

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549**

**FORM 10-QSB**

(Mark One)

Quarterly report under Section 13 or 15(d) of  
the Securities Exchange Act of 1934

For the quarterly period ended September 30, 2005

Transition report under Section 13 or 15(d) of  
the Securities Exchange Act of 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

*Commission File Number: 0-24431*

InkSure Technologies Inc.  
(Exact Name of Small Business Issuer as Specified in Its Charter)

Delaware  
(State or Other Jurisdiction of  
Incorporation or Organization)

84-1417774  
(I.R.S. Employer  
Identification No.)

1770 N.W. 64<sup>th</sup> Street, Ste. 350, Fort Lauderdale, FL 33309  
(Address of Principal Executive Offices, Including Zip Code)

(954) 772-8507  
(Issuer's Telephone Number, Including Area Code)

\_\_\_\_\_  
(Former Name, Former Address and Former Fiscal Year,  
if Changed Since Last Report)

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

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

The number of shares outstanding of our Common Stock, par value \$0.01 per share, as of November 9, 2005, was 15,161,325 shares.

**Transitional Small Business Disclosure Format (check one):**

Yes  No

# InkSure Technologies Inc.

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**PART I. FINANCIAL INFORMATION**

**Item 1. Financial Statements**

**INKSURE TECHNOLOGIES INC.**

**CONDENSED CONSOLIDATED BALANCE SHEET**

(U.S. dollars in thousands)

	<u>September 30, 2005</u> <u>Unaudited</u>
<b>ASSETS</b>	
<b>CURRENT ASSETS:</b>	
Cash and cash equivalents	\$ 6,058
Trade receivables	184
Other accounts receivable and prepaid expenses	131
Inventories	<u>576</u>
Total current assets	6,949
<b>SEVERANCE PAY FUND</b>	<u>133</u>
<b>PROPERTY AND EQUIPMENT, NET</b>	<u>225</u>
<b>GOODWILL</b>	<u>271</u>
<b>DEFERRED CHARGES</b>	<u>631</u>
Total assets	<u>\$ 8,209</u>

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

**INKSURE TECHNOLOGIES INC.**

**CONDENSED CONSOLIDATED BALANCE SHEET**

(U.S. dollars in thousands, except share data)

	<b>September 30,</b> <b>2005</b>
	<b>Unaudited</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>	
<b>CURRENT LIABILITIES:</b>	
Trade payables	\$ 364
Employees and payroll accruals	94
Deferred income	206
Accrued expenses and other payables	616
Total current liabilities	1,280
ACCRUED SEVERANCE PAY	149
CONVERTIBLE NOTES, NET	4,260
<b>STOCKHOLDERS' EQUITY:</b>	
Share capital:	
Preferred stock of \$ 0.01 par value:	
Authorized: 10,000,000 stocks at September 30, 2005; Issued and outstanding: 0 stocks at September 30, 2005	
Common Stock of \$ 0.01 par value -	
Authorized: 35,000,000 stocks at September 30, 2005; Issued and outstanding: 15,161,325 stocks at September 30, 2005	152
Additional paid-in capital	13,827
Deferred compensation	(26)
Accumulated other comprehensive income	118
Accumulated deficit	(11,551)
Total stockholders' equity	2,520
Total liabilities and stockholders' equity	\$ 8,209

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

**INKSURE TECHNOLOGIES INC.**

**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**

(U.S. dollars in thousands, except share and per share data)

	Nine months ended September 30,		Three months ended September 30,	
	2005	2004	2005	2004
	Unaudited		Unaudited	
Revenues	\$ 1,020	\$ 624	\$ 239	\$ 85
Cost of revenues	638	283	149	59
Gross profit	382	341	90	26
Operating expenses:				
Research and development	607	573	237	179
Selling and marketing	1,088	879	388	324
General and administrative	456	474	190	165
Amortization of deferred stock-based Compensation (relating to General and administrative expenses)	32	-	14	-
Total operating expenses	2,183	1,926	829	668
Operating loss	(1,801)	(1,585)	(739)	(642)
Financial income, net	24	13	7	3
Net loss	\$ (1,777)	\$ (1,572)	\$ (732)	\$ (639)
Basic and diluted net loss per share	\$ (0.12)	\$ (0.12)	\$ (0.05)	\$ (0.04)
Weighted average number of Common Stock used in computing basic and diluted net loss per share	15,039,571	13,601,429	15,094,337	14,789,051

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

**INKSURE TECHNOLOGIES INC.**

**STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY**

U.S. dollars in thousands

	<u>Share capital</u>	<u>Additional paid-in capital</u>	<u>Deferred compensation</u>	<u>Accumulated other comprehensive income</u>	<u>Accumulated deficit</u>	<u>Total stockholders' equity</u>
Balance as of January 1, 2005	\$ 150	\$ 12,031	\$ -	\$ 118	\$ (9,774)	\$ 2,525
Grant of stock options	-	58	(58)	-	-	-
Amortization of deferred compensation	-	-	32	-	-	32
Conversion of 294,900 warrants into 149,746 ordinary shares	2	(2)	-	-	-	-
Beneficial conversion feature of convertible notes	-	1,740	-	-	-	1,740
Net loss	-	-	-	-	(1,777)	(1,777)
Balance as of September 30, 2005 (Unaudited)	<u>\$ 152</u>	<u>\$ 13,827</u>	<u>\$ (26)</u>	<u>\$ 118</u>	<u>\$ (11,551)</u>	<u>\$ 2,520</u>

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

**INKSURE TECHNOLOGIES INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**U.S. dollars in thousands**

	<b>Nine months ended September 30,</b>		<b>Three months ended September 30,</b>	
	<b>2005</b>	<b>2004</b>	<b>2005</b>	<b>2004</b>
	<b>Unaudited</b>		<b>Unaudited</b>	
<u>Cash flows from operating activities:</u>				
Net loss	\$ (1,777)	\$ (1,572)	\$ (732)	\$ (639)
Adjustments to reconcile net loss to net cash used in operating activities:				
Depreciation and amortization	100	111	35	38
Accrued severance pay, net	2	(6)	2	-
Decrease in trade receivables	133	306	98	162
Decrease (increase) in other accounts receivable and prepaid expenses	(20)	(6)	(5)	47
Increase in inventories	(46)	(347)	(85)	(153)
Increase (decrease) in trade payables	(17)	(161)	92	(173)
Decrease in employees and payroll accruals	(13)	(24)	(5)	(5)
Increase (decrease) in other payables	240	10	(37)	17
Accumulated interest on short-term bank deposits	-	-	-	1
Net cash used in operating activities	<u>(1,398)</u>	<u>(1,689)</u>	<u>(637)</u>	<u>(705)</u>
<u>Cash flows from investing activities:</u>				
Purchase of property and equipment	(30)	(56)	(19)	(2)
Net cash used in investing activities	<u>(30)</u>	<u>(56)</u>	<u>(19)</u>	<u>(2)</u>
<u>Cash flows from financing activities:</u>				
Issuance of convertible notes, net	5,838	-	5,838	-
Issuance of common stock, net	-	2,386	-	1,119
Net cash provided by financing activities	<u>5,838</u>	<u>2,386</u>	<u>5,838</u>	<u>1,119</u>
Increase in cash and cash equivalents	4,410	641	5,182	412
Cash and cash equivalents at the beginning of the period	<u>1,648</u>	<u>1,432</u>	<u>876</u>	<u>1,661</u>
Cash and cash equivalents at the end of the period	<u>\$ 6,058</u>	<u>\$ 2,073</u>	<u>\$ 6,058</u>	<u>\$ 2,073</u>

**Non cash activity**

Conversion of 294,900 warrants into 149,746 ordinary shares.

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

**INKSURE TECHNOLOGIES INC.**

**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS  
(UNAUDITED)**

**NOTE 1 - BASIS OF PRESENTATION**

The accompanying condensed unaudited interim condensed consolidated financial statements have been prepared by INKSURE TECHNOLOGIES INC. (the "Company") in accordance with accounting principles generally accepted in the United States of America for interim financial information and the instructions to Form 10-QSB and Article 10 of Regulation S-X. These financial statements reflect all adjustments, consisting of normal recurring adjustments and accruals, which are, in the opinion of management, necessary for a fair presentation of the financial position of the Company as of September 30, 2005 and the results of operations and cash flows for the interim periods indicated in conformity with generally accepted accounting principles applicable to interim periods. Accordingly, certain information and footnote disclosures normally included in annual financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. These financial statements should be read in conjunction with the audited financial statements and notes thereto of the Company for the year ended December 31, 2004 that are included in the Company's Form 10-KSB filed with the Securities and Exchange Commission on March 31, 2005 (the "2004 10-KSB"). The results of operations presented are not necessarily indicative of the results to be expected for future quarters or for the year ending December 31, 2005.

**NOTE 2:- STOCK-BASED COMPENSATION**

The Company has elected to follow Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB No. 25") and FASB Interpretation No. 44, "Accounting for Certain Transactions Involving Stock Compensation" ("FIN No. 44") in accounting for its employee stock option plans. Under APB No. 25, when the exercise price of the Company's stock options is less than the market price of the underlying shares on the date of grant, compensation expense is recognized.

Under Statement of Financial Accounting Standard No. 123, "Accounting for Stock Based Compensation" ("SFAS No. 123"), pro forma information regarding net loss and loss per share is required, and has been determined as if the Company had accounted for its employee stock options under the fair value method of that statement. The fair value for these options was estimated at the date of grant using a Black-Scholes Option Valuation model with the following weighted-average assumptions for nine months ended September 30, 2005 and 2004: weighted-risk-free interest rate of 3.94% and 1.5% for each period respectively, with dividend yields of 0% for each period, volatility factors of the expected market price of the Company's Common Stock of 1.16 and 1.04, and a weighted-average expected life of the options of 5 and 2 years. Stock compensation, for pro forma purposes, is amortized over the vesting period.

**INKSURE TECHNOLOGIES INC.**

**NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS  
(UNAUDITED)**

**NOTE 2:- STOCK-BASED COMPENSATION (cont.)**

The following table illustrates the effect on net loss and loss per share as if the fair value method had been applied to all outstanding and unvested awards in each period:

	<b>Nine months ended</b>		<b>Three months ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2005</b>	<b>2004</b>	<b>2005</b>	<b>2004</b>
	<u>Unaudited</u>		<u>Unaudited</u>	
Net loss, as reported	\$ (1,777)	\$ (1,572)	\$ (732)	\$ (639)
Deduct: Total stock-based compensation expense determined under fair value method for all awards	<u>(244)</u>	<u>(172)</u>	<u>(84)</u>	<u>(64)</u>
Pro forma net loss	<u>\$ (2,021)</u>	<u>\$ (1,744)</u>	<u>\$ (816)</u>	<u>\$ (703)</u>
Basic and diluted net loss per share, as reported	<u>\$ (0.12)</u>	<u>\$ (0.12)</u>	<u>\$ (0.05)</u>	<u>\$ (0.04)</u>
Basic and diluted net loss per share, pro forma	<u>\$ (0.13)</u>	<u>\$ (0.13)</u>	<u>\$ (0.05)</u>	<u>\$ (0.05)</u>

**NOTE 3:- CONVERTIBLE NOTE**

On September 30, 2005 the company Completed a private placement of convertible notes in the aggregate principal amount of \$6,000,000 pursuant to the Securities Purchase Agreement as of such date between the Company and certain investors.

The convertible notes are unsecured and will become due on September 30, 2010. Prior to maturity, the convertible notes will be interest-only, with interest payments due quarterly at yearly rate of 4%.

The convertible notes are convertible into 2,000,000 shares of the Company's common stock at conversion price per share of \$3.00. The Company recorded a discount in the amount of \$1,740,000, which reflects the beneficial conversion feature of the notes. The discount will be amortized over five years period.

In accordance with the issuing of the notes, the Company accrued issuance charges in the amount of \$631 thousands, which will be amortized over five years period.

## **Item 2. Management's Discussion and Analysis or Plan of Operation**

In this section, "Management's Discussion and Analysis or Plan of Operation," references to "we," "us," "our," and "ours" refer to InkSure Technologies Inc. and its consolidated subsidiaries.

This Quarterly Report on Form 10-QSB contains statements that may constitute "forward-looking statements" within the meaning, and made pursuant to the Safe Harbor provisions, of the Private Securities Litigation Reform Act of 1995. Such statements are based on management's current expectations and are subject to a number of risks and uncertainties, including, but not limited to, the difficulty inherent in operating an early-stage company in a new and rapidly evolving market, market and economic conditions, the impact of competitive products, product demand and market acceptance risks, changes in product mix, costs and availability of raw materials, fluctuations in operating results, delays in development of highly complex products, risk of customer contract or sales order cancellations and other risks detailed from time to time in our filings with the Securities and Exchange Commission, or the Commission. These risks and uncertainties could cause our actual results to differ materially from those described in the forward-looking statements. Any forward-looking statement represents our expectations or forecasts only as of the date it was made and should not be relied upon as representing its expectations or forecasts as of any subsequent date. Except as required by law, we undertake no obligation to correct or update any forward-looking statement, whether as a result of new information, future events or otherwise, even if our expectations or forecasts change.

The following discussion and analysis should be read in conjunction with the financial statements, related notes and other information included in this Quarterly Report on Form 10-QSB.

### **Overview**

We specialize in comprehensive security solutions, designed to protect branded products and documents of value from counterfeiting, fraud, and diversion. By creating "Smart Protection" systems from proprietary machine-readable authentication technologies, we help companies and organizations worldwide regain control over their most valuable assets, their products, their reputation and their revenues. We employ a team of experts in the fields of material science, electro-optics and software. We utilize cross-disciplinary technological innovations to implement customized and cost efficient security systems for data and asset integrity within the customer's existing infrastructure and environment.

Our SmartInk<sup>™</sup> solutions enable authentication and tracking of documents and products by adding special chemical markers to standard inks and coatings. The combination of markers, inks and materials produce electro-optic "signatures", unique codes that are seamlessly incorporated into the printed media used by the customer. Proprietary computerized readers, available in hand-held, stationary and modular kit configurations, quickly verify these codes by manual or automatic operation. By focusing on customer driven solutions, we are able to offer added value through enhanced reader functionality, including high-speed automatic sorting, one-to-many code matching, first and second level track and trace, code activation at the point of distribution and detrimental authentication for debit applications. The inherent flexibility of our technology also enables overlaying the machine-readable codes onto holograms and other overt features, resulting in multi-layered security that is both effective and economical.

### **Factors Affecting Future Results**

*Industry and Economic Factors:* Our operations and earnings are affected by local, regional and global events or conditions that affect supply and demand for products and services. These events or conditions are generally not predictable and include, among other things, general economic growth rates and the occurrence of economic recessions; the development of new supply sources; supply disruptions; technological advances, including advances in security technology and advances in technology relating to security usage; changes in demographics, including population growth rates and consumer preferences; and the competitiveness of alternative security sources or product substitutes. Currently, the economy in general is suffering. As a result, raising capital has become extremely difficult, and there is pressure on the pricing of our products and services.

*Competitive Factors:* The brand and document protection industry is competitive. There is competition with the traditional document protection suppliers (mainly protection for bank notes) and also with other emergent "next generation" technology providers. We compete with other firms in the sale and purchase of various products

and services in many national and international markets and employ all methods of competition, which are lawful and appropriate for such purposes. We believe that a key component of our competitive position is our technology.

*Political Factors:* Our operations and earnings have been, and may in the future be, affected from time to time in varying degree by political instability and by other political developments and laws and regulations, such as forced divestiture of assets; restrictions on production; imports and exports; war or other international conflicts; civil unrest and local security concerns that threaten the safe operation of our facilities, particularly those that are located in Israel; price controls; expropriation of property; and the cancellation of contract rights. Both the likelihood of such occurrences and their overall effect upon us vary greatly from country to country and are not predictable.

*Project Factors:* In addition to the factors cited above, the advancement, cost and results of particular projects depend on the outcome of negotiations with potential partners, governments, suppliers, customers or other third parties; changes in operating conditions or costs; and the occurrence of unforeseen technical difficulties.

## **Revenues**

We are currently concentrating on entering and implementing large-scale projects. These potential contracts are subject to a long sales cycle and the timetable is lengthy for entering and implementing such projects. These projects involve high volume sales through multiple-year sales contracts. We have completed several successful field trials during the last year related to these projects. Our revenues in the third quarter of 2005 consisted of revenues from (i) our sales agreements for brand protection with two North American customers; and (ii) initial sales to new North American customers. In the third quarter of 2005 approximately 99% of our revenues were earned from customers located in the United States.

## **Costs and Operating Expenses**

Costs and operating expenses consist of cost of revenues, research and development expenses, selling and marketing expenses, general and administrative expenses and depreciation.

Our cost of revenues consists primarily of materials including taggants and electronic and optical parts, payments to sub-contractors and compensation costs for our operations staff.

Our research and development expenses consist primarily of costs associated with development of new generic products and the development of new products related to customer projects. These expenses may fluctuate as a percentage of revenue depending on the projects undertaken during the reporting period. Since our inception, we have expensed all research and development costs in each of the periods in which they were incurred.

Our selling and marketing expenses consist primarily of costs associated with our direct sales force that have been incurred to attract potential business customers, professional advisors and commissions. We anticipate that as we add new customers we will be able to spread these costs over a larger revenue base and accordingly improve our operating margins.

Our general and administrative expenses consist primarily of costs related to compensation and employees benefits of our management (including the costs of directors' and officers' insurance), legal and accounting fees, as well as the expenses associated with being a publicly traded company.

We have not recorded any income tax benefit for net losses and credits incurred for any period from inception to September 30, 2005. The utilization of these losses and credits depends on our ability to generate taxable income in the future. Because of the uncertainty of our generating taxable income, we have recorded a full valuation allowance with respect to these deferred assets.

## **Critical Accounting Policies**

Our financial statements are prepared in accordance with US GAAP. The significant accounting policies followed in the preparation of the financial statements, applied on a consistent basis and which have been prepared in accordance with the historical cost convention, are set forth in Note 2 to the Consolidated Financial Statements as

of December 31, 2004.

Of these significant accounting policies, certain policies may be considered critical because they are most important to the portrayal of our financial condition and results, and they require management's most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. We believe the following critical accounting policies affect our more significant judgments and estimates used in the preparation of our consolidated financial statements.

*Revenue recognition.* Revenues from product sales are recognized in accordance with Staff Accounting Bulletin No. 104, "Revenue Recognition in Financial Statements", or SAB No. 104, when delivery has occurred, persuasive evidence of an agreement exists, the vendor's fee is fixed or determinable, no further obligation exists and collectability is probable. Delivery is considered to have occurred upon shipment of products. When a right of return exists, we defer revenues until the right of return expires. We do not grant a right of return to our customers.

Revenues from certain arrangements may include multiple elements within a single contract. Our accounting policy complies with the provisions of Emerging Issues Task Force Issue 00-21, "Revenue Arrangements with Multiple Deliverables" ("EITF 00-21"), relating to the separation of multiple deliverables into individual accounting units with determinable fair value.

In cases where we have partial delivery at the cut off dates and no fair value exists for the undelivered elements, revenues are being deferred and recognized only at the point where the entire arrangement has been delivered.

*Inventories.* Inventories are stated at the lower of cost or net realizable value. Cost is determined by calculating raw materials, work in process and finished products using the "first in, first out" method.

*Other accrued expenses.* We also maintain other accrued expenses. These accruals are based on a variety of factors including past experience and various actuarial assumptions and, in many cases, require estimates of events not yet reported to us. If future experience differs from these estimates, operating results in future periods would be impacted.

### **Three Months Ended September 30, 2005 Compared with Three Months Ended September 30, 2004**

*Revenues.* Revenues consist of gross sales of products less discounts. We are currently concentrating on entering and implementing large-scale projects. In the three months ended September 30, 2005, we had revenue of \$239,000, compared to \$85,000 in the three months ended September 30, 2004. Revenues increased by \$154,000, or 181.1%, in the three months ended September 30, 2005 compared to the three months ended September 30, 2004. The increase is mainly related to higher sales to our North American customers.

*Cost of Revenue.* Our cost of revenue consists of materials, sub-contractors and compensation costs. Cost of revenues increased by \$90,000, or 152.5%, to \$149,000 in the three months ended September 30, 2005 from \$59,000 in the three months ended September 30, 2004. Cost of revenues as a percentage of sales was 62.3% in the three months ended September 30, 2005, compared with 69.4% in the three months ended September 30, 2004.

*Research and Development Expenses.* Research and development expenses consist primarily of compensation costs attributable to employees engaged in ongoing research and development activities, development-related raw materials and sub-contractors, and other related costs. Research and development expenses increased by \$58,000, or 32.4%, to \$237,000 in the three months ended September 30, 2005 from \$179,000 in the three months ended September 30, 2004. This increase in research and development expenses is primarily related to the development and implementation of our RFID technology.

*Selling and Marketing Expenses.* Selling and marketing expenses consist primarily of costs relating to compensation attributable to employees engaged in sales and marketing activities, promotion, advertising, trade shows and exhibitions, sales support, travel, commissions and related expenses. Selling and marketing expenses increased by \$64,000, or 19.7%, to \$388,000 in the three months ended September 30, 2005 from \$324,000 in the three months ended September 30, 2004. This increase in selling and marketing expenses was primarily due to higher marketing expenses related to the new sales agreements we have entered into. We believe that the significant

investment in pre-sales and marketing activities will contribute to our short-term and long-term sales levels.

*General and Administrative Expenses.* General and administrative expenses consist primarily of compensation costs for administration, finance and general management personnel, insurance, legal, accounting and administrative costs. General and administrative expenses increased by \$25,000, or 15.1%, to \$190,000 in the three months ended September 30, 2005 from \$165,000 in the three months ended September 30, 2004. The increase was primarily related to higher accounting expenses.

*Financial Income, Net.* Financial income, net increased by \$4,000, or 133.3%, to \$7,000 in the three months ended September 30, 2005 from \$3,000 in the three months ended September 30, 2004. This increase is due to changes in the exchange rate between the United States Dollar and the Israeli New Shekel.

*Net loss.* We had a net loss of \$732,000 in the three months ended September 30, 2005, compared with a net loss of \$639,000 in the three months ended September 30, 2004. The 14.5 % increase in net loss in the three months ended September 30, 2005 in comparison with the three months ended September 30, 2004 is attributable mainly to the increase in operating expenses.

### **Nine Months Ended September 30, 2005 Compared with Nine Months Ended September 30, 2004**

*Revenue.* Revenue consists of gross sales of products less discounts. We are currently concentrating on entering and implementing large-scale projects. These potential contracts are subject to a long sales cycle and fluctuated timetable for entering and implementing such projects. Revenues increased by \$396,000, or 63.4%, in the nine months ended September 30, 2005 compared to the nine months ended September 30, 2004. In the nine months ended September 30, 2005, we had revenue of \$1,020,000, compared to \$624,000 in the nine months ended September 30, 2004, primarily due to higher sales to our North American customers.

*Cost of Revenue.* Our cost of revenue consists of materials, sub-contractors and compensation costs. Cost of revenue in the nine months ended September 30, 2005 was \$638,000, compared to \$283,000 in the nine months ended September 30, 2004. Cost of revenues as a percentage of sales was 62.5% in the nine months ended September 30, 2005, compared with 45.3% in the nine months ended September 30, 2004. The increase in cost of revenues is the result of our strategic decision to reduce the price paid by one of our customers in connection with one of our new major contracts.

*Research and Development Expenses.* Research and development expenses consist primarily of compensation costs attributable to employees engaged in ongoing research and development activities, development-related raw materials and sub-contractors, and other related costs. Research and development expenses increased by \$34,000, or 5.9%, to \$607,000 in the nine months ended September 30, 2005 from \$573,000 in the nine months ended September 30, 2004. This increase in research and development expenses is primarily related to the development and implementation of our RFID technology.

*Selling and Marketing Expenses.* Selling and marketing expenses consist primarily of costs relating to compensation attributable to employees engaged in sales and marketing activities, promotion, advertising, trade shows and exhibitions, sales support, travel, commissions and related expenses. Selling and marketing expenses increased by \$209,000, or 23.7%, to \$1,088,000 in the nine months ended September 30, 2005 from \$879,000 in the nine months ended September 30, 2004. This increase in selling and marketing expenses was primarily due to higher marketing expenses related to the new sales agreements we have entered into. We believe that the significant investment in pre-sales and marketing activities will contribute to our short-term and long-term sales levels.

*General and Administrative Expenses.* General and administrative expenses consist primarily of compensation costs for administration, finance and general management personnel, insurance, legal, accounting and administrative costs. General and administrative expenses decreased by \$18,000, or 3.9%, to \$456,000 in the nine months ended September 30, 2005 from \$474,000 in the nine months ended September 30, 2004. This decrease was primarily related to lower legal expenses.

*Financial Income, Net.* Financial income, net increased by \$11,000 or 84.6%, to \$24,000 in the nine months ended September 30, 2005 from \$13,000 in the nine months ended September 30, 2004. This increase is due to changes in the exchange rate between the United States Dollar and the Israeli New Shekel.

*Net loss.* We had a net loss of \$1,777,000 in the nine months ended September 30, 2005, compared with a net loss of \$1,572,000 in the nine months ended September 30, 2004. The 13.0% increase in net loss in the nine months ended September 30, 2005 in comparison with the nine months ended September 30, 2004 is attributable to the various influences described above.

### **Liquidity and Capital Resources**

We have incurred substantial losses since our inception in May 2000. We had an accumulated deficit of approximately \$11,551,000 at September 30, 2005, and had working capital (current assets less current liabilities) of approximately \$5,669,000 at September 30, 2005.

Capital expenditures were approximately \$19,000 in the three months ended September 30, 2005 and \$2,000 in the three months ended September 30, 2004. Capital expenditures were approximately \$30,000 in the nine months ended September 30, 2005 and \$56,000 in the nine months ended September 30, 2004. We do not have any material commitments for capital expenditures for the year ending December 31, 2005.

At September 30, 2005, we had cash, cash equivalents and short-term deposits of approximately \$6,058,000, compared to \$2,073,000 at September 30, 2004. The differences from September 30, 2005 to September 30, 2004 are due to the negative cash flow from operating activities during the last fiscal year and the gross amount of \$6,000,000 raised in the private placement of convertible notes.

We generated negative cash flow from operating activities of approximately \$637,000 in the three months ended September 30, 2005 compared to \$705,000 in the three months ended September 30, 2004. We generated negative cash flow from operating activities of approximately \$1,398,000 in the nine months ended September 30, 2005 compared to \$1,689,000 in the nine months ended September 30, 2004.

We believe that cash generated from operations will provide sufficient cash resources to finance our operations and the projected expansion of our marketing and research and development activities for the next twelve months. However, if our operations do not generate cash to the extent currently anticipated, or we grow more rapidly than currently anticipated, it is possible that we would require more funds than presently anticipated.

### **Research and Development, Patents and Licenses**

We believe that our future success will depend upon our ability to enhance our existing products and systems and introduce new commercially viable products and systems addressing the demands of the evolving markets for brand and document protection. As part of the product development process, we work closely with current and potential customers, distribution channels and leaders in certain industry segments to identify market needs and define appropriate product specifications. Our employees also participate in industry forums in order to stay informed about the latest industry developments.

Our research and development expenses were approximately \$237,000 in the three months ended September 30, 2005, compared to \$179,000 in the three months ended September 30, 2004. Our research and development expenses were approximately \$607,000 in the nine months ended September 30, 2005, compared to \$573,000 in the nine months ended September 30, 2004. To date, all research and development expenses have been charged to operating expense as incurred.

We currently hold five pending patents on our technologies and we have been issued two patents related to our RF technology in the United States. In addition a patent application for such technology has been approved in the European Union. Currently we are seeking additional protection for such technology in certain European countries.

### **Contractual Obligations and Commitments**

Our contractual obligations and commitments at September 30, 2005 principally include obligations associated with operating lease obligations and the lease of several automobiles. Our total future obligation is approximately \$153,000 until 2007. We expect to finance these contractual commitments from cash on hand and cash generated from operations.

### Item 3. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures. Our principal executive officer and principal financial officer, after evaluating the effectiveness of our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of the end of the period covered by this Quarterly Report on Form 10-QSB, have concluded that, based on such evaluation, our disclosure controls and procedures were adequate and effective to ensure that material information relating to us, including our consolidated subsidiaries, was made known to them by others within those entities, particularly during the period in which this Quarterly Report on Form 10-QSB was being prepared.

(b) Changes in Internal Controls. There were no changes in our internal control over financial reporting, identified in connection with the evaluation of such internal control that occurred during our last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II. OTHER INFORMATION

### Item 4. Submission of Matters to a Vote of Security Holders

The Company held its Annual Meeting of Stockholders on July 7, 2005. The following matters were voted on at the Annual Meeting of Stockholders:

Proposal 1: Election of a Board of Directors.

	<b><u>NUMBER OF SHARES VOTED FOR</u></b>	<b><u>WITHHELD</u></b>
Elie Housman	<b>8,182,971</b>	<b>0</b>
Yaron Meerfeld	<b>8,182,971</b>	<b>0</b>
James Lineberger	<b>8,182,971</b>	<b>0</b>
Philip Getter	<b>8,182,971</b>	<b>0</b>
Michael Acks	<b>8,182,971</b>	<b>0</b>
Albert Attias	<b>8,182,971</b>	<b>0</b>
David Sass	<b>8,182,971</b>	<b>0</b>

Proposal 2: Ratification of the appointment of Brightman Almagor & Co., Certified Public Accountants, A member firm of Deloitte Touche Tohmatsu, as the independent auditors and accountants for the Company for the year ending December 31, 2005.

	<b><u>NUMBER OF SHARES</u></b>		
	<b><u>FOR</u></b>	<b><u>AGAINST</u></b>	<b><u>ABSTAIN</u></b>
	<b>8,182,971</b>	<b>0</b>	<b>0</b>

## Item 6. Exhibits and Reports on Form 8-K

### (a) Exhibits

The following exhibits are being filed with this Report:

<u>Exhibit Number</u>	<u>Description</u>
2.1	Agreement and Plan of Merger, dated July 5, 2002, among the Company, LILM Acquisition and InkSure Delaware. (Incorporated by reference to the Company's Information Statement on Schedule 14C, filed with the Commission on October 8, 2002.)
2.2	Agreement and Plan of Merger, dated July 3, 2003 among the Company and InkSure Technologies (Delaware) Inc. (Incorporated by reference to the Company's report filed on Form 8-K, filed with the Commission on July 22, 2003.)
3.1	Certificate of Incorporation of the Company. (Incorporated by reference to the Company's report filed on Form 8-K, filed with the Commission on July 22, 2003.)
3.2	By-Laws of the Company. (Incorporated by reference to the Company's report filed on Form 8-K, filed with the Commission on July 22, 2003.)
31.1*	Certification of Principal Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350.
31.2*	Certification of Principal Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350.
32.1*	Certification of Principal Executive Officer and Principal Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350.

\* Filed herewith

### (b) Reports on Form 8-K

During the three months ended September 30, 2005, we did not file any reports on Form 8-K with the Commission.

## SIGNATURES

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

### **InkSure Technologies Inc.**

Dated: As of November 9, 2005

By: /s/ Eyal Bigon  
Eyal Bigon  
Chief Financial Officer,  
Secretary and Treasurer  
(Principal Financial and  
Accounting Officer)

Dated: As of November 9, 2005

By: /s/ Elie Housman  
Elie Housman  
Chief Executive Officer  
(Principal Executive Officer)

Exhibit 31.1

CERTIFICATION

I, Eyal Bigon, certify that:

1. I have reviewed this quarterly report of InkSure Technologies Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 9, 2005

/s/ Eyal Bigon

Eyal Bigon

Chief Financial Officer, Secretary and Treasurer

Exhibit 31.2

CERTIFICATION

I, Elie Housman, certify that:

1. I have reviewed this quarterly report of InkSure Technologies Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 9, 2005

/s/ Elie Housman  
Elie Housman, Chief Executive Officer

Exhibit 32.1

CERTIFICATION

PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

(SUBSECTIONS (A) AND (B) OF SECTION 1350, CHAPTER 63 OF

TITLE 18, UNITED STATES CODE)

Pursuant to section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of section 1350, chapter 63 of title 18, United States Code), each of the undersigned officers of InkSure Technologies Inc., a Delaware corporation (the "Company"), does hereby certify, to such officer's knowledge, that:

The Form 10-QSB for the quarter ended September 30, 2005 (the "Form 10-QSB") of the Company fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, and the information contained in the Form 10-QSB fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: November 9, 2005

/s/ Elie Housman

Elie Housman, Chief Executive Officer

Dated: November 9, 2005

/s/ Eyal Bigon

Eyal Bigon, Chief Financial Officer

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