

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

FORM 10-Q

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

For the quarterly period ended June 30, 2019
Commission File Number: 000-55838



Wrap Technologies, Inc.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

98-0551945
(I.R.S. Employer
Identification Number)

4620 Arville Street, Ste E
Las Vegas, Nevada 89103
(Address of principal executive offices) (Zip Code)

(800) 583-2652
(Registrant's Telephone Number, Including Area Code)

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

Indicate by check mark whether the registrant has submitted every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large Accelerated Filer	<input type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input checked="" type="checkbox"/>	Smaller reporting company	<input checked="" type="checkbox"/>
		Emerging growth company	<input checked="" type="checkbox"/>

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of August 3, 2019 a total of 29,656,500 shares of the Registrant's Common Stock, par value \$0.0001, were issued and outstanding.

WRAP TECHNOLOGIES, INC.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Wrap Technologies, Inc.
Condensed Balance Sheets

	June 30, 2019 <u>(unaudited)</u>	December 31, 2018
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 21,377,807	\$ 12,358,896
Accounts receivable	31,259	4,396
Inventories, net	1,255,587	158,267
Prepaid expenses and other current assets	186,045	114,863
Total current assets	22,850,698	12,636,422
Property and equipment, net	126,803	30,373
Operating lease right-of-use asset, net	318,789	-
Intangible assets, net	186,829	118,715
Other assets, net	12,681	1,512
Total assets	\$ 23,495,800	\$ 12,787,022
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 416,393	\$ 232,915
Accrued liabilities	131,372	68,453
Deferred revenue	3,357	-
Operating lease liability- short term	104,327	-
Deferred and accrued officer compensation	96,000	96,000
Total current liabilities	751,449	397,368
Operating Lease Liability - Long Term	215,780	-
Total liabilities	967,229	397,368
Commitments and contingencies (Note 10)		
Stockholders' equity:		
Preferred stock - 5,000,000 authorized; par value \$0.0001 per share; none issued and outstanding	-	-
Common stock - 150,000,000 authorized; par value \$0.0001 per share; 29,640,250 and 27,364,607 shares issued and outstanding each period, respectively	2,964	2,736
Additional paid-in capital	30,324,798	16,791,254
Accumulated deficit	(7,799,191)	(4,404,336)
Total stockholders' equity	22,528,571	12,389,654
Total liabilities and stockholders' equity	\$ 23,495,800	\$ 12,787,022

See accompanying notes to condensed interim financial statements.

Wrap Technologies, Inc.
Condensed Statements of Operations
(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
Revenues:				
Product sales	\$ 48,948	\$ -	\$ 162,901	\$ -
Other revenue	10,496	-	14,354	-
Total revenues	<u>59,444</u>	<u>-</u>	<u>177,255</u>	<u>-</u>
Cost of revenues	35,695	-	96,915	-
Gross profit	<u>23,749</u>	<u>-</u>	<u>80,340</u>	<u>-</u>
Operating expenses:				
Selling, general and administrative	1,481,187	581,575	2,669,063	920,742
Research and development	516,213	193,629	891,032	289,614
Total operating expenses	<u>1,997,400</u>	<u>775,204</u>	<u>3,560,095</u>	<u>1,210,356</u>
Loss from operations	<u>(1,973,651)</u>	<u>(775,204)</u>	<u>(3,479,755)</u>	<u>(1,210,356)</u>
Other income (expense):				
Interest income	61,777	537	87,187	758
Other	(2,200)	(875)	(2,287)	(1,322)
	<u>59,577</u>	<u>(338)</u>	<u>84,900</u>	<u>(564)</u>
Net loss	<u>\$ (1,914,074)</u>	<u>\$ (775,542)</u>	<u>\$ (3,394,855)</u>	<u>\$ (1,210,920)</u>
Net loss per basic common share	<u>\$ (0.07)</u>	<u>\$ (0.03)</u>	<u>\$ (0.12)</u>	<u>\$ (0.05)</u>
Weighted average common shares used to compute net loss per basic common share	<u>27,848,421</u>	<u>22,803,533</u>	<u>27,606,514</u>	<u>22,803,533</u>

See accompanying notes to condensed interim financial statements.

Wrap Technologies, Inc.
Condensed Statements of Stockholders Equity
(unaudited)

	Three Months Ended June 30, 2019				
	Common Stock		Additional	Accumulated	Total
	Shares	Amount	Paid-In	Deficit	Stockholders'
			Capital		Equity
Balance at March 31, 2019	27,364,607	\$ 2,736	\$ 17,018,301	\$ (5,885,117)	\$ 11,135,920
Sale of common stock and warrants at \$6.50 per share and placement agent warrants in public offering, net of issuance costs	1,923,076	192	11,351,022		11,351,214
Common shares issued upon exercise of warrants at \$3.00 per share	62,150	6	186,444		186,450
Common shares issued upon exercise of warrants at \$5.00 per share	274,167	28	1,370,807		1,370,835
Common shares issued upon exercise of stock options	16,250	2	24,373		24,375
Share-based compensation expense			373,851		373,851
Net loss for the period	-	-	-	(1,914,074)	(1,914,074)
Balance at June 30, 2019	<u>29,640,250</u>	<u>\$ 2,964</u>	<u>\$ 30,324,798</u>	<u>\$ (7,799,191)</u>	<u>\$ 22,528,571</u>
	Six Months Ended June 30, 2019				
	Common Stock		Additional	Accumulated	Total
	Shares	Amount	Paid-In	Deficit	Stockholders'
			Capital		Equity
Balance at December 31, 2018	27,364,607	\$ 2,736	\$ 16,791,254	\$ (4,404,336)	\$ 12,389,654
Sale of common stock and warrants at \$6.50 per share and placement agent warrants in public offering, net of issuance costs	1,923,076	192	11,351,022		11,351,214
Common shares issued upon exercise of warrants at \$3.00 per share	62,150	6	186,444		186,450
Common shares issued upon exercise of warrants at \$5.00 per share	274,167	28	1,370,807		1,370,835
Common shares issued upon exercise of stock options	16,250	2	24,373		24,375
Share-based compensation expense			600,898		600,898
Net loss for the period	-	-	-	(3,394,855)	(3,394,855)
Balance at June 30, 2019	<u>29,640,250</u>	<u>\$ 2,964</u>	<u>\$ 30,324,798</u>	<u>\$ (7,799,191)</u>	<u>\$ 22,528,571</u>
	Three Months Ended June 30, 2018				
	Common Stock		Additional	Accumulated	Total
	Shares	Amount	Paid-In	Deficit	Stockholders'
			Capital		Equity
Balance at March 31, 2018	22,803,533	\$ 2,280	\$ 4,137,936	\$ (1,503,279)	\$ 2,636,937
Share-based compensation expense			172,973		172,973
Net loss for the period	-	-	-	(775,542)	(775,542)
Balance at June 30, 2018	<u>22,803,533</u>	<u>\$ 2,280</u>	<u>\$ 4,310,909</u>	<u>\$ (2,278,821)</u>	<u>\$ 2,034,368</u>
	Six Months Ended June 30, 2018				
	Common Stock		Additional	Accumulated	Total
	Shares	Amount	Paid-In	Deficit	Stockholders'
			Capital		Equity
Balance at December 31, 2017	22,803,533	\$ 2,280	\$ 4,137,936	\$ (1,067,901)	\$ 3,072,315
Share-based compensation expense			172,973		172,973
Net loss for the period	-	-	-	(1,210,920)	(1,210,920)
Balance at June 30, 2018	<u>22,803,533</u>	<u>\$ 2,280</u>	<u>\$ 4,310,909</u>	<u>\$ (2,278,821)</u>	<u>\$ 2,034,368</u>

See accompanying notes to condensed interim financial statements.

Wrap Technologies, Inc.
Condensed Statements of Cash Flows
(unaudited)

	Six Months Ended June 30,	
	2019	2018
Cash Flows From Operating Activities:		
Net loss	\$ (3,394,855)	\$ (1,210,920)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	12,573	4,846
Warranty provision	3,503	-
Inventory write-off	(65,012)	-
Non-cash lease expense	22,211	-
Share-based compensation	600,898	172,973
Changes in assets and liabilities:		
Accounts receivable	(26,863)	-
Inventories	(1,032,308)	(15,222)
Prepaid expenses and other current assets	(71,182)	(5,695)
Accounts payable	183,478	11,018
Operating lease liability	(20,893)	-
Accrued liabilities and other	59,416	(17,758)
Deferred revenue	3,357	-
Net cash used in operating activities	(3,725,677)	(1,060,758)
Cash Flows From Investing Activities:		
Capital expenditures for property and equipment	(108,616)	(8,015)
Investment in patents and trademarks	(68,501)	-
Long-term deposits	(11,169)	-
Net cash used in investing activities	(188,286)	(8,015)
Cash Flows From Financing Activities:		
Sale of common stock and warrants	11,351,214	-
Proceeds from exercise of warrants	1,557,285	-
Proceeds from exercise of stock options	24,375	-
Net cash provided by financing activities	12,932,874	-
Net increase (decrease) in cash and cash equivalents	9,018,911	(1,068,773)
Cash and cash equivalents, beginning of period	12,358,896	3,083,976
Cash and cash equivalents, end of period	\$ 21,377,807	\$ 2,015,203
Supplemental Disclosure of Non-Cash Investing and Financing Activities:		
Prepaid insurance financed with note payable	\$ -	\$ 39,435
Right-of-use assets and liabilities recorded during period	\$ 341,000	\$ -
Issuance costs relating to warrants issued to public offering selling agent	\$ 205,894	\$ -

See accompanying notes to condensed interim financial statements.

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization and Business Description

Wrap Technologies, Inc., a Delaware corporation (the “Company”), is a developer of security products designed for use by law enforcement and security personnel. The Company’s first product is the BolaWrap® 100 remote restraint device.

On June 18, 2019, the Company received gross cash proceeds of \$12.50 million, or net cash proceeds of approximately \$11.35 million after deduction of commissions and offering costs, from the public offering and sale of 1,923,076 units (“Units”) for a public offering price of \$6.50 per Unit in a follow-on public offering completed under the Company’s effective shelf registration statement on Form S-3 (File No. 333-228974) (the “June 2019 Follow-On Offering”). Each Unit sold during the June 2019 Follow-On Offering consisted of one share of common stock and one detachable two-year warrant to purchase one share of common stock at an exercise price of \$6.50 per share.

Basis of Presentation and Use of Estimates

The Company’s unaudited interim financial statements and related notes included herein have been prepared in accordance with accounting principles generally accepted in the United States of America (“US GAAP”) for interim financial information and in accordance with Article 8 of Regulation S-X and the rules and regulations of the Securities and Exchange Commission (“SEC”). The condensed balance sheet at December 31, 2018 was derived from audited financial statements but certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. In management’s opinion, the accompanying statements reflect adjustments necessary to present fairly the financial position, results of operations, and cash flows for the periods indicated, and contain adequate disclosure to make the information presented not misleading. Adjustments included herein are of a normal, recurring nature unless otherwise disclosed in the footnotes. The interim financial statements and notes thereto should be read in conjunction with the Company’s audited financial statements and notes thereto for the year ended December 31, 2018. Results of operations for interim periods are not necessarily indicative of the results of operations for a full year.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions (e.g., recognition and measurement of contingencies and accrued costs) that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements and affect the reported amounts of revenue and expense during the reporting period. Actual results could materially differ from those estimates.

Concentrations of Risk

Credit Risk – Financial instruments that potentially subject the Company to concentration of credit risk consisted primarily of cash and cash equivalents and accounts receivable from customers. The Company maintains its cash deposits at two domestic financial institutions. The Company is exposed to credit risk in the event of default by a financial institution to the extent that cash and cash equivalents are in excess of the amount insured by the Federal Deposit Insurance Corporation. The Company places its cash and cash equivalents with high-credit quality financial institutions. To date, the Company has not experienced any losses on its cash and cash equivalents.

Concentrations of Accounts Receivable and Revenues – The Company has recently commenced sales activities with a limited number of customers, accounts receivable and revenues. The Company may experience concentrations in both accounts receivable and revenues due to the timing of sales and collections of related payments.

Concentration of Suppliers – The Company relies on a limited number of component suppliers and contract suppliers. In particular, a single supplier is currently the sole manufacturer of the Company’s laser assembly with some parts sole sourced from other suppliers. If supplier shortages occur, or quality problems arise, then production schedules could be significantly delayed or costs significantly increased, which could in turn have a material adverse effect on the Company’s financial condition, results of operation and cash flows.

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Share-Based Compensation

The Company follows the fair value recognition provisions issued by the Financial Accounting Standards Board (“FASB”) in Accounting Standards Codification (“ASC”) Topic 718, Stock Compensation (“ASC 718”) and has adopted Accounting Standards Update (“ASU”) 2018-07 for share-based transactions with non-employees. Share-based compensation expense recognized during the six months ended June 30, 2019 includes stock option and restricted stock unit compensation expense. The grant date fair value of stock options is determined using the Black-Scholes option-pricing model. The grant date is the date at which an employer and employee or non-employee reach a mutual understanding of the key terms and conditions of a share-based payment award. The Black-Scholes option-pricing model requires inputs including the market price of the Company’s common stock on the date of grant, the term that the stock options are expected to be outstanding, the implied stock volatilities of several publicly-traded peers over the expected term of stock options, risk-free interest rate and expected dividend. Each of these inputs is subjective and generally requires significant judgment to determine. The grant date fair value of restricted stock units is based upon the market price of the Company’s common stock on the date of the grant. The fair value of share-based compensation is amortized to compensation expense over the vesting term.

Revenue Recognition

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (“ASU 2014-09”) and ASC Subtopic 340-40, Other Assets and Deferred Costs - Contracts with Customers (“ASC 340-40”), (collectively, “Topic 606”). On January 1, 2018, the Company adopted Topic 606 and, as it had no prior revenue or contracts with customers, there was no transition required nor any impact on prior results. ASU 2014-09 requires entities to recognize revenue through the application of a five-step model, which includes identification of the contract, identification of the performance obligations, determination of the transaction price, allocation of the transaction price to the performance obligations and recognition of revenue as the entity satisfies the performance obligations. See Note 2 for additional information.

Accounts Receivable

Accounts receivable, net consists of trade accounts receivables from customers, net of allowance for doubtful accounts if deemed necessary. Accounts receivables are recorded at the invoiced amount. The Company does not require collateral or other security for accounts receivable. The Company periodically evaluates the collectability of its accounts receivable and provides an allowance for potential credit losses, based on the historical experience. At June 30, 2019 and December 31, 2018, the Company did not have an allowance for potential credit losses as there were no estimated credit losses.

Net Loss per Share

Basic loss per common share is computed by dividing net loss for the period by the weighted-average number of shares of common stock outstanding during the period. Diluted net loss per common share reflects the potential dilution of securities that could share in the earnings of an entity. The Company’s losses for the periods presented cause the inclusion of potential common stock instruments outstanding to be antidilutive. Stock options, restricted stock units and warrants exercisable or issuable for a total of 9,997,123 shares of common stock were outstanding at June 30, 2019. These securities are not included in the computation of diluted net loss per common share for the periods presented as their inclusion would be antidilutive due to losses incurred by the Company.

Income Taxes

Until its conversion to a corporation on March 31, 2017, the Company was treated as a partnership for federal and state income tax purposes and did not incur income taxes. Instead, its losses were included in the income tax returns of the member partners. No income tax expense was recorded for period ended June 30, 2019 due to losses incurred.

Deferred tax assets and liabilities are determined based on temporary differences between the bases of certain assets and liabilities for income tax and financial reporting purposes.

The Company maintains a valuation allowance with respect to deferred tax assets. The Company establishes a valuation allowance based upon the potential likelihood of realizing the deferred tax asset and taking into consideration the Company’s financial position and results of operations for the current period. Future realization of the deferred tax benefit depends on the existence of sufficient taxable income within the carry-forward period under the Federal tax laws. Changes in circumstances, such as the Company generating taxable income, could cause a change in judgment about the realizability of the related deferred tax asset. Any change in the valuation allowance will be included in income in the year of the change in estimates.

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Recent Issued Accounting Guidance

Recently Adopted Accounting Pronouncement:

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842), which is intended to increase transparency and comparability among organizations by requiring the recognition of right-of-use (“ROU”) assets and lease liabilities on the balance sheet. In July 2018, the FASB issued additional guidance which provided an additional transition method for adopting the updated guidance. Under the additional transition method, entities may elect to recognize a cumulative-effect adjustment to the opening balance of retained earnings in the year of adoption. The Company adopted this standard on January 1, 2019 using this modified retrospective approach. The adoption of the standard resulted in the recognition of a ROU asset and lease liability of approximately \$12,900 for one operating lease as of January 1, 2019, with no impact to retained earnings.

Effective the first quarter of 2020:

In August 2018, the FASB issued ASU No. 2018-13, Fair Value Measurement (“Topic 820”): Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement. The ASU modifies the disclosure requirements in Topic 820, Fair Value Measurement, to improve the effectiveness of fair value measurement disclosures by removing or modifying certain disclosure requirements and adding other requirements. This ASU is effective for public companies for annual reporting periods and interim periods within those annual periods beginning after December 15, 2019. The Company is currently evaluating the effect, if any, that ASU 2018-13 will have on its financial statements.

Other pronouncements:

The Company has reviewed other recently issued, but not yet effective, accounting pronouncements and does not believe the future adoptions of any such pronouncements will be expected to cause a material impact on its financial condition or the results of operations.

2. REVENUE AND PRODUCT COSTS

The Company enters into contracts that include various combinations of products, accessories and services, such as training, each of which are generally distinct and are accounted for as separate performance obligations.

A performance obligation is a promise in a contract to transfer a distinct good or service to a customer, and is the unit of account in Topic 606. For contracts with a single performance obligation, the entire transaction price is allocated to the single performance obligation. For contracts with multiple performance obligations, the Company allocates the contract transaction price to each performance obligation using the Company’s estimate of the standalone selling price (“SSP”) of each distinct good or service in a contract. The Company determines standalone selling prices based on the price at which the performance obligation is sold separately. If the standalone selling price is not observable through past transactions, the Company estimates the standalone selling price considering available information such as market conditions and internally approved pricing guidelines related to the performance obligations.

Performance obligations to deliver products and accessories are generally satisfied at the point in time the Company ships the product, as this is when the customer obtains control of the asset under our standard terms and conditions. The Company has elected to recognize shipping costs as an expense in cost of revenues when control has transferred to the customer. The revenues and costs of training are recognized when the training is completed, generally following delivery of related products.

The timing of revenue recognition may differ from the timing of invoicing to customers. The Company generally has an unconditional right to consideration when customers are invoiced and a receivable is recorded. A contract asset is recognized when revenue is recognized prior to invoicing, or a contract liability (deferred revenue) when revenue will be recognized subsequent to invoicing. At December 31, 2018 the Company had no contract assets and no deferred revenue related to products or training for product delivered during the year. At June 30, 2019 the Company had deferred revenue of \$3,357 related to future training.

2. REVENUE AND PRODUCT COSTS (continued)

The Company recognizes an asset if there are incremental costs of obtaining a contract with a customer such as commissions. These costs are ascribed to or allocated to the underlying performance obligations in the contract and amortized consistent with the recognition timing of the revenue for any such underlying performance obligations. The Company had no such assets at June 30, 2019 and December 31, 2018. The Company will apply the practical expedient to expense any sales commissions related to performance obligations with an amortization of one year or less when incurred within selling, general and administrative expenses.

Estimated costs for the Company's standard one-year warranty are charged to cost of products sold when revenue is recorded for the related product. Royalties are also charged to cost of products sold.

3. INVENTORIES, NET

Inventory is recorded at the lower of cost or net realizable value. The cost of substantially all the Company's inventory is determined by the weighted average cost method. Inventories consisted of the following:

	June 30, 2019	December 31, 2018
Finished goods	\$ 106,460	\$ 82,313
Work in process	63,241	12,695
Raw materials	1,085,886	63,259
	<u>\$ 1,255,587</u>	<u>\$ 158,267</u>

During the three and six months ended June 30, 2019 the Company wrote off \$52,937 and \$65,012, respectively, of raw material parts primarily due to model improvements.

4. PROPERTY AND EQUIPMENT, NET

Property and equipment consisted of the following:

	June 30, 2019	December 31, 2018
Laboratory equipment	\$ 30,047	\$ 13,980
Tooling	56,234	22,683
Computer equipment	19,560	12,608
Furniture, fixtures and improvements	52,086	9,595
	<u>157,927</u>	<u>58,866</u>
Accumulated depreciation	(31,124)	(28,493)
	<u>\$ 126,803</u>	<u>\$ 30,373</u>

Depreciation expense was \$7,621 and \$12,186 for the three and six months ended June 30, 2019 and was \$2,585 and \$4,846 for the three and six months ended June 30, 2018, respectively.

5. INTANGIBLE ASSETS, NET

Intangible assets consisted of the following:

	June 30, 2019	December 31, 2018
Patents	\$ 150,174	\$ 111,160
Trademarks	38,397	8,910
	<u>188,571</u>	<u>120,070</u>
Accumulated amortization	(1,742)	(1,355)
	<u>\$ 186,829</u>	<u>\$ 118,715</u>

The costs related to issued patents will be amortized using the straight-line method over the estimated remaining lives of issued patents which is 20 years from the initial filing. An impairment charge is recognized if the carrying amount is not recoverable and the carrying amount exceeds the fair value of the intangible assets as determined by projected discounted net future cash flows.

Amortization expense was \$203 and \$387 for the three and six months ended June 30, 2019. There was no amortization for the three or six months ended June 30, 2018.

6. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable includes \$7,590 due to related party Syzygy Licensing, LLC (“Syzygy”). See Note 10.

Accrued liabilities consist of the following:

	June 30, 2019	December 31, 2018
Patent costs	\$ 7,800	\$ 11,600
Accrued compensation	116,841	55,493
Warranty costs	3,931	428
Other	2,800	932
	<u>\$ 131,372</u>	<u>\$ 68,453</u>

7. LEASES

The Company adopted ASU 2016-02, Leases (Topic 842) on January 1, 2019 using the modified retrospective approach. The Company has elected not to apply ASC Topic 842 to arrangements with lease terms of 12 months or less. The adoption of the standard resulted in the recognition of a ROU asset and lease liability of \$12,900 for one operating lease as of January 1, 2019, with no impact to retained earnings. Prior year amounts have not been restated. That lease is for 1,890 square feet of improved office, assembly and warehouse space in Las Vegas, Nevada. In January 2019 the Company recorded an additional \$17,101 ROU remeasurement asset and liability from an extension of the operating facility lease to December 31, 2020.

In March 2019 the Company recorded a \$57,587 ROU asset and liability for a two-year facility operating lease for 1,906 square feet of improved office, assembly and warehouse space in Lake Forest, California expiring in February 2021.

In June 2019 the Company recorded a \$253,412 ROU asset and liability for a 38-month facility operating lease for 11,256 square feet of improved office, assembly, training and warehouse space in Tempe, Arizona expiring in July 2022.

7. LEASES (continued)

Due to lack of borrowing history or ability the Company used as its incremental borrowing rate a low-grade debt rate published by the Federal Reserve Bank and determined a discount rate of 7.5% for the remeasurement in January 2019, 6.8% for the March 2019 operating lease and 7.0% for the June 2019 operating lease. Management determined these are reasonable borrowing rates.

Amortization of ROU operating lease assets was \$16,432 and \$22,211 for the three and six months ended June 30, 2019.

Operating lease expense for capitalized operating leases included in operating activities was \$19,305 and \$25,956 for the three and six months ended June 30, 2019. Operating lease obligations recorded on the balance sheet at June 30, 2019 are:

Operating lease liability- short term	\$ 104,327
Operating lease liability - long term	215,780
Total Operating Lease Liability	<u>\$ 320,107</u>

Future lease payments included in the measurement of lease liabilities on the balance sheet at June 30, 2019 for future periods are as follows:

Remainder of 2019 (six months)	\$ 53,705
2020	143,574
2021	101,406
2022	57,328
Total future minimum lease payments	<u>356,013</u>
Less imputed interest	(35,996)
Total	<u>\$ 320,017</u>

The weighted average remaining lease term is 2.7 years and the weighted average discount rate is 7.0%.

The Company does not have any finance leases.

8. DEFERRED AND ACCRUED COMPENSATION

From March 2016 through February 2017, the Company accrued monthly compensation for the services of two officers in the aggregate amount of \$7,000 per month payable to Syzygy. In March 2017 the Company accrued and deferred \$6,000 compensation to each of the two officers. The balance payable to Syzygy as of June 30, 2019 was \$84,000 and the accrued deferred compensation aggregated \$12,000. These balances accrue without interest. No payment terms or schedule has been established.

9. STOCKHOLDERS' EQUITY AND SHARE-BASED COMPENSATION

The Company's authorized capital consists of 150,000,000 shares of common stock, par value \$0.0001 per share, and 5,000,000 shares of preferred stock, par value \$0.0001 per share.

Public Offering

On June 18, 2019, the Company consummated the June 2019 Follow-On Offering, pursuant to which a total of 1,923,076 Units were offered and sold at the public offering price of \$6.50 per Unit. Each Unit sold consisted of one share of common stock and one detachable two-year warrant to purchase one share of common stock at an exercise price of \$6.50 per share. The offering resulted in the Company's receipt of gross cash proceeds of \$12.5 million, or net cash proceeds of \$11.35 million after deduction of commissions and offering costs.

9. STOCKHOLDERS' EQUITY AND SHARE-BASED COMPENSATION (continued)

In connection with the June 2019 Follow-On Offering, the Company also issued placement agent warrants exercisable for 153,846 shares of common stock for two years at an exercise price of \$8.125 per share. The estimated fair value of these warrants was \$205,894, as determined using the Black-Scholes methodology (assuming estimated volatility of 49%, risk-free interest rate of 1.86%, and expected dividend yield of 0.0%). This amount was recorded as both an increase to additional paid in capital and as a non-cash issuance cost of the offering.

Share-Based Compensation

On March 31, 2017, the Company adopted and the shareholders approved the 2017 Stock Incentive Plan (the "Plan") authorizing 2,000,000 shares of Company common stock for issuance as stock options and restricted stock units to employees, directors or consultants. In March 2019 the Company's directors approved and in May 2019 the shareholders ratified an increase in the Plan authorizing an additional 2,100,000 shares of common stock for a total of 4,100,000 shares.

The Company generally recognizes share-based compensation expense on the grant date and over the period of vesting or period that services will be provided.

The following table summarizes stock option activity under the Plan for the six months ended June 30, 2019:

	Options on Common Shares	Weighted Average		Aggregate Intrinsic Value
		Exercise Price	Remaining Contractual Term	
Outstanding January 1, 2019	2,067,500	\$ 1.68	4.44	\$ 3,063,375
Granted	1,000,000	5.41	5.00	-
Exercised	(16,250)	1.50	-	-
Forfeited, cancelled, expired	(75,000)	1.50	-	-
Outstanding June 30, 2019	2,976,250	\$ 2.94	4.21	\$ 9,757,700
Vested and exercisable at June 30, 2019	1,208,438	\$ 1.58	3.92	\$ 5,611,323

The Company uses the Black-Scholes option pricing model to determine the fair value of the options granted. The following table summarizes the assumptions used to compute the fair value of options granted to employees and nonemployees:

	Six Months Ended June 30, 2019
Expected stock price volatility	49%
Risk-free interest rate	2.41%
Forfeiture rate	0%
Expected dividend yield	0%
Expected life of options - years	3.50
Weighted-average fair value of options granted	\$ 2.06

Estimated volatility is a measure of the amount by which the Company's stock price is expected to fluctuate each year during the expected life of awards. The Company's estimated volatility was based on an average of the historical volatility of peer entities whose stock prices were publicly available. The Company's calculation of estimated volatility is based on historical stock prices of these peer entities over a period equal to the expected life of the awards. The Company uses the historical volatility of peer entities due to the lack of sufficient historical data of its stock price, as it only recently commenced trading.

9. STOCKHOLDERS' EQUITY AND SHARE-BASED COMPENSATION (continued)

The risk-free interest rate assumption is based upon observed interest rates on zero coupon U.S. Treasury bonds whose maturity period is appropriate for the term of the options. The dividend yield of zero is based on the fact that the Company has never paid cash dividends and has no present intention to pay cash dividends. The Company calculates the expected life of the options using the Simplified Method for the employee stock options as the Company does not have sufficient historical data.

On May 23, 2019 the Company granted a total of 263,087 of service-based RSU's to employees and consultants vesting over three years that convert to common stock as vesting occurs. A summary is set forth below:

	<u>Service-Based RSU's</u>	<u>Grant Date Fair Value</u>	<u>Vesting Period</u>
Unvested at January 1, 2019	-		
Granted at May 23, 2019	263,087	\$ 7.24	3 Years
Vested	-		
Forfeited and cancelled	-		
Unvested at June 30, 2019	<u>263,087</u>		

The Company recorded stock-based compensation in its statements of operations for the relevant periods as follows:

	<u>For the Three Months Ended June 30,</u>		<u>For the Six Months Ended June 30,</u>	
	<u>2019</u>	<u>2018</u>	<u>2019</u>	<u>2018</u>
Selling, general and administrative	\$ 345,217	\$ 125,878	\$ 548,417	\$ 125,878
Research and development	28,634	47,095	52,481	47,095
Total stock-based expense	<u>\$ 373,851</u>	<u>\$ 172,973</u>	<u>\$ 600,898</u>	<u>\$ 172,973</u>

As of June 30, 2019, total estimated compensation cost of stock options and RSUs granted but not yet vested was \$4.3 million which is expected to be recognized over the weighted average period of 2.5 years.

Warrants

The following table summarizes warrant activity during the six months ended June 30, 2019:

	<u>Number</u>	<u>Average Purchase Price Per Share</u>
Shares purchasable under outstanding warrants at January 1, 2019	5,017,181	\$ 4.82
Stock purchase warrants issued	2,076,922	\$ 6.62
Stock purchase warrants exercised	(336,317)	\$ 4.63
Shares purchasable under outstanding warrants at June 30, 2019	<u>6,757,786</u>	\$ 5.38

The Company determined that the warrants issued in connection with the June 2019 Follow-On Offering should be classified as equity in accordance with ASC 480. However, changes in director and officer ownership or other factors in future periods could require reclassification of outstanding warrants as a liability with changes in value thereafter reflected in the statement of operations.

9. STOCKHOLDERS' EQUITY AND SHARE-BASED COMPENSATION (continued)

The Company has outstanding common stock purchase warrants as of June 30, 2019 as follows:

Description	Number of Common Shares	Exercise Price Per Share	Expiration Date
Purchase Warrants (1)	4,286,907	\$ 5.00	October 30, 2020
Agent Warrants	393,957	\$ 3.00	October 30, 2020
Purchase Warrants	1,923,076	\$ 6.50	June 18, 2021
Agent Warrants	153,846	\$ 8.125	June 18, 2021

(1) 333,334 warrants are held by a family trust of officer Elwood G. Norris.

Subsequent to June 30, 2019 a total of 15,000 of the \$3.00 warrants were exercised for cash proceeds of \$45,000.

10. COMMITMENTS AND CONTINGENCIES

Facility Leases

See Note 7.

Related Party Technology License Agreement

The Company is obligated to pay royalties and pay development and patent costs pursuant to an exclusive Amended and Restated Intellectual Property License Agreement dated as of September 30, 2016 with Syzygy, a company owned and controlled by stockholders/officers Mr. Elwood Norris and Mr. James Barnes. The agreement provides for royalty payments of 4% of revenue from products employing the licensed ensnarement device technology up to an aggregate of \$1,000,000 in royalties or until September 30, 2026, whichever occurs earlier. The Company recorded \$2,231 and \$6,719 for royalties incurred during the three and six months ended June 30, 2019, respectively.

Purchase Commitments

At June 30, 2019 the Company was committed for approximately \$1.1 million for future component deliveries that are generally subject to modification or rescheduling in the normal course of business.

11. RELATED PARTY TRANSACTIONS

Commencing in October 2017 the Company began reimbursing Mr. Elwood Norris, an officer and stockholder of the Company, \$1,500 per month on a month to month basis for laboratory facility costs, for an aggregate of \$9,000 during the six months ended June 30, 2019 and 2018.

See Notes 1, 6, 8 and 10 for information on related party transactions and information.

12. SUBSEQUENT EVENTS

The Company evaluated subsequent events for their potential impact on the financial statements and disclosures through the date the financial statements were available to be issued, and determined that, except as disclosed herein, no subsequent events occurred that were reasonably expected to impact the financial statements presented herein. Specifically, see Note 9 for subsequent event information related to warrant exercises.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

You should read the following discussion in conjunction with the financial statements and other financial information included elsewhere in this Quarterly Report on Form 10-Q and with our audited financial statements and other information presented in our Annual Report on Form 10-K for the year ended December 31, 2018. The following discussion may contain forward-looking statements that reflect our plans, estimates and beliefs. Words such as "expect," "anticipate," "intend," "plan," "believe," "seek," "estimate," "continue," "may," "will," "could," "would," or the negative or plural of such words and similar expressions or variations of such words are intended to identify forward-looking statements, but are not the only means of identifying forward-looking statements. Such forward-looking statements are subject to a number of risks, uncertainties, assumptions and other factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by the forward-looking statements. Factors that could cause or contribute to these differences include, but are not limited to, those discussed below and elsewhere in this Quarterly Report on Form 10-Q and in our other SEC filings, including particularly matters set forth under Part I, Item 1A (Risk Factors) of our Annual Report on Form 10-K. Furthermore such forward-looking statements speak only as of the date of this report. Except as required by law, we undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements.

We are a security technology company organized in March 2016 focused on delivering modern policing solutions to customers, primarily consisting of law enforcement and security personnel.

Business Highlights, Outlook and Challenges

In June 2019 we completed a follow-on public offering under our effective shelf registration statement on Form S-3 (File No. 333-228974) (the "*June 2019 Follow-On Offering*"), which offering resulted in net cash proceeds to the Company of approximately \$11.35 million after deduction of commissions and offering costs, and, at June 30, 2019, we had cash and cash equivalents of \$21.38 million. We are rapidly growing business functions, including production, marketing, sales, distribution, service and administration. Until we generate additional revenue and net cash flow from operations, we still expect to have limited personnel to accomplish these functions and will primarily rely on our executives along with outside consultants, contractors and suppliers for production and certain other services. Given our limited personnel, substantial risk and uncertainty exists with respect to whether we can timely execute our business plan and achieve our operating objectives, including obtaining orders from customers and introducing new products in the future.

We currently have five U.S. patents issued and eight U.S. patents pending on our remote restraint device and technology. In September 2018 we commenced filing our first foreign patent applications, targeting the European Union (17 countries) and 17 other countries. We have additional patents being drafted as part of our strategy to protect our innovations in the U.S. and in targeted countries internationally.

We began demonstrations of our first product, the BolaWrap 100 remote restraint device, in November 2017 and in 2018 developed initial production capability. We have demonstrated our BolaWrap 100 product to over 150 agencies across the country, often with media in attendance, resulting in dozens of media reports including television and print that have driven hundreds of inquiries from domestic and international prospects. Over 70 law enforcement agencies took delivery of the BolaWrap 100 devices during 2018 and the first half of 2019. In addition to the sale of a limited number of small domestic and international orders, we have delivered over 330 devices at no cost to strategic agencies for evaluation and feedback. Our product is gaining important worldwide awareness and recognition through media exposure, trade show participations, product demonstrations and word of mouth as a result of positive responses to our product. We believe we are establishing a global brand and the product foundation for business growth. We believe we have strong market opportunities for our restraint product offering within the law enforcement, military and homeland security business sectors domestically and internationally.

In March 2019 we welcomed less-lethal industry pioneer and 25-year veteran Thomas Smith as our President. He is responsible for scaling our domestic and international sales. We have accelerated our focus on international distribution and began to engage with domestic distributors to address the over 1,100 product inquiries from domestic law enforcement agencies. While our strategy includes a combination of both direct and distributor sales we are adding distributors to sell products especially targeting smaller law enforcement agencies. At June 30, 2019 we had distribution agreements with nine domestic distributors representing 38 states and seven international distributors representing 12 countries.

To support our increased sales and distribution activities we have expanded our training and product support functions with the addition of less-lethal industry veterans and engagement of professional regional trainers. At June 30, 2019, in addition to our internal training executives, we had eight contract regional Master Instructors. As of June 30, 2019 over 65 agencies had received BolaWrap 100 training with approximately 390 training officers at those agencies certified as BolaWrap 100 instructors qualified to train the rest of their departments.

In late May 2019 we began shipping an updated version of our BolaWrap 100 remote restraint device featuring a green line laser to strategic police departments and international distributors. In June 2019 we also leased and occupied a 11,000 square foot facility in Tempe, Arizona that we expect to provide additional assembly, warehouse and training space for future growth.

In July 2019 we announced our first large international distributor order valued at over \$1 million and secured three additional international orders and our first five domestic distributor orders. We believe we can accelerate orders in 2019 but orders and sales may be sporadic as we grow our distributor and customer base. However, there can be no assurance of the timing or quantity of orders or sales in future periods.

The focus of our sales strategy is the immediate addressable domestic market of approximately 701,000 full-time sworn law enforcement officers in 15,300 federal, state and local law enforcement agencies while also beginning to explore other markets, including military, border patrol. We are also aggressively addressing international markets. According to Statistics MRC, we participate in a segment of the non-lethal products market expected to grow to \$11.85 billion by 2023.

Since inception in March 2016, we have generated significant losses from operations and anticipate that we will continue to generate significant losses from operations for the foreseeable future. Although we believe that we have adequate financial resources to sustain our operations for the next year, no assurances can be given, and we may need additional capital for future operations and to market and further develop our products and introduce new products.

We face significant challenges in operating and growing our business. We expect that we will need to continue to innovate new applications for our security technology, develop new products and technologies to meet diverse customer requirements and identify and develop new markets for our products.

Critical Accounting Policies and Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States (*U.S. GAAP*) requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expense, and related disclosure of contingent assets and liabilities. We evaluate our estimates, on an on-going basis, including those estimates related to recognition and measurement of contingencies and accrued costs. We base our estimates on historical experience and on various other assumptions we believe to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions.

As part of the process of preparing our financial statements, we are required to estimate our provision for income taxes. Significant management judgment will be required in determining our provision for income taxes, deferred tax assets and liabilities, tax contingencies, unrecognized tax benefits, and any required valuation allowance, including taking into consideration the probability of the tax contingencies being incurred. Management assesses this probability based upon information provided by its tax advisers, its legal advisers and similar tax cases. If at a later time our assessment of the probability of these tax contingencies changes, our accrual for such tax uncertainties may increase or decrease. Our effective tax rate for annual and interim reporting periods could be impacted if uncertain tax positions that are not recognized are settled at an amount which differs from our estimates.

Some of our accounting policies require higher degrees of judgment than others in their application. These include share-based compensation and contingencies and areas such as revenue recognition, operating lease liabilities, warranty liabilities, impairments and valuation of intangible assets.

We sell our products to customers including law enforcement agencies, domestic distributors and international distributors and revenue from such transactions is recognized in the periods that products are shipped (free on board ("*FOB*") shipping point) or received by customers (FOB destination), when the fee is fixed or determinable and when collection of resulting receivables is reasonably assured. We identify customer performance obligations, determine the transaction price, allocate the transaction price to the performance obligations and recognize revenue as we satisfy the performance obligations. Our primary performance obligations are products/accessories and training. Our customers do not have the right to return product unless the product is found to be defective.

Historically, our assumptions, judgments and estimates relative to our critical accounting policies have not differed materially from actual results. There were no significant changes or modification of our critical accounting policies and estimates involving management valuation adjustments affecting our results for the six months ended June 30, 2019.

Operating Expense

Our operating expense includes (i) selling, general and administrative expense, and (ii) research and development expense. Research and development expense is comprised of the costs incurred in performing research and development activities and developing production on our behalf, including compensation and consulting, design and prototype costs, contract services, patent costs and other outside expenses. The scope and magnitude of our future research and development expense is difficult to predict at this time and will depend on elections made regarding research projects, staffing levels and outside consulting and contract costs. However, in the near term, we expect our research and development expenses to increase in absolute dollars as we increase our research and development headcount and increase new product development activities.

The actual level of future selling, general and administrative expense will be dependent on staffing levels, elections regarding expenditures on sales, marketing and customer training, the use of outside resources, public company and regulatory costs, and other factors, some of which are outside of our control. We expect our operating costs will increase as we expand product distribution activities and expand our research and development, production, distribution, training, service and administrative functions in the near term. We may also incur substantial noncash share-based compensation costs depending on future option and restricted stock unit grants that are impacted by stock prices and other valuation factors. Historical expenditures are not indicative of future expenditures.

Results of Operations**Three Months Ended June 30, 2019 Compared to Three Months Ended June 30, 2018**

The following table sets forth for the periods indicated certain items of our condensed statement of operations. The financial information and the discussion below should be read in conjunction with the condensed financial statements and notes contained in this report.

	Three Months Ended June 30,		Change	
	2019	2018	\$	%
Revenues:				
Product sales	\$ 48,948	\$ -	\$ 48,948	
Other revenue	10,496	-	10,496	
Total revenues	59,444	-	59,444	
Cost of revenues	35,695	-	35,695	
Gross profit	23,749	-	23,749	
Operating expenses:				
Selling, general and administrative	1,481,187	581,575	899,612	155%
Research and development	516,213	193,629	322,584	167%
Total operating expenses	1,997,400	775,204	1,222,196	158%
Loss from operations	\$ (1,973,651)	\$ (775,204)	\$ (1,198,447)	155%

Revenues

We had no revenues for the three months ended June 30, 2018 as we commenced product sales in late 2018. Our recent marketing and selling efforts have focused on creating demand for our improved generation of BolaWrap 100® product with our green line laser. Initial deliveries of the improved product began in late May 2019. We incurred product promotional costs of \$67,565 during the three months ended June 30, 2019 related to the cost of demonstration products and accessories delivered to law enforcement agencies that were expensed as marketing costs. A total of \$53,470 of such product marketing costs were incurred during the three months ended June 30, 2018.

We had \$3,357 of deferred revenue at June 30, 2019 related to products sold for which the training revenue component had not been completed.

We believe we can accelerate sales in the second half of 2019 but sales may be sporadic as we grow our distributor and customer base

Gross Profit

Our cost of revenues for the three months ended June 30, 2019 were \$35,695 resulting in a gross margin of 40%. Due to our history of minimal revenues and the changes being made to our product as we establish volume manufacturing such margin may not be indicative of future margins. In addition, our margins vary based on the sales channels through which our products are sold. We continue to implement product updates and changes, including raw material and component changes that may impact product costs. With such product updates and changes we have limited warranty cost experience and estimated future warranty costs can impact our gross margins. We do not believe that historical gross profit margins should be relied upon as an indicator of future gross profit margins.

Selling, General and Administrative Expense

Selling, general and administrative expense for the three months ended June 30, 2019 increased by \$899,612 when compared to the three months ended June 30, 2018. We incurred a \$219,339 increase in non-cash share-based compensation expense allocated to selling, general and administrative expenses from \$345,217 in the three months ended June 30, 2019 compared to \$125,878 in the three months ended June 30, 2018. Other increases included a \$312,388 increase in cash compensation costs from an increase in headcount since June 30, 2018 and a \$62,316 increase in travel costs. Marketing and promotion costs increased \$165,328 due primarily to promotional products. Occupancy costs increased \$50,552 due to the addition of office, training, assembly and warehouse space in Tempe, Arizona, and public company costs increased \$50,429 due to Nasdaq fees and related public company costs incurred in 2019.

In the near term we expect to expend additional resources on the marketing and selling of our products, training distributors and customers and administratively supporting our operations.

Research and Development Expense

Research and development expenses increased \$322,584 during the three months ended June 30, 2019, when compared to the comparable period in 2018. We incurred a \$18,101 period over period decrease in non-cash share-based compensation expense allocated to research and development expenses as a result of timing of vesting of certain awards. The increase in costs during the 2019 period, when compared to the comparable period in 2018, included a \$147,355 increase in cash compensation costs resulting from an increase in headcount primarily associated with production development. Prototype related costs increased \$113,481 in the 2019 period, primarily related to developing the updated version of the BolaWrap 100 product. Consulting costs increased \$54,952 in the 2019 period related to developing systems for monitoring research and production. We expect our research and development costs will vary depending on specific research projects and levels of internal and external staffing and prototype costs.

Net Loss

Loss from operations during the three months ended June 30, 2019 increased by \$1,198,447 when compared to the three months ended June 30, 2018, resulting, primarily, from increased operating costs due to increased personnel and marketing and selling and supporting activities.

Six Months Ended June 30, 2019 Compared to Six Months Ended June 30, 2018

The following table sets forth for the periods indicated certain items of our condensed statement of operations. The financial information and the discussion below should be read in conjunction with the condensed financial statements and notes contained in this report.

	Six Months Ended June 30,		Change	
	2019	2018	\$	%
Revenues:				
Product sales	\$ 162,901	\$ -	\$ 162,901	
Other revenue	14,354	-	14,354	
Total revenues	177,255	-	177,255	
Cost of revenues	96,915	-	96,915	
Gross profit	80,340	-	80,340	
Operating expenses:				
Selling, general and administrative	2,669,063	920,742	1,748,321	190%
Research and development	891,032	289,614	601,418	208%
Total operating expenses	3,560,095	1,210,356	2,349,739	194%
Loss from operations	\$ (3,479,755)	\$ (1,210,356)	\$ (2,269,399)	187%

Revenues

We had no revenues for the six months ended June 30, 2018 as we commenced product sales in late 2018. Our recent marketing and selling efforts have focused on creating demand for our improved generation BolaWrap 100 product with our green line laser. Initial deliveries of the improved product began in late May 2019. We incurred product promotional costs of \$135,060 for the six months ended June 30, 2019 related to the cost of demonstration products and accessories delivered to law enforcement agencies that were expensed as marketing costs. A total of \$59,271 such product marketing costs were incurred during the six months ended June 30, 2018.

We had \$3,357 of deferred revenue at June 30, 2019 related to products sold for which the training revenue component had not been completed.

We believe we can accelerate sales in the second half of 2019 but sales may be sporadic as we grow our distributor and customer base

Gross Profit

Our cost of revenues for the six months ended June 30, 2019 were \$96,915 resulting in a gross margin of 45%. Due to the minimal revenues and the changes being made to our product as we establish volume manufacturing such margin may not be indicative of future margins. In addition, our margins vary based on the sales channels through which our products are sold. We continue to implement product updates and changes, including raw material and component changes that may impact product costs. With such product updates and changes we have limited warranty cost experience and estimated future warranty costs can impact our gross margins. We do not believe that historical gross profit margins should be relied upon as an indicator of future gross profit margins.

Selling, General and Administrative Expense

Selling, general and administrative expense increased by \$1,748,321 during the six months ended June 30, 2019, when compared to the six months ended June 30, 2018. During the six months ended June 30, 2019, we incurred a \$422,539 increase in non-cash share-based compensation expense allocated to selling, general and administrative expenses from \$548,417 in the six months ended June 30, 2019 compared to \$125,878 in the six months ended June 30, 2018. Other increases in the 2019 period included a \$542,829 increase in cash compensation costs from an increase in headcount since June 30, 2018 and a \$143,263 increase in travel costs. Marketing and promotion costs increased \$267,359 in the 2019 period when compared to the 2018 period, due, primarily to promotional products. Occupancy costs increased \$85,577 due to the addition of facilities in Lake Forest, California and Tempe, Arizona, and public company costs increased \$127,198 due to Nasdaq fees, insurance and related public costs incurred in 2019.

In the near term we expect to expend additional resources on the marketing and selling of our products, training distributors and customers and administratively supporting our operations.

Research and Development Expense

Research and development expenses increased \$601,418 during the six months ended June 30, 2019, when compared to the six months ended June 30, 2018. In addition, we incurred a \$5,386 period over period increase in non-cash share-based compensation expense allocated to research and development expenses. The increase in costs for the 2019 period, when compared to the 2018 period included a \$247,153 increase in cash compensation costs from an increase in headcount primarily associated with production development. Prototype related costs increased \$138,133 in the 2019 period, primarily related to developing the updated version of the BolaWrap 100 product. Consulting costs during the 2019 period increased \$162,469 related to developing systems for monitoring research and production. We expect our research and development costs will vary depending on specific research projects and levels of internal and external staffing and prototype costs.

Net Loss

Loss from operations during the six months ended June 30, 2019 increased by \$2,269,399 when compared to the six months ended June 30, 2018, resulting, primarily from increased operating costs due to increased personnel and marketing and selling and supporting activities.

Liquidity and Capital Resources

Overview

We have experienced net losses and negative cash flows from operations since our inception. As of June 30, 2019, we had cash of \$21,377,807 and positive working capital of \$22,099,249, and had sustained cumulative losses attributable to common stockholders of \$7,799,191. We believe that our cash on hand will sustain our operations for at least the next twelve months from the date of this Quarterly Report on Form 10-Q (the "*Report*").

Our sole source of liquidity to date has been funding from our stockholders and the sale and exercise of equity securities. We expect our primary source of future liquidity will be from the sale of products, exercise of stock options and warrants and if required from future equity or debt financings. Subsequent to June 30, 2019 we received \$45,000 from the exercise of common stock purchase warrants.

Capital Requirements

In December 2017, we completed our self-underwritten IPO, raising gross proceeds of approximately \$3.49 million from the sale of 2,328,533 shares of common stock at the public offering price of \$1.50 per share.

In October 2018 we received approximately \$12.14 million in net cash proceeds from the private sale of equity securities to certain accredited investors.

In May 2019 we obtained net cash proceeds of approximately \$11.35 million from the June 2019 Follow-On Offering. During the three months ended June 30, 2019 we also obtained \$1.58 million from the exercise of previously issued warrants and stock options.

We cannot currently estimate our future liquidity requirements or future capital needs, which will depend on, among other things, capital required to introduce our products and the staffing and support requirements, as well as the timing and amount of future revenue and product costs. We anticipate that demands for operating and working capital will grow as we are increasing staffing, development, production, marketing, training and other functions and based on other factors outside of our control. We believe we have sufficient capital to sustain our operations for the next twelve months, although no assurances can be given. Additionally, no assurances can be provided that any future debt or equity capital will be available to us under favorable terms, if at all. Failure to quickly produce and sell products and timely obtain any required additional capital in the future will have a material adverse effect on the Company.

Our future capital requirements, cash flows and results of operations could be affected by, and will depend on, many factors, some of which are currently unknown to us, including, among other things:

- decisions regarding staffing, development, production, marketing and other functions;
- the timing and extent of any market acceptance of our products;
- the costs, timing and outcome of planned production and required customer and regulatory compliance of our new products;
- the costs of preparing, filing and prosecuting our patent applications and defending any future intellectual property-related claims;
- the costs and timing of additional product development;
- the costs, timing and outcome of any future warranty claims or litigation against us associated with any of our products and
- the timing and costs associated with any new financing.

Off-Balance Sheet Arrangements

We have no off-balance sheet arrangements.

Cash Flow

Operating Activities.

During the six months ended June 30, 2019, net cash used in operating activities was \$3,725,677. The net loss of \$3,394,855 was decreased by non-cash expenses of \$574,173 consisting primarily of share-based compensation expense of \$600,898. Other major component changes using operating cash included a \$1,032,308 increase in inventories, an increase of \$71,182 in prepaid expense and other current assets and an increase of \$26,863 in accounts receivable. An increase of \$242,894 in accounts payable and accrued liabilities reduced the cash used in operating activities.

During the six months ended June 30, 2018, net cash used in operating activities was \$1,060,758 consisting primarily of the net loss of \$1,210,920.

Investing Activities.

We used \$108,616 and \$8,015 of cash for the purchase of property and equipment during the six months ended June 30, 2019 and 2018, respectively. We began capitalizing patent costs during mid-2018 and invested \$68,501 in patents during the six months ended June 30, 2019.

Financing Activities.

We received \$11,351,214 of net proceeds from the June 2019 Follow-On Offering, and, during the six months ended June 30, 2019 obtained \$1,581,660 from the exercise of previously issued warrants and stock options. There were no financing activities for the six months ended June 30, 2018.

Contractual Obligations and Commitments

We are obligated to pay to Syzygy Licensing, LLC (“Syzygy”) a 4% royalty fee on future product sales up to an aggregate amount of \$1.0 million in royalties or until September 30, 2026, whichever occurs earlier.

In January 2019 we extended our Las Vegas, Nevada corporate and production facility lease through December 31, 2020. In February 2019 we entered into a two-year lease for an office and warehouse space in Lake Forest, California. In June 2019 we entered into a 38-month lease for office, training, assembly and warehouse space in Tempe, Arizona. We are committed to aggregate lease payments on these leases of \$53,705 for the balance of 2019, \$143,574 in 2020, \$101,406 in 2021 and \$57,328 in 2022.

At June 30, 2019 we were committed to approximately \$1.1 million of purchase commitments for product components. These purchase commitments are generally subject to modification as to timing, quantities and scheduling and in certain instances may be cancelable without penalty.

Effects of Inflation

We do not believe that inflation has had a material impact on our business, revenue or operating results during the periods presented.

Recent Accounting Pronouncements

Other than our adoption of ASU 2016-02, Leases (Topic 842), there have been no recent accounting pronouncements or changes in accounting pronouncements during the period ended June 30, 2019, or subsequently thereto, that we believe are of potential significance to our financial statements.

Item 3. Quantitative and Qualitative Disclosures about Market Risk.

Not applicable.

Item 4. Controls and Procedures.

We are required to maintain disclosure controls and procedures designed to ensure that material information related to us, including our consolidated subsidiaries, is recorded, processed, summarized and reported within the time periods specified in the SEC rules and forms.

Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our principal executive officer and our principal financial officer, as of June 30, 2019 we conducted an evaluation of our disclosure controls and procedures as such term is defined under Rules 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended. Based on this evaluation, our principal executive officer and our principal financial officer concluded that our disclosure controls and procedures were effective at the reasonable assurance level.

Changes in Internal Control over Financial Reporting

There have been no changes in our internal control over financial reporting during our fiscal quarter ended June 30, 2019, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. Our process for evaluating controls and procedures is continuous and encompasses constant improvement of the design and effectiveness of established controls and procedures and the remediation of any deficiencies, which may be identified during this process.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

We may at times become involved in litigation in the ordinary course of business. We will also, from time to time, when appropriate in management's estimation, record adequate reserves in our financial statements for pending litigation. Currently, there are no pending material legal proceedings to which the Company is a party or to which any of its property is subject.

Item 1A. Risk Factors

As a Smaller Reporting Company as defined by Rule 12b-2 of the Exchange Act and in item 10(f)(1) of Regulation S-K, we are electing scaled disclosure reporting obligations and therefore are not required to provide the information requested by this item.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

No unregistered securities were issued during the three months ended June 30, 2019 that were not previously reported.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not Applicable.

Item 5. Other Information

None.

Item 6. Exhibits

Exhibit 4.1	Form of Investor Warrant, dated June 18, 2019 (incorporated by reference from Exhibit 4.1 to the Current Report on Form 8-K, filed on June 18, 2019).
Exhibit 4.2	Form of Offering Agent Warrant, dated June 18, 2019 (incorporated by reference from Exhibit 4.2 to the Current Report on Form 8-K, filed on June 18, 2019).
Exhibit 10.1	Industrial Real Estate Lease, dated May 10, 2019, by and between Wrap Technologies, Inc. and JM Sky Harbor Properties LLC (incorporated by reference from Exhibit 10.1 to the Current Report on Form 8-K, filed on June 6, 2019).
Exhibit 10.2	Supplemental Engagement Letter by and between Wrap Technologies, Inc. and Katalyst Securities LLC, dated June 7, 2019 (incorporated by reference from Exhibit 10.1 to the Current Report on Form 8-K, filed on June 13, 2019).
Exhibit 10.3	Form of Subscription Agreement, dated June 14, 2019 (incorporated by reference from Exhibit 10.1 to the Current Report on Form 8-K, filed on June 18, 2019).
Exhibit 10.4	Engagement Letter by and between Wrap Technologies, Inc., Dinosaur Financial Group, LLC and Katalyst Securities LLC, dated June 12, 2019 (incorporated by reference from Exhibit 10.2 to the Current Report on Form 8-K, filed on June 18, 2019).
Exhibit 31.1	Certification of David Norris, Principal Executive Officer, pursuant to Rule 13a-14(a) or 15d-14(a) of the Securities and Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*
Exhibit 31.2	Certification of James A. Barnes, Principal Financial Officer, pursuant to Rule 13a-14(a) or 15d-14(a) of the Securities and Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*
Exhibit 32.1	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, executed by David Norris, Principal Executive Officer, and James A. Barnes, Principal Financial Officer.*

Extensible Business Reporting Language (XBRL) Exhibits*

101.INS	XBRL Instance Document*
101.SCH	XBRL Taxonomy Extension Schema Document*
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document*
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document*
101.LAB	XBRL Taxonomy Extension Labels Linkbase Document*
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document*

* Filed concurrently herewith

SIGNATURES

Pursuant to the requirements 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.

WRAP TECHNOLOGIES, INC.

By: /s/ JAMES A BARNES
James A Barnes
Chief Financial Officer, Secretary and Treasurer
(Principal Accounting Officer)

Date: August 5, 2019

CERTIFICATION

I, David Norris, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Wrap 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 officers 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):
 - b) 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
 - c) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 5, 2019

/s/ DAVID NORRIS

David Norris

Chief Executive Officer

(Principal Executive Officer)

CERTIFICATION

I, James A. Barnes, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Wrap 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 officers 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: August 5, 2019

/s/ JAMES A BARNES

James A Barnes
Chief Financial Officer, Secretary and Treasurer
(Principal Accounting Officer)

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER AND PRINCIPAL FINANCIAL OFFICER
PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

Each of the undersigned hereby certifies, in accordance with 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, in his or her capacity as an officer of Wrap Technologies, Inc. (the “*Company*”), that, to his or her knowledge, the Quarterly Report of the Company on Form 10-Q for the period ended June 30, 2019, fully complies with the requirements of Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934, as amended, and that the information contained in such report fairly presents, in all material respects, the financial condition and results of operation of the Company.

Date: August 5, 2019

/s/ DAVID NORRIS

David Norris
Chief Executive Officer
(Principal Executive Officer)

Date: August 5, 2019

/s/ JAMES A BARNES

James A Barnes
Chief Financial Officer, Secretary and Treasurer
(Principal Accounting Officer)

The foregoing certification is being furnished solely to accompany the Report pursuant to 18 U.S.C. Section 1350, and is not being filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and is not to be incorporated by reference into any filing of the Company, whether made before or after the date hereof, regardless of any general incorporation language in such filing. 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.
