimates and assumptions on the best information available at the time of valuation, however, changes in these estimates and assumptions could have a material effect on the valuation of the underlying instruments.

- *Stock-Based Compensation.* We account for employee and non-employee director stock-based compensation using the fair value method of accounting. Compensation cost arising from stock options to employees and non-employee directors is recognized using the straight-line method over the vesting period, which represents the requisite service or performance period. The calculation of stock-based compensation requires us to estimate several factors, most notably the term, volatility and forfeitures. We estimate the option term using historical terms and estimate volatility based on historical volatility of our common stock over the option's expected term. Expected forfeitures based on historical forfeitures in calculating the expense related to stock-based compensation associated with stock awards. Our estimates and assumptions are based on the best information available at the time of valuation, however, changes in these estimates and assumptions could have a material effect on the valuation of the underlying instruments.

Results of Operations

For the Year Ended June 30, 2015 vs. June 30, 2014

Revenues

	For the Year Ended June 30, 2015		For the Year Ended June 30, 2014		
(In thousands)	Amount	Mix	Amount	Mix	Change %
QS-H150	$ 3,464	26.7 %	$ 4,060	47.5 %	(14.7)%
QS-B220	8,511	65.5 %	3,907	45.7 %	117.8 %
Parts & supplies	1,016	7.8 %	585	6.8 %	73.7 %
Total	$ 12,991	100.0 %	$ 8,552	100.0 %	51.9 %

Revenues for the year ended June 30, 2015 were $12,991,000 as compared with $8,552,000 for the comparable prior year period, an increase of $4,439,000, or 51.9%. The increase in revenue is due primarily to the 139.7% increase in the number of QS-B220 desktop units sold in the year ended June 30, 2015, due to increased shipments to European airports, due to the ECAC mandate to implement passenger checkpoint and checked baggage ETD screening at airports serving more than 500,000 passengers annually, by no later than September 1, 2015, increased shipments to U.S. air cargo screening facilities, increased shipments into Latin America for use in drug detection and increased shipments to agencies of the U.S. government, which resulted in a 117.8% increase in QS-B220 revenues and, to a lesser extent, a 73.7% increase in sales of parts and supplies in the year ended June 30, 2015, as compared to the comparable prior year period. Partially offsetting these increases are a 9.6% decrease in the number of QS-H150 handheld units sold in the year ended June 30, 2015, primarily due to decreased shipments into Mexico and China in the year ended June 30, 2015, which resulted in a 14.7% decrease in QS-H150 revenues. The average unit sell prices on sales of our QS-B220 desktop units and on sales of our QS-H150 handheld units, decreased 9.1% and 5.6%, respectively, in the current fiscal period as compared to the comparable prior period.

Sales of QS-B220 were favorably impacted in the current period due to the acceptance of the QS-B220 into the "Qualified" section of the TSA's Air Cargo Screening Technology List and achieving European Civil Aviation Conference ("ECAC") Common Evaluation Process of Security Equipment for airport checkpoint screening of passengers and baggage. Competitive market conditions are expected to continue to have a negative impact on our average unit sales prices for the foreseeable future.

Cost of Revenues

Cost of revenues for the year ended June 30, 2015 were $8,472,000 as compared with $6,498,000 for the comparable prior year period, an increase of $1,974,000 or 30.4%. The increase in cost of revenues recorded in the year ended June 30, 2015 is primarily due to increased unit sales of our QS-B220 desktop units and a $71,000 increase in stock-based compensation, due primarily to the accelerated vesting of certain options issued on July 2, 2014, partially offset by a $150,000 decrease in royalty costs, as compared to the prior year period.

Gross Margin

Gross margin for the year ended June 30, 2015 was $4,519,000 or 34.8% of revenues as compared with $2,054,000 or 24.0% of revenues for the comparable prior year period. The increase in gross margin as a percent of revenues is primarily due to increased manufacturing overhead absorption due to increased QS-B220 unit volume and a $150,000 decrease in royalty costs, partially offset by a decrease in the average unit sell price on sales of our QS-B220 desktop units and on sales of our QS-H150 handheld units, which decreased 9.1% and 5.6%, respectively and by a $71,000 increase in stock-based compensation.

Research and Development Expense

Research and development expense for the year ended June 30, 2015 was $5,014,000 as compared with $4,787,000 for the comparable prior year period, an increase of $227,000 or 4.7%. The increase in research and development expense is due primarily to a $151,000 increase in payroll and related benefit costs due to the increased employee bonuses approved by the board of directors, a $69,000 increase in travel cost in support of our sales process in Europe, $42,000 of costs incurred to relocate the San Diego, CA advanced technology office, and a $69,000 increase in stock-based compensation, due primarily to the accelerated vesting of certain options issued on July 2, 2014, offset partially by a $111,000 decrease in engineering consulting. We continue to expend funds to further the development of new products in the areas of explosives and narcotics detection, as well as expenses

incurred to obtain the necessary approvals from the TSA and other non-U.S. government approvals. Spending on research and development will increase in the next nine to twelve months due to the ongoing development of the QS-B220 desktop detector, the development of the QS-H150E portable explosives and narcotics detector and continued development of a hyphenated system employing conventional ion mobility, differential mobility and quadrupole mass spectrometry.

Selling, General and Administrative Expenses

Selling, general and administrative expenses for the year ended June 30, 2015 were $12,201,000 as compared with $11,388,000 for the comparable prior year period, an increase of $813,000, or 7.1%. The increase in selling, general and administrative expenses is due primarily to a $1,196,000 increase in payroll and related benefits due primarily to separation benefits of $725,000 provided to our former CEO due to his resignation, and to a lesser extent, $331,000 of bonuses approved by the board of directors, $274,000 of charges incurred pursuant to our Letter Agreement with Luveti, a $214,000 increase in legal expenses, a $125,000 increase in consulting expenses, due to the issuance of 550,000 shares of our common stock to certain consultants, a $75,000 increase in variable selling expenses, a $46,000 increase in bad debt expenses and $28,000 of restructuring cost incurred to close our Shanghai office. Partially offsetting these increases are a $697,000 decrease in stock-based compensation expense on non-employee warrants, a $93,000 decrease in travel expenses, a $109,000 decrease in stock-based compensation on employee stock options, a $97,000 decrease in occupancy costs due to the relocation of our corporate offices in July 2013 and the $47,000 loss on the disposal of machinery and equipment recorded in the prior year period.

Other Expense, net

For the year ended June 30, 2015, other expense was $8,847,000 as compared with other expense of $6,889,000, for the comparable prior year period, an increase of $1,958,000. The increase is due to increased interest expense on higher borrowings under our credit facility with DMRJ and our credit facility with BAM, and, to a lesser extent, an increase in the BAM interest rate to 16% per annum from 15% per annum, effective April 1, 2015.

Net Loss

Our net loss for the year ended June 30, 2015 was $21,543,000 as compared with a net loss of $21,010,000 for the comparable prior year period, an increase of $533,000, or 2.5%. The increase in the net loss is primarily due to increased operating expenses and increased interest expense.

For the Year Ended June 30, 2014 vs. June 30, 2013

Revenues

	For the Year Ended June 30, 2014			For the Year Ended June 30, 2013			
(In thousands)	Amount	Mix		Amount	Mix		Change %
QS-H150	$ 4,060	47.5	%	$ 9,561	79.6	%	(57.5)%
QS-B220	3,907	45.7	%	1,270	10.6	%	207.6 %
Parts & supplies	585	6.8	%	1,186	9.8	%	(50.7)%
Total	$ 8,552	100.0	%	$ 12,017	100.0	%	(28.8)%

Revenues for the year ended June 30, 2014 were $8,552,000 as compared with $12,017,000 for the comparable prior year period, a decrease of $3,465,000, or 28.8%. The decrease in revenue is due primarily to a 55.4% decrease in the number of QS-H150 handheld units sold in the year ended June 30, 2014, primarily due to the shipment of QS-H150 handheld units under our contract with the India Ministry of Defence in the year ended June 30, 2013, which resulted in a 57.5% decrease in QS-H150 revenues, and, to a lesser extent, decreased sales of parts and supplies in the year ended June 30, 2014, as compared to the comparable prior year period, and a 4.7% decrease in the average unit sell prices on sales of our QS-H150 handheld units, partially offset by a 210.3% increase in the number of QS-B220 desktop units sold in the year ended June 30, 2014, due to increased shipments to U.S. air cargo screening facilities, increased shipments into Latin America, Europe and agencies of the U.S. government, which resulted in a 207.6% increase in QS-B220 revenues.

Cost of Revenues

Cost of revenues for the year ended June 30, 2014 were $6,498,000 as compared with $8,588,000 for the comparable prior year period, a decrease of $2,090,000 or 24.3%. The decrease in cost of revenues recorded in the year ended June 30, 2014 is primarily due to decreased unit sales of our QS-H150 handheld units and a $664,000 decrease in stock-based compensation recorded on stock option grants to officers and directors in September 2012, partially offset by a $796,000 increase in manufacturing overhead due to an increase in manufacturing personnel

costs and increased occupancy costs, as compared to the prior year period and a $160,000 increase in our provision for obsolete inventories.

Gross Margin

Gross margin for the year ended June 30, 2014 was $2,054,000 or 24.0% of revenues as compared with $3,429,000 or 28.5% of revenues for the comparable prior year period. The decrease in gross margin as a percent of revenues is primarily the result of increased manufacturing overhead due to a $796,000 increase in manufacturing personnel costs and increased occupancy costs, a $160,000 increase in our provision for obsolete inventory, partially offset by the $664,000 decrease in stock-based compensation recorded on stock option grants to officers and directors in September 2012, as compared to the prior year period.

Research and Development Expense

Research and development expense for the year ended June 30, 2014 was $4,787,000 as compared with $4,754,000 for the comparable prior year period, an increase of $33,000 or 0.7%. The increase in research and development expense is due primarily to a $360,000 increase in payroll and related benefit costs, a $194,000 increase in occupancy costs, a $54,000 increase in government testing fees and a $82,000 increase in prototype expense, offset partially by a $626,000 decrease in stock-based compensation recorded on the September 2012 officer and director option grants and a $32,000 decrease in material costs. We continue to expend funds to further the development of new products in the areas of explosives and narcotics detection, as well as expenses incurred to obtain the necessary approvals from the TSA and other non-U.S. government approvals. Spending on research and development will increase in the next nine to twelve months due to the ongoing development of the QS-B220 desktop detector, the development of the QS-H150E portable explosives and narcotics detector and continued development of a hyphenated system employing conventional ion mobility, differential mobility and quadrupole mass spectrometry.

Selling, General and Administrative Expenses

Selling, general and administrative expenses for the year ended June 30, 2014 were $11,388,000 as compared with $20,630,000 for the comparable prior year period, a decrease of $9,242,000, or 44.8%. The decrease in selling, general and administrative expenses is due primarily to a $9,969,000 decrease in stock-based compensation recorded on the September 2012 officer and director option grants, the imposition of liquidated damages of $298,000 under our contract with the India Ministry of Defence in the prior year period, a $174,000 decrease in bank charges, a $261,000 decrease in legal expenses, offset partially by a $399,000 increase in payroll, related benefit costs and travel expense resulting from the addition of sales personnel, a $649,000 increase in occupancy costs, due to the relocation of our corporate offices, the $295,000 benefit recognized as a result of the litigation settlement with Fulong in the prior year period, a $297,000 increase in stock-based compensation on non-employee warrants, a $62,000 increase in variable selling expenses due to increased non-employee sales commissions, a $191,000 increase in selling expenses due to the opening of our Shanghai representative office, increased participation at industry trade shows and an increase in demonstration units provided to our sales force and a $64,000 increase in depreciation expense.

Other Expense, net

For the year ended June 30, 2014, other expense was $6,889,000 as compared with other expense of $5,399,000, for the comparable prior year period, an increase of $1,490,000. The increase is due to increased interest expense on higher borrowings under our credit facilities.

Net Loss

Our net loss for the year ended June 30, 2014 was $21,010,000 as compared with a net loss of $27,354,000 for the comparable prior year period, a decrease of $6,344,000, or 23.2%. The decrease in the net loss is primarily due to the decrease in stock-based compensation recorded on the September 2012 officer and director option grants in the year ended June 30, 2014, partially offset by increased operating expenses and increased interest expense.

Liquidity and Capital Resources

As of June 30, 2015, we had cash of approximately $1,985,000, an increase of $1,594,000 when compared with cash of $391,000 at June 30, 2014.

We will be required to repay all of our borrowings from DMRJ, Montsant and from a group of institutional investors for which BAM Administrative Services LLC ("BAM") acts as administrative agent, on March 31, 2016. Our obligations to BAM are secured by a security interest in substantially all of our assets. DMRJ and Montsant agreed to subordinate their security interest in all of our assets to the security interest held by BAM (See Note 13).

As of June 30, 2015, our obligations to DMRJ under each of the three promissory notes and a revolving line of credit approximated $12,000,000, $12,000,000, $1,000,000 and $16,662,000, respectively. Further, as of June 30, 2015, our obligation to DMRJ for accrued interest under these instruments approximated $11,350,000 and is included in current liabilities in the consolidated financial statements.

As of June 30, 2015, our obligations to Montsant under a promissory note approximated $3,184,000. Further, as of June 30, 2015, our obligation to Montsant for accrued interest under this instrument approximated $1,860,000 and is included in current liabilities in the consolidated financial statements.

As of June 30, 2015, our obligations under the senior secured promissory notes for which BAM is the agent were $20,000,000. Further, as of June 30, 2015, our obligation under such notes for accrued interest amounted to approximately $54,000 and is included in current liabilities in the consolidated financial statements.

As of September 15, 2015, our obligations to DMRJ under each of the three promissory notes and a revolving line of credit approximated $12,000,000, $12,000,000, $1,000,000 and $16,862,000, respectively. Further, as of September 15, 2015, our obligation to DMRJ for accrued interest under these instruments approximated $12,692,000.

As of September 15, 2015, our obligations to Montsant under a promissory note approximated $3,184,000. Further, as of September 15, 2015, our obligation to Montsant for accrued interest under this instrument approximated $1,963,000.

As of September 15, 2015, our obligations under the senior secured promissory notes for which BAM is the agent were $20,000,000. Further, as of September 15, 2015, our obligation under such notes for accrued interest amounted to approximately $738,000.

For the Year Ended June 30, 2015 vs. June 30, 2014

For the year ended June 30, 2015, we had net cash outflows of $12,150,000 from operating activities as compared to net cash outflows from operating activities of $9,989,000 for the comparable prior year period. The $2,161,000 increase in net cash outflows used in operating activities during the year ended June 30, 2015, as compared to the comparable prior year period, was due to the following changes in working capital: (i) a $375,000 increase in accounts receivable, compared to a $669,000 decrease in the prior period, due to the timing of our product shipments in the year ended June 30, 2015; (ii) a $2,376,000 increase in inventories compared to a $723,000 increase in the prior period, due primarily to increased QS-B220 raw material inventory purchased in the quarter ended June 30, 2015 to fulfill ECAC customer orders, shipment of which is required in our first quarter of fiscal 2016; (iii) an increase in accrued expenses of $6,834,000, compared to a $4,703,000 increase in the prior period, due to higher borrowings under our credit facilities with DMRJ and BAM, and to a lesser extent, by an increase in accrued expenses in the current period due to costs incurred due to the resignation of our former CEO and the Luveti Letter Agreement, partially offset by the payment of $3,905,000 of interest on our borrowings with BAM in the year ended June 30, 2015 and an increase in accrued compensation and benefits, due to bonuses approved by our board of directors; (iv) a $3,050,000 increase in deferred revenue, compared to a $516,000 increase in deferred revenue in the prior year period, due primarily to advance payment received from ECAC customers in the year ended June 30, 2015 and increased deferrals of extended warranty revenues; (v) an $612,000 increase in prepaid expenses, compared to a $85,000 decrease in prepaid expenses, due to increased advance payments required from several of our QS-B220 component suppliers; and, (vi) an $820,000 decrease in accounts payable, compared to a $1,522,000 increase in the prior period, due to the timing of payments to our inventory supply chain.

For the year ended June 30, 2015, we had net cash outflows of $176,000 from investing activities as compared to net cash outflows of $287,000 from investing activities for the prior year period. The $111,000 decrease in net cash used in investing activities during the year ended June 30, 2015, as compared to the prior year period, was primarily due an increase in restricted funds of $257,000 received in the year ended June 30, 2015, compared to $121,000 of restricted funds received in the prior comparable period, due to the receipt of restricted funds which had collateralized a certain performance security bond with the India Ministry of Defence, which bond was released on May 1, 2015, partially offset by a $24,000 decrease in cash expended for the purchase of equipment.

For the year ended June 30, 2015 we had net cash inflows of $13,919,000 from financing activities as compared to net cash inflows of $10,585,000 for the comparable prior year period. The $3,334,000 increase in net cash from financing activities during the year ended June 30, 2015, as compared to the prior year period, was primarily due to $13,667,000 in borrowings under our credit facility with DMRJ, compared to a net increase of $10,592,000 in borrowings under our credit facilities with DMRJ and BAM, due to the receipt of $20,000,000 under the note purchase agreement with BAM on March 19, 2014 and a $9,408,000 decrease in borrowings under our credit facility with DMRJ due primarily to the March 19, 2014 BAM borrowing , and a $239,000 increase in proceeds received due to the exercise of stock options and warrants.

For the Year Ended June 30, 2014 vs. June 30, 2013

For the year ended June 30, 2014, we had net cash outflows of $9,989,000 from operating activities as compared to net cash outflows from operating activities of $10,890,000 for the comparable prior year period. The $901,000 decrease in net cash outflows used in operating activities during the year ended June 30, 2014, as compared to the comparable prior year period, was due to the following changes in working capital: (i) a $669,000 decrease in accounts receivable, compared to a $1,035,000 increase in the prior period, due to the timing of our product shipments during the year ended June 30, 2012; (ii) a $723,000 increase in inventories compared to a $1,048,000 decrease in the prior period, due primarily to the November 2012 shipment of our order with India Ministry of Defence and increased QS-B220 inventory; (iii) an increase in accrued expenses of $4,703,000, compared to a $2,569,000 increase in the prior period, due to primarily to increased accruals for unpaid interest on borrowings from our secured lenders; (iv) a $516,000 increase in deferred revenue, compared to a $972,000 decrease in deferred revenue in the prior year period, due primarily to the release of the India Ministry of Defence advance deposit due to the November 2012 shipment and increased deferrals of extended warranty revenues; (v) an $85,000 decrease in prepaid expenses, compared to a $455,000 decrease in prepaid expenses, due to the decreases in prepaid inventory; and, (vi) a $1,522,000 increase in accounts payable, compared to a $305,000 decrease in the prior period, due to increased operating expenses and increased inventories.

For the year ended June 30, 2014, we had net cash outflows of $287,000 from investing activities as compared to net cash inflows of $710,000 from investing activities for the prior year period. The $997,000 increase in net cash used in investing activities during the year ended June 30, 2014, as compared to the prior year period, was primarily due to the receipt of $121,000 in restricted funds, compared to the receipt of restricted funds of $841,000 in the prior year period, primarily due to the cancelation of the letter of credit providing security for the India Ministry of Defence advance deposit resulted in the release of $937,000 held in a restricted deposit, by a $258,000 increase in purchases of equipment and fixtures, due to the July 2013 move to our new corporate offices and the build out of our manufacturing facility and a $19,000 decrease in proceeds from the sale of equipment.

For the year ended June 30, 2014 we had net cash inflows of $10,585,000 from financing activities as compared to net cash inflows of $10,176,000 from financing activities for the comparable prior year period. The $409,000 increase in net cash from financing activities during the year ended June 30, 2014, as compared to the comparable prior year period, was primarily due to the receipt of $20,000,000 under a note purchase agreement with several institutional investors, a $9,408,000 decrease in borrowings under our credit facility with DMRJ, compared to an increase in borrowings of $10,172,000 in the prior fiscal year, due to the repayment of the DMRJ line of credit from the BAM loan proceeds and a $30,000 increase in proceeds received due to the exercise of stock options, partially offset by a $41,000 increase in principal repayments of capital lease obligations.

Credit Facilities with DMRJ Group LLC, Montsant Partners LLC and BAM Administrative Services LLC

In December 2008, we entered into a note and warrant purchase agreement with DMRJ, pursuant to which we issued a senior secured convertible promissory note in the principal amount of $5,600,000 and a warrant to purchase 1,000,000 shares of our common stock. Thereafter, we entered into a series of amendments, waivers and modifications of this facility. The notes mature on March 31, 2016.

On May 4, 2015, we entered into an assignment agreement with DMRJ and Montsant, wherein DMRJ assigned its rights, title and interest in the senior secured promissory note dated December 10, 2008 and appointed DMRJ as its collateral agent under the promissory note agreement. The note matures on March 31, 2016. DMRJ and Montsant are funds managed by Platinum Partners Value Arbitrage Fund LP.

In March, 2014, we entered into a note purchase agreement with a group of institutional investors and BAM, an administrative agent for the investors, pursuant to which we issued senior secured promissory notes in the aggregate principal amount of $20,000,000. The notes bear interest at 16% per annum and mature on March 31, 2016. We used all of the proceeds from the sale of the notes to repay (i) $17,624,000 of our outstanding indebtedness to DMRJ under revolving promissory note (ii) $1,809,000 of interest outstanding under that facility and (iii) $567,000 of interest outstanding under our senior secured convertible promissory note.

See Note 13 of Notes to Consolidated Financial Statements, accompanying this Annual Report. There can be no assurance that we will be successful in refinancing or extending our obligations to our secured lenders.

Our ability to comply with our debt covenants in the future depends on our ability to generate sufficient sales and to control expenses, and will require that we seek additional capital through private financing sources. There can be no assurances that we will achieve our forecasted financial results or that we will be able to raise additional capital to operate our business. Any such failure would have a material adverse impact on our liquidity and financial condition and could force us to curtail or discontinue operations entirely. Further, upon the occurrence of an event of default under certain provisions of our credit agreements, we could be required to pay default rate

interest equal to the lesser of 2.5% per month and the maximum applicable legal rate per annum on the outstanding principal balance outstanding. The failure to refinance or otherwise negotiate further extensions of our obligations to our secured lenders would have a material adverse impact on our liquidity and financial condition and could force us to curtail or discontinue operations entirely and/or file for protection under bankruptcy laws.

Any failure to comply with our debt covenants, to achieve our projections and/or obtain sufficient capital on acceptable terms would have a material adverse impact on our liquidity, financial condition and operations and could force us to curtail or discontinue operations entirely and/or file for protection under bankruptcy laws. Further, upon the occurrence of an event of default under certain provisions of our agreements with our secured lenders, we could be required to pay default rate interest equal to the lesser of 2.5% per month and the maximum applicable legal rate per annum on the outstanding principal balance outstanding.

Based on current sales, operating expense and cash flow projections, and the cash available from our line of credit, management believes there are plans in place to sustain operations for the next several months. These plans depend on a substantial increase in sales of our handheld trace explosives detector product and our desktop explosives and narcotics trade detector product. However, there can be no assurances that sales will materialize as forecasted, and/or that management will be successful in refinancing or extending our obligations to our secured lenders, which mature on March 31, 2016. To further sustain us, improve our cash position, and enable us to grow while reducing debt, management plans to continue to seek additional capital through private financing sources. However, there can be no assurance that management will be successful in executing these plans. Management will continue to closely monitor and attempt to control our costs and actively seek needed capital through sales of our products, equity infusions, government grants and awards, strategic alliances, and through our lenders.

Despite our current sales, expense and cash flow projections and the cash available from our line of credit with DMRJ, we will require additional capital in the third quarter of fiscal 2016 to fund operations and continue the development, commercialization and marketing of our products. Our failure to achieve our projections and/or obtain sufficient additional capital on acceptable terms would have a material adverse effect on our liquidity and operations and could require us to file for protection under bankruptcy laws. These conditions raise substantial doubt as to our ability to continue as a going concern.

We intend to explore available strategic alternatives in fiscal 2016 to provide and enhance the financial stability of the company, but there can be no assurances that these efforts will be successful.

Off-Balance Sheet Arrangements

As of June 30, 2015, we had one irrevocable standby letter of credit outstanding in the approximate amount of $297,000. The letter of credit provides warranty performance security equal to 5% of the contract amount with the India Ministry of Defence. We have amended the letter of credit, extending the expiration date to May 4, 2015. On May 1, 2015, we obtained the release of the performance security bond, which expired on November 4, 2014, from the India Ministry of Defence and received the collateralized deposit.

As of June 30, 2015, we did not have any other off-balance sheet arrangements that have, or are reasonably likely to have, a current or future material effect on our consolidated financial condition, results of operations, liquidity, capital expenditures or capital resources.

Recent Accounting Pronouncements

In May 2014, the FASB issued Accounting Standards Update 2014-09, *Revenue from Contracts with Customers* ("ASU 2014-09"), which supersedes the revenue recognition requirements in ASC 605, *"Revenue Recognition"*. The FASB issued ASU 2014-09 to clarify the principles for recognizing revenue and to develop a common revenue standard for U.S. GAAP and International Financial Reporting Standards. The core principle of this updated guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The new rule also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. This guidance is effective for annual reporting periods beginning after December 15, 2016, including interim reporting periods therein, which is effective for our fiscal year beginning July 1, 2017, the first day of our 2018 fiscal year. We are currently evaluating the impact of this accounting guidance and do not expect any significant impact on our consolidated financial statements.

In June 2014, the FASB issued Accounting Standards Update 2014-12, *Compensation-Stock Compensation* ("ASU 2014-12"). The FASB issued ASU 2014-12 to provide specific guidance on share-based payment awards that provide for achievement of a specific performance target that could be achieved after the requisite service

period. ASU 2014-12 requires that a performance target that affects vesting and that could be achieved after the requisite service period should be treated as a performance condition. As such, the performance target should not be reflected in estimating the grant-date fair value of the award. Compensation cost should be recognized in the period in which it becomes probable that the performance target will be achieved and should represent the compensation cost attributable to the period(s) for which the requisite service has already been rendered. This guidance is effective for annual periods and interim periods within those annual periods beginning after December 15, 2015, which is effective for our fiscal year beginning July 1, 2016, the first day of our 2017 fiscal year. Earlier adoption is permitted. ASU 2014-12 may be applied prospectively to all awards granted or modified after the effective date or retrospectively to all awards with performance targets that are outstanding as of the beginning of the earliest annual period presented in the financial statements and to all new or modified awards thereafter. If retrospective transition is adopted, the cumulative effect of applying this guidance should be recognized in the financial statements as an adjustment to the opening retained earnings balance at that date. We are currently evaluating the impact of this accounting guidance and do not expect any significant impact on our consolidated financial statements.

In August 2014, the FASB issued Accounting Standards Update 2014-15, *Presentation of Financial Statements-Going Concern (Subtopic 205-40)* ("ASU 2014-15"). ASU 2014-15 provides guidance to U.S. GAAP about management's responsibility to evaluate whether there is a substantial doubt about an entity's ability to continue as a going concern and to provide related footnote disclosures. This new rule requires management to assess an entity's ability to continue as a going concern by incorporating and expanding upon certain principles currently in U.S. auditing standards. Specifically, ASU 2014-15 (1) defines the term substantial doubt, (2) requires an evaluation of every reporting period including interim periods, (3) provides principles for considering the mitigating effect of management's plan, (4) requires certain disclosures when substantial doubt is alleviated as a result of consideration of management's plans, (5) requires an express statement and other disclosures when substantial doubt is not alleviated, and (6) requires an assessment for a period of one year after the date that the financial statements are issued. This guidance is effective for annual periods ending after December 15, 2016, which is effective for our fiscal year beginning July 1, 2016, the first day of our 2017 fiscal year. We are currently evaluating the impact of this accounting guidance and do not expect any significant impact on our consolidated financial statements.

In July 2015, the FASB issued Accounting Standards Update 2015-11, *Inventory (Topic 330)* ("ASU 2015-11"). ASU 2015-11 was issued to more closely align the measurement of inventory in U.S. GAAP with the measurement of inventory in International Financial Reporting Standards. The core principle of this updated guidance is that an entity should measure inventory at the lower of cost or net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. The amendments in ASU 2015-11 apply to inventory that is measured using the first-in, first-out or average cost methods. ASU 2015-11 amends some of the guidance in Topic 330 to more clearly articulate the requirements for the measurement and disclosure of inventory, but the clarifications are not intended to result in any changes in practice other than the change in the subsequent measurement guidance from the lower of cost or market to the lower of cost or net realizable value for inventory. There are no other substantive changes to the guidance on the measurement of inventory. This guidance is effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years, which is effective for our fiscal year beginning July 1, 2017, the first day of our 2018 fiscal year. We are currently evaluation the impact of this accounting guidance and do not expect any significant impact on our consolidated financial statements.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

Not Applicable.

Item 8. Financial Statements and Supplementary Data

The following documents are filed as part of this report on Form 10-K

	Page
Report of Marcum LLP, Independent Registered Public Accounting Firm	F-1
Consolidated Balance Sheets at June 30, 2015 and 2014	F-2
Consolidated Statements of Operations and Comprehensive Loss for the years ended June 30, 2015, 2014 and 2013	F-3
Consolidated Statements of Stockholders' Deficit for the years ended June 30, 2015, 2014 and 2013	F-4
Consolidated Statements of Cash Flows for the years ended June 30, 2015, 2014 and 2013	F-5
Notes to Consolidated Financial Statements	F-6

Item 9. Changes In and Disagreements With Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

The certifications of our Chief Executive Officer and Chief Financial Officer attached as Exhibits 31.1 and 31.2 to this Annual Report on Form 10-K include, in paragraph 4 of such certifications, information concerning our disclosure controls and procedures, and internal control over financial reporting. Such certifications should be read in conjunction with the information contained in this Item 9A for a more complete understanding of the matters covered by such certifications.

Disclosure Controls and Procedures.

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of June 30, 2015. The term "disclosure controls and procedures," as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by the company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized, and reported, within the time periods specified in the rules and forms of the Securities and Exchange Commission. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions to be made regarding required disclosure. It should be noted that any system of controls and procedures, however well designed and operated, can provide only reasonable, and not absolute, assurance that the objectives of the system are met and that management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

Our management identified material weaknesses in respect of our internal controls over financial reporting. A material weakness is a control deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the Company's financial statements will not be prevented or detected in a timely basis. The following material weaknesses have been identified:

1. Insufficient segregation of duties, oversight of work performed and lack of compensating controls in our finance function due to limited personnel.
2. Lack of documentation to support occurrences and approval procedures.
3. Design deficiencies that do not meet stated objectives that elevate the level of risk of a material misstatement to the financial statements.
4. Policies and procedures with respect to the review, supervision and monitoring of the accounting operations were not designed effectively, due to insufficient segregation of duties.
5. The Company did not maintain an adequate risk oversight function to evaluate and report on risks to financial reporting throughout the Company, including completion of a comprehensive risk assessment to identify all potential risk areas and evaluate the adequacy of controls to mitigate identified risk.

As a result of these material weaknesses, our Chief Executive Officer and Chief Financial Officer concluded that, we did not maintain effective internal control over financial reporting as of June 30, 2015 and further concluded that, as of such date, our disclosure controls and procedures were not effective at the reasonable assurance level.

Management's Annual Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act). A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles. Internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of

management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the interim or annual consolidated financial statements. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, conducted an evaluation of the effectiveness of our internal control over financial reporting as of June 30, 2015 based on the framework in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission in 1992. Based on this assessment, our management concluded that in light of the material weaknesses described above, as of June 30, 2015, our internal control over financial reporting was not effective based on those criteria.

This Annual Report on Form 10-K includes an attestation report of our registered public accounting firm regarding internal control over financial reporting.

As part of our independent registered public accountants' communication with our audit committee with respect to audit procedures for the year ended June 30, 2015, our independent registered public accountants informed the audit committee that these deficiencies constituted material weaknesses, as defined under Auditing Standard No. 5, "An Audit of Internal Control Over Financial Reporting that is Integrated with an Audit of Financial Statements and Related Independence Rule and Conforming Amendments," established by the Public Company Accounting Oversight Board.

Remediation

We are committed to remediating the material weaknesses identified in internal controls over financial reporting and have begun the process to remediate these material weaknesses, however the timing of completing our remediation efforts is uncertain. Our efforts will focus on instituting mitigating controls to address segregation of duties and undertake a thorough review of the finance functions position responsibilities and the hiring of additional staff; implement additional controls to address system access deficiencies; establish independent review and verification procedures for our vendor and customer master files; enhance the documentation to support review occurrences and approval procedures; and, commence regular periodic reviews of our internal controls over financial reporting with our Board of Directors and Audit Committee to address the inadequate risk oversight function and institute procedures to evaluate and report on risks to financial reporting, including the documentation and completion of a comprehensive risk assessment to identify all potential risk areas and evaluate the adequacy of our controls to mitigate these risks.

Our Independent Registered Public Accounting Firm has issued a report on our internal control over financial reporting. This report appears below.

Attestation Report of the Independent Registered Public Accounting Firm

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders of Implant Sciences Corporation:

We have audited Implant Sciences Corporation internal control over financial reporting as of June 30, 2015, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (1992). The Company's management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over

financial reporting included in the accompanying Management's Annual Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed 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. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

A material weakness is a control deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the company's annual or interim financial statements will not be prevented or detected on a timely basis. The following material weaknesses have been identified and included in Management's Annual Report on Internal Control over Financial Reporting:

1. Insufficient segregation of duties, oversight of work performed and lack of compensating controls in our finance function due to limited personnel.
2. Lack of documentation to support occurrences and approval procedures.
3. Design deficiencies that do not meet stated objectives that elevate the level of risk of a material misstatement to the financial statements.
4. Policies and procedures with respect to the review, supervision and monitoring of the accounting operations were not designed effectively, due to insufficient segregation of duties.
5. The Company did not maintain an adequate risk oversight function to evaluate and report on risks to financial reporting throughout the Company, including completion of a comprehensive risk assessment to identify all potential risk areas and evaluate the adequacy of controls to mitigate identified risk.

These material weaknesses were considered in determining the nature, timing and extent of audit tests applied in our audit of the company's consolidated financial statements for the year ending June 30, 2015, based on criteria established in Internal Control – Integrated Framework issued by the Committee on Sponsoring Organizations of the Treadway Commission.

In our opinion, because of the effect of the material weaknesses described above on the achievement of the objectives of the control criteria, Implant Sciences Corporation has not maintained effective internal control over financial reporting as of June 30, 2015, based on the criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Implant Sciences Corporation, Inc. as of June 30, 2015 and 2014 and the

related consolidated statements of operations and comprehensive loss, stockholders' deficit and cash flows for the three years ended June 30, 2015, 2014 and 2013 and our report dated September 28, 2015 expressed an unqualified opinion, which includes an explanatory paragraph as to the Company's ability to continue as a going concern.

/s/ Marcum LLP
Boston, Massachusetts
September 28, 2015

Changes in Internal Control Over Financial Reporting

There were no changes to our internal control over financial reporting during the fourth quarter ended June 30, 2015 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 9B. Other Information

None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance

The information required by this Item 10 is incorporated by reference to our definitive proxy statement to be filed with the Commission on or before October 13, 2015.

Item 11. Executive Compensation

The information required by this Item 11 is incorporated by reference to our definitive proxy statement to be filed with the Commission on or before October 13, 2015.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information required by this Item 12 is incorporated by reference to our definitive proxy statement to be filed with the Commission on or before October 13, 2015.

Item 13. Certain Relationships and Related Transactions, and Director Independence

The information required by this Item 13 is incorporated by reference to our definitive proxy statement to be filed with the Commission on or before October 13, 2015.

Item 14. Principal Accounting Fees and Services

The information required by this Item 14 is incorporated by reference to our definitive proxy statement to be filed with the Commission on or before October 13, 2015.

PART IV

Item 15. Exhibits, Financial Statement Schedules

The following are filed as part of this Form 10-K:

(1) Financial Statements: For a list of financial statements which are filed as part of this Annual Report on Form 10-K, see Page 32.

(2) Exhibits

Exhibit No.	Description
3.1	Restated Articles of Organization, as amended, of Implant Sciences Corporation (incorporated herein by reference to Exhibit 3.1 to Implant Sciences Corporation's Quarterly Report on Form 10-Q for the fiscal quarter ended March 31, 2013).
3.2	Amended and Restated By-Laws of Implant Sciences Corporation (incorporated herein by reference to Exhibit 3.1 to Implant Sciences Corporation's Current Report on Form 8-K dated December 12, 2007 and filed December 18, 2007).
4.1	Specimen certificate for the Common Stock of Implant Sciences Corporation (incorporated herein by reference to Exhibit 4.1 to Amendment No. 1 to Implant Sciences Corporation's Registration Statement on Form SB-2 (Registration 333-644999), filed on December 21, 1998).
10.1	1998 Incentive and Nonqualified Stock Option Plan (incorporated herein by reference to Exhibit 10.35 to Implant Sciences Corporation's Registration Statement on Form SB-2 (Registration 333-644999), filed on September 29, 1998).*
10.2	Form of Incentive Stock Option under the 1998 Incentive and Nonqualified Stock Option Plan (incorporated herein by reference to Exhibit 10.33 to Amendment No. 1 to Implant Sciences Corporation's Registration Statement on Form SB-2 (Registration 333-644999), filed on December 21, 1998).*
10.3	Form of Nonqualified Stock Option under the 1998 Incentive and Nonqualified Stock Option Plan (incorporated herein by reference to Exhibit 10.34 to Amendment No. 1 to Implant Sciences Corporation's Registration Statement on Form SB-2 (Registration 333-644999), filed on December 21, 1998).*
10.4	Form of Nonqualified Stock Option for Non-Employee Directors under the 1998 Incentive and Nonqualified Stock Option Plan (incorporated herein by reference to Exhibit 10.35 to Amendment No. 1 to Implant Sciences Corporation's Registration Statement on Form SB-2 (Registration 333-644999), filed on December 21, 1998).*
10.5	2000 Incentive and Non-Qualified Stock Option Plan of Implant Sciences Corporation (incorporated by reference to Exhibit 10.1 to Implant Sciences Corporation's Registration Statement on Form S-8, filed on December 12, 2003).*
10.6	2004 Stock Option Plan of Implant Sciences Corporation, as amended through March 14, 2011 (incorporated by reference herein to Exhibit 10.4 to Implant Sciences Quarterly Report on Form 10-Q for the fiscal quarter ended March 31, 2011).*
10.7	Amendment to 2004 Stock Option Plan of Implant Sciences Corporation, effective September 7, 2012 (incorporated herein by reference to Exhibit 10.1 to Implant Sciences Corporation's Current Report on Form 8-K dated September 7, 2012 and filed on September 13, 2012).*
10.8	2006 Employee Stock Purchase Plan of Implant Sciences Corporation (incorporated herein by reference to Exhibit 4.1 to Implant Sciences Registration Statement on Form S-8 filed on July 26, 2007).*
10.9	Implant Sciences Corporation's 2014 Stock Option Plan (incorporated herein by reference to Exhibit 10.2 to Implant Sciences Corporation's Current Report on Form 8-K dated July 2, 2014 and filed on July 8, 2014).*
10.10	Implant Sciences Corporation Change of Control Payment Plan (incorporated herein by reference to Exhibit 10.2 to Implant Sciences Corporation's Current Report on Form 8-K dated September 7, 2012 and filed September 13, 2012).*

10.11 Amended and Restated Employment Agreement, dated as of June 25, 2013, between Implant Sciences Corporation and Glenn D. Bolduc (incorporated herein by reference to Exhibit 10.1 to Implant Sciences Corporation's Current Report on Form 8-K dated July 1, 2015 and filed on July 1, 2015.*

10.12 Employment Agreement between Implant Sciences Corporation and William McGann, dated March 19, 2012 (incorporated herein by reference to Exhibit 10.1 to Implant Sciences Corporation's Current Report on Form 8-K dated March 19, 2012 and filed on March 23, 2012).*

10.13 Employment Agreement between Implant Sciences Corporation and Darryl Jones, dated May 7, 2012 (incorporated herein by reference to Exhibit 10.1 to Implant Sciences Corporation's Current Report on Form 8-K dated May 7, 2012 and filed May 11, 2012).*

10.14 Lease, dated December 11, 2008, between Implant Sciences Corporation and Wakefield Investments, Inc (incorporated herein by reference to Exhibit 10.1 to Implant Sciences Corporation's Current Report on Form 8-K dated December 11, 2008 and filed December 17, 2008)..

10.15 Amended and Restated Employment Agreement between Implant Sciences Corporation and William McGann, dated January 16, 2015.*

10.16 Employment Agreement between Implant Sciences Corporation and Brenda Baron, dated March 13, 2015.*

10.17 Employment Agreement between Implant Sciences Corporation and Todd Silvestri, dated March 13, 2015.*

10.18 Employment Agreement between Implant Sciences Corporation and Roger Deschenes, dated September 16, 2015.*

10.19 First Amendment, dated February 1, 2010, to Lease between Implant Sciences Corporation and Wakefield Investments, Inc (incorporated herein by reference to Exhibit 10.60 to Implant Sciences Corporation's annual report on Form 10-K for the year ended June 30, 2010).

10.20 Lease, dated April 1, 2013, between the Implant Sciences Corporation and Wakefield Investments, Inc (incorporated herein by reference to Implant Sciences Corporation's Annual Report on Form 10-K for the fiscal year ended June 30, 2013).

10.21 Note and Warrant Purchase Agreement, dated as of December 10, 2008, between Implant Sciences Corporation and DMRJ Group LLC (incorporated herein by reference to Exhibit 10.1 to Implant Sciences Corporation's Current Report on Form 8-K dated December 10, 2008 and filed December 16, 2008).

10.22 Senior Secured Convertible Promissory Note, dated December 10, 2008, in the principal amount of $5,600,000, issued by Implant Sciences Corporation to DMRJ Group LLC (incorporated herein by reference to Exhibit 10.2 to Implant Sciences Corporation's Current Report on Form 8-K dated December 10, 2008 and filed December 16, 2008) (superseded by Exhibit 10.28).

10.23 Warrant to Purchase Shares of Common Stock, dated December 10, 2008, issued by Implant Sciences Corporation to DMRJ Group LLC (incorporated herein by reference to Exhibit 10.3 to Implant Sciences Corporation's Current Report on Form 8-K dated December 10, 2008 and filed December 16, 2008) (superseded by Exhibit 10.29).

10.24 Security Agreement, dated as of December 10, 2008, among Implant Sciences Corporation, C Acquisition Corp., Accurel Systems International Corporation and IMX Acquisition Corp., as grantors, and DMRJ Group LLC, as secured party (incorporated herein by reference to Exhibit 10.4 to Implant Sciences Corporation's Current Report on Form 8-K dated December 10, 2008 and filed December 16, 2008).

10.25 Patent Security Agreement, dated as of December 10, 2008, among Implant Sciences Corporation, C Acquisition Corp., Accurel Systems International Corporation and IMX Acquisition Corp., as grantors, and DMRJ Group LLC, as secured party (incorporated herein by reference to Exhibit 10.5 to Implant Sciences Corporation's Current Report on Form 8-K dated December 10, 2008 and filed December 16, 2008).

10.26 Guaranty, dated as of December 10, 2008, of the obligations of Implant Sciences Corporation by C Acquisition Corp., Accurel Systems International Corporation and IMX Acquisition Corp. in favor of DMRJ Group LLC (incorporated herein by reference to Exhibit 10.6 to Implant Sciences Corporation's Current Report on Form 8-K dated December 10, 2008 and filed December 16, 2008).

10.27 Letter Agreement, dated as of March 12, 2009, between Implant Sciences Corporation and DMRJ Group LLC (incorporated herein by reference to Exhibit 10.1 to Implant Sciences Corporation's Current Report on Form 8-K dated March 12, 2009 and filed March 18, 2009).

10.28 Amended and Restated Senior Secured Convertible Promissory Note, dated December 10, 2008, in the principal amount of $5,600,000, issued by Implant Sciences Corporation to DMRJ Group LLC (incorporated herein by reference to Exhibit 10.2 to Implant Sciences Corporation's Current Report on Form 8-K dated March 12, 2009 and filed March 18, 2009).

10.29 Amended and Restated Warrant to Purchase Shares of Common Stock, dated March 12, 2009, issued by Implant Sciences Corporation to DMRJ Group LLC (incorporated herein by reference to Exhibit 10.3 to Implant Sciences Corporation's Current Report on Form 8-K dated March 12, 2009 and filed March 18, 2009).

10.30 First Amendment, dated July 1, 2009, to Note and Warrant Purchase Agreement, dated as of December 10, 2008, between Implant Sciences Corporation and DMRJ Group LLC (incorporated herein by reference to Exhibit 10.1 to Implant Sciences Corporation Current Report on Form 8-K dated July 1, 2009 and filed July 8, 2009).

10.31 Senior Secured Promissory Note, dated July 1, 2009, in the principal amount of $1,000,000, issued by Implant Sciences Corporation to DMRJ Group LLC (incorporated herein by reference to Exhibit 10.2 to Implant Sciences Corporation Current Report on Form 8-K dated July 1, 2009 and filed July 8, 2009).

10.32 Credit Amendment, dated September 4, 2009, among Implant Sciences Corporation, C Acquisition Corp., Accurel Systems International Corporation, IMX Acquisition Corp. and DMRJ Group LLC (incorporated herein by reference to Exhibit 10.1 to Implant Sciences Corporation Current Report on Form 8-K dated September 4, 2009 and filed September 11, 2009).

10.33 Promissory Note, dated September 4, 2009, in the maximum principal amount of $3,000,000, issued by Implant Sciences Corporation to DMRJ Group LLC (incorporated herein by reference to Exhibit 10.2 to Implant Sciences Corporation Current Report on Form 8-K dated September 4, 2009 and filed September 11, 2009) (superseded by Exhibit 10.37).

10.34 Security Agreement, dated as of September 4, 2009, among Implant Sciences Corporation, C Acquisition Corp., Accurel Systems International Corporation and IMX Acquisition Corp., as grantors, and DMRJ Group LLC, as secured party (incorporated herein by reference to Exhibit 10.3 to Implant Sciences Corporation Current Report on Form 8-K dated September 4, 2009 and filed September 11, 2009).

10.35 Patent Security Agreement, dated as of September 4, 2009, among Implant Sciences Corporation, C Acquisition Corp., Accurel Systems International Corporation and IMX Acquisition Corp., as grantors, and DMRJ Group LLC, as secured party (incorporated herein by reference to Exhibit 10.4 to Implant Sciences Corporation Current Report on Form 8-K dated September 4, 2009 and filed September 11, 2009).

10.36 Guaranty, dated as of September 4, 2009, of the obligations of Implant Sciences Corporation by C Acquisition Corp., Accurel Systems International Corporation and IMX Acquisition Corp. in favor of DMRJ Group LLC (incorporated herein by reference to Exhibit 10.5 to Implant Sciences Corporation Current Report on Form 8-K dated September 4, 2009 and filed September 11, 2009).

10.37 Omnibus Waiver and First Amendment to Credit Agreement and Third Amendment to Note and Warrant Purchase Agreement, dated as of January 12, 2010 between Implant Sciences Corporation and DMRJ Group LLC (incorporated herein by reference to Exhibit 10.1 to Implant Sciences Corporation Current Report on Form 8-K dated January 13, 2010 and filed January 14, 2010).

10.38 Amended and Restated Promissory Note, dated as of January 12, 2010, in the maximum principal amount of $5,000,000, issued by Implant Sciences Corporation to DMRJ Group LLC (incorporated herein by reference to Exhibit 10.2 to Implant Sciences Corporation Current Report on Form 8-K dated January 13, 2010 and filed January 14, 2010) (superseded by Exhibit 10.40).

10.39 Omnibus Second Amendment to Credit Agreement and Fourth Amendment to Note and Warrant Purchase Agreement, dated as of April 23, 2010 between Implant Sciences Corporation and DMRJ Group LLC (incorporated herein by reference to Exhibit 10.1 to Implant Sciences Corporation Current Report on Form 8-K dated April 23, 2010 and filed April 28, 2010).

10.40 Amended and Restated Promissory Note, dated as of April 23, 2010, and effective as of April 7, 2011, in the maximum principal amount of $10,000,000, issued by Implant Sciences Corporation to DMRJ Group LLC (incorporated herein by reference to Exhibit 10.2 to Implant Sciences Corporation Current Report on Form 8-K dated April 23, 2010 and filed April 28, 2010) (superseded by Exhibit 10.43).

10.41 Omnibus Third Amendment to Credit Agreement and Fifth Amendment to Note and Warrant Purchase Agreement, dated as of September 30, 2010 between Implant Sciences Corporation and DMRJ Group LLC (incorporated herein by reference to Exhibit 10.1 to Implant Sciences Corporation's Current Report on Form 8-K dated September 30, 2010 filed October 6, 2010).

10.42 Omnibus Fourth Amendment to Credit Agreement and Sixth Amendment to Note and Warrant Purchase Agreement, dated as of March 30, 2011 between Implant Sciences Corporation and DMRJ Group LLC (incorporated herein by reference to Exhibit 10.1 to Implant Sciences Corporation's Current Report on Form 8-K dated March 30, 2011 filed April 4, 2011).

10.43 Amended and Restated Promissory Note, dated as of March 30, 2011 in the maximum principal amount of $15,000,000, issued by Implant Sciences Corporation to DMRJ Group LLC (incorporated herein by reference to Exhibit 10.2 to Implant Sciences Corporation's Quarterly Report on Form 10-Q for the quarter ended March 31, 2011) (superseded by Exhibit 10.46).

10.44 Omnibus Fifth Amendment to Credit Agreement and Seventh Amendment to Note and Warrant Purchase Agreement, dated as of April 7, 2011 between Implant Sciences Corporation and DMRJ Group LLC (incorporated herein by reference to Exhibit 10.3 to Implant Sciences Corporation's Current Report on Form 8-K dated April 7, 2011 filed April 12, 2011).

10.45 Omnibus Sixth Amendment to Credit Agreement and Eighth Amendment to Note and Warrant Purchase Agreement, dated as of September 29, 2011 between Implant Sciences Corporation and DMRJ Group LLC (incorporated herein by reference to Exhibit 10.1 to Implant Sciences Corporation's Current Report on Form 8-K dated September 29, 2011 and filed September 30, 2011).

10.46 Amended and Restated Promissory Note, dated as of September 29, 2011 in the maximum principal amount of $23,000,000, issued by Implant Sciences Corporation to DMRJ Group LLC (incorporated herein by reference to Exhibit 10.2 to Implant Sciences Corporation's Current Report on Form 8-K dated September 29, 2011 and filed September 30, 2011).

10.47 Omnibus Seventh Amendment to Credit Agreement and Ninth Amendment to Note and Warrant Purchase Agreement, dated as of October 13, 2011 between Implant Sciences Corporation and DMRJ Group LLC (incorporated herein by reference to Exhibit 10.1 to Implant Sciences Corporation's Current Report on Form 8-K dated October 13, 2011 filed October 19, 2011).

10.48 Omnibus Eighth Amendment to Credit Agreement and Tenth Amendment to Note and Warrant Purchase Agreement, dated as of February 21, 2012 between Implant Sciences Corporation and DMRJ Group LLC (incorporated herein by reference to Exhibit 10.1 to Implant Sciences Corporation's Current Report on Form 8-K for dated February 21, 2012 filed February 24, 2012).

10.49 Omnibus Ninth Amendment to Credit Agreement and Eleventh Amendment to Note and Warrant Purchase Agreement, dated as of September 5, 2012 between Implant Sciences Corporation and DMRJ Group LLC (incorporated herein by reference to Exhibit 10.1 to Implant Sciences Corporation's Current Report on Form 8-K dated September 5, 2012 filed September 11, 2012).

10.50 Senior Secured Convertible Promissory Note, dated as of September 5, 2012, issued by Implant Sciences Corporation (incorporated herein by reference to Exhibit 10.2 to Implant Sciences Corporation's Current Report on Form 8-K dated September 5, 2012 filed September 11, 2012).

10.51 Omnibus Tenth Amendment to Credit Agreement and Twelfth Amendment to Note and Warrant Purchase Agreement, dated as of February 28, 2013 between Implant Sciences Corporation and DMRJ Group LLC (incorporated herein by reference to Exhibit 10.1 to Implant Sciences Corporation's Current Report on Form 8-K dated February 28, 2013 filed March 1, 2013).

10.52 Senior Secured Convertible Promissory Note, dated as of February 28, 2013, issued by Implant Sciences Corporation (incorporated herein by reference to Exhibit 10.2 to Implant Sciences Corporation's Current Report on Form 8-K dated February 28, 2013 filed March 1, 2013).

10.53 Omnibus Eleventh Amendment to Credit Agreement and Thirteenth Amendment to Note and Warrant Purchase Agreement, dated as of November 14, 2013 between Implant Sciences Corporation and DMRJ Group LLC (incorporated herein by reference to Exhibit 10.1 to Implant Sciences Corporation's Current Report on Form 8-K dated November 18, 2013 and filed November 18, 2013).

10.54 Note Purchase Agreement dated as of March 19, 2014, between Implant Sciences Corporation, certain Investors and the Agent (incorporated herein by reference to Exhibit 10.1 to Implant Sciences Corporation's Current Report on Form 8-K dated March 19, 2014 and filed March 26, 2014).

10.54 Form of Senior Secured Promissory Note issued pursuant to the Note Purchase Agreement (incorporated herein by reference to Exhibit 10.2 to Implant Sciences Corporation's Current Report on Form 8-K dated March 19, 2014 and filed March 26, 2014).

10.56 Letter dated as of March 19, 2014, from the Agent to Implant Sciences Corporation waiving certain financial covenants through March 31, 2015 (incorporated herein by reference to Exhibit 10.3 to Implant Sciences Corporation's Current Report on Form 8-K dated March 19, 2014 and filed March 26, 2014).

10.57 Security Agreement dated as of March 19, 2014, among Implant Sciences Corporation, C Acquisition Corp., Accurel Systems International Corporation and IMX Acquisition Corp., as grantors, and the Agent (incorporated herein by reference to Exhibit 10.4 to Implant Sciences Corporation's Current Report on Form 8-K dated March 19, 2014 and filed March 26, 2014).

10.58 Guaranty dated as of March 19, 2014, of the obligations of Implant Sciences Corporation by C Acquisition Corp., Accurel Systems International Corporation and IMX Acquisition Corp. in favor of the Agent and the Investors (incorporated herein by reference to Exhibit 10.5 to Implant Sciences Corporation's Current Report on Form 8-K dated March 19, 2014 and filed March 26, 2014)

10.59 Omnibus Twelfth Amendment to Credit Agreement and Fourteenth Amendment to Note and Warrant Purchase Agreement dated as of March 19, 2014 between Implant Sciences Corporation and DMRJ Group LLC (incorporated herein by reference to Exhibit 10.6 to Implant Sciences Corporation's Current Report on Form 8-K dated March 19, 2014 and filed March 26 2014).

10.60 Intercreditor Agreement dated as of March 19, 2014, by and between the Agent and DMRJ Group, LLC, and acknowledged and agreed by Implant Sciences Corporation, C Acquisition Corp., Accurel Systems International Corporation and IMX Acquisition Corp (incorporated herein by reference to Exhibit 10.7 to Implant Sciences Corporation's Current Report on Form 8-K dated March 19, 2014 and filed March 26, 2014).

10.61 Agreement for Consulting Services between Implant Sciences Corporation and Robert Liscouski, dated as of April 1, 2011 (incorporated herein by reference to Exhibit 10.46 to Implant Sciences Annual Report on Form 10-K for the fiscal year ended June 30, 2011).*

10.62 Consent and Omnibus Amendment to Secured Term Notes, dated as of March 19, 2015, between Implant Sciences Corporation, certain Investors and BAM Administrative Services, LLC, as Agent (incorporated herein by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K dated March 19, 2015 and filed March 25, 2015).

10.63	Omnibus Thirteenth Amendment to Credit Agreement and Fifteenth Amendment to Note and Warrant Purchase Agreement dated as of March 19, 2015 between Implant Sciences Corporation and DMRJ Group LLC (incorporated herein by reference to Exhibit 10.2 to the Registrant's Current Report on Form 8-K dated March 19, 2015 and filed March 25, 2015).
10.64	Amended and Restated Change of Control Plan(incorporated herein by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K dated February 26, 2015 and filed March 4, 2015).*
10.65	Assignment Agreement by and between DMRJ Group LLC, Montsant Partners LLC and Implant Sciences Corporation dated as of May 4, 2015.
21.1	Subsidiaries of Implant Sciences Corporation.
23.1	Consent of Marcum LLP.
31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of the Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of the Chief Executive Officer Pursuant to 18 U.S.C. 1350, as adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. **
32.2	Certification of the Chief Financial 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 Document.
101.CAL	XBRL Taxomony Extension Calculation Linkbase Document.
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.

*	Indicates a management contract or compensatory plan or arrangement.
**	In accordance with Item 601(b)(32)(ii) of Regulation S-K, the certifications furnished in Exhibits 32.1 and 32.2 hereto are deemed to accompany this Form 10-K and will not be deemed to be "filed" for purposes of Section 18 of the Exchange Act. Such certifications will not be deemed to be incorporated by reference into any filings under the Securities Act or the Exchange Act, except to the extent that the registrant specifically incorporates it by reference.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders of Implant Sciences Corporation:

We have audited the accompanying consolidated balance sheets of Implant Sciences Corporation as of June 30, 2015 and 2014 and the related consolidated statements of operations and comprehensive loss, changes in stockholders' deficit, and cash flows for the years ended June 30, 2015, June 30, 2014 and June 30, 2013. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Implant Sciences Corporation as of June 30, 2015, 2014 and 2013 and the consolidated results of its operations and comprehensive loss and its cash flows for the years ended June 30, 2015, 2014 and 2013, in conformity with U.S. accounting principles generally accepted in the United States of America.

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1 to the consolidated financial statements, the Company has had recurring net losses and continues to experience negative cash flows from operations. As of September 15, 2015, the Company's principal obligation to its primary lenders was approximately $65,046,000 and accrued interest of approximately $15,393,000. The Company is required to repay all borrowings and accrued interest to these lenders on March 31, 2016. These conditions raise substantial doubt about its ability to continue as a going concern. Management's plans regarding these matters are also described in Note 1. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Implant Sciences Corporation's internal control over financial reporting as of June 30, 2015, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations the Treadway Commission (1992) and our report dated September 28, 2015 expresses an adverse opinion thereon on the effectiveness of the Company's internal control over financial reporting because of the existence of material weaknesses.

/s/ Marcum LLP
Boston, Massachusetts
September 28, 2015

Implant Sciences Corporation
Consolidated Balance Sheets
(In thousands except share and per share amounts)

	June 30, 2015	June 30, 2014
ASSETS		
Current assets:		
Cash and cash equivalents	$ 1,985	$ 391
Restricted cash and investments	367	312
Accounts receivable-trade, net of allowances of $47 and $1, respectively	872	545
Inventories, net	5,244	2,868
Prepaid expenses and other current assets	946	315
Total current assets	9,414	4,431
Property and equipment, net	880	619
Restricted cash and investments	-	312
Other non-current assets	98	117
Total assets	$ 10,392	$ 5,479
LIABILITIES AND STOCKHOLDERS' DEFICIT		
Current liabilities:		
Senior secured promissory note – BAM	$ 20,000	$ 20,000
Senior secured convertible promissory note – Montsant Partners	3,184	3,184
Senior secured promissory note – DMRJ	1,000	1,000
Second senior secured convertible promissory note – DMRJ	12,000	12,000
Third senior secured convertible promissory note – DMRJ	12,000	12,000
Line of credit - DMRJ	16,662	2,995
Current maturities of obligations under capital lease	45	45
Accrued expenses	17,080	11,094
Accounts payable	2,855	3,675
Deferred revenue	3,454	483
Total current liabilities	88,280	66,476
Long-term liabilities:		
Long-term obligations under capital lease, net of current maturities	20	66
Accrued liabilities other – long-term	48	-
Deferred revenue, net of current	221	142
Total long-term liabilities	289	208
Total liabilities	88,569	66,684
Commitments and contingencies (Note 9)		
Stockholders' deficit:		
Common stock; $0.001 par value; 200,000,000 shares authorized; 75,113,665 and 75,103,120 issued and outstanding at June 30, 2015 and 63,634,171 and 63,623,626 shares issued and outstanding at June 30, 2014	75	64
Preferred stock; no stated value; 5,000,000 shares authorized		
Series G Convertible Preferred Stock, no stated value; 650,000 shares authorized, no shares issued and outstanding	-	-
Series H Convertible Preferred Stock; no stated value; 15,000 shares authorized, no shares issued and outstanding	-	-
Series I Convertible Preferred Stock; no stated value; 15,000 shares authorized, no shares issued and outstanding	-	-
Series J Convertible Preferred Stock; no stated value; 6,000 shares authorized, no shares issued and outstanding	-	-
Additional paid-in capital	112,613	107,055
Accumulated deficit	(189,429)	(167,886)
Deferred compensation	(1,366)	(367)
Other comprehensive income	3	2
Treasury stock, 10,545 common shares, at cost	(73)	(73)
Total stockholders' deficit	(78,177)	(61,205)
Total liabilities and stockholders' deficit	$ 10,392	$ 5,479

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

Implant Sciences Corporation
Consolidated Statements of Operations and Comprehensive Loss
(In thousands except share and per share amounts)

	For the Years Ended June 30,		
	2015	**2014**	**2013**
Revenues	$ 12,991	$ 8,552	$ 12,017
Cost of revenues	8,472	6,498	8,588
Gross margin	4,519	2,054	3,429
Operating expenses:			
Research and development	5,014	4,787	4,754
Selling, general and administrative	12,201	11,388	20,630
Total operating expenses	17,215	16,175	25,384
Loss from operations	(12,696)	(14,121)	(21,955)
Other income (expense), net:			
Interest income	1	1	2
Interest expense	(8,848)	(6,890)	(5,401)
Total other expense, net	(8,847)	(6,889)	(5,399)
Net loss	(21,543)	(21,010)	(27,354)
Other comprehensive income, net of tax:			
Foreign currency translation adjustments	1	2	-
Other comprehensive income	1	2	-
Comprehensive loss	$ (21,542)	$ (21,008)	$ (27,354)
Net loss per share, basic and diluted	$ (0.30)	$ (0.35)	$ (0.56)
Weighted average shares used in computing net loss per common share, basic and diluted	70,770,705	60,753,054	49,124,942

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

Implant Sciences Corporation
Consolidated Statement of Stockholders' Deficit
For the Years Ended June 30, 2015, 2014 and 2013

(In thousands except share amounts)

	Common Stock		Series G Convertible Preferred Stock	Additional Paid-in Capital	Accumulated Deficit	Deferred Compensation	Other Comprehensive Income	Treasury Stock		Total Stockholders' Deficit
	Number of Shares	Amount						Number of Shares	Amount	
Balance at July 1, 2012	39,163,540	$ 39	$ 274	$ 87,313	$ (119,522)	$ (432)	-	10,545	$ (73)	$ (32,401)
Issuance of common stock in connection with exercise of stock options	1,421,183	1	-	227	-	-	-	-	-	228
Issuance of common stock in connection with exercise of stock purchase warrants	1,104,204	1	-	15	-	-	-	-	-	16
Conversion of senior secured convertible promissory note	500,000	1	-	39	-	-	-	-	-	40
Conversion of Series G preferred stock	14,850,000	15	(247)	232	-	-	-	-	-	-
Fair value of warrants issued to consultants	-	-	-	1,534	-	(1,534)	-	-	-	-
Amortization of deferred compensation	-	-	-	-	-	696	-	-	-	696
Share-based compensation	-	-	-	13,908	-	-	-	-	-	13,908
Common stock issued to consultants	616,667	1	-	669	-	(351)	-	-	-	319
Net loss	-	-	-	-	(27,354)	-	-	-	-	(27,354)
Balance at June 30, 2013	57,655,594	$ 58	$ 27	$ 103,937	$ (146,876)	$ (1,621)	$ -	10,545	$ (73)	$ (44,548)
Issuance of common stock in connection with exercise of stock options	407,066	1	-	105	-	-	-	-	-	106
Issuance of common stock in connection with exercise of stock purchase warrants	36,492	-	-	11	-	-	-	-	-	11
Conversion of accrued interest on senior secured convertible promissory notes	3,918,319	4	-	310	-	-	-	-	-	314
Conversion of Series G preferred stock	1,616,700	1	(27)	27	-	-	-	-	-	1
Fair value of warrants issued to consultants	-	-	-	16	-	(16)	-	-	-	-
Amortization of deferred compensation	-	-	-	-	-	1,270	-	-	-	1,270
Share-based compensation	-	-	-	2,649	-	-	-	-	-	2,649
Other comprehensive income	-	-	-	-	-		2	-	-	2
Net loss	-	-	-	-	(21,010)	-	-	-	-	(21,010)
Balance at June 30, 2014	63,634,171	$ 64	$ -	$ 107,055	$ (167,886)	$ (367)	$ 2	10,545	$ (73)	$ (61,205)

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

Implant Sciences Corporation
Consolidated Statement of Stockholders' Deficit
For the Years Ended June 30, 2015, 2014 and 2013
(In thousands except share amounts)

	Common Stock							Treasury Stock		
	Number of Shares	Amount	Series G Convertible Preferred Stock	Additional Paid-in Capital	Accumulated Deficit	Deferred Compensation	Other Comprehensive Income	Number of Shares	Amount	Total Stockholders' Deficit
Issuance of common stock in connection with exercise of stock options	741,499	1	-	282	-	-	-	-	-	283
Issuance of common stock in connection with exercise of stock purchase warrants	180,495	-	-	16	-	-	-	-	-	16
Conversion of accrued interest on senior secured convertible promissory notes	9,987,500	10	-	789	-	-	-	-	-	799
Fair value of warrants issued to consultants, net of forfeitures	-	-	-	119	-	(154)	-	-	-	(35)
Amortization of deferred compensation	-	-	-	-	-	324	-	-	-	324
Common stock issued to consultants	570,000	-	-	1,672	-	(1,169)	-	-	-	503
Share-based compensation	-	-	-	2,680	-	-	-	-	-	2,680
Other comprehensive income	-	-	-	-	-		1	-	-	1
Net loss	-	-	-	-	(21,543)	-	-	-	-	(21,543)
Balance at June 30, 2015	75,113,665	$ 75	$ -	$ 112,613	$ (189,429)	$ (1,366)	$ 3	10,545	$ (73)	$ (78,177)

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

Implant Sciences Corporation
Consolidated Statements of Cash Flows
(In thousands)

	For the Years Ended June 30,		
	2015	**2014**	**2013**
Cash flows from operating activities:			
Net loss	$ (21,543)	$ (21,010)	$ (27,354)
Adjustments to reconcile net loss to net cash flows used in operating activities:			
Depreciation and amortization	171	154	84
Bad debt expense	48	2	1
Stock-based compensation expense	2,680	2,649	13,908
Loss (gain) on disposal of equipment	1	56	(9)
Warrants issued to non-employees	289	1,270	696
Common stock issued to consultants	503	-	319
Settlement agreements	-	118	(295)
Changes in assets and liabilities:			
Accounts receivable	(375)	669	(1,035)
Inventories	(2,376)	(723)	1,048
Prepaid expenses and other current assets	(612)	85	455
Accounts payable	(820)	1,522	(305)
Accrued expenses	6,834	4,703	2,569
Deferred revenue	3,050	516	(972)
Net cash used in operating activities	(12,150)	(9,989)	(10,890)
Cash flows from investing activities:			
Purchases of property and equipment	(433)	(409)	(151)
Transfer from restricted funds, net	257	121	841
Proceeds from the sale of equipment	-	1	20
Net cash (used in) provided by investing activities	(176)	(287)	710
Cash flows from financing activities:			
Proceeds from common stock issued in connection with exercise of stock options and warrants	298	59	29
Principal repayments of long-term debt and capital lease obligations	(46)	(66)	(25)
Proceeds from the issuance of senior secured promissory note	-	20,000	-
Net borrowings on line of credit	13,667	(9,408)	10,172
Net cash provided by financing activities	13,919	10,585	10,176
Effect of exchange rate changes on cash and cash equivalents	1	2	-
Net change in cash and cash equivalents	1,594	311	(4)
Cash and cash equivalents at beginning of period	391	80	84
Cash and cash equivalents at end of period	$ 1,985	$ 391	$ 80
Supplemental Disclosure of Cash Flow Information:			
Interest paid	$ 3,934	$ 2,528	$ 2,861
Non-cash Investing and Financing Activity:			
Conversions of senior secured convertible promissory note to common shares	$ -	$ -	$ 40
Conversion of convertible preferred stock to common shares	-	27	247
Conversion of senior secured convertible promissory note interest to common shares	799	314	-
Conversion of line of credit to second senior convertible promissory note	-	-	12,000
Conversion of line of credit to third senior convertible promissory note	-	-	12,000
Common stock issued to consultants	503	-	319
Equipment purchased under capital lease	-	25	125
Exercise of stock purchase warrants	-	11	-
Exercise of stock options	-	47	199

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

1. Description of Business

Implant Sciences Corporation provides systems and sensors for the homeland security market and related industries. We have developed and acquired technologies using ion mobility spectrometry to develop a product line for use in trace explosives and narcotics detection. We currently market and sell our existing trace explosives and narcotics detector products while continuing to make significant investments in developing the next generation of these products.

Our fiscal year ends on June 30. References herein to fiscal 2015, fiscal 2014, and fiscal 2013 refer to the fiscal years ended June 30, 2015, June 30, 2014 and June 30, 2013, respectively.

Liquidity, Going Concern and Management's Plans

On December 10, 2008, we entered into a note and warrant purchase agreement with DMRJ Group LLC ("DMRJ") pursuant to which we issued a senior secured convertible promissory note in the principal amount of $5,600,000 and a warrant to purchase 1,000,000 shares of our common stock. We have entered into a series of amendments, waivers and modifications with DMRJ. On March 19, 2015, we amended our credit agreements with DMRJ pursuant to which, amongst other matters, we extended the maturity date of all of our indebtedness from March 31, 2015 to March 31, 2016.

On May 4, 2015, we entered into an assignment agreement with DMRJ and Montsant Partners, LLC, wherein DMRJ assigned its rights, title and interest in the senior secured promissory note dated December 10, 2008 and appointed DMRJ as its collateral agent under the promissory note agreement. The note matures on March 31, 2016. DMRJ and Montsant Partners, LLC are funds managed by Platinum Partners Value Arbitrage Fund LP.

On March 19, 2014, we entered into a note purchase agreement with a group of institutional investors and BAM Administrative Services LLC ("BAM"), an administrative agent for the investors, pursuant to which we issued senior secured promissory notes in the aggregate principal amount of $20,000,000. The notes bear interest at 16% per annum and mature on March 31, 2016. We used all of the proceeds from the sale of the notes to repay (i) $17,624,000 of our outstanding indebtedness to DMRJ under revolving promissory note (ii) $1,809,000 of interest outstanding under that facility and (iii) $567,000 of interest outstanding under our senior secured convertible promissory note (see Note 13).

Despite our current sales, expense and cash flow projections and $4,089,000 in cash available from our line of credit with DMRJ, at September 15, 2015, we will require additional capital in the third quarter of fiscal 2016 to fund operations and continue the development, commercialization and marketing of our products. Our failure to achieve our projections and/or obtain sufficient additional capital on acceptable terms would have a material adverse effect on our liquidity and operations and could require us to file for protection under bankruptcy laws.

Our common stock was delisted by the NYSE Amex LLC in June 2009 as result of our failure to comply with certain continued listing requirements. Our common stock has been quoted on the OTC Bulletin Board since May 2009 and is also quoted on the OTC Markets Group's OTCQB tier under the symbol "IMSC". We believe that trading 'over the counter' has limited our stock's liquidity and has impaired our ability to raise capital.

In addition, while we strive to bring new products to market, we are subject to a number of risks similar to the risks faced by other technology-based companies, including risks related to: (a) our dependence on key individuals and collaborative research partners; (b) competition from substitute products and larger companies; (c) our ability to develop and market commercially usable products and obtain regulatory approval for our products under development; and (d) our ability to obtain substantial additional financing necessary to adequately fund the development, commercialization and marketing of our products. For the year ended June 30, 2015, we reported a net loss of $21,542,000 and used $12,150,000 in cash for operations. As of June 30, 2015, the Company had an accumulated deficit of approximately $189,429,000 and a working capital deficit of $78,866,000. Management continually evaluates its operating expenses and its cash flow from operations. Failure of the Company to achieve its projections will require that we seek additional financing or discontinue operations.

As of June 30, 2015, our obligations to DMRJ under each of the three promissory notes and a revolving line of credit approximated $12,000,000, $12,000,000, $1,000,000 and $16,662,000, respectively. Further, as of June 30, 2015, our obligation to DMRJ for accrued interest under these instruments approximated $11,350,000 and is included in current liabilities in the consolidated financial statements.

As of June 30, 2015, our obligations to Montsant under a promissory note approximated $3,184,000. Further, as of June 30, 2015, our obligation to Montsant for accrued interest under this instrument approximated $1,860,000 and is included in current liabilities in the consolidated financial statements.

As of June 30, 2015, our obligations under the senior secured promissory notes for which BAM is the agent

were $20,000,000. Further, as of June 30, 2015, our obligation under such notes for accrued interest amounted to approximately $54,000 and is included in current liabilities in the consolidated financial statements.

As of September 15, 2015, our obligations to DMRJ under each of the three promissory notes and a revolving line of credit approximated $12,000,000, $12,000,000, $1,000,000 and $16,862,000, respectively. Further, as of September 15, 2015, our obligation to DMRJ for accrued interest under these instruments approximated $12,692,000.

As of September 15, 2015, our obligations to Montsant under a promissory note approximated $3,184,000. Further, as of September 15, 2015, our obligation to Montsant for accrued interest under this instrument approximated $1,963,000.

As of September 15, 2015, our obligations under the senior secured promissory notes for which BAM is the agent were $20,000,000. Further, as of September 15, 2015, our obligation under such notes for accrued interest amounted to approximately $738,000.

These conditions raise substantial doubt as to our ability to continue as a going concern.

Our ability to comply with our debt covenants in the future depends on our ability to generate sufficient sales and to control expenses, and will require that we seek additional capital through private financing sources. There can be no assurances that we will achieve our forecasted financial results or that we will be able to raise additional capital to operate our business. Any such failure would have a material adverse impact on our liquidity and financial condition and could force us to curtail or discontinue operations entirely. Further, upon the occurrence of an event of default under certain provisions of our credit agreements, we could be required to pay default rate interest equal to the lesser of 2.5% per month and the maximum applicable legal rate per annum on the outstanding principal balance outstanding. The failure to refinance or otherwise negotiate further extensions of our obligations to our secured lenders would have a material adverse impact on our liquidity and financial condition and could force us to curtail or discontinue operations entirely and/or file for protection under bankruptcy laws.

Based on current sales, operating expense and cash flow projections, and the cash available from our line of credit, management believes there are plans in place to sustain operations for the next several months. These plans depend on a substantial increase in sales of our handheld trace explosives detector product and our desktop explosives and narcotics trade detector product. However, there can be no assurances that sales will materialize as forecasted, and/or that management will be successful in refinancing or extending our obligations to our secured lenders, which mature on March 31, 2016. To further sustain us, improve our cash position, and enable us to grow while reducing debt, management plans to continue to seek additional capital through private financing sources. However, there can be no assurance that management will be successful in executing these plans. Management will continue to closely monitor and attempt to control our costs and actively seek needed capital through sales of our products, equity infusions, government grants and awards, strategic alliances, and through our lending institutions.

We have suffered recurring losses from operations. Our consolidated financial statements have been presented on the basis that it is a going concern, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business.

There can be no assurances that our forecasted results will be achieved or that we will be able to raise additional capital necessary to operate our business. These conditions raise substantial doubt about our ability to continue as a going concern. The consolidated financial statements do not include any adjustments relating to the recoverability and classification of asset amounts or the amounts and classification of liabilities that might be necessary should we be unable to continue as a going concern.

Security product sales tend to have a long sales cycle, and are often subject to export controls. In an effort to identify new opportunities and stimulate sales, we have hired additional sales personnel during fiscal 2013 that have specific industry experience and have retained new distributors. However, there can be no assurance that these efforts will increase revenue.

We have a history of being active in submitting proposals for government sponsored grants and contracts and successful in being awarded grants and contracts from government agencies. However, we have recorded no revenues from government contracts, due to the expiration of several contracts and our inability to secure new contracts. Management will continue to pursue these grants and contracts to support our research and development efforts primarily in the areas of trace explosives detection.

On October 16, 2014, the U.S. Department of Homeland Security ("DHS") selected our proposal to develop next generation explosives trace detection screening systems for funding. The project, pending successful

negotiations, is potentially worth up to approximately $2 million. Subject to successful conclusion of negotiations with the DHS, we expect the project to commence in the second of quarter of fiscal 2016.

We are currently expending significant resources to develop the next generation of our current products and to develop new products. We will require additional funding in order to continue the advancement of the commercial development and manufacturing of the explosives detection system. We will attempt to obtain such financing by: (i) government grants, (ii) private financing, or (iii) strategic partnerships. However, there can be no assurance that we will be successful in our attempts to raise such additional financing.

We will require substantial funds for further research and development, regulatory approvals, and the marketing of our explosives detection products. Our capital requirements depend on numerous factors, including but not limited to the progress of our research and development programs; the cost of filing, prosecuting, defending and enforcing any intellectual property rights; competing technological and market developments; changes in our development of commercialization activities and arrangements; and the hiring of additional personnel, and acquiring capital equipment. Our failure to achieve our projections and/or obtain sufficient additional capital on acceptable terms would have a material adverse effect on our liquidity and operations and could require us to file for protection under bankruptcy laws.

2. Summary of Significant Accounting Policies

Principles of Consolidation

The accompanying consolidated financial statements include our operations in Massachusetts, California and Shanghai, China, and those of our wholly-owned subsidiaries (See Note 12). All intercompany transactions and accounts have been eliminated in consolidation.

Accounting Principles

The consolidated financial statements and accompanying notes are prepared in accordance with U.S. generally accepted accounting principles ("U.S. GAAP").

Use of Accounting Estimates

The preparation of these financial statements in conformity with U.S. 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 financial statements and the reported amounts of revenues and expenses during the reporting periods. Some of the more significant estimates include allowance for doubtful accounts, allowance for sales returns, inventory valuation, warranty reserves, accounting for derivatives, and impairment of intangibles and long-lived assets. Management's estimates are based on the facts and circumstances available at the time estimates are made, past historical experience, risk of loss, general economic conditions and trends and management's assessments of the probable future outcome of these matters. Consequently, actual results could differ from such estimates.

Foreign Currency Translation

The assets and liabilities of our Shanghai representative office are translated into U.S. dollars at current exchange rates as of the balance sheet date, expenses are translated at average monthly exchange rates. Net unrealized translation gains or losses associated with the Shanghai office are recorded directly to other comprehensive income. Realized gains and losses from foreign currency transactions were not material for any of the periods presented. We have short-term inter-company receivables from our Shanghai office which are adjusted each period for changes in foreign currency exchange rates with a corresponding entry recorded as a component of the consolidated statement of operations.

Retroactive Adjustment

In January 2013, we filed Articles of Amendment to our Restated Articles of Organization with the Commonwealth of Massachusetts to effect an increase in the total number of shares of common stock we are authorized to issue to 200,000,000 shares and to reduce the par value of our common stock from $0.10 per share to $0.001 per share. All share information has been retroactively adjusted to reflect the change in the par value of our common stock.

Cash and Cash Equivalents

We consider any securities with original maturities of 90 days or less at the time of investment to be cash equivalents. We place our cash with financial institutions which we believe are of high credit quality. At June 30,

2015, there are significant concentrations of credit risk arising from cash deposits in excess of federally insured limits.

Equity Transactions

We evaluate the proper classification of our equity instruments that embody an unconditional obligation requiring the issuer to redeem it by transferring assets at a determinable date or that contain certain conditional obligations, typically classified as equity, be classified as a liability. We record financing costs associated with our capital raising efforts in our statements of operations. These include amortization of debt issue costs such as cash, warrants and other securities issued to finders and placement agents, and amortization of preferred stock discount created by in-the-money conversion features on convertible debt and the allocation of the proceeds amongst the securities based on relative fair values or based upon the residual method. We based our estimates and assumptions on the best information available at the time of valuation, however, changes in these estimates and assumptions could have a material effect on the valuation of the underlying instruments.

Fair Value Measurements

Accounting Standards Codification ("ASC") ASC 820, "Fair Value Measurements and Disclosures," establishes a three level fair value hierarchy to classify the inputs used in measuring fair value, which are as follows:

Level 1 inputs to the valuation methodology are based on quoted prices (unadjusted) in active markets for identical assets or liabilities;

Level 2 inputs to the valuation methodology are based on inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly; and

Level 3 inputs to the valuation methodology are based on unobservable inputs that reflect the Company's own assumptions about the assumptions market participants would use in pricing the asset or liability.

Financial 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 of Financial Instruments

Our financial instruments at June 30, 2015 and 2014 include cash equivalents, restricted cash, accounts receivable accounts payable and borrowings under our senior secured convertible promissory note, senior secured promissory note and a revolving line of credit. The carrying amounts of cash and cash equivalents, restricted cash, receivables, and accounts payable are representative of their respective fair values because of the short-term maturities or expected settlement dates of these instruments. The fair value of debt, included in Note 13, is based on the fair value of similar instruments. These instruments are short-term in nature and there is no known trading market for our debt.

The following table provides the non-recurring fair value measurements of assets and liabilities as of June 30, 2015:

		Fair Value Measurements as of June 30, 2015		
Description *(In thousands)*	**Carrying Value at June 30, 2015**	**Quoted Prices in Active Markets for Identical Asset Level 1**	**Significant Other Observable Inputs Level 2**	**Significant Unobservable Inputs Level 3**
Certificates of deposit	$ 312	$ 312	$ -	$ -
Senior secured promissory note – BAM	20,000	-	-	20,000
Senior secured convertible promissory note – Montsant	3,184	-	-	3,184
Senior secured promissory note - DMRJ	1,000	-	-	1,000
Second senior secured convertible promissory note – DMRJ	12,000	-	-	12,000
Third senior secured convertible promissory note – DMRJ	12,000	-	-	12,000
Line of credit - DMRJ	16,662	-	-	16,662

The following table provides the non-recurring fair value measurements of assets and liabilities as of June 30, 2014:

		Fair Value Measurements as of June 30, 2014		
Description *(In thousands)*	**Carrying Value at June 30, 2014**	**Quoted Prices in Active Markets for Identical Asset Level 1**	**Significant Other Observable Inputs Level 2**	**Significant Unobservable Inputs Level 3**
Certificates of deposit	$ 624	$ 624	$ -	$ -
Senior secured promissory note – BAM	20,000	-	-	20,000
Senior secured convertible promissory note – DMRJ	3,184	-	-	3,184
Senior secured promissory note - DMRJ	1,000	-	-	1,000
Second senior secured convertible promissory note – DMRJ	12,000	-	-	12,000
Third senior secured convertible promissory note – DMRJ	12,000	-	-	12,000
Line of credit - DMRJ	2,995	-	-	2,995

Inventories

Inventories consist of raw materials, work-in-process and finished goods. Work-in-process and finished goods includes labor and overhead, and are stated at the lower of cost (first in, first out) or market.

Property and Equipment

Property and equipment are stated at cost, less accumulated depreciation and amortization, are depreciated using the straight-line method over the estimated useful lives of the assets, ranging from three to seven years. Equipment purchased under capital leases and leasehold improvements are amortized based upon the lesser of the term of the lease or the useful life of the asset and such expense is included in depreciation expense. Expenditures for repairs and maintenance are charged to expense as incurred.

Warranty Costs

We accrue warranty costs in the period the related revenue is recognized and adjust the reserve balance as needed to address potential future liabilities.

The following table presents the activity in our warranty reserve for the years ended June 30, 2015 and 2014:

	Years Ended June 30,	
(In thousands)	**2015**	**2014**
Beginning balance	$ 547	$ 517
Warranty provision	354	93
Warranty expenditures	(345)	(63)
Ending Balance, June 30	$ 556	$ 547

Income Taxes

The liability method is used to account for income taxes. Deferred tax assets and liabilities are determined based on differences between the financial reporting and income tax bases of assets and liabilities as well as net operating loss and tax credit carry forwards and are measured using the enacted tax rates and laws that will be in effect when the differences reverse. Deferred tax assets may be reduced by a valuation allowance to reflect the uncertainty associated with their ultimate realization.

Patent Costs

As of June 30, 2015, there were nineteen active patents issued. We expense legal costs and fees associated with patent applications and patent maintenance as incurred.

Intangible Assets and Impairment of Long-Lived Assets

We evaluate finite-lived intangible assets for impairment as events and circumstances indicate that the carrying amount may not be recoverable and at a minimum at each balance sheet date in accordance with Accounting Standards Codification ("ASC") 350 "Intangibles – Goodwill and Other" ("ASC 350"). Long-lived assets, which includes property and equipment are evaluated for impairment as events and circumstances indicated that the carrying amount may not be recoverable and at a minimum at each balance sheet date in accordance with ASC 360 "Property, Plant and Equipment." We evaluate the realizability of our long-lived assets based on profitability and undiscounted cash flow expectations for the related asset or subsidiary.

ASC 350 requires that intangible assets with indefinite lives be measured for impairment at least annually or whenever events indicate that there may be an impairment. We recognize an impairment of a long-lived asset if the carrying value of the long-lived asset is not recoverable from its estimated future cash flows. We measure an impairment loss as the difference between the carrying amount of the asset and its estimated fair value.

Concentration of Credit Risk and Major Customers

Financial instruments that potentially subject us to concentration of credit risk consist of trade receivables.

We grant credit to our customers, primarily large corporations, foreign governments and the U.S. government. We perform periodic evaluations of customer's payment history and generally do not require collateral. Receivables are generally due within thirty days. Credit losses have historically been minimal, which is consistent with our expectations. Allowances are provided for estimated amounts of accounts receivable which may not be collected.

As of June 30, 2015, we had one irrevocable standby letter of credit outstanding in the approximate amount of $297,000. The letter of credit provides warranty performance security equal to 5% of the contract amount with the India Ministry of Defence. We have amended the letter of credit, extending the expiration date to May 4, 2015. On May 1, 2015, we obtained the release of the performance security bond, which expired on November 4, 2014, from the India Ministry of Defence and received the collateralized deposit.

We have no other significant off-balance sheet risk such as foreign-exchange contracts, option contracts or other foreign hedging arrangements.

We place our cash with financial institutions which we believe are of high credit quality.

Our revenues are derived from both domestic and international sales. During the fiscal years ended June 30, 2015, 2014 and 2013, international sales represented approximately 85%, 76% and 88%, respectively, of our revenue. For the fiscal year ended June 30, 2015, a customer from the Netherlands and a customer from Norway represented approximately 18% and 16% of our revenue, respectively. During the fiscal year ended June 30, 2014, a customer from Japan and a Taiwanese customer represented 18% and 11%, respectively, of our revenue. For the fiscal year ended June 30, 2013, a customer from India and a customer from France represented approximately 48% and 10% of our revenue, respectively.

At June 30, 2015, three customers accounted for approximately $675,000 of accounts receivable, or 73% of accounts receivable outstanding as of that date. At June 30, 2014, three customers accounted for approximately $341,000 of accounts receivable, or 63% of accounts receivable outstanding as of that date.

We rely on a single contract manufacturer to provide manufacturing services for our QS-H150 handheld explosives detection product. If these services become unavailable, we would be required to identify and enter into an agreement with a new contract manufacturer or take the manufacturing in-house. From time to time in fiscal 2015, this manufacturer has limited the number of detectors it would manufacture due to our inability to pay for the detectors on a timely basis. In addition, this manufacturer has required that we prepay for materials and component parts in advance of procurement. The refusal to manufacture detectors for a substantial period, or the loss of our contract manufacturer altogether, could significantly disrupt production as well as increase the cost of production, thereby increasing the prices of our products. These changes could have a material adverse effect on our business and results of operations.

Stock-Based Compensation

For the fiscal years ended June 30, 2015, 2014 and 2013, we recorded stock-based compensation expense for options that vested of approximately $2,680,000, $2,649,000 and $13,908,000, respectively, as follows:

	Years Ended June 30,		
(In thousands)	**2015**	**2014**	**2013**
Cost of revenues	$ 202	$ 131	$ 795
Research and development	456	387	1,013
Selling, general and administrative	2,022	2,131	12,100
Total	$ 2,680	$ 2,649	$ 13,908

As of June 30, 2015, the Company has approximately $1,536,000 of unrecognized compensation cost related to stock options that is expected to be recognized as expense over a weighted average period of 1.0 years.

The valuation of employee stock options is an inherently subjective process, since market values are generally not available for long-term, non-transferable employee stock options. Accordingly, an option pricing model is utilized to derive an estimated fair value. The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options, which have no vesting restrictions and are fully transferable. In calculating the estimated fair value of our stock options we use the Black-Scholes pricing model, which requires the consideration of the following six variables for purposes of estimating fair value:

- the stock option exercise price;
- the expected term of the option;
- the grant price of the our common stock, which is issuable upon exercise of the option;
- the expected volatility of our common stock;
- the expected dividends on our common stock; and
- the risk free interest rate for the expected option term.

The fair value of each option granted during fiscal years 2015, 2014 and 2013 is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions:

	Stock Option Plans Years Ended June 30,		
	2015	**2014**	**2013**
Dividend yield	0.0%	0.0%	0.0%
Expected volatility	68% - 80%	73% - 123%	127% - 145%
Range of risk-free interest rate	1.23% - 1.94%	1.11% - 1.84%	0.34% - 0.93%
Expected life (years)	5.4 years	5.6 years	5.8 years
Forfeiture rate	9.3%	6.6%	6.3%

Stock Option Exercise Price and Grant Date Price of Common Stock. The closing market price of our common stock on the date of grant.

Expected Term. The expected term of options granted is calculated using our historical option exercise transactions and reflects the period of time that options granted are expected to be outstanding.

Expected Volatility. The expected volatility is a measure of the amount by which our stock price is expected to fluctuate during the expected term of options granted. We determine the expected volatility solely based upon the historical volatility of our common stock over a period commensurate with the option's expected term. We do not believe that the future volatility of our common stock over an option's expected term is likely to differ significantly from the past.

Expected Dividends. We have never declared or paid any cash dividends on any of our capital stock and do not expect to do so in the foreseeable future. Accordingly, we use an expected dividend yield of zero to calculate the grant-date fair value of a stock option.

Risk-Free Interest Rate. The risk-free interest rate is the implied yield available on U.S. Treasury zero-coupon issues with a remaining term equal to the option's expected term on the grant date.

We were also required to estimate the level of award forfeitures expected to occur and record compensation expense only for those awards that are ultimately expected to vest. This requirement applies to all awards that are not yet vested. We have determined, based on actual forfeitures, that our forfeiture rate is approximately 10%. We revisit this assumption periodically and as changes in the composition of our option pool dictate.

Changes in the inputs and assumptions as described above can materially affect the measure of estimated fair value of share-based compensation. We anticipate the amount of stock-based compensation will increase in the future as additional options are granted.

Revenue Recognition

We recognize revenue when there is persuasive evidence of an arrangement with the customer which states a fixed or determinable price and terms, delivery of the product has occurred or the service has been performed in accordance with the terms of the sale, and collectibility of the related receivable is reasonably assured. We provide for estimated returns at the time of shipment based on historical data. Shipping costs charged to the customer are included in revenues and are not significant.

We allocate consideration for each deliverable as a separate unit of accounting based on its relative selling price. We determine selling price using vendor specific objective evidence ("VSOE"), if it exists, and otherwise third party evidence ("TPE"). If neither VSOE nor TPE of selling price exists for a unit of accounting, we use estimated selling price ("ESP"). We generally expect that we will not be able to determine TPE due to the nature of the markets in which we compete, and, as such, we typically determine selling price using VSOE or if not available, ESP. VSOE is the price charged when the same or similar product or service is sold separately. If a product or service is seldom sold separately, it is unlikely that we can determine VSOE for the product or service. TPE is determined based on prices charged by competitors of us for a similar deliverable when sold separately. Generally we are not able to use TPE, as we are usually not able to obtain sufficient information on competitor pricing to substantiate TPE. The objective of ESP is to determine the price at which we would transact if the product or service were sold on a standalone basis. We determine ESP for product or services based on the specific facts and circumstances of the arrangement. Maintenance or service revenues are recognized over the term of the contract.

Contract revenue under fixed price and cost-plus agreements with the Department of Defense and the Department of Homeland Security are recognized as eligible research and development expenses are incurred. Our obligation with respect to these agreements is to perform the research on a best-efforts basis.

Deferred revenues are recorded when we receive payments for product or services for which we have not yet completed our obligation to deliver product or have not completed services required by contractual agreements.

Accounts Receivable

Contract revenue under cost sharing research and development agreements is recognized as eligible expenses are incurred. Invoicing of research and development contracts occurs in accordance with the terms of the contract. Revenue recognized but unbilled is recorded as unbilled accounts receivable. At June 30, 2015 and 2014, there were no unbilled accounts receivable. Generally, there are no prerequisites necessary to invoice.

We grant credit to domestic and foreign customers and perform ongoing credit evaluations of our customers' financial condition. We continuously monitor collections and payments from our customers and maintain a provision for estimated credit losses based upon specific customer collection issues.

Research and Development Costs

All costs of research and development activities are expensed as incurred. We spent approximately $5,014,000, $4,787,000 and $4,754,000 on internally funded research and development in the fiscal years ended June 30, 2015, 2014 and 2013, respectively.

Software Development Costs

The development costs of new software and substantial enhancements to existing software are expensed as incurred until technological feasibility has been established, at which time any additional costs are capitalized. We believe technological feasibility has been established at the time at which a working model of the software has been completed. Costs eligible for capitalization have been immaterial.

Advertising Costs

Advertising costs are expensed when incurred and are included in selling, general and administrative expense. Advertising costs were immaterial for the years ended June 30, 2015, 2014 and 2013.

Shipping and Handling

We account for shipping and handling cost within our cost of revenues.

Basic and Diluted Earnings Per Share

Basic earnings per share is computed by dividing net income (loss) by the weighted average number of common shares outstanding during the period. Diluted earnings per share are based upon the weighted average number of common shares outstanding during the period plus additional weighted average common equivalent shares outstanding during the period. Common equivalent shares result from the assumed exercise of outstanding stock options and warrants, the proceeds of which are then assumed to have been used to repurchase outstanding common stock using the treasury stock method and assumed conversion of certain convertible promissory notes and convertible preferred stock. In addition, the numerator is adjusted for any changes in income or loss that would result from the assumed conversion of potential shares. As of June 30, 2015, 2014 and 2013, potentially dilutive shares would have been excluded from the earnings per share calculation, because their effect would be antidilutive. Shares deemed to be antidilutive include stock options, warrants, convertible debt and convertible preferred stock.

	For the Years Ended June 30,		
(In thousands, except share and per share amounts)	**2015**	**2014**	**2013**
Basic loss per share:			
Numerator:			
Net loss	$ (21,543)	$ (21,010)	$ (27,354)
Denominator:			
Weighted average shares	70,770,705	60,753,054	49,124,942
Basic loss per share	$ (0.30)	$ (0.35)	$ (0.56)
Diluted loss per share:			
Numerator:			
Net loss	$ (21,543)	$ (21,010)	$ (27,354)
Denominator:			
Weighted average shares	70,770,705	60,753,054	49,124,942
Effect of dilutive securities:			
Stock options	-	-	-
Warrants	-	-	-
Convertible debt	-	-	-
Convertible preferred stock	-	-	-
	-	-	-
Weighted average shares and equivalents	70,770,705	60,753,054	49,124,942
Diluted loss per share	$ (0.30)	$ (0.35)	$ (0.56)

Common stock equivalents excluded from the earnings per share calculation, because their effect would be antidilutive, for the years ended June 30, 2015, 2014 and 2013 were as follows:

	For the Years Ended June 30,		
	2015	**2014**	**2013**
Common stock equivalents excluded:			
Stock options	1,321,215	1,690,757	2,582,322
Warrants	345,529	293,213	742,248
Convertible debt	39,800,000	39,800,000	52,981,368
Convertible preferred stock	-	407,500	9,140,500
	41,466,744	42,191,470	65,446,438

Recent Accounting Pronouncements

In May 2014, the FASB issued Accounting Standards Update 2014-09, *Revenue from Contracts with Customers* ("ASU 2014-09"), which supersedes the revenue recognition requirements in ASC 605, *"Revenue Recognition"*. The FASB issued ASU 2014-09 to clarify the principles for recognizing revenue and to develop a common revenue

standard for U.S. GAAP and International Financial Reporting Standards. The core principle of this updated guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The new rule also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. This guidance is effective for annual reporting periods beginning after December 15, 2016, including interim reporting periods therein, which is effective for our fiscal year beginning July 1, 2017, the first day of our 2018 fiscal year. We are currently evaluating the impact of this accounting guidance and do not expect any significant impact on our consolidated financial statements.

In June 2014, the FASB issued Accounting Standards Update 2014-12, *Compensation-Stock Compensation* ("ASU 2014-12"). The FASB issued ASU 2014-12 to provide specific guidance on share-based payment awards that provide for achievement of a specific performance target that could be achieved after the requisite service period. ASU 2014-12 requires that a performance target that affects vesting and that could be achieved after the requisite service period should be treated as a performance condition. As such, the performance target should not be reflected in estimating the grant-date fair value of the award. Compensation cost should be recognized in the period in which it becomes probable that the performance target will be achieved and should represent the compensation cost attributable to the period(s) for which the requisite service has already been rendered. This guidance is effective for annual periods and interim periods within those annual periods beginning after December 15, 2015, which is effective for our fiscal year beginning July 1, 2016, the first day of our 2017 fiscal year. Earlier adoption is permitted. ASU 2014-12 may be applied prospectively to all awards granted or modified after the effective date or retrospectively to all awards with performance targets that are outstanding as of the beginning of the earliest annual period presented in the financial statements and to all new or modified awards thereafter. If retrospective transition is adopted, the cumulative effect of applying this guidance should be recognized in the financial statements as an adjustment to the opening retained earnings balance at that date. We are currently evaluating the impact of this accounting guidance and do not expect any significant impact on our consolidated financial statements.

In August 2014, the FASB issued Accounting Standards Update 2014-15, *Presentation of Financial Statements-Going Concern (Subtopic 205-40)* ("ASU 2014-15"). ASU 2014-15 provides guidance to U.S. GAAP about management's responsibility to evaluate whether there is a substantial doubt about an entity's ability to continue as a going concern and to provide related footnote disclosures. This new rule requires management to assess an entity's ability to continue as a going concern by incorporating and expanding upon certain principles currently in U.S. auditing standards. Specifically, ASU 2014-15 (1) defines the term substantial doubt, (2) requires an evaluation of every reporting period including interim periods, (3) provides principles for considering the mitigating effect of management's plan, (4) requires certain disclosures when substantial doubt is alleviated as a result of consideration of management's plans, (5) requires an express statement and other disclosures when substantial doubt is not alleviated, and (6) requires an assessment for a period of one year after the date that the financial statements are issued. This guidance is effective for annual periods ending after December 15, 2016, which is effective for our fiscal year beginning July 1, 2016, the first day of our 2017 fiscal year. We are currently evaluating the impact of this accounting guidance and do not expect any significant impact on our consolidated financial statements.

In July 2015, the FASB issued Accounting Standards Update 2015-11, *Inventory (Topic 330)* ("ASU 2015-11"). ASU 2015-11 was issued to more closely align the measurement of inventory in U.S. GAAP with the measurement of inventory in International Financial Reporting Standards. The core principle of this updated guidance is that an entity should measure inventory at the lower of cost or net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. The amendments in ASU 2015-11 apply to inventory that is measured using the first-in, first-out or average cost methods. ASU 2015-11 amends some of the guidance in Topic 330 to more clearly articulate the requirements for the measurement and disclosure of inventory, but the clarifications are not intended to result in any changes in practice other than the change in the subsequent measurement guidance from the lower of cost or market to the lower of cost or net realizable value for inventory. There are no other substantive changes to the guidance on the measurement of inventory. This guidance is effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years, which is effective for our fiscal year beginning July 1, 2017, the first day of our 2018 fiscal year. We are currently evaluation the impact of this accounting guidance and do not expect any significant impact on our consolidated financial statements.

3. Restricted Cash and Investments – Current and Long-Term

As of both June 30, 2015 and 2014, we had restricted cash and investments, with maturities of less than one year, of $367,000 and $312,000, respectively, and as of June 30, 2014 we had restricted investments with maturities

of more than one year, of $312,000. Restricted cash and investments consisted of the following:

(In thousands)	June 30, 2015	2014
Current assets		
Certificates of deposit	$ 312	$ 312
Cash maintained to secure corporate credit card	55	-
	$ 367	$ 312
Long-term assets		
Certificates of deposit	$ -	$ 312
	$ -	$ 312

The restricted investments of $312,000 held in certificates of deposit collateralize our performance under an irrevocable letter of credit issued in April 2010, aggregating to $297,000, in connection with our contract with the India Ministry of Defence, plus the bank required collateralization deposit of $15,000. The letter of credit provides warranty performance security equal to 5% of the contract amount under the terms of the contract with the India Ministry of Defence. We have amended the letter of credit, extending the expiration date to May 4, 2015, respectively. On May 1, 2015, we obtained the release of the performance security bond, which expired on November 4, 2014, from the India Ministry of Defence and received the collateralized deposit of $312,000.

In May 2015, we entered into a corporate credit card agreement with our primary bank, pursuant to which the bank reserves $55,000 of our available cash held in our operating account maintained with the bank to collateralize 105% of the credit limit that is available under the credit card agreement.

4. Inventories, net

We value our inventories at lower of cost or market. Cost is determined by the first-in, first-out (FIFO) method, including material, labor and factory overhead. The components of inventories, net of reserves for excess and slow-moving inventories, consist of the following:

(In thousands)	June 30, 2015	2014
Raw materials	$ 3,283	$ 1,897
Work in progress	1,455	616
Finished goods	525	355
Total inventories	$ 5,244	$ 2,868

As of June 30, 2015 and 2014, our reserves for excess and slow-moving inventories were $218,000 and $213,000, respectively.

5. Prepaid Expenses and Other Current Assets

Prepaid expenses and other current assets consist of the following:

(In thousands)	June 30, 2015	2014
Inventory deposits	$ 677	$ -
Insurance	87	61
Bank fees	14	18
Other prepaid expenses	168	236
	$ 946	$ 315

6. Property, Plant and Equipment, net

Property and equipment consist of the following:

(In thousands)	June 30, 2015	2014
Machinery and equipment	$ 875	$ 484
Computers and software	415	413
Furniture and fixtures	83	69
Leasehold improvements	159	151

Equipment under capital lease	157	157
	1,689	1,274
Less: accumulated depreciation and amortization	809	655
	$ 880	$ 619

Depreciation expense for the fiscal years ended June 30, 2015, 2014 and 2013 was approximately $171,000, $154,000 and $84,000, respectively. During the fiscal year ended June 30, 2013, we recognized a gain of $9,000 on the disposition of property, plant and equipment with a cost of approximately $161,000 and no net book value. During the fiscal year ended June 30, 2014, we recognized a $56,000 loss on the disposition of property, plant and equipment with a cost of approximately $135,000 and a net book value of $57,000. During the fiscal year ended June 30, 2015, we recognized a loss of $1,000 on the disposition of property, plant and equipment with a cost of approximately $18,000 and a net book value of $1,000.

7. Accrued Expenses – Current and Long-Term

Accrued expenses consist of the following:

	June 30,	
(In thousands)	**2015**	**2014**
Accrued interest	$ 13,264	$ 9,149
Accrued compensation and benefits	1,774	862
Accrued warranty costs	556	547
Accrued legal and accounting	257	187
Accrued taxes	74	106
Other accrued liabilities	1,155	243
	$ 17,080	$ 11,094
Long-term liabilities		
Accrued termination benefits	$ 48	$ -
	$ 48	$ -

On April 6, 2015, we entered into a letter agreement ("Letter Agreement") with Luveti d.o.o. ("Luveti") pursuant to which we received notification of termination of the prior letter agreement we entered into with Luveti on July 31, 2014 ("Prior Letter Agreement") to provide customized explosive trace detectors to Luveti for distribution under an agreement for the procurement of explosives and narcotics detectors ("Procurement Agreement') between Luveti and the Republic of Croatia, Ministry of the Interior, dated August 20, 2014. Pursuant to such termination, we agreed to pay the sum of $1,315,000 ("Settlement Amount") to Luveti, representing a refund of Luveti's advance payment deposit of $1,212,000 that was received by us on September 4, 2014 and $103,000 of interest and other charges Luveti incurred as a result of the cancellation of their agreement with the Republic of Croatia, Ministry of the Interior. The Settlement Amount will be paid in six monthly payments of $219,000 which commenced on April 8, 2015 and continuing thereafter on a monthly basis up to and including September 5, 2015. As of June 30, 2015, we had paid three installments to Luveti, aggregating to $657,000 and our obligation to Luveti as of that date was $658,000. The Settlement Amount is included in current liabilities on our consolidated balance sheets at June 30, 2015.

In addition, on February 26, 2015, we paid Luveti the sum of $171,000, representing penalties owed by Luveti to the Republic of Croatia, Ministry of the Interior.

During the year ended June 30, 2015, we recorded charges of $274,000 in our consolidated statement of operations and comprehensive loss, to record the additional charges pursuant to the Letter Agreement with Luveti and to reimburse Luveti for penalties owed to the Republic of Croatia, Ministry of the Interior.

8. Income Taxes

We are required to file federal and state income tax returns in the United States. The preparation of these tax returns requires us to interpret the applicable tax laws and regulations in effect in such jurisdictions, which could

affect the amount of tax paid by us. In consultation with our tax advisors, we base our tax returns on interpretations that are believed to be reasonable under the circumstances. The tax returns, however, are subject to routine reviews by the various federal and state taxing authorities in the jurisdictions in which we file tax returns. As part of these reviews, a taxing authority may disagree with respect to the income tax positions taken by us ("uncertain tax positions") and, therefore, may require us to pay additional taxes. As required under applicable accounting rules, we accrue an amount for our estimate of additional income tax liability, including interest and penalties, which we could incur as a result of the ultimate or effective resolution of the uncertain tax positions. We account for income taxes using the asset and liability method. Under the asset and liability method, deferred tax assets and liabilities are recognized for the future tax consequences attributed to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences and carry-forwards are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is established when necessary to reduce deferred tax assets to amounts expected to be realized.

We account for uncertain income tax positions by accruing for the estimated additional amount of taxes for the uncertain tax positions when the uncertain tax position does not meet the more likely than not standard for sustaining the position. We review and update our accrual as more definitive information becomes available from taxing authorities, upon completion of tax audits, upon expiration of statutes of limitation, or upon occurrence of other events. This requires significant judgment, the use of estimates, and the interpretation and application of complex tax laws. Significant judgment is required in assessing the timing and amounts of deductible and taxable items and the probability of sustaining uncertain tax positions. The benefits of uncertain tax positions are recorded in our consolidated financial statements only after determining a more-likely-than-not probability that the uncertain tax positions will withstand challenge, if any, from tax authorities. When facts and circumstances change, we reassess these probabilities and record any changes in the consolidated financial statements as appropriate.

Reconciliation between our effective tax rate and the United States statutory rate is as follows:

	For the Years Ended June 30,		
	2015	2014	2013
Expected federal tax rate	-34.0%	-34.0%	-34.0%
State income taxes, net of federal tax benefit	-3.9%	-2.8%	-3.7%
Non-deductible expenses	2.8%	3.0%	2.5%
Credits and other, net	-0.8%	-0.9%	-0.6%
Changes in valuation allowance	35.9%	34.7%	35.8%
Effective tax rate	0.0%	0.0%	0.0%

Deferred tax assets and liabilities are determined based on the differences between the financial statement carrying amounts and the tax basis of the assets and liabilities using the enacted tax rate in effect in the years in which the differences are expected to reverse. A valuation allowance has been recorded against the deferred tax asset as it is more likely than not, based upon our analysis of all available evidence, that the tax benefit of the deferred tax asset will not be realized.

Significant components of our deferred tax assets and deferred tax liabilities as of June 30, 2015 and 2014 consists of the following:

	June 30,	
(In thousands)	2015	2014
Deferred tax assets:		
Net operating loss and tax credit carryforwards	$ 42,715	$ 35,966
Accrued expenses deductible when paid	1,197	705
Stock-based compensation	5,931	5,472
Financial statement over tax depreciation	-	6
Deferred tax assets	49,843	42,149
Deferred tax liabilities		
Tax over financial statement depreciation	48	33
Deferred tax liabilities	48	33
Net deferred tax assets	49,795	42,116
Valuation allowance	(49,795)	(42,116)

Net deferred tax assets	$ -	$ -

A valuation allowance has been established for our tax assets as their use is dependent on the generation of sufficient future taxable income, which cannot be predicted at this time. Included in the valuation allowance is approximately $800,000 related to certain operating loss carryforwards resulting from the exercise of employee stock options, the tax benefit of which, when recognized, will be accounted for as a credit to additional paid-in capital rather than a reduction in income tax.

The following table summarizes the changes in our deferred tax valuation allowance for the years ended June 30, 2015 and 2014:

	Deferred Tax Valuation Allowance			
(In thousands)	Balance at Beginning of Year	Current Year Additions	Expired Loss Carryforwards	Balance at End of Year
2015	$ 42,116	$ 7,763	$ (84)	$ 49,795
2014	34,834	7,762	(480)	42,116

As of June 30, 2015, the Company has the following unused net operating loss and tax credit carryforwards available to offset future federal and state taxable income, both of which expire at various times as noted below:

(In thousands)	Net Operating Losses	Investment AMT & Research Credits	Expiration Dates
Federal	$ 107,818	$ 1,455	2022 to 2035
State	$ 74,879	$ 983	2016 to 2035

We have recorded a full valuation allowance against our net deferred tax assets of $49,795,000 as of June 30, 2015, due to uncertainties related to our ability to utilize these assets. The valuation allowance is based on our estimates of taxable income and the period over which our deferred tax assets will be recoverable.

Potential 382 Limitation

Our net operating loss and tax credit carryforwards are subject to review and possible adjustment by the Internal Revenue Service. Our ability to utilize our net operating loss ("NOL") and alternative minimum tax ("AMT") and research and development credit ("R&D") carryforwards may be substantially limited due to ownership changes that may have occurred or that could occur in the future, as required by Section 382 of the Internal Revenue Code of 1986, as amended (the "Code"), as well as similar state provisions. These ownership changes may limit the amount of NOL, AMT and R&D credit carryforwards that can be utilized annually to offset future taxable income and tax, respectively. In general, an ownership change, as defined in Section 382 of the Code, results from a transaction or series of transactions over a three-year period resulting in an ownership change of more than 50% of the outstanding stock of a company by certain stockholders or public groups.

We have not completed a study to assess whether one or more ownership changes have occurred since we became a loss corporation as defined in Section 382 of the Code, but we believe that it is likely that an ownership change has occurred. If we have experienced an ownership change, utilization of the NOL, AMT and R&D credit carryforwards would be subject to an annual limitation, which is determined by first multiplying the value of our common stock at the time of the ownership change by the applicable long-term, tax-exempt rate, and then could be subject to additional adjustments, as required. Any such limitation may result in the expiration of a portion of the NOL, AMT or R&D credit carryforwards before utilization. Until a study is completed and any limitation known, no amounts are being considered as an uncertain tax position or disclosed as an unrecognized tax benefit under ASC 740. Any carryforwards that expire prior to utilization as a result of such limitations will be removed from deferred tax assets with a corresponding adjustment to the valuation allowance. Due to the existence of the valuation allowance, it is not expected that any potential limitation will have a material impact on our operating results.

From time to time we may be assessed interest or penalties by major tax jurisdictions, namely the states of Massachusetts and California. We adopted the accounting standards related to accounting for uncertainty in income taxes recognized in an enterprise's financial statements on April 1, 2007. As of June 30, 2015, we had no material unrecognized tax benefits and no adjustments to liabilities or operations were required. No interest and penalties have been recognized by the Company to date.

Tax years 2012 through 2015 are subject to examination by the federal and state taxing authorities. There are

no income tax examinations currently in process.

For the years ended June 30, 2015, 2014 and 2013, we provided for no taxes in our consolidated statement of operations as we have significant net loss carryforwards.

Our net operating loss carryforwards are subject to review and possible adjustment by the Internal Revenue Service and are subject to certain limitations in the event of cumulative changes in the ownership interest of significant stockholders over a three-year period in excess of 50%.

9. Commitments and Contingencies

Capital and Operating Leases

On April 1, 2013, we entered into a lease for manufacturing, research and office space in Wilmington, Massachusetts, the lease of which expires on June 30, 2020. Under the terms of the lease, we are responsible for our proportionate share of real estate taxes and operating expenses relating to this facility. We leased research and office space in San Diego, California and leased 300 square feet of office space in Shanghai, China. On March 25, 2015, our Board of Directors approved restructuring actions to better align costs with current and future geographic revenue sources and to improve efficiencies. Our Shanghai office closing will be completed in the second quarter of fiscal 2016 and we have exited from our lease in San Diego, CA (See Note 12). Total rent expense, including assessments for maintenance and real estate taxes for the years ended June 30, 2015, 2014 and 2013, was $910,000, $919,000 and $395,000, respectively.

Future minimum rental payments required under capital and operating leases with non-cancelable terms in excess of one year at June 30, 2015, together with the present value of net minimum lease payments, are as follows:

(In thousands)	Capital Lease Payments	Operating Lease Payments
Years ending June 30:		
2016	$ 51	$ 562
2017	16	583
2018	7	613
2019	1	642
2020 and thereafter	-	656
	75	$ 3,056
Less: Amounts representing interest	(10)	
Present value of future minimum lease payments	65	
Less: Current portion	(45)	
Long-term obligation under capital leases	$ 20	

License Agreements

We are obligated under one license agreement, assumed in connection with the acquisition of Ion Metrics, whereby we were granted rights to use certain intellectual property for safety, security and narcotic applications, which we intend to incorporate into future security product offerings for certain minimum guaranteed annual payments.

For the years ended June 30, 2015, 2014 and 2013, payments under a license agreement amounted to $0, $150,000 and $125,000, respectively. The license agreement expires on September 30, 2016 and as of June 30, 2015, we have no obligation under this license agreement for future minimum guaranteed payments.

10. Financial Information by Segment

Operating segments are defined as components of an enterprise about which separate financial information is available that is regularly evaluated by the chief operating decision maker or decision making group, in determining how to allocate resources and in accessing performance. Our chief operating decision making group is composed of the chief executive officer and members of senior management. Based on qualitative and quantitative criteria we have determined that we operate within one reportable segment, which is the Security Products Segment.

During the fiscal years ended June 30, 2015, 2014 and 2013, international sales represented approximately 85%, 76% and 88%, respectively, of our revenue. For the fiscal year ended June 30, 2015, a customer from the Netherlands and a customer from Norway represented approximately 18% and 16% of our revenue, respectively. During the fiscal year ended June 30, 2014, a customer from Japan and a Taiwanese customer represented 18% and

11%, respectively, of our revenue. For the fiscal year ended June 30, 2013, a customer from India and a customer from France represented approximately 48% and 10% of our revenue, respectively.

11. Related Party Transactions

Robert Liscouski, a member of our Board of Directors, had served as a partner at Secure Strategy Group, a homeland security-focused banking and strategic advisory firm that has been retained by us to assist with our efforts to acquire additional capital. During the years ended June 30, 2015, 2014 and 2013, this advisory firm was paid $0, $0 and $66,000, respectively. We terminated our relationship with Secure Strategy Group on March 31, 2013. On March 5, 2014, we executed a settlement agreement and release with Secure Strategy Group and recognized a non-cash benefit of $118,000 in our consolidated statement of operations and comprehensive income and, as of June 30, 2015, our obligation to Secure Strategy Group was $0.

In April 2011, we entered into an advisory and consulting agreement with Mr. Liscouski to assist our U.S. government sales and marketing team with our efforts to advance our interests with the U.S. government. During the years ended June 30, 2015, 2014 and 2013, Mr. Liscouski was paid $105,000, $180,000 and $180,000, respectively. As of June 30, 2015, we had no obligation to Mr. Liscouski.

Mr. Liscouski also serves as a senior partner at Edge360, a leading security technology and situational awareness solutions provider to the homeland security marketplace that has been retained by us. During the fiscal years ended June 30, 2015, 2014 and 2013, this advisory firm was paid $0, $4,000 and $27,000, respectively. On August 31, 2013, we terminated our relationship with Edge360 and, as of June 30, 2015, we had no obligation to Edge360.

On August 15, 2014, August 29, 2014, September 18, 2014 and October 2, 2014, Roger Deschenes, our Chief Financial Officer, advanced $100,000, $125,000, $125,000 and $100,000, respectively, for general working capital purposes, of which $450,000 of principal and $12,000 of interest has been repaid to Mr. Deschenes during the year ended June 30, 2015. The advances were payable on demand and bore interest at 15%. As of June 30, 2015 our obligation to Mr. Deschenes was $0.

12. Restructuring Charge

On March 25, 2015, our Board of Directors approved restructuring actions to better align costs with current and future geographic revenue sources and to improve efficiencies. For year ended June 30, 2015, we recorded a charge of $150,000 in our consolidated statement of operations and comprehensive income for expenses expected to be incurred to relocate the San Diego, CA advanced technology office, costs related to closing our Shanghai office and converting our sales model in Southeast Asia from direct selling to in-country distribution. Details of the restructuring charge are as follows:

	For the Year Ended June 30, 2015				
(In thousands)	Severance	Lease Commitments	Relocation	Other	Total
Cost of Revenues	$ 9	$ -	$ -	$ -	$ 9
Research & Development	38	59	10	3	110
Selling, General and Administrative	-	16	15	-	31
Total	$ 47	$ 75	$ 25	$ 3	$ 150

The following table presents the activity in our restructuring reserve for the year ended June 30, 2015, which is included in current liabilities on our consolidated balance sheet at that date;

(In thousands)	For the Year Ended June 30, 2015
Beginning balance	$ -
Initial restructuring charge	150
Payments	(52)
Restructuring charge adjustments	(72)
Ending Balance, June 30	$ 26

13. Long-Term Debt and Credit Arrangements

Term Debt and Revolving Credit Facility with DMRJ Group, LLC and Term Debt with Montsant Partners, LLC

We are a party to several loan and credit agreements with DMRJ Group LLC ("DMRJ"), an accredited institutional investor. In December 2008, we entered into a note and warrant purchase agreement with DMRJ pursuant to which we issued a senior secured convertible promissory note in the principal amount of $5,600,000 and a warrant to purchase 1,000,000 shares of our common stock. Thereafter, we entered into a series of amendments, waivers and modifications of this facility. The note, which is collateralized by all of our assets, originally bore interest at 11.0% per annum.

The note contains restrictions and financial covenants including: (i) restrictions against declaring or paying dividends or making any distributions; against creating, assuming or incurring any liens; against creating, assuming or incurring any indebtedness; against merging or consolidating with any other company, *provided, however*, that a merger or consolidation is permitted if we are the surviving entity; against the sale, assignment, transfer or lease of our assets, other than in the ordinary course of business and excluding inventory and certain asset sales expressly permitted by the note purchase agreement; against making investments in any company, extending credit or loans, or purchasing stock or other ownership interest of any company; and (ii) covenants that we have authorized or reserved for the purpose of issuance, 150% of the aggregate number of shares of our common stock issuable upon exercise of the warrant; that we maintain a minimum cash balance of at least $500,000; that the aggregate dollar amount of all accounts payable be no more than 100 days past due; and that we maintain a current ratio, defined as current assets divided by current liabilities, of no less than 0.60 to 1.00.

In September 2011, we amended each of our credit instruments with DMRJ. Pursuant to those amendments: (i) the maturity of our indebtedness to DMRJ was extended from September 30, 2011 to March 31, 2013; (ii) DMRJ waived our compliance with certain financial covenants in the notes and all related credit agreements through maturity; (iii) our line of credit under the September 2009 credit agreement was increased from $15,000,000 to $23,000,000; and (iv) we were required to repay sufficient amounts of our outstanding indebtedness under the notes and related credit agreements and other amounts owing to DMR such that as of December 31, 2011, the outstanding obligations to DMRJ shall not exceed $15,000,000.

In October 2011, we further amended each of our credit instruments with DMRJ, to eliminate the obligation to repay any portion of our outstanding indebtedness to DMRJ by December 31, 2011.

In February 2012, we amended each of our credit instruments with DMRJ, to extend the maturity of all of our indebtedness to DMRJ to September 30, 2012.

In September 2012, we further amended each of our credit instruments with DMRJ. Pursuant to those amendments: (i) we extended the maturity date of all of our indebtedness from September 30, 2012 to March 31, 2013 and (ii) issued to DMRJ a second senior secured convertible promissory note in the principal amount of $12,000,000 (the "September 2012 Note").

The second senior secured convertible promissory note bears interest at the rate of 15% per annum. The principal balance of this note, together with all outstanding interest and all other amounts owed thereunder, was due and payable on March 31, 2013. The second senior secured convertible promissory note is convertible in whole or in part, at DMRJ's option, into shares of Series H Convertible Preferred Stock at an initial conversion rate of $1,000 per share (as adjusted in the event of any stock dividend, stock split, combination or other similar recapitalization with respect to the Series H Preferred Stock, the "Series H Original Issue Price").

The second senior secured convertible promissory note originally gave DMRJ the option to require us to repurchase any or all of the shares of Series H Preferred Stock owned by DMRJ, at the Series H Original Issue Price per share, if we did not (i) by March 31, 2013, have at least one of our products receive qualified or approved status on the "Transportation Security Administration Air Cargo Screening Technology List (ACSTL) – For Passenger Aircraft" or placed on the Transportation Security Administration's "Explosive Trace Detector Qualified Product List (QPL)"; or (ii) achieve revenues of at least $7,500,000 per fiscal quarter, commencing with fiscal quarter ending June 30, 2013. As described below, the note was subsequently amended to eliminate this option.

The holders of the Series H Preferred Stock will be entitled to receive, prior to the payment of any dividends with respect to our Common Stock and/or Series G Convertible Preferred Stock, cumulative dividends on each share of Series H Preferred Stock at a rate equal to 15% of the Series H Original Issue Price per annum, (i) when, as and if declared by our Board of Directors, (ii) upon a liquidation, dissolution or winding up of the Company (a "Liquidation Event"), or (iii) upon the repurchase or conversion of the Series H Preferred Stock All dividends accruing on the Series H Preferred Stock are payable by the issuance of additional shares of Series H Preferred Stock.

Upon a Liquidation Event, the holders of shares of Series H Preferred Stock then outstanding will be entitled to be paid out of the assets of the company available for distribution to its stockholders, before any payment is made to the holders of Common Stock and/or Series G Preferred Stock in respect of such stock, an amount per share equal to the Series H Original Issue Price, plus any accrued but updated dividends thereon, whether or not declared. At the option of holders of a majority of the outstanding Series H Preferred Stock, (i) a consolidation or merger of us with or into another entity or person, or any other corporate reorganization, in which our stockholders immediately prior to such consolidation, merger or reorganization do not hold at least a majority of the resulting or surviving entities' voting power immediately following such consolidation, merger or reorganization, or (ii) a sale or transfer of all or substantially all of our assets for cash, securities or other property, will be deemed to be a Liquidation Event.

Each share of Series H Preferred Stock will be convertible, at the option of the holder, into that number of shares of Common Stock as is determined by (i) dividing the Series H Original Issue Price by the Series H Conversion Price (as defined below) in effect at the time of conversion and (ii) multiply the result by 1,000. The "Series H Conversion Price" will initially be equal to $1,090, and is subject to adjustment in the event that (a) we issue additional shares of Common Stock as a dividend or other distribution on outstanding shares of Common Stock, (b) there is a split or subdivision of outstanding shares of Common Stock, or (c) there is a combination or reverse stock split of outstanding shares of Common Stock into a smaller number of shares of Common Stock. Assuming no adjustments to the Series H Original Issue Price or the Series H Conversion Price, the New Note will be convertible indirectly, at DMRJ's option, into shares of Common Stock at an effective conversion price of $1.09 per share, which represents a discount of approximately 20% from the daily volume weighted average price of the Common Stock over the 20 trading days preceding the date of the amendment.

The holders of the Series H Preferred Stock will have no voting rights except as required by applicable law. However, without the consent of the holders of a majority of the outstanding Series H Preferred Stock, we may not (i) amend, alter or repeal any provision of its Articles of Organization or By-laws in a manner that adversely affects the powers, preferences or rights of the Series H Preferred Stock; (ii) authorize or issue any equity securities (or any equity or debt securities convertible into equity securities) ranking prior and superior to the Series H Preferred Stock with respect to dividends, distributions, redemption rights or rights upon liquidation, dissolution or winding up; or (iii) consummate any capital reorganization or reclassification of any of its equity securities (or debt securities convertible into equity securities) into equity securities ranking prior and superior to the Series H Preferred Stock with respect to dividends, distributions, redemption rights or rights upon liquidation, dissolution or winding up.

On February 28, 2013, we further amended each of our credit instruments with DMRJ. Pursuant to those amendments:

- the maturity of all of our indebtedness to DMRJ was extended from March 31, 2013 to March 31, 2014;
- DMRJ waived our compliance with certain financial covenants in each of our promissory notes and all related credit agreements through the new maturity date;
- DMRJ's option to require us to repurchase any or all of the shares of Series H Convertible Preferred Stock) which may be issued upon conversion of the September 2012 Note was eliminated;
- we issued to DMRJ a third senior secured convertible promissory note dated February 28, 2013, in the aggregate principal amount of $12,000,000. Payment for the February 2013 Note was made by the cancellation of $12,000,000 of principal of the outstanding indebtedness under our credit agreement;
- DMRJ acquired the option to convert the amended and restated senior secured convertible promissory note dated March 12, 2012 (the "March 2012 Note") into shares of Series J Convertible Preferred Stock in lieu of shares of Common Stock; and
- the March 2012 Note and the September 2012 Note were amended to permit us to prepay any or all of our indebtedness thereunder on 30 days' prior notice.

The third senior secured convertible promissory note bears interest at the rate of 15% per annum. The principal balance of this note, together with all outstanding interest and all other amounts owed thereunder, will be due and payable on March 31, 2015. The third senior secured convertible promissory note is convertible in whole or in part, at DMRJ's option, into shares of Series I Convertible Preferred Stock at an initial conversion rate of $1,000 per share (as adjusted in the event of any stock dividend, stock split, combination or other similar recapitalization with respect to the Series I Preferred Stock, the "Series I Original Issue Price"). We may prepay this note on 30 days prior notice.

As amended, the March 2012 Note is convertible in whole or in part, at DMRJ's option, into shares of Series J Convertible Preferred Stock at an initial conversion rate of $1,000 per share (as adjusted in the event of any stock

dividend, stock split, combination or other similar recapitalization with respect to the Series J Preferred Stock, the "Series J Original Issue Price").

The holders of the Series I Preferred Stock will be entitled to receive, prior to the payment of any dividends with respect to our Common Stock and/or Series G Preferred Stock, cumulative dividends on each share of Series I Preferred Stock at a rate equal to 15% of the Series I Original Issue Price per annum, (i) when, as and if declared by our Board of Directors, (ii) upon a "Liquidation Event", or (iii) upon the conversion of the Series I Preferred Stock All dividends accruing on the Series I Preferred Stock are payable by the issuance of additional shares of Series I Preferred Stock.

The holders of Series J Preferred Stock will be entitled to participate on an "as converted" basis in all dividends or distributions declared or paid on our Common Stock.

Upon a Liquidation Event, the holders of shares of Series I Preferred Stock and Series J Preferred Stock then outstanding will be entitled to be paid out of the assets of the company available for distribution to its stockholders, *pari passu* with distributions made with respect to the Series H Preferred Stock but before any payment is made to the holders of Common Stock and /or Series G Preferred Stock in respect of such stock, (i) an amount per share of Series I Preferred Stock equal to the Series I Original Issue Price, plus any accrued but updated dividends thereon, whether or not declared, and (ii) an amount per share of Series J Preferred Stock equal to the Series J Original Issue Price, plus any dividends declared but unpaid thereon. At the option of holders of a majority of the outstanding Series I Preferred Stock, (i) a consolidation or merger of the company with or into another entity or person, or any other corporate reorganization, in which the stockholders of the company immediately prior to such consolidation, merger or reorganization do not hold at least a majority of the resulting or surviving entities' voting power immediately following such consolidation, merger or reorganization, or (ii) a sale or transfer of all or substantially all of our assets for cash, securities or other property, will be deemed to be a Liquidation Event.

Upon any such Liquidation Event, and after all payments described in the preceding paragraph are made in full in respect of the Series H Preferred Stock, the Series I Preferred Stock and the Series J Preferred Stock, the holders of the Series G Preferred Stock will be entitled to be paid out of the assets of the company available for distribution to its stockholders an amount equal to $8.00 per share of Series G Preferred Stock, plus any declared but unpaid dividends, prior to the payment of any amounts to the holders of our Common Stock by reason of their ownership of such stock.

Each share of Series I Preferred Stock will be convertible, at the option of the holder, into that number of shares of Common Stock as is determined by (i) dividing the Series I Original Issue Price by the Series I Conversion Price (as defined below) in effect at the time of conversion and (ii) multiplying the result by 1,000. The "Series 1 Conversion Price" will initially be equal to $1,180.00, and is subject to adjustment in the event that (a) we issue additional shares of Common Stock as a dividend or other distribution on outstanding shares of Common Stock, (b) there is a split or subdivision of outstanding shares of Common Stock, or (c) there is a combination or reverse stock split of outstanding shares of Common Stock into a smaller number of shares of Common Stock. Assuming no adjustments to the Series I Original Issue Price or the Series I Conversion Price, the February 2013 Note will be convertible indirectly, at DMRJ's option, into shares of Common Stock at an effective conversion price of $1.18 per share, which represents premium of approximately 3% over the closing price of the Common Stock on the trading day preceding the date of the February 28, 2013 amendments.

Each share of Series J Preferred Stock will be convertible, at the option of the holder, into that number of shares of Common Stock as is determined by dividing the Series J Original Issue Price by the Series J Conversion Price (as defined below) in effect at the time of conversion. The "Series J Conversion Price" will initially be equal to $.08, and is subject to adjustment in the event that (a) the Company issues additional shares of Common Stock as a dividend or other distribution on outstanding shares of Common Stock, (b) there is a split or subdivision of outstanding shares of Common Stock, or (c) there is a combination or reverse stock split of outstanding shares of Common Stock into a smaller number of shares of Common Stock. Assuming no adjustments to the Series J Original Issue Price or the Series J Conversion Price, the March 2012 Note will be convertible indirectly, at DMRJ's option, into shares of Common Stock at an effective conversion price of $.08 per share. Prior to the execution of the amendment, the March 2012 Note was convertible directly into shares of Common Stock at a conversion price of $.08 per share. Accordingly, we do not believe this change to be material.

The holders of the Series I Preferred Stock and the Series J Preferred Stock will have no voting rights except as required by applicable law. However, without the consent of the holders of a majority of the outstanding Series I Preferred Stock or Series J Preferred Stock, as the case may be, with each such series voting as a separate class, we may not (i) amend, alter or repeal any provision of our Articles of Organization or By-laws in a manner that adversely affects the powers, preferences or rights of the Series I Preferred Stock or Series J Preferred Stock, as the

case may be; (ii) authorize or issue any equity securities (or any equity or debt securities convertible into equity securities) ranking prior and superior to the Series I Preferred Stock or Series J Preferred Stock, as the case may be, with respect to dividends, distributions, redemption rights or rights upon liquidation, dissolution or winding up; or (iii) consummate any capital reorganization or reclassification of any of its equity securities (or debt securities convertible into equity securities) into equity securities ranking prior and superior to the Series I Preferred Stock or Series J Preferred Stock, as the case may be, with respect to dividends, distributions, redemption rights or rights upon liquidation, dissolution or winding up.

As of June 30, 2015, there were no shares of Series H Preferred Stock, Series I Preferred Stock or Series J Preferred Stock outstanding.

On November 14, 2013, we amended each of our credit agreements with DMRJ to extend the maturity date of all of our indebtedness to DMRJ from March 31, 2014 to September 30, 2014.

On March 19, 2014, we further amended each of our credit instruments with DMRJ. Pursuant to those amendments:

- the maturity of all of our indebtedness to DMRJ was extended from September 30, 2014 to March 31, 2015;
- DMRJ waived our compliance with certain financial covenants in each of our promissory notes and all related credit agreements through the new maturity date;
- DMRJ consented to the execution and delivery of the note purchase agreement with BAM and agreed to waive all prepayment limitations and prepayment notice requirements set forth in any of the credit documents to which DMRJ and the company are parties with respect to the repayments and prepayments financed by the sale of the notes.
- DMRJ agreed to subordinate its first position security interest in all of our assets to BAM.

On March 19, 2015, we further amended each of our credit instruments with DMRJ, pursuant to which the maturity of all our indebtedness to DMRJ was extended from March 31, 2015 to March 31, 2016 and DMRJ waived our compliance with certain financial covenants contained in each of our promissory notes and all related credit agreements through the new maturity date.

Further, upon the occurrence of an event of default under certain provisions of our agreements with DMRJ, we could be required to pay default rate interest equal to the lesser of 2.5% per month and the maximum applicable legal rate per annum on the outstanding principal balance outstanding.

On May 4, 2015, we entered into an assignment agreement with DMRJ and Montsant Partners, LLC, wherein DMRJ assigned its rights, title and interest in the senior secured promissory note dated December 10, 2008 and appointed DMRJ as its collateral agent under the promissory note agreement. The note matures on March 31, 2016. DMRJ and Montsant Partners, LLC are funds managed by Platinum Partners Value Arbitrage Fund LP.

As of June 30, 2015, our obligations to DMRJ under each of the three promissory notes and a revolving line of credit approximated $12,000,000, $12,000,000, $1,000,000 and $16,662,000, respectively. Further, as of June 30, 2015, our obligation to DMRJ for accrued interest under these instruments approximated $11,350,000 and is included in current liabilities in the consolidated financial statements.

As of September 15, 2015, our obligations to DMRJ under each of the three promissory notes and a revolving line of credit approximated $12,000,000, $12,000,000, $1,000,000 and $16,862,000, respectively. Further, as of September 15, 2015, our obligation to DMRJ for accrued interest under these instruments approximated $12,692,000.

The note purchase agreement with Montsant contains restrictions and financial covenants including: (i) restrictions against declaring or paying dividends or making any distributions; against creating, assuming or incurring any liens; against creating, assuming or incurring any indebtedness; against merging or consolidating with any other company, against the sale, assignment, transfer or lease of our assets, other than in the inventory ordinary course of business ; against making investments in any company, extending credit or loans, or purchasing stock or other ownership interest of any company; and (ii) covenants that we maintain a minimum cash balance of at least $500,000; that the weighted average age of all accounts payable be no more than 100 days past due; and that we maintain a current ratio, defined as current assets divided by current liabilities, of no less than 0.60 to 1.00. Montsant waived our compliance with certain financial covenants in our promissory notes through the maturity date, consistent with the financial covenants which have been waived in each of our promissory notes and all related credit agreements with DMRJ.

Further, upon the occurrence of an event of default under certain provisions of our agreement with Montsant, we could be required to pay default rate interest equal to the lesser of 2.5% per month and the maximum applicable legal rate per annum on the outstanding principal balance outstanding.

As of June 30, 2015, our obligations to Montsant under a promissory note approximated $3,184,000. Further, as of June 30, 2015, our obligation to Montsant for accrued interest under this instrument approximated $1,860,000 and is included in current liabilities in the consolidated financial statements.

As of September 15, 2015, our obligations to Montsant under a promissory note approximated $3,184,000. Further, as of September 15, 2015, our obligation to Montsant for accrued interest under this instrument approximated $1,963,000.

Term Debt with BAM

On March 19, 2014, we entered into a note purchase agreement with a group of institutional investors and BAM Administrative Services LLC ("BAM"), an administrative agent for the investors, pursuant to which we issued senior secured promissory notes in the aggregate principal amount of $20,000,000. The notes bear interest at 15% per annum and mature on March 31, 2015. The proceeds from the sale of the notes were used to repay (i) $17,624,000 of our outstanding indebtedness to DMRJ under the amended and restated revolving promissory note dated September 29, 2011 (ii) $1,809,000 of interest outstanding under the amended and restated promissory note and (iii) $567,000 of interest outstanding under our senior secured convertible promissory note dated September 5, 2012.

On March 19, 2015, we extended our credit agreement with BAM pursuant to which, amongst other matters, the interest rate increased to 16% per annum, commencing on April 1, 2015 and we extended the maturity date of our indebtedness from March 31, 2015 to March 31, 2016.

The notes purchase agreement contains restrictions and financial covenants including: (i) restrictions against declaring or paying dividends or making any distributions; against creating, assuming or incurring any liens; against creating, assuming or incurring any indebtedness; against merging or consolidating with any other company, against the sale, assignment, transfer or lease of our assets, other than in the inventory ordinary course of business ; against making investments in any company, extending credit or loans, or purchasing stock or other ownership interest of any company; and (ii) covenants that we maintain a minimum cash balance of at least $500,000; that the weighted average age of all accounts payable be no more than 100 days past due; and that we maintain a current ratio, defined as current assets divided by current liabilities, of no less than 0.60 to 1.00. BAM waived our compliance with certain financial covenants in our promissory notes through the maturity date, consistent with the financial covenants which have been waived in each of our promissory notes and all related credit agreements with DMRJ.

Further, upon the occurrence of an event of default under certain provisions of our agreements with BAM, we could be required to pay default rate interest equal to the lesser of 2.5% per month and the maximum applicable legal rate per annum on the outstanding principal balance outstanding.

As of June 30, 2015, our obligations under the senior secured promissory notes for which BAM is the agent were $20,000,000. Further, as of June 30, 2015, our obligation under such notes for accrued interest amounted to approximately $54,000 and is included in current liabilities in the consolidated financial statements.

As of September 15, 2015, our obligations under the senior secured promissory notes for which BAM is the agent were $20,000,000. Further, as of September 15, 2015, our obligation under such notes for accrued interest amounted to approximately $738,000.

14. Stock Options and Warrants

Common Stock Options and Stock Purchase Warrants

In connection with various financing agreements and services provided by consultants, we have issued warrants to purchase shares of our common stock. The fair value of warrants issued is determined using a binomial option pricing model.

Common Stock Options

In December 2000, we adopted the 2000 Incentive and Non-Qualified Stock Option Plan (the "2000 Plan"). The 2000 Plan provides for the grant of incentive stock options and non-qualified stock options to employees and affiliates. The exercise price of the options equal 100% of the fair market value on the date of the grant or 110% of the fair market value for beneficial owners of more than 5% of our stock. Options expire between five and ten years from the date of the option grant and have various vesting periods. Options may be exercised by delivering to the company cash in an amount equal to such aggregate exercise price of the options exercised, or with the consent of

the Committee, shares of our common stock having a fair market value equal to such aggregate exercise price, a personal recourse note issued to the company in a principal amount equal to such aggregate exercise price, other acceptable consideration including a cashless exercise/resale procedure, or any combination of the foregoing. The Committee may in its discretion provide upon the grant of any option that we may repurchase, upon terms and conditions determined by the Committee, all or any number of shares purchased upon exercise of such option. A total of 600,000 shares were originally reserved for issuance under the 2000 Plan. In December 2003, our stockholders approved an increase in the 2000 Plan from 600,000 shares to 1,000,000 shares. In December 2004, our stockholders approved an increase in the 2000 Plan from 1,000,000 shares to 1,500,000 shares. The 2000 Plan expired in October 2010, as such no further options grants may be issued under this plan.

In December 2004, we adopted the 2004 Stock Option Plan (the "2004 Plan"). The 2004 Plan provides for the grant of incentive stock options and non-qualified stock options to employees and affiliates. The exercise price of the options equal 100% of the fair market value on the date of the grant or 110% of the fair market value for beneficial owners of more than 10% of our stock. Options expire between five and ten years from the date of the option grant and have various vesting periods. Options may be exercised by delivering to the company cash in an amount equal to such aggregate exercise price of the options exercised, or with the consent of the Committee, shares of our common stock having a fair market value equal to such aggregate exercise price, a personal recourse note issued to the company in a principal amount equal to such aggregate exercise price, other acceptable consideration including a cashless exercise/resale procedure, or any combination of the foregoing. A total of 500,000 shares were originally reserved for issuance under the 2004 Plan. In December 2005, our stockholders approved an increase in the 2004 Plan from 500,000 shares to 1,000,000 shares. In December 2007, our stockholders approved an increase in the 2004 Plan from 1,000,000 shares to 2,000,000 shares. In March 2012, our stockholders approved an increase in the 2004 Plan from 2,000,000 shares to 4,000,000. The 2004 Plan expired in May 2014, as such no further options grants may be issued under this plan.

In September 2012, our Board of Directors adopted an amendment to our 2004 Stock Option increasing the total number of shares of our common stock issuable thereunder from 4,000,000 shares to 20,000,000 shares and approved the following grants of options under the amended plan:

Named Executives and Directors	Shares Granted
Glenn D. Bolduc	5,442,490
Dr. William J. McGann	1,498,972
Roger P. Deschenes	1,058,498
Dr. Darryl K. Jones	1,258,498
Michael C. Turmelle	640,949
Howard Safir	303,399
Robert P. Liscouski	806,798
John A. Keating	303,399
Todd A. Silvestri	730,949
Brenda L. Baron	730,949
Estate of Joseph E. Levangie	525,099
	13,300,000

On July 1, 2015, at the 2015 Annual Meeting of Stockholders, the September 2012 amendment was approved by our stockholders.

Each of the options has an exercise price of $1.40 per share. One-half of options granted to each of Messrs. Bolduc, Deschenes, Silvestri and Ms. Baron were immediately exercisable and the other one-half became exercisable on September 7, 2013. One-third of the new options granted to each of Drs. McGann and Jones were immediately exercisable, one-third became exercisable on September 7, 2013, and the remaining one-third became exercisable on September 7, 2014. Options granted to Messrs. Turmelle, Safir, Liscouski, Keating and the Estate of Mr. Levangie are immediately exercisable in full. All of the options will expire on September 6, 2022, subject to earlier expiration with respect to Messrs. Bolduc, McGann, Deschenes, Jones, Silvestri and Ms. Baron in connection with the termination or cessation of their respective employment with the company.

On September 7, 2012, the Board of Directors adopted the Implant Sciences Corporation Change of Control Payment Plan (the "COC Plan"), the purpose of which is to reward management for the increases in shareholder value generated between January 2009 and September 7, 2012.

On January 2, 2009, the closing price of our common stock on the NYSE Amex LLC was $0.18 per share. On the date the plan was adopted, the closing price of the common stock on the OTC Markets Group's OTCPK tier was

$1.40. Our Board of Directors believes that this increase in shareholder value is directly attributable to the dedication and hard work of our management team, employees and directors. Accordingly, our management and directors have not significantly benefitted from the increase in shareholder value between January 2009 and September 7, 2012, and the COC Plan is intended to provide value to our management and directors equivalent to the value they would have earned had they owned a more significant portion of our equity.

Pursuant to the COC Plan, the Board established a target level of stock ownership for each officer as a percentage of our fully diluted capitalization, and a corresponding ownership percentage for directors. To reflect the increase in shareholder value between January 2009 and the adoption of the plan, the Board determined that each officer and director should be allocated a "Change of Control Payment" equal to the product of (x) the closing price of our common stock on September 7, 2012 (*i.e.*, $1.40) less a "floor price," multiplied by (y) the number of additional stock options granted to each participant on the same date. The floor price applicable to directors and officers who served us at the beginning of the turn-around is $0.20, *i.e.*, slightly above the closing price of the common stock on January 2, 2009. The floor prices for Dr. McGann and Dr. Jones are $0.51 and $0.67, respectively, reflecting the closing prices of the common stock on the dates those officers joined us. The benefits under the plan are payable upon, and only upon, a "Change of Control," as defined in the plan, involving the company. Accordingly, the payment of the benefits allocated under the plan will be further deferred until such time that all shareholders receive payments for or in respect of their common stock in a transaction constituting a Change of Control.

Pursuant to the terms of the Separation Agreement (see Note 16): (i) Mr. Bolduc agreed to consent to a modification of the Company's Change in Control Payment Plan ("CIC Plan"), currently being considered by the Board of Directors, under which, in the event the Company is sold, Mr. Bolduc's share in the CIC Plan will be reduced to 4% of the net sales price of the Company, as defined in an amended CIC Plan, and under which the aggregate share of all other participants in the CIC Plan will be 8.5% of the net sales price. The Company amended Mr. Bolduc's existing stock options permitting Mr. Bolduc to exercise those options.

On February 26, 2015, our Board of Directors amended and restated the Change in Control Plan which was originally adopted by the Board of Directors on September 7, 2012 (the "Original Plan," and as amended and restated, the "Amended Plan"). The Amended Plan modifies certain provisions of the Original Plan relating to the calculation and amounts of payment to which certain key employees and directors of the Company are entitled following a Change in Control (as defined in the Amended Plan) as well as certain terms and conditions of payment, as described below.

The Original Plan provided that Participants would receive certain fixed amounts upon a Change of Control. The Amended Plan does not provide such fixed amounts. Instead, the Amended Plan provides for Change of Control Payments based on a percentage of Net Proceeds of a Change of Control after subtracting amounts that the Participant would receive in the Change of Control transaction as a result of the Participant's ownership of certain stock options of the Company. Change of Control Payments are calculated as (a) the product of (i) Net Proceeds of a Change of Control, multiplied by (ii) the applicable percentage granted to the Participant, reduced, but not below zero, by (b) any portion of the Net Proceeds or any other consideration which are payable to such Participant with respect to the At-Risk Options or with respect to shares of capital stock of the Company acquired upon the exercise of the At-Risk Options. The options deemed to be "At- Risk" are identified in Appendix A of the Amended Plan.

In the Amended Plan, Net Proceeds is defined as the aggregate consideration paid in connection with a Change of Control, after payment of (i) all secured indebtedness of the Company and any controlled subsidiary, together with all accrued but unpaid interest thereon and all other obligations related thereto, including without limitation all indebtedness owed to DMRJ Group, LLC, and to the holders of promissory notes issued pursuant to that certain Note Purchase Agreement dated as of March 19, 2014, between the Company and certain other parties thereto, and (ii) all other obligations and liabilities of the Company and any Controlled Subsidiary, including all expenses related to such Change of Control. Net Proceeds shall be deemed to include (i) any consideration to be paid to the Company, any Controlled Subsidiary, or the Company's stockholders (as the case may be) that is to be held in escrow and (ii) any consideration to be paid to the Company, any Controlled Subsidiary, or the Company's stockholders (as the case may be) that is based on the future outcome or performance of the Company or any Controlled Subsidiary in the form of an earn-out according to the terms of the Change of Control. Upon any release from escrow and/or any payment of an earn-out, the Company shall make the Change of Control Payments attributable to such amounts upon the same payment schedule and under the same terms and conditions as apply to the corresponding payments to the Company, any Controlled Subsidiary, or the Company's stockholders (as the case may be) and in compliance with Section 409A of the Code.

In the Amended Plan, the definition of "Change of Control" was revised to mean the occurrence of any one of the following events:

(a) a merger or consolidation in which:
  (i) the Company is a constituent party, or
  (ii) more than fifty percent (50%) owned subsidiary of the Company, measured by the total fair market value and the total voting power of the outstanding shares of the capital stock of such subsidiary (a "Controlled Subsidiary") is a constituent party, where any one Person, or more than one Person Acting as a Group, other than Excluded Person(s), acquires ownership of the stock of the Company or Controlled Subsidiary that, together with the stock then held by such Person or Group, constitutes more than fifty percent (50%) of the total fair market value or total voting power of the stock of the Company or Controlled Subsidiary (determined on a fully diluted basis assuming the exercise, conversion or exchange of all exercisable, convertible or exchangeable securities, respectively). However, if any one Person or more than one Person Acting as a Group is considered to own more than fifty percent (50%) of the total fair market value or total voting power of the stock of the Company, the acquisition of additional stock by the same Person or Persons is not considered to cause a Change of Control.

(b) the sale, lease, transfer, exclusive license or other disposition by the Company or any subsidiary of the Company of all or substantially all the assets of the Company and its subsidiaries taken as a whole to any one Person, or more than one Person Acting as a Group, other than Excluded Person(s), in a single transaction or in a series of related transactions during the twelve (12) month period ending on the date of the most recent disposition to such Person or Persons, except where such sale, lease, transfer, exclusive license or other disposition is to a wholly owned subsidiary of the Company; or

(c) the sale, exchange or transfer to any one Person, or more than one Person Acting as a Group, other than Excluded Person(s), in a single transaction or in a series of related transactions during the twelve (12) month period ending on the date of the most recent transfer to such Person or Persons, of at least a majority, by voting power (determined on a fully diluted basis, assuming the exercise, conversion or exchange of all exercisable, convertible or exchangeable securities, respectively), of the outstanding shares of capital stock of the Company.

Under the Original Plan a termination of employment of a Participant did not affect such Participant's ability to receive a Change of Control Payment. Under the Amended Plan, in the event that a Participant is terminated by the Company for Cause or resigns without Good Reason, such Participant's eligibility immediately terminates.

Additionally, a Participant's termination without Cause or Resignation for Good Reason prior to or after a Change of Control will not affect the eligibility of such Participant or his or her Beneficiary to receive a Change of Control Payment; provided, however, that, (x) in the event of a Participant's termination without Cause or Resignation for Good Reason after the Effective Date but on or before June 30, 2015, then, for purposes of the definition of Change of Control Payment, the percentage applicable to such Participant shall be as set forth in Column B of Appendix B of the Amended Plan; and (y) in the event of a Participant's termination without Cause or Resignation for Good Reason after June 30, 2015 but on or before December 31, 2015, the percentage applicable to such Participant shall be as set forth in Column C of Appendix B of the Amended Plan.

Termination for Cause is defined as the termination by the Company or any affiliate of any Participant's employment with the Company or any affiliate for any of the following reasons: (a) the Participant's conviction or entry of a plea of nolo contendere to any felony or a crime involving moral turpitude, fraud or embezzlement of the property of the Company or any affiliate; or (b) the Participant's dishonesty, gross negligence or gross misconduct that is materially injurious to the Company or any affiliate or material breach of his duties to the Company or any affiliate, which has not been cured by the Participant within 10 days (or longer period as is reasonably required to cure such breach, negligence or misconduct) after he shall have received written notice from the Company or such affiliate stating with reasonable specificity the nature of such breach; or (c) the Participant's illegal use or abuse of drugs, alcohol, or other related substances that is materially injurious to the Company or any affiliate.

Resignation for Good Reason is defined as the voluntary resignation of a Participant's employment with the Company or any affiliate for any of the following reasons: (a) a "material diminution" (as such term is used in Section 409A of the Code) of the duties assigned to Participant; or (b) a material reduction in the Participant's base salary or other benefits (other than a reduction or change in benefits generally applicable to all executive employees of the Company and its affiliates); or (c) relocation by the Company or any affiliate of any Participant who is an employee of the Company to an office more than 50 miles outside the Participant's current workplace. However,

resignation by a Participant shall be not deemed to be a Resignation for Good Reason unless (i) the Participant reports the event or condition to the Board, in writing, within 45 days of such event or condition occurring and (ii) within 30 days after the Participant provides such written notice, the Company or the appropriate affiliate

The Change in Control Payments will be payable to Participants, or their respective beneficiaries, in cash, no later than 30 days after the Net Proceeds are received by the Company.

The Original Plan stated that any termination or amendment of the Original Plan that imposed additional obligations on, or impaired the rights of, a Participant would not be effective without the written consent of the Participant. The Amended Plan states that any termination or amendment to the Plan that imposes additional obligations on, or impairs the rights of, a Participant shall not be effective without the Participant's written consent unless such termination or amendment shall apply with the same force and effect to all of the Participants, in which case no consent of the Participants, or of any individual Participant, shall be required.

The applicable percentage of Net Proceeds to be received by each Participant is set forth below and in Appendix B of the Amended Plan. As described above, the Change in Control Payment to which a Participant will be entitled based upon the applicable percentage below will be reduced by any consideration that the Participant receives as a result of the At-Risk Options.

PARTICIPANTS AND CHANGE IN CONTROL PERCENTAGES

	Applicable Percentage		
Participant	A	B*	C**
Glenn D. Bolduc	4.00%	4.00%	4.00%
William McGann	1.47%	1.47%	1.47%
Darryl Jones	1.10%	.60%	.80%
Roger P. Deschenes	.97%	.60%	.80%
Todd Silvestri	1.00%	.60%	.80%
Brenda Baron	1.00%	.60%	.80%
Robert Liscouski	.65%	.65%	.65%
Howard Safir	.32%	.32%	.32%
John Keating	.32%	.32%	.32%
Michael Turmelle	.55%	.55%	.55%
Estate of Joseph Levangie	.25%	.25%	.25%
Total	11.63%	9.96%	10.76%

*Applicable percentage received by a Participant in the event of Participant's termination without Cause or Resignation for Good Reason after the Effective Date but on or before June 30, 2015.
**Applicable percentage received by a Participant in the event of Participant's termination without Cause or Resignation for Good Reason after June 30, 2015 but on or before December 31, 2015.

On July 2, 2014, our Board of Directors adopted the 2014 Stock Option Plan (the "2014 Plan"). The 2014 Plan provides for the grant of incentive stock options and non-qualified stock options to employees and affiliates. The exercise price of the options equal 100% of the fair market value on the date of the grant or 110% of the fair market value for beneficial owners of more than 10% of our stock. Options expire between five and ten years from the date of the option grant and have various vesting periods. Options may be exercised by delivering to the company cash in an amount equal to such aggregate exercise price of the options exercised, or with the consent of the Committee, shares of our common stock having a fair market value equal to such aggregate exercise price, a personal recourse note issued to the company in a principal amount equal to such aggregate exercise price, other acceptable consideration including a cashless exercise/resale procedure, or any combination of the foregoing. A total of 15,000,000 shares were originally reserved for issuance under the 2014 Plan. The 2014 Plan was approved by our stockholders on July 1, 2015 at the 2015 Annual Meeting of Stockholders.

On July 2, 2014, our Board of Directors approved grants of stock options to purchase an aggregate of 4,210,000 shares, including the following grants to our directors and officers:

Named Executives and Directors	Shares Granted
Glenn D. Bolduc	300,000
Dr. William J. McGann	300,000
Roger P. Deschenes	300,000
Dr. Darryl K. Jones	300,000
Michael C. Turmelle	300,000
Howard Safir	300,000
Robert P. Liscouski	300,000
John H. Hassett	100,000
John A. Keating	300,000
Todd A. Silvestri	300,000
Brenda L. Baron	300,000
Total	3,100,000

Each of these options has an exercise price of $1.10 per share and vest one-third upon the last to occur of (i) addition of the Company's QS-B220 Product to the Transportation Security Administration ("TSA") Qualified Product List for passenger checkpoint screening, (ii) the execution of an indefinite delivery/indefinite quantity contract with the TSA, and (iii) receipt of orders under that contract. The remaining options will vest in two equal installments on the first and second anniversary of the initial vesting date. We achieved the three criteria established for the July 2, 2014 option grant and, as such, the initial one-third vested on March 3, 2015.

As of June 30, 2015, there were options outstanding to purchase 21,513,485 shares of our common stock at exercise prices ranging from $0.08 to $3.89.

We issued 741,499, 407,066 and 1,421,183 shares of common stock during the years ended June 30, 2015, 2014 and 2013, respectively, as a result of the exercise of options by employees and consultants.

The following table presents the activity of the 2000, 2004 and 2014 Stock Option Plans for the year ended June 30, 2015:

	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Life in Years	Aggregate Intrinsic Value *(in thousands)*
Options outstanding as of July 1, 2014	18,420,316	$ 1.22	7.1	$ -
Issued	4,342,500	1.09		
Exercised	(741,499)	0.38		
Cancelled	(507,832)	1.41		
Options outstanding as of June 30, 2015	21,513,485	$ 1.22	6.7	$ -
Options exercisable as of June 30, 2015	17,810,983	$ 1.25	6.6	$ -
Options vested or expected to vest as of June 30, 2015	21,067,985	$ 1.22	6.6	$ -

The following table presents the activity of the 2000 and 2004 Stock Option Plans for the year ended June 30, 2014:

	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Life in Years	Aggregate Intrinsic Value *(in thousands)*
Options outstanding as of July 1, 2013	17,905,001	$ 1.22	7.9	$ -
Issued	2,164,654	0.99		
Exercised	(407,066)	0.14		
Cancelled	(1,242,273)	1.06		
Options outstanding as of June 30, 2014	18,420,316	$ 1.22	7.1	$ -
Options exercisable as of June 30, 2014	15,385,445	$ 1.25	7.2	$ -
Options vested or expected to vest as of June 30, 2014	18,048,715	$ 1.23	7.1	$ -

The following table presents the activity of the 2000 and 2004 Stock Option Plans for the year ended June 30, 2013:

	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Life in Years	Aggregate Intrinsic Value *(in thousands)*
Options outstanding as of July 1, 2012	4,986,000	$ 0.43	5.0	$ 4,861
Issued	14,565,000	1.38		
Exercised	(1,421,183)	0.16		
Cancelled	(224,816)	0.98		
Options outstanding as of June 30, 2013	17,905,001	$ 1.22	7.8	$ -
Options exercisable as of June 30, 2013	9,924,140	$ 1.17	7.9	$ -
Options vested or expected to vest as of June 30, 2013	17,181,792	$ 1.22	7.9	$ -

The weighted average grant date fair value of options granted for the years ended June 30, 2015, 2014 and 2013 were $0.70, $0.72 and $1.22, respectively. See Note 2 for further discussion on the methods and assumptions used in determining the fair value of our options.

The following table sets forth information regarding outstanding options at June 30, 2015:

	Outstanding Options			Options Exercisable	
Range of Exercise Prices	Shares	Weighted-Average Remaining Contractual Life in Years	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
$0.08 - $0.49	1,109,984	2.8	$ 0.26	1,109,984	$ 0.26
$0.52 - $1.00	2,279,168	4.5	$ 0.82	1,747,500	$ 0.82
$1.15 - $2.30	18,114,333	7.1	$ 1.33	14,943,499	$ 1.37
$3.07 - $3.89	10,000	0.5	$ 3.89	10,000	$ 3.89
	21,513,485	6.7	$ 1.22	17,810,983	$ 1.25

As of June 30, 2015 there was $1,536,000 of total unrecognized compensation expense related to unvested share based compensation arrangements under the various share-based compensation plans. This expense is expected to be recognized as follows:

Years Ending June 30: *(In thousands)*		
2016	$	1,097
2018		428
2018		11
	$	1,536

As of June 30, 2015, the unrecognized compensation expense related to stock option awards is expected to be recognized as expense over a weighted-average period of 1.0 years.

The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value (the difference between the closing price of the common stock on June 30, 2015 of $0.80 and the exercise price of each in-the-money option) that would have been received by the option holders had all option holders exercised their options on June 30, 2015. Total intrinsic value of stock options exercised under the stock option plans for the years ended June 30, 2015, 2014 and 2013 was $518,000, $240,000 and $1,557,000, respectively. The total fair value of stock options that vested during the years ended June 30, 2015 and 2014 was $2,896,000 and $460,000, respectively.

Stock Purchase Warrants and Stock Issuances

In April 2013, we issued 600,000 shares of common stock having a value of $660,000 and warrants to purchase an aggregate of 2,000,000 shares of our common stock to two advisors, in consideration of services rendered to us under two advisory and consulting services agreements. The issued shares were valued at the closing stock price of $1.10 per share at April 1, 2013.

In June 2015, we issued 550,000 shares of common stock having a value of $412,000 to two advisors, in consideration of services rendered to us under two advisory and consulting services agreements. The issued shares were valued at the closing stock price of $0.75 per share at May 6, 2013. The advisory and services agreements provide for the issuance of an additional 1,650,000 shares in equal monthly installments of 110,000 shares commencing in September 2015.

As of June 30, 2015, there were warrants outstanding to purchase 3,155,000, shares of our common stock at exercise prices ranging from $0.54 to $1.22 expiring at various dates between May 25, 2016 and April 1, 2021.

We estimated the fair value of the warrants issued during fiscal 2015, 2014 and 2013 using the Black-Scholes option pricing model with the following input assumptions:

	Years Ended		
	June 30, 2015	June 30, 2014	June 30, 2013
Dividend yield	0.0%	0.0%	0.0%
Weighted-average volatility	80.0%	124.2%	80.9%
Weighted-average risk-free interest rate	1.70%	1.52%	0.79%
Weighted-average life of warrants	5.0 years	4.7 years	4.8 years

We issued one warrant in fiscal 2015, one warrant in fiscal 2014 and eight warrants in fiscal 2013. For the years ended June 30, 2015, 2014 and 2013, we recorded non-cash charges for warrants that vested of $289,000, $1,270,000 and $696,000, respectively, in our consolidated statements of operations.

The following table presents the weighted average exercise price of warrants outstanding at June 30, 2015:

	Warrants Outstanding and Exercisable		
Range of Exercise Prices	Number of Shares	Weighted-Average Exercise Price	Weighted-Average Intrinsic Value per Share
$0.54 - $0.54	200,000	$ 0.54	$ 0.26
$0.79 - $1.00	1,105,000	$ 0.81	$ (0.01)
$1.10 - $1.22	1,850,000	$ 1.12	$ (0.32)
	3,155,000	$ 0.97	$ (0.17)

The following table presents the weighted average exercise price of warrants outstanding at June 30, 2014:

Range of Exercise Prices	Warrants Outstanding and Exercisable					
	Number of Shares		Weighted-Average Exercise Price		Weighted-Average Intrinsic Value per Share	
$0.54 - $0.54	200,000	$	0.54	$	0.50	
$0.79 - $1.00	1,125,000	$	0.81	$	0.23	
$1.10 - $1.22	2,243,860	$	1.11	$	(0.07)	
	3,568,860	$	0.98	$	0.06	

The following table presents the warrant activity for the years ended June 30, 2015, 2014 and 2013:

	Shares		Weighted-Average Exercise Price
Warrants outstanding as of July 1, 2014	3,568,860	$	0.93
Issued	200,000		1.20
Exercised	(180,495)		1.07
Expired	(433,365)		1.11
Warrants outstanding as of June 30, 2015	3,155,000	$	0.97
Warrants exercisable as of June 30, 2015	2,905,000	$	0.96
Weighted-average fair value of warrants granted during the year		$	0.77
Warrants outstanding as of July 1, 2013	3,780,352	$	0.99
Issued	25,000		0.79
Exercised	(36,492)		0.30
Expired	(200,000)		1.20
Warrants outstanding as of June 30, 2014	3,568,860	$	0.93
Warrants exercisable as of June 30, 2014	3,093,859	$	0.96
Weighted-average fair value of warrants granted during the year		$	0.66
Warrants outstanding as of July 1, 2012	3,555,352	$	0.59
Issued	2,400,000		1.12
Exercised	(1,104,204)		0.08
Expired	(1,070,796)		0.92
Warrants outstanding as of June 30, 2013	3,780,352	$	0.99
Warrants exercisable as of June 30, 2013	1,958,688	$	0.88
Weighted-average fair value of warrants granted during the year		$	0.71

Employee Stock Purchase Plan

In December 2006, we adopted the 2006 Employee Stock Purchase Plan. This plan provides a method whereby our employees have an opportunity to acquire an ownership interest in the company through the purchase of shares of our common stock through payroll deductions. After 12 months of employment, an employee is eligible to participate and can defer up to 10% of their wages into this plan, with a maximum of $25,000 in any calendar year. The purchase price of the common stock is calculated at the lower of 85% of the closing price of the stock on the first day of the plan period or the last day of the plan period. The plan periods are January 1 to June 30 and July 1 to December 31. Fractional shares are not issued. Participants may withdraw at any time by giving written notice to us and will be credited the amounts of deferrals in their account. The maximum number of shares eligible to be issued under the 2006 Plan is 500,000. As of June 30, 2015 and 2014, a total of 380,543 shares are available for issuance under the 2006 Plan.

We issued no shares of common stock during the years ended June 30, 2015 and 2014, under the employee stock purchase plan.

15. Benefit Plans and Employment Agreements of Executive Officers

We have a defined contribution plan, the Implant Sciences Corporation 401(k) Profit Sharing Plan, established under Section 401(k) of the Internal Revenue Code. All full-time employees who are 21 years of age are eligible to participate on the beginning of the first month after 30 days of employment. The company's contributions are discretionary. We made no matching contributions during either of fiscal 2015, 2014 or 2013.

In March 2012, we entered into a three-year employment agreement with Dr. William J. McGann, our Chief Operating Officer, pursuant to which Dr. McGann receives a base salary of $250,000 per year, commencing on April 2, 2012. After the third year, the agreement will automatically continue unless notice of termination is given by either party.

On January 16, 2015, the Board of Directors appointed Dr. McGann as our President and Chief Executive Officer and amended and restated the employment agreement with Dr. McGann. The new agreement will remain in effect until the first to occur of the following events: 1) the voluntary termination of Dr. McGann; 2) Dr. McGann resigns for Good Reason, as defined in the restated and amended agreement; 3) we terminate Dr. McGann's employment for Cause, as defined in the restated and amended agreement; 4) the death or disability of Dr. McGann; or 5) the Board of Directors elects a new President of CEO, in which case Dr. McGann would continue his employment as our Chief Operating Officer.

The amended and restated employment agreement establishes Dr. McGann's base salary at the rate of $270,000 per year, which amount is equal to Dr. McGann's annualized base salary immediately prior to the agreement. Dr. McGann's base salary is subject to annual review, and any increases will be made in the discretion of the Board of Directors upon the recommendation of the Compensation Committee.

We may terminate the agreement at any time without cause, on 30 days' written notice. The agreement, however, provides for payment of twelve months' salary and a pro rata portion of any bonus compensation earned during the year of termination, as well as the continuation of certain benefits, as separation payments in the event that Dr. McGann employment is terminated by us without "cause" or Dr. McGann resigns for "good reason" (as those terms are defined in the agreement). Dr. McGann's base salary is subject to annual review, and any increases will be made in the discretion of the Board of Directors upon the recommendation of the Compensation Committee.

The agreement provides for Dr. McGann to be eligible to receive incentive compensation in an amount up to $135,000, for each of the fiscal years ended June 30, 2015 and June 30, 2014 upon the achievement of certain performance milestones established by the Board of Directors. We did achieve these milestones and a bonus in the amount of $67,500 was payable to Dr. McGann for the fiscal year ended June 30, 2015. We did not achieve these milestones and no bonus was payable to Dr. McGann for the fiscal year ended June 30, 2014. In August 2013, however, the Board agreed to pay Dr. McGann a bonus of $41,250 with respect to the fiscal year ended June 30, 2013 if the company achieved the Bonus Milestones described above. We did not achieve these milestones and no bonus was payable to Dr. McGann for the fiscal year ended June 30, 2013. Incentive compensation, if any, for subsequent fiscal years will be based on performance milestones to be established by mutual agreement between the Company and Dr. McGann within 60 days after commencement of each such fiscal year.

The agreement also provides that within 30 days after the completion of an equity financing, the gross proceeds of which to the Company are not less than $15,000,000, the Company will grant Dr. McGann an incentive stock option to purchase that number of shares of common stock of the Company which, together with all other option and equity awards previously issued by the Company, will equal approximately 1% of the Company's fully diluted equity.

In May, 2012, we entered into a three-year employment agreement with Dr. Darryl Jones, our Vice President of Sales and Marketing, pursuant to which Dr. Jones will receive a base annual salary of $235,000 per year, commencing on May 7, 2012. After the third year, the agreement will automatically continue unless notice of termination is given by either party. We may terminate the agreement at any time without cause, on 30 days' written notice. The agreement, however, provides for payment of twelve months' salary and a pro rata portion of any bonus compensation earned during the year of termination, as well as the continuation of certain benefits, as separation payments in the event that Dr. Jones employment is terminated by us without "cause" or Dr. Jones resigns for "good reason" (as those terms are defined in the agreement). Dr. Jones's base salary is subject to annual review, and any increases will be made in the discretion of the Board of Directors upon the recommendation of the Compensation Committee.

The agreement provides for Dr. Jones to be eligible to receive incentive compensation in an amount of up to $122,500 for each of the fiscal year ended June 30, 2015 and June 30, 2014 upon the achievement of certain performance milestones to be established by the Board of Directors. We did achieve these milestones and a bonus in

the amount of $61,250 was payable to Dr. Jones for the fiscal year ended June 30, 2015. We did not achieve these milestones and no bonus was payable to Dr. Jones for the fiscal year ended June 30, 2014. In August 2013, however, the Board agreed to pay Dr. Jones a bonus of $29,375 with respect to the fiscal year ended June 30, 2013 if the company achieved the Bonus Milestones described above. We did not achieve these milestones and no bonus was payable to Dr. Jones for the fiscal year ended June 30, 2013. Incentive compensation, if any, for subsequent fiscal years will be based on performance milestones to be established by mutual agreement between the Company and Dr. Jones within 60 days after commencement of each such fiscal year.

The agreement also provides that within 30 days after the completion of an equity financing, the gross proceeds of which to the Company are not less than $15,000,000, the Company will grant Dr. Jones an incentive stock option to purchase that number of shares of common stock of the Company which, together with all other option and equity awards previously issued by the Company, will equal approximately 1% of the Company's fully diluted equity.

On March 13, 2015, we entered into an employment agreement with Ms. Brenda Baron, our Vice President of Manufacturing, pursuant to which Ms. Baron will receive a base annual salary of $180,000 per year, commencing on March 13, 2015. The employment agreement does not contain a specified term of employment. We may terminate the agreement at any time without cause, on 30 days' written notice. The agreement, however, provides for payment of six months' salary and a pro rata portion of any bonus compensation earned during the year of termination, as well as the continuation of certain benefits, as separation payments in the event that Ms. Baron employment is terminated by us without "cause" or Ms. Baron resigns for "good reason" (as those terms are defined in the agreement). Ms. Baron's base salary is subject to annual review, and any increases will be made in the discretion of the Board of Directors upon the recommendation of the Compensation Committee.

The agreement provides for Ms. Baron to be eligible to receive incentive compensation in an amount equal to 50% of her annual base salary. Ms. Baron was eligible to receive incentive compensation of $90,000 for the fiscal year ended June 30, 2015 upon the achievement of certain performance milestones to be established by the Board of Directors. We did achieve these milestones and a bonus in the amount of $45,000 was payable to Ms. Baron for the fiscal year ended June 30, 2015. Incentive compensation, if any, for subsequent fiscal years will be based on performance milestones to be established by mutual agreement between the Company and Ms. Baron within 60 days after commencement of each such fiscal year.

On March 13, 2015, we entered into an employment agreement with Mr. Todd Silvestri, our Vice President of Advanced Technology and Product Development, pursuant to which Mr. Silvestri will receive a base annual salary of $200,000 per year, commencing on March 13, 2015. The employment agreement does not contain a specified term of employment. We may terminate the agreement at any time without cause, on 30 days' written notice. The agreement, however, provides for payment of six months' salary and a pro rata portion of any bonus compensation earned during the year of termination, as well as the continuation of certain benefits, as separation payments in the event that Mr. Silvestri employment is terminated by us without "cause" or Mr. Silvestri resigns for "good reason" (as those terms are defined in the agreement). Mr. Silvestri's base salary is subject to annual review, and any increases will be made in the discretion of the Board of Directors upon the recommendation of the Compensation Committee.

The agreement provides for Mr. Silvestri to be eligible to receive incentive compensation in an amount equal to 50% of his annual base salary. Mr. Silvestri was eligible to receive incentive compensation of $100,000 for the fiscal year ended June 30, 2015 upon the achievement of certain performance milestones to be established by the Board of Directors. We did achieve these milestones and a bonus in the amount of $100,000 was payable to Mr. Silvestri for the fiscal year ended June 30, 2015. Incentive compensation, if any, for subsequent fiscal years will be based on performance milestones to be established by mutual agreement between the Company and Mr. Silvestri within 60 days after commencement of each such fiscal year.

On September 16, 2015, we entered into an employment agreement with Mr. Roger Deschenes, our Chief Financial Officer, pursuant to which Mr. Deschenes will receive a base annual salary of $246,000 per year, commencing on September 16, 2015. The employment agreement does not contain a specified term of employment. We may terminate the agreement at any time without cause, on 30 days' written notice. The agreement, however, provides for payment of six months' salary and a pro rata portion of any bonus compensation earned during the year of termination, as well as the continuation of certain benefits, as separation payments in the event that Mr. Deschenes employment is terminated by us without "cause" or Mr. Deschenes resigns for "good reason" (as those terms are defined in the agreement). Mr. Deschenes' base salary is subject to annual review, and any increases will be made in the discretion of the Board of Directors upon the recommendation of the Compensation Committee.

The agreement provides for Mr. Deschenes to be eligible to receive incentive compensation in an amount equal to 50% of his annual base salary. Mr. Deschenes was eligible to receive incentive compensation of $117,000 for the

fiscal year ended June 30, 2015 upon the achievement of certain performance milestones to be established by the Board of Directors. We did achieve these milestones and a bonus in the amount of $57,500 was payable to Mr. Deschenes for the fiscal year ended June 30, 2015. Incentive compensation, if any, for subsequent fiscal years will be based on performance milestones to be established by mutual agreement between the Company and Mr. Deschenes within 60 days after commencement of each such fiscal year.

16. Separation Agreement

In February 2009, we entered into a new three-year employment agreement with Mr. Glenn D. Bolduc our President and Chief Executive Officer, pursuant to which Mr. Bolduc initially received a base salary of $275,000 per year, commencing on January 1, 2009. After the third year, the agreement will automatically renew for additional one-year periods. The agreement also provided for Mr. Bolduc to be eligible to receive incentive compensation in an amount of up to 50% of his base salary, upon the achievement of certain performance milestones established by the Board of Directors and a car allowance. Incentive compensation, if any, for subsequent fiscal years was based on performance milestones to be established by mutual agreement between us and Mr. Bolduc.

On June 25, 2013, we amended and restated our employment agreement with Mr. Bolduc. The amended agreement contemplated that it would remain in effect through June 30, 2016, after which, the agreement would automatically renew for additional one-year periods unless notice of non-renewal was given by either party. The agreement establishes Mr. Bolduc's base salary at the rate of $400,000 per year. Mr. Bolduc's base salary was subject to annual review, and any increases would be made in the discretion of the Board of Directors upon the recommendation of the Compensation Committee.

The agreement also provided that Mr. Bolduc was eligible to receive cash bonuses of up to 50% of his annualized base salary for the fiscal years ended June 30, 2013, June 30, 2014 and for subsequent fiscal years. The amount of the bonus payable with respect to any fiscal year, if any, was determined by the Board, in its sole discretion, provided that no bonus would be payable unless we achieved certain revenue and adjusted earnings before interest, taxes, depreciation and amortization ("EBITDA") targets established by the Board for the respective fiscal year. We did not achieve these targets and no bonus was payable to Mr. Bolduc for the fiscal year ended June 30, 2014. In August 2013, the Board awarded Mr. Bolduc a bonus of $50,000 with respect to the fiscal year ended June 30, 2013, which payment of was contingent on the Company receipt of certain governmental approvals for its QS-B220 desktop explosives and narcotics detector by December 31, 2013 and the execution of a procurement contract with a specific agency of the United States government on or before February 1, 2014 (the "Bonus Milestones"). We did not achieve these milestones and no bonus was paid to Mr. Bolduc for the fiscal year ended June 30, 2013. During the year ended June 30, 2013, Mr. Bolduc was paid bonuses of $136,250 and $162,500, representing bonuses earned in our fiscal years ended June 30, 2009 and June 30, 2012, respectively.

Mr. Bolduc was eligible to receive such additional compensation as the Board may, in its sole discretion, have awarded from time to time. In addition, Mr. Bolduc received a car allowance and was eligible to participate in our employee fringe benefit programs or programs readily available to employees of comparable status and position.

Under the terms of the agreement, the Company could have terminated the agreement at any time without cause, on 30 days' prior written notice. The agreement provides, however, for the payment of 18 months' salary and a pro rata portion of any bonus compensation earned during the year of termination, as well as the continuation of certain benefits for 12 months, as separation payments in the event that Mr. Bolduc's employment was terminated by us without "cause" or if Mr. Bolduc resigned for "good reason" (as those terms were defined in the agreement). The agreement also provided that, if Mr. Bolduc resigned for "good reason," all stock options and shares of restricted stock then held by Mr. Bolduc would become fully vested and exercisable as of the date of such resignation.

In the event that, within 12 months after a "change of control" (as that term was defined in the Company's Change of Control Plan, as adopted by the Board on September 7, 2012), Mr. Bolduc's employment was terminated without cause, or Mr. Bolduc resigned for good reason, the agreement provided (i) for the payment of 36 months' salary and a pro rata portion of any bonus compensation earned during the year of termination, and (ii) that all stock options and shares of restricted stock then held by Mr. Bolduc would become fully vested and exercisable as of the date of such termination or resignation.

The Company was not required to continue to pay any amounts to Mr. Bolduc or to continue to provide certain benefits following termination of the agreement unless Mr. Bolduc executed a general release in favor of us substantially in the form annexed to the agreement and the period during which Mr. Bolduc revoked the release had expired without any such revocation.

The agreement included certain restrictions against competition and solicitation of our employees and customers for a period of one year after Mr. Bolduc's resignation or termination.

The Agreement includes certain restrictions against competition and solicitation of our employees and customers for a period of one year after Mr. Bolduc's resignation or termination.

On January 16, 2015, Glenn D. Bolduc, resigned his positions as Chief Executive Officer and President of the Company, as well as his seat on the Company's Board of Directors and his position as Chairman of the Board. In connection with and prior to Mr. Bolduc's resignations, Mr. Bolduc entered into a Separation Agreement and Release (the "Separation Agreement") with the Company. The Separation Agreement provides that Mr. Bolduc's resignation will be deemed an involuntary termination without cause pursuant to his Amended and Restated Employment Agreement dated as of June 25, 2013. In this regard, and subject to the terms contained in the Employment Agreement, Mr. Bolduc is entitled to receive: (i) annual base salary for 18 months on a regular payroll basis; (ii) a pro rata portion of any bonus earned in 2015; (iii) continuation of coverage under and contributions to health care, dental and life insurance benefits for a 12 month period; and (iv) transfer of any key man life insurance. In connection with Mr. Bolduc's resignation, we recorded a non-recurring charge of $725,000 in our consolidated statements of operations and comprehensive loss for the year ended June 30, 2015.

The agreement provides for Mr. Bolduc to be eligible to receive pro-rate incentive compensation in an amount equal to 25% of his annual base salary. Mr. Bolduc was eligible to receive incentive compensation of $50,000 for the fiscal year ended June 30, 2015 upon the achievement of certain performance milestones to be established by the Board of Directors. We did achieve these milestones and a bonus in the amount of $50,000 was payable to Mr. Bolduc for the fiscal year ended June 30, 2015.

Pursuant to the terms of the Separation Agreement: (i) Mr. Bolduc agreed to consent to a modification of the Company's Change of Control Payment Plan ("CIC Plan"), currently being considered by the Board of Directors, under which, in the event the Company is sold, Mr. Bolduc's share in the CIC Plan will be reduced to 4% of the net sales price of the Company, as defined in an amended CIC Plan, and under which the aggregate share of all other participants in the CIC Plan will be 8.5% of the net sales price; (ii) the Company agreed that Mr. Bolduc shall continue to have the use of an apartment in New York City through the end of the current lease, all lease obligations of said apartment, including but not limited to rent payments and utilities, to be paid by the Company; (iii) the Company agreed to pay Mr. Bolduc's attorney the sum of $40,000 towards legal fees related to the negotiation of the Separation Agreement and related matters; (iv) the Company amended Mr. Bolduc's existing stock options permitting Mr. Bolduc to exercise those options which are vested as of his separation date through the maturity date of said options and to provide for the ability to exercise the vested options on a cashless basis, all other terms of Mr. Bolduc's options remained unchanged ; and (v) Mr. Bolduc agreed to release all claims against the Company. We recorded a non-cash charge of $440,000 in our consolidated statements of operations and comprehensive loss in the year ended June 30, 2015 to record additional stock-based compensation expense resulting from the amendments to Mr. Bolduc's existing vested stock options.

17. Legal Proceedings

On March 23, 2015, Bernard Miller ("Mr. Miller"), individually and on behalf of all others similarly situated shareholders of the company, filed a complaint against Dr. William J. McGann, Messrs. Glenn D. Bolduc, John H. Hassett, John A. Keating, Robert P. Liscouski, Howard Safir and Michael C. Turmelle and the Company in the Suffolk Superior Court of the Commonwealth of Massachusetts, seeking derivative action as a result of director breaches of fiduciary duty and unjust enrichment. Amongst other things, the plaintiff requested that the court compel the Company to hold an annual stockholders' meeting; subject the September 2012 Amendment to the 2004 Plan to a vote at the next annual stockholders' meeting; rescind the stock option awards granted under the September 2012 Amendment to 2004 Plan in the event that the amendment is not approved by a majority of our stockholders'; impose a trust, in favor of the Company, for any benefits improperly received; and award costs and expenses, including reasonable attorney fees.

On July 1, 2015 we held our 2015 Annual Meeting of Stockholders. Stockholders approved an amendment to the Company's 2004 Stock Option Plan to increase the aggregate number of shares of the Company's common stock, par value $0.001 per share available for issuance under the Plan by 16,000,000 shares to 20,000,000 shares and approve the Company's Amended and Restated 2014 Stock Option Plan.

We believe the case was without merit and that we had substantial defenses against the plaintiff's claims. We are contesting the matter vigorously; on May 22, 2015, a motion to dismiss the Complaint with prejudice was served on the plaintiff and subsequently filed with the Court. On July 21, 2015, the Court endorsed as an Order of Stipulation the parties entered into. The Stipulation provides, among other things, that the Complaint is dismissed

with prejudice and the Motion to Dismiss is moot. The sole matter to be decided is whether the Plaintiff or we will recover their respective attorney's fees and expenses incurred as a result of this litigation. We believe that an unfavorable outcome on the case is possible, but not probable and the amount of the loss is estimated at $280,000. If, however, Mr. Miller is ultimately successful, it could have a material adverse effect on our business and financial condition.

In January 2011, Fulong Integrated Technique, Ltd. filed a complaint against us in the Middlesex Superior Court of the Commonwealth of Massachusetts, alleging non-payment of amounts owed for services provided to us in connection with the sale of handheld explosives detection equipment to a customer in China in the first quarter of fiscal 2009. Fulong sought general monetary damages, other statutory damages, attorneys' fees and costs.

In March 2013, we entered into a settlement agreement with Fulong, which provided for the payment of $200,000 and the transfer of ownership of five QS-H150 detectors to Fulong. We recognized a non-cash benefit of $295,000 in general and administrative expenses in the year ended June 30, 2013 as a result of the settlement.

We are not currently a party to any legal proceedings, other than routine litigation incidental to our business that which we believe will not have a material effect on our business, assets or results of operations. From time to time, we are subject to various claims, legal proceedings and investigations covering a wide range of matters that arise in the ordinary course of our business activities. Each of these matters may be subject to various uncertainties.

18. Subsequent Events

An Annual Meeting of Stockholders of the Company was held on July 1, 2015. At the meeting, the following proposals were voted upon and approved:

- Election of Robert P. Liscouski, William J. McGann, James M. Simon, Jr. and Michael C. Turmelle to the Board of Directors.
- Ratify the selection of the firm of Marcum LLP the Company's independent registered public accountants for the fiscal year ending June 30, 2015.
- Approve an amendment to the Company's Restated Articles of Organization to increase the number of authorized shares of Common Stock by 50,000,000 shares to 250,000,000 shares.
- Approved an amendment to the Company's 2004 Stock Option Plan (the "Plan") to increase the aggregate number of shares of the Company's common stock, par value $0.001 per share (the "Common Stock") available for issuance under the Plan by 16,000,000 shares to 20,000,000 shares.
- Approved the Company's Amended and Restated 2014 Stock Option Plan (the "Plan").
- Approved named executive officer compensation, as disclosed in the Proxy Statement, on a non-binding advisory basis.
- Approved the frequency of holding an advisory vote on executive compensation, on a non-binding advisory basis.

On August 7, 2015, the Board of Directors approved a sign-on bonus to Mr. Liscouski in the amount of $200,000, which bonus will be payable to Mr. Liscouski in our fiscal year ended June 30, 2016.

On September 1, 2015, the Board of Directors of the Company split the roles of Chief Executive Officer and President and appointed Robert Liscouski, formerly the Executive Vice President of the Company, as the Company's President. Mr. Liscouski will continue to serve on the Company's Board of Directors. Dr. Bill McGann will continue to serve as the Company's Chief Executive Officer and as a member of the Company's Board of Directors.

On September 24, 2015, Montsant converted $245,000 of the accrued interest owed by us under a promissory note into 3,062,500 shares of our common stock, at an adjusted conversion price of $0.08 per share.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Dated: September 28, 2015

Implant Sciences Corporation

By: /s/ William J. McGann
William J. McGann
Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Dated: September 28, 2015

/s/ William J. McGann
William J. McGann
Chief Executive Officer and Director
(Principal Executive Officer)

Dated: September 28, 2015

/s/ Michael C. Turmelle
Michael C. Turmelle
Chairman of the Board and Director

Dated: September 28, 2015

/s/ Robert P. Liscouski
Robert P. Liscouski
President and Director

Dated: September 28, 2015

/s/ Roger P. Deschenes
Roger P. Deschenes
Vice President, Finance and Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)

Dated: September 28, 2015

/s/ James M. Simon, Jr.
James M. Simon, Jr.
Director