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Iveda Solutions, Inc.  
Form 10-K  
April 01, 2013

United States Securities and Exchange Commission

Washington , D.C. 20549

FORM 10-K

Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the fiscal year ended December 31, 2012

or

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

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

Commission File No. 000-53285

Iveda Solutions, Inc.

(Exact name of registrant as specified in its charter)

Nevada

20-2222203

(State of incorporation)

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

1201 S. Alma School, Suite 8500

85210

Mesa, Arizona

(Zip code)

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(Address of principal executive offices)

Registrant's telephone number, including area code: (480) 307-8700

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

Securities registered pursuant to Section 12(g) of the Exchange Act – Common Stock - \$0.00001 par value

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

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

Large accelerated filer  Accelerated filer  Non-accelerated filer

Smaller reporting company  x

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

The aggregate market value of voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold was approximately \$15,044,892 as of the last business day of the registrant's most recently completed fiscal quarter.

As of March 15, 2013, 22,611,048 shares of the registrant's common stock were outstanding.

**IVEDA SOLUTIONS, INC.**

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### **Caution Regarding Forward-Looking Information**

*In addition to historical information, this Form 10-K contains certain “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995 (PSLRA). This statement is included for the express purpose of availing Iveda Solutions, Inc. of the protections of the safe harbor provisions of the PSLRA.*

*All statements contained in this Form 10-K, other than statements of historical facts, that address future activities, events or developments are forward-looking statements, including, but not limited to, statements containing the words “believe,” “expect,” “anticipate,” “intends,” “estimate,” “forecast,” “project,” and similar expressions. All statements other than statements of historical fact are statements that could be deemed forward-looking statements, including any statements of the plans, strategies and objectives of management for future operations; any statements concerning proposed new products, services, developments or industry rankings; any statements regarding future revenue, economic conditions or performance; any statements of belief; and any statements of assumptions underlying any of the foregoing. These statements are based on certain assumptions and analyses made by us in light of our experience and our assessment of historical trends, current conditions and expected future developments as well as other factors we believe are appropriate under the circumstances. However, whether actual results will conform to the expectations and predictions of management is subject to a number of risks and uncertainties described under Item 1A – Risk Factors beginning on page 19 below that may cause actual results to differ materially.*

*Consequently, all of the forward-looking statements made in this Form 10-K are qualified by these cautionary statements and there can be no assurance that the actual results anticipated by management will be realized or, even if substantially realized, that they will have the expected consequences to or effects on our business operations. Readers are cautioned not to place undue reliance on such forward-looking statements as they speak only of the Company’s views as of the date the statement was made. The Company undertakes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.*

## **PART I**

All references in this Form 10-K to the terms “Iveda Solutions, Inc.,” “Iveda,” “Company,” “we,” “us,” and “our” refer to Iveda Solutions, Inc. and our predecessors, unless the context otherwise requires.

### **ITEM 1 – BUSINESS**

#### **General**

Iveda Solutions, Inc. began operations on January 24, 2005, under the name IntelaSight, Inc., a Washington corporation doing business as Iveda Solutions (“IntelaSight”). On October 15, 2009, IntelaSight completed a reverse merger with Charmed Homes, Inc., a Nevada corporation (“Charmed”), pursuant to which IntelaSight became a wholly-owned subsidiary of Charmed and Charmed changed its name to Iveda Corporation.

All Company operations were conducted through IntelaSight until December 31, 2010, at which time IntelaSight merged with and into Iveda Corporation and Iveda Corporation changed its name to Iveda Solutions, Inc.

The Company’s principal executive offices are located at 1201 S. Alma School Rd., Suite 8500, Mesa, Arizona 85210.

On April 30, 2011, the Company completed its acquisition of Sole-Vision Technologies, Inc. (doing business as MegaSys) (“MegaSys”). MegaSys was incorporated in the Republic of China (Taiwan) on July 5, 1999. MegaSys is in the business of design and manufacturing of central security management system products and providing security integration solutions. MegaSys specializes in deploying new and integrating existing video surveillance systems for airports, commercial buildings, government customers, shopping centers, hotels, banks, and Safe City initiatives in Taiwan and other neighboring countries.

MegaSys’ headquarters are located at 2F,-15, No. 14, Lane 609, Sec. 5, Chongxin Rd. ,Sanchong City, Taipei County 241, Taiwan (R.O.C.)

## **Business Operations**

### **Overview**

Iveda Solutions, Inc. is an established and innovative company, delivering secure, open source and enterprise class managed video services by leveraging the power of cloud computing. The Company’s robust enterprise class video hosting architecture, utilizing data centers, allows scalability, flexibility, and centralized video management, access, and storage, without the burden of buying and maintaining software and equipment. Iveda Solutions’ customers simply log in online, access their cameras and begin watching live and/or recorded video data from anywhere in the world at any time using any Internet enabled device. From one camera locally to hundreds around the world, each camera can be accessed from one secure login. Iveda Solutions delivers the true essence of video surveillance through cloud computing, like no other.



The Company's open-source technology is interoperable with any existing camera system and enables multiple, simultaneous access without degradation of video quality. Utilizing video hosting technology, Iveda Solutions revolutionizes the functionality of security cameras, through a proactive real-time surveillance service rather than event or trigger-based system.

There are millions of security cameras in the U.S. today; a great majority of which run unmonitored. Oftentimes, they cannot be used to stop a crime in progress, and are merely observers keeping silent record of any illegal activity. Iveda Solutions takes security beyond boundaries by ensuring that each camera in its care remains under expertly-trained eyes. By placing a person behind the lens, a security camera goes from mute witness to active patroller, fully capable of police dispatch and assistance as events unfold. Officers can often be directed to the scene before a criminal has left the premises, leading to a higher arrest rate and greatly increasing the likelihood of recovering any stolen goods.

To management's knowledge, at this time, Iveda Solutions is the only major provider of enterprise class real-time video surveillance in the U.S.

MegaSys, our Taiwanese subsidiary, specializes in deploying video surveillance systems for airports, commercial buildings, government customers, data centers, shopping centers, hotels, banks, and Safe City initiatives in Taiwan and other neighboring countries. MegaSys integrates security surveillance products, software and services to provide integrated security solutions to the end user. Most of MegaSys's revenues are derived from one-time sales, which differs from Iveda's business model of on-going video hosting, remote video storage, and real-time surveillance revenues. MegaSys does not own any proprietary technology or intellectual property other than certain trademarks in China and Taiwan used in its business.

Historically, Iveda has derived revenues from security systems integration, equipment sales and installation, conversion of analog cameras to digital, and per hour, per camera service fees from video hosting and real-time surveillance. Additional revenues are derived from extended video storage and extended maintenance contracts. Iveda has grown only through direct sales of equipment/installation and video surveillance services through its direct sales team. In June 2012, Iveda began transition from direct to indirect sales channel by signing up independent representative agents and their network of security integrators. Iveda is building its reseller distribution channels to sell predominantly through resellers. As the reseller channel matures, Iveda's channel partners are expected to take over its equipment sales and installation functions, and help drive Iveda's recurring service revenue.

After months of rigorous application and due diligence process, in April 2009, Iveda Solutions was approved as a Qualified Anti-Terrorism Technology provider under a formal SAFETY Act Designation by the Department of Homeland Security (DHS). The designation gives the Company, its partners and customers certain liability protection. Iveda Solutions is the first and currently the only company, offering real-time IP video hosting and remote surveillance services with a SAFETY Act Designation.



In October 2009, the Company completed a reverse merger with a publicly traded company. The Company's stock is now trading on the Over-The-Counter Bulletin Board (OTCBB) under the trading symbol "IVDA."

In September 2010, Iveda Solutions acquired its first international customer. The Company is now providing IvedaOnBoard, its in-vehicle live streaming video service, and remote video storage to a government agency in Mexico.

In April, 2011, Iveda Solutions completed the acquisition of MEGAsys Taiwan. MEGAsys designs and manufactures electronic security and surveillance products, software, and services. MEGAsys was founded in 1998 by a group of sales and research and development professionals from Taiwan Panasonic Company. Iveda Solutions leverages MEGAsys' relationships with manufacturing and software companies in Asia, potentially reducing costs and improving services and capabilities. The acquisition also opens doors to the Asian market.

In October 2011, Iveda Solutions signed a strategic collaboration agreement with Telmex, U.S.A., a subsidiary of the Mexico-based Telmex, the 4th largest telecommunications company in the world. Telmex has presence in the U.S., Latin America, Europe, and Africa. Telmex will collaborate with Iveda Solutions to build cloud-based video surveillance infrastructure in the markets they are in and resell Iveda Solutions' services.

In November 2012, Iveda signed a cooperation agreement with Industrial Technology Research Institute (ITRI). ITRI is a research and development organization based in Taiwan. Iveda and ITRI have been co-developing cloud-video services. ITRI has given Iveda license to some of their patents being used in the development. Iveda will have exclusive rights to the products and services being co-developed.

### **Cloud Video Surveillance Services**

Iveda has multiple recurring revenue streams based on its cloud-video management platform, including video hosting, in-vehicle mobile video streaming, real-time remote surveillance services, and live streaming video mapping service, using a combination of Internet-enabled cameras, a secure IP network infrastructure utilizing robust data centers, and intervention specialists. Iveda's services are all web-based and accessible through any Internet-accessible device (e.g., computer, smartphone, tablets).

## **IvedaEnterprise**

IvedaEnterprise is the Company's managed video hosting platform and is the basis for the Company's cloud-video surveillance products and service offerings. IvedaEnterprise utilizes a robust data center that is capable of hosting a massive number of live and recorded video from IP-enabled security cameras. This capability allows Iveda to offer real-time video surveillance, in-vehicle streaming video, remote simultaneous access, and data archiving services.

Hosting and remote access services are ideal for customers managing multiple locations. The user's video is transmitted to the data center and distributed to an almost unlimited number of users simultaneously. Live and archived video can be accessed using any Internet-enabled device.

### *Benefits :*

- One login, one interface to multiple cameras anywhere in the world
- Interoperable with most IP Cameras & CCTV with Video Encoders
- Anywhere, Anytime from any Internet-accessible Device
- Web-based, 24/7 Remote Live & Archived Video Access
- Centralized, Multiple Simultaneous Access
- Secure, High Reliability & Availability
- Fully Fault-Tolerant Data Center

## **IvedaXpress**

IvedaXpress is a simple surveillance solution for home, office, or small business. It provides an inexpensive and easy to install enterprise-level camera management solution. While DVRs require hours of network setup and upkeep for an experienced IT professional, IvedaXpress is virtually effortless to set up. No software to install, no recording device to set up, and no configuration required. It is a plug and play video surveillance solution.

## IvedaSentry

IvedaSentry is the Company's real-time remote video surveillance service, providing remote, real-time surveillance of security cameras. Iveda's remote surveillance facility is designed to be operational 24/7 and houses its highly trained intervention specialists who monitor its customer's properties at any time the customers specify. Using sophisticated software, Iveda's intervention specialists are there as events unfold and they can act accordingly on its customers' behalf. By watching a customer's cameras in real time, Iveda is able to notify the police more quickly than other companies that wait for an alarm to be triggered or only review tapes after-the-fact. Iveda is also able to send police a link to real-time video.

This proactive versus after-the-fact security solution monitors facilities live and analyzes and proactively responds to situations in real time. No waiting for alarms to be triggered. Human intervention behind the technology is a key component and is combined with Iveda's DSR (Daily Surveillance Report), a proprietary reporting system that provides customers a detailed daily report of events. Real-time video surveillance provides live visual verification, eliminating costly false alarms and escalating police response priorities.

Traditional security services are classified into two types: 1) electronic or non-human; and 2) security guard-based, comprised of humans patrolling a site and human surveillance via closed-circuit television (CCTV). While the former is generally considered to be affordable to the greater market, the latter still remains rather expensive. Several factors and market dynamics have contributed to demand for Iveda's products and services, including:

- The recent wide-spread availability of high-bandwidth Internet connections (known as IP-based networks);
  - Drastic reductions in digital camera component costs; and
  - The introduction of innovative "smart scanning" software.

As a result of these dynamics, management believes that Iveda is able to offer a superior combination of human video surveillance and electronic security systems at a lower price than other currently available human-based security services.

### *Benefits :*

**Proactive versus after-the-fact** – With humans behind the cameras assessing situations in real-time, they can call the police when necessary to prevent a crime. Recorded video footage only helps to investigate after a crime has already been committed.

**Daily Monitoring Report** – Every morning, customers get an activity report in their email box, consisting of time-stamped video footage and a detailed description of events from the previous night.

**Cost Savings** – Savings of up to 75% are possible compared to traditional guard services.

**Secure Data** – Iveda utilizes a third party, highly secure datacenter to process, store, and protect its customers' video footage

**Live Visual Verification** – Several cities nationwide have adopted ordinances that impose a substantial fine for every false alarm. An alarm system may be declared a nuisance for excessive false alarms. Live video verification can reduce or even eliminate false alarms. With live video verification, police departments of some cities escalate response priority, depending on the seriousness of the event.

**Redundancy** – Video data are stored in Iveda's datacenter, remote monitoring facility, and its customers' facilities.

### *Problems with Existing Systems*

Electronic security tends to be extremely error prone. False alarms are so prevalent that cities and counties have sued alarm companies for the unnecessary allocations of available resources. When police officers have to be dispatched or re-directed to provide visual verification of a property that is emitting a false alarm, the cost in time and money becomes exorbitant.

While electronic security tends to be error prone, human security is often poorly trained and expensive. Unless well-trained security guards are present, human security is not viewed as a credible counter threat to a potential crime. While a security guard can give independent verification, cost can make guards prohibitive. A single security guard cannot be in several locations at the same time, resulting in a need for multiple guards to cover the entire property, at a per guard cost of \$15 to \$26 per hour.

Traditional security companies are proving to be slow to adapt to high-tech, IP-based networks, simply because their core competency does not include the sophisticated software, hardware, and Internet technology required. Companies that understand the technology are missing the knowledge of the security business and lack expertise in security systems design and the actual management of a crew of intervention specialists.

What management believes has been missing from the industry is a proactive security solution that will deter crime and help the police catch criminals in the act; not merely through using video data as an after-the-fact investigative tool for solving a crime. This security solution requires a company able to competently offer superior security systems and video communications via IP-based networks.

## **IvedaOnBoard**

IvedaOnBoard utilizes any in-car camera available in the market today with our Streaming Video Converter (SVC) and IvedaEnterprise. IvedaOnBoard allows our customers real-time situational assessment of field activities. This untethered surveillance solution utilizes Wide-area data services such as cellular, mesh wireless, and Wi-Fi. Centralized video management of an entire mobile fleet includes high quality real-time streaming video and instant review of footage remotely, thus no need to have a recording device onboard.

## **IvedaPinpoint**

IvedaPinpoint is a live streaming video mapping application and is a video management system (VMS) consolidator and online mapping service that shows location of surveillance cameras on Google Maps(TM) or other third party mapping platforms. Through a single login, users are able to pull live streaming video feeds from a centralized video management platform. IvedaPinpoint is completely web-based, accessible from any Flash-enabled browser on your computer or smartphone.

In collaboration with Pinkerton/Securitas, Iveda Solutions conducted a successful pilot of IvedaPinpoint at the 2012 G8/NATO meeting in Chicago. IvedaPinpoint was integrated into Pinkerton's Vigilance incident & trend data monitoring system, its cloud-based, 24/7 situational awareness and risk aggregation service that gathers data and evaluates threats.

Applications for IvedaPinpoint range from safe city, , executive protection, facility protection, border protection, supply chain security, transportation, utilities, federal and local governments. When a user clicks on a "Pinpoint" the live video of the camera will appear.

## **IvedaXchange**

IvedaXchange uses cloud-based technology to provide a suite of threat assessment dashboards and alerting capabilities to schools, school districts, government agencies—or any organization wishing to upgrade their threat monitoring capability.

IvedaXchange enables school, law enforcement, emergency personnel and others to receive targeted emergency alerts, share key information on potential threats, and locate critical assets—students, staff, and buses, in real time.



## **Products**

Iveda's core competency is based on its cloud-video management platform. Iveda focuses on recurring service revenue, but we also sell and integrate products to enable Iveda services.

### **Express Surveillance System (ESS)**

The Express Surveillance System (ESS) is a self-contained wireless surveillance unit, equipped with an integrated cellular router for an "always on" Internet connection. The camera is shipped pre-configured and ready for deployment on leading broadband cellular networks. All that is needed is a cellular data card and power.

The ESS is portable and remotely accessible, thus well suited for applications that require temporary high-quality video surveillance, such as special events, stake outs, and construction sites. The unit is bundled with IvedaEnterprise for a complete plug-and-play system, ideal for remote surveillance, where a typical ISP (Internet Service Provider) is not available and a local server or DVR is not practical. ESS enables fast and easy video surveillance deployment.

### **Streaming Video Converter (SVC)**

The Streaming Video Converter (SVC) is a fully integrated device that combines the functionality of a high performance video encoder and cellular broadband router. This rugged and portable unit was specifically designed for digitizing analog in-vehicle mobile video systems. This digital conversion enables live mobile streaming video using cellular data network for remote access and storage. The SVC is capable of delivering up to four simultaneous video streams.

The device allows for rapid deployment of live mobile streaming video ideal for in-vehicle applications, such as police cars, school buses, taxicabs, delivery trucks, tow trucks, and freight trucks. With the SVC, video footage that is traditionally stored inside the vehicle through a local recording device can now be virtualized and stored remotely at Iveda's fully fault-tolerant data center with no concerns of redundancy, reliability, and lost or damaged data.

## **Systems Integration**



Our core competency is our ability to deliver cloud video management services. We offer our customers a variety of products that enable our services and from which we create customized solutions for our customers. We call these solutions our cloud video validators.

### **SafeCiti®**

SafeCiti is a comprehensive turnkey solution for central management and processing of critical information and surveillance technology throughout an entire metropolitan area. Our SafeCiti solution offers infrastructure owners to effectively bridge the gap between their current technology capabilities with much needed upgrades and expansion of new capabilities. Iveda's cloud technology promotes faster, more affordable public safety and security system implementation and all with much greater sustainability. MegaSys is our expert in SafeCiti deployments, having completed a large project for the New Taipei Police Department in 2010. The police department has awarded MegaSys additional SafeCiti deployments for \$2.2 million in January 2012 and \$1.3 million in December 2012.

### **Surveillance Equipment Installation and System Integration**

Iveda partners with security integrators with expertise in full deployment of new IP-based video surveillance systems and converting existing analog or CCTV systems to IP-based systems. With these integrators, Iveda designs, recommends, sells, and installs camera systems to enable video hosting, real-time surveillance services, and mobile video services.

### **Technology Architecture**

Iveda's infrastructure utilizes the power of cloud computing. Cloud computing refers to applications running on a remote server instead of on a local computer, and the user accesses it via the Internet. Using a web browser, the user logs onto a hosted website to access account information and all computations and data manipulations are done at the server level.

Iveda has applied the same principle to create an IP video hosting platform, which paved the way for other service offerings such as real-time surveillance services and in-vehicle mobile streaming video. By consolidating computing power into a single location at the server level, Iveda creates efficiencies due to economies of scale, and offers more features and flexibility than ever before offered.

Iveda utilizes robust data centers that are capable of centrally hosting live and recorded video from a massive number of IP-enabled security cameras. Our HA (high-availability) IP (Internet Protocol) infrastructure is scalable, redundant,

and secure.

Using cloud computing is a better way to consolidate surveillance video, especially if it is coming from disparate geographic locations or facilities. Instead of running multiple video recording devices (DVR) and software (NVR), the video is centrally hosted at a data center and the user accesses it using a Web browser. This is sometimes referred to as Managed Video as a Service (MVaaS), or Video Surveillance as a Service (VSaaS). When surveillance video is in the cloud, the user logs in through any Internet-accessible device, wherever the user may be. The user does not need to install proprietary software or worry about safety of recorded video. Everything is hosted and recorded remotely and can be accessed 24/7 using a web browser.

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Getting surveillance video into the cloud can be set up almost immediately in many cases. Plus, upgrades and patches can be achieved remotely for immediate access to enhanced security, features and performance over time.

Access to multiple properties or locations anywhere around the world has never been easier. When surveillance video is in the cloud, the user has full access to it from anywhere with an Internet connection. Also a huge advantage of bringing surveillance video into the cloud is that you never have to worry about bandwidth when multiple users want to access video simultaneously.

Cloud-based video surveillance reduces capital expenditure. User cost to deploy is captured in a predictable monthly subscription fee.

*Features :*

- **Internet Access** - Allows customers 24/7 secure, remote access to video.

- **Data Center** - Iveda utilizes data centers equipped with emergency power and redundant bandwidth.

- **VOIP** - Iveda can utilize voice-over-IP to allow a 1-way or 2-way communication between its intervention specialists and suspicious individuals on its customers' properties.

- **Camera Manufacturer Agnostic** - Iveda can monitor security cameras from the majority of manufacturers, whether analog (CCTV) or digital.

- **Carrier/ISP Neutral** - Iveda can work with customers' current Internet providers as long as minimum bandwidth requirements are met.

*Network Camera IP-Based Technology* .. Network camera IP-based technology is the core of Iveda's security solution. The cameras Iveda utilizes are not typical Web cams or CCTV. They are all mini computers with enabled Web servers. Each camera has the capability of becoming its own Web site on the Internet, which allows Iveda's intervention specialists to log into each camera and control the cameras' operation. When combined with "PTZ" (pan, tilt, zoom) cameras, the intervention specialist can make the camera pan, tilt, zoom or rotate as needed remotely. Clients can also log into each camera through Iveda's web access tool, and can view the images real-time, 24/7. The software that powers the camera technology is generally open source, which allows Iveda to develop unique applications in the future to service a wide variety of industries and clients.

*Security* . Iveda anticipates its customers' video networks, which will include a variety of public sector security applications, will be high-value targets for criminals. As a result, Iveda's network security standards must be and are very high, meeting standards used by banks in providing online banking services.

As the leading online surveillance provider, the security of surveillance video is always a priority at Iveda. We are committed to implementing stringent measures to ensure data stays secure. Multiple layers of network redundancy ensure the security of video assets. Every critical network component within the Iveda's Cloud is redundant; including a second copy of video to ensure stability, uptime, and that video is not lost.

Iveda's networks are protected from external threats by ICSA certified products to block unauthorized external entry. Internal data and network access is controlled by permission and policy based ACLs.

Video security between the camera and the Iveda's Cloud can be secured utilizing the IvedaXpress product which integrates AES 256 bit encryption into the connection between the camera and our Cloud. Video security can also be secured by incorporating encrypted VPNs (Virtual Private Network).

Iveda plans to continue to develop and improve its network security protocol as it rolls out new applications of its services. Of course, any network security measure can fail, and any security breach could result in significant liability for Iveda.

*Remote Surveillance Center.* Iveda's 24-hour remote surveillance facility is the nerve center of its unique IP-enabled services. It is connected to the data center through a massive pipe of redundant point-to-point broadband bandwidth, which allows streaming video, enabling real-time video surveillance. Iveda has been monitoring cameras since 2005 and has proven the effectiveness, robustness, and reliability of its service. Some of the operational features of the facility include:

- Rapid visual verification to every alert
- Full escalation to the police
- Automatic notification to clients of serious incidents



- Full audit trail including date and time stamped images of every incident securely stored
- Video can be used for evidence in court
- Regular updated site details
- Specially-trained intervention specialists
- Direct visual link can be sent via email to police instantly

Below is a diagram of how the Iveda system works.

### **Pricing Strategy**

Iveda's cloud video hosting solutions provide a less expensive alternative to typical CCTV/DVR solutions and live human security guards. Iveda can affordably upgrade a standard CCTV system to an Internet-based surveillance system, through digital conversion. As a result of all of these factors, Iveda has removed several cost barriers for its customers.

- Less capital expenditure. No hardware or software to install.
- Less operating expense, reduces overhead. No infrastructure to maintain and replace.
- Reduced false alarm costs that are historically high for alarm-based security solutions.
- No costly Virtual Private Network (VPN) required to link multiple cameras.

Integrating the customer's existing cameras into its solution, reducing the high cost of purchasing and installing new cameras.

Iveda has developed a pricing model for its products and services that will allow its resellers an attractive profit margin from residual revenues while allowing Iveda to garner about 60% profit margin when its video hosting infrastructure is fully utilized.

**Equipment Sales and Installation.** Iveda has historically realized a gross margin of 10% to 40% on equipment sales. Iveda does not manufacture any of the components used in its video surveillance services business. Due to the general availability of the components, Iveda is able to obtain the components of its systems from a number of different sources and to supply its customers with the latest technology generally available in the industry. Iveda is not dependent on any single source for its supplies and components and has not experienced any material shortages in the past. Typically, the Company does not maintain inventory of equipment.

In distribution channel sales, Iveda sells equipment to its resellers and integrators, who in turn sell the equipment to the end user. In certain select large corporate account sales, Iveda will sell the equipment directly to the large accounts, and in turn utilize integrators or other third parties for installation activities.

**Cloud Video Hosting and Remote Surveillance.** Upon full utilization of the current video hosting infrastructure, Iveda has implemented a pricing structure for its services at approximately a 60% gross margin. Gross margin may improve with software enhancements to enable intervention specialists to monitor more cameras at the same time, and when the cost of bandwidth drops with increased usage. Iveda compensates intervention specialists well and has historically attracted and retained high-quality and loyal employees, thus reducing the cost of turnover and training.

**Video Data Storage.** One day of video storage is provided free of charge with hosting service and seven days with real-time surveillance. The customer pays a minimal fee for each additional day of storage.

**Maintenance Agreement.** In the past, Iveda charged an additional 25% to 48% of the total equipment cost for an optional maintenance contract, payable upfront. Iveda's maintenance agreement would cover what is not covered by the camera manufacturer's 3-year warranty. Government customers typically request this contract. A recent new customer in Mexico has agreed to sign up for this service, along with video hosting, and extended video storage.

#### *Government Contracts*

Iveda plans to seek government contracts for its products and services. These contracts are typically awarded through a competitive bid process. Iveda intends to grow its business in part by obtaining new government contracts through the competitive bidding process. Sole-Vision has been successful in this arena and the Company has leveraged their expertise in potential Safe City projects in Mexico.

Certain agencies may also permit negotiated contracting. Contracts awarded through a competitive bidding process generally have lower profit margins than negotiated contracts because in a competitive bidding process bidders compete predominantly on price. The U.S. Federal government is the largest procurer of products and services in the world, and the Federal contract market may provide significant business opportunities for Iveda.

#### *Private Sector Contracts*

Private sector contracts can be awarded through either a competitive bidding process or a negotiating process. Unlike government contracts, the terms of private sector contracts can vary based on individual client situations. Price is not the only key element in winning contracts with this market segment. Other elements such as service quality, responsiveness and various peripheral services come into consideration. Iveda believes that the private sector represents the company's largest growth potential. Private sector customers generally privately negotiate contracts for such services, resulting in contracts with higher profit margins because price is not always the primary basis for



competition.

### **Customers**

Iveda's customers in 2012 included data centers, banks, storage facilities, homeowner associations, food processing plants, public pools and parks, and government agencies in Mexico and Asia. In 2012, the New Taipei City police department account for 69% of the Company's overall revenue.

There are a large number of industries that could potentially benefit from Iveda's video hosting, in-vehicle mobile video, and real-time surveillance services. As Iveda grows and increases public awareness of its services, it believes that it will acquire customers from a wide variety of industries.

The following is a sample list of the Company's video surveillance service customers over the prior two years.

- American Security & Investigations
- City of El Mirage
- City of Mesa
- Farnsworth Realty
- Glendale Police, CA
- Green Valley Agriculture and Turf
- Helix Properties
- i/o Data Center
- Leisure World
- Mexican Government
- Pacific Coast Producers
- Porsche Dealership
- San Diego Police Department
- San Joaquin County Public Works
- Sun Eagle Corporation
- Sunland Storage
- Sunol Golf Course
- United Road Towing
- Watermark Community
- West Valley Child Crisis

The following is a sample list of SafeCiti, equipment sales, and systems integration customers over the prior two years:

- City of Glendale, CA
- Sui Industry
- New Taipei City Police Department
- Taiwan Stock Exchange
- Ystarding
- Taiwan Energy Systems
- Taoyuan County Council
- The Tivoli Cable Engineering
- Zhongxing
- Futai
- Secom Taipei

*Market Segmentation*

Iveda views the following markets as its primary target markets:

· Companies who wish to save on traditional security services, while maintaining live surveillance of their properties.

· Customers who wish to integrate or enable an existing video surveillance system for hosted video and remote surveillance.

· Real-time, in-vehicle streaming video accessibility for operational efficiency for transportation management and traffic safety.

· Educational institutions that want to integrate surveillance systems in their facilities.

· Security and remote surveillance of school playground areas, corridors, halls and classrooms.

Municipalities for Safe City projects.

## **Business Strategy**

Iveda is implementing the following business strategy:

### *Reseller Sales:*

o Provide assistance to its growing reseller channel distribution to utilize resellers' camera installed base and thereby seek to increase Iveda's video surveillance subscribers.

Build a high-caliber indirect channel sales team to support reps and integrators.

o Provide co-op marketing funds to resellers to promote Iveda products and services on our behalf utilizing their customer and prospect lists.

o Fund demo units for product seeding of Iveda's services in sales opportunities.

o Fund road shows for live customer demos.

o Build indirect sales channel to support

### *Marketing:*

o Conduct regional marketing campaigns in Iveda's existing markets, while strategically launching in other key markets.

o Expand online marketing and non-traditional viral marketing.

o Participate in vertical and technology tradeshow.

o Produce online and printed sales and marketing materials for end users and resellers.

- o Implement and manage PR and marketing campaigns.
- o Work with research firms on independent case studies, industry research, and white papers.
- o Enhance search engine optimization (SEO) of the Company's websites.

*Infrastructure/Security/Operations/R&D :*

o Develop new products with technology partners in India and Asia to enhance and enable Iveda's video surveillance services.

o Incorporate another layer of security to Iveda's edge devices to further enhance the value of our products and services.

- o Fund in-house development of software for Iveda's backend that may be patentable.

- o Further develop Cerebro, Iveda's proprietary centralized security reporting system.

o Fund backend equipment/hardware and software to demonstrate Iveda's system capabilities to prospective enterprise clients (white label demos).

o Qualify Iveda on safety and cyber security compliance requirements for government standards and expectations as well as fulfill customer commitment to be as secure as possible to garner customer trust and loyalty.

o Provide a test lab environment which includes dedicated equipment and resources for further customer application testing, development and enhancements as well as new product and/or system evaluation.

*International Business Development :*

- o Form business alliances with overseas companies for revenue generation.
- o Fund customer demo meetings and presentations abroad.
- o Leverage MegaSys relationships with developers and manufacturing companies in Asia for cost reductions.
- o Leverage MegaSys' acquisition to establish presence and access to the Asian market to implement Iveda's recurring revenue model.

*Mergers and Acquisition*

- o Identify companies in Asia with broad market reach.
- o Explore companies with business and technologies that are complementary to ours.

*Sales Strategy*

In the last two years, Iveda's activities were geared toward building its global strategy, starting with its acquisition of MegaSys, which was completed on April 30, 2011. The Company hired a senior vice president of global sales and support to build and manage domestic and international sales.

Historically, Iveda generated sales through its direct sales force. In June 2012, Iveda began its transition to a reseller distribution channel program in the U.S. Iveda believes that leveraging resellers' existing customer base, many of which already have cameras installed, provides a more effective strategy to grow the number of cameras the company hosts and monitors. Over the last few months, Iveda has built necessary sales and marketing tools to support the indirect sales channel including training modules, partner portal, demo program, datasheets, and co-op program. Iveda also transitioned its small direct sales team to channel sales managers and hired new members to the team with expertise in managing and developing indirect sales channel.

Management believes that once this indirect sales channel is fully trained and mobilized, it will expedite securing a larger percentage of the market by leveraging its channel partners' customer base. This is also a potentially faster way to make Iveda a national provider of video surveillance services compared to relying solely on internal sales efforts. In October 2011, the Company signed an agreement with a large telecommunications company for them to resell Iveda's products and services in the U.S. and Latin America. In 2012, Iveda has also signed ten independent manufacturers'

representatives which provide coverage to 42 states, the Carribbean, and Canada. The names of the partner firms that have signed a partner agreement are as follows: Coaxial Systems Associates, Inc., GP Marketing, HMR Associates, IDMC Associates, Intech Sales, Langbaum & Associates, Milsk Company, R.W. Kunz & Associates, Warren Associates and SECURaGLOBE Solutions, Inc. Each rep firm has a network of security integrators that serve as their feet-on-the-street salesforce.

The Iveda Reseller Program is designed to build a community of dedicated Iveda partners to help realize its vision, while providing them with additional revenue streams and boosting their competitive edge by offering a security solution that makes sense. Iveda believes that the active partnerships between Iveda and its resellers will assist them in capturing market share before competitors are able to move into the market. The reseller receives 25% discount off of MSRP for reselling Iveda's services. The reseller may decide to attain an even higher margin by charging its customers above MSRP.



Resellers are responsible for any issues regarding equipment they installed, including but not limited to: equipment maintenance, replacement, and training. Iveda will only be responsible for video surveillance service issues. It is the reseller's responsibility to make sure that their installation is working properly to enable Iveda's video surveillance services.

*Reseller Benefits:*

Derive monthly recurring revenue stream from offering a complimentary service for their line of security products, without having to build network infrastructure for video surveillance services.

Camera deployments are normally a one-time sell, until it is time for a replacement. With Iveda, installers can offer a new service to their installed base to generate additional revenue from existing customers.

Leverage Iveda's SAFETY Act Designation

Boost Competitive Edge & Value Proposition

Expand Technology Offerings & Integration Services

*Law Enforcement and Government Contracts*

In 2012, Iveda sold approximately \$345,653 in products and services to law enforcement, cities and municipalities in the U.S. and approximately \$2,718,537 in Taiwan. In 2010 Iveda began servicing a government agency in Mexico which has opened doors for Iveda with other law enforcement agencies to implement Iveda's services. Iveda sold \$270,001 to this agency in 2012. In January 2012, MegaSys was awarded a \$2.2 million Safe City contract from New Taipei City. In December of 2012 New Taipei City awarded a \$1.3 million project that expands the Safe City project into the Linkou district. Iveda has already earned "preferred vendor" status from its existing police department customer as well as from the United States Department of Homeland Security (DHS).

In April 2009, Iveda was granted a Certificate of SAFETY Act Designation by the Department of Homeland Security. The SAFETY Act creates a system of "litigation management" for both Iveda and its customers by imposing important liability limitations for "claims arising out of, relating to, or resulting from an act of terrorism" where Iveda products and services have been deployed. This benefit covers all new customers and current customers dating back to January 1,

2005. Certification is required for Iveda to be able to seek certain government contracts.

### *Marketing Strategy*

Over the years, Iveda has not sustained ongoing public relations and marketing campaigns due to limited resources. Limited marketing activities have not generated considerable amount of leads for sales. Marketing budget was not sufficient to launch an early-adapter product into the marketplace. In 2012, Iveda spent insignificant amounts in marketing.

In 2012, Iveda invested in demo equipment for customer seeding. The Company believes that the best way to market its products and services is to provide a hands-on demo.

Iveda recently hired a full-time PR and Marketing Communications Manager to assist the Chief Marketing Officer implement Iveda's marketing plan, including actively pitching our press releases to trade publications and enhancing our presence in social media.

### *Public Relations*

First, Iveda needs to establish a known presence within the security industry, with key security industry analysts and influencers being briefed on Iveda and its unique security solution. Iveda continues to generate media interest whenever it sends out a press release. The Company is internally managing its PR efforts, including proactively pitching Iveda products and services and, working with partners for joint articles and case studies on trade magazines. The Company's internal PR efforts have proved to be more effective than utilizing a PR agency. The company's press room section of its website contains articles, interviews, and other media coverage, which demonstrates the success of its PR efforts.

### *Co-op Program*

As the reseller distribution channel matures, Iveda's marketing strategy is expected to be increasingly concentrated on co-op programs, public relations, and branding instead of lead generation for its direct sales force. This strategy will mobilize resellers and utilize their existing customer base. The resellers will be encouraged to conduct direct marketing campaigns to their existing customers and prospect lists. Iveda will match their marketing spend on any lead-generation activities. Iveda expects its resellers to do the heavy lifting in lead generation.

*Website*

Iveda's marketing campaign starts with its website. The company has laid the groundwork for this strategy by investing a lot of search engine optimization (SEO) development time on the Company's website. As a result, the Company's search ranking on Google and other search engines on certain key words have dramatically climbed to top 5 search results. With no marketing budget, majority of sales leads come from random searches of people looking for video hosting, cloud-based surveillance, in-vehicle surveillance, or real-time remote surveillance solutions.

*Collateral*

Iveda has developed a wide array of marketing materials to highlight the Company's products, services, technology, and capabilities. The various pieces cater to all kinds of audiences: potential customers, partners, investors, and employees.

*Online Marketing*

Instead of more traditional print advertising, Iveda will use its online banner advertising on security technology websites and vertical market websites with application-specific messaging.

According to a recent study by Performics and ROI Research, 75% of shoppers use search engines to research products and services. Iveda will allocate a significant amount of its online marketing budget on Yahoo and Google Adwords pay-per-click campaign.

With the proliferation of social media as a new marketing vehicle, Iveda has established Facebook, Twitter, and LinkedIn presence. Management expects that these sites will generate online buzz about the Company, which will increase the Company's followers, and website traffic. The Company anticipates these activities to fuel lead generation and increase brand awareness. Iveda will also explore webinars which has started to become a popular sales and marketing vehicle to promote products and services.

The Company will continue its internal PR activities, including following editorial calendars of various trade and vertical publications, seek speaking engagements for the CEO to reach specific captive audience at a tradeshow or event, and write articles relevant to the company's interests.

### *Tradeshows*

Iveda intends to allocate approximately 30% of its marketing budget in tradeshow participation. Tradeshows are still very effective in generating hundreds of leads during a 2 or 3-day event, amongst a captive audience who are influencers or decision makers.

Iveda's primary goals for exhibiting at tradeshows are to generate leads for sales and build brand in the process. We will participate at these shows with our resellers. We will identify vertical tradeshows, where the company's services may be of high interest to both exhibitors and attendees (e.g., law enforcement, government, self-storage, hospitality). These will be local and regional tradeshows, plus one big national tradeshow.

Iveda will exhibit at International Security Convention West (ISC West) in April 2013. The show is the biggest security technology show with over 1000 companies exhibiting. Attendees include security integrators and end users. This is Iveda's first big show and we are participating in a big way. One of our new products has been entered into New Product Showcase competition. This will provide a lot of exposure for the company before, during, and after the show.

In addition, Iveda plans to attend major industry functions and pursue various key speaking opportunities to further spread the cost savings and customer convenience of the services provided by Iveda.

### *Other Information*

**Proprietary Rights.** Iveda regards certain aspects of its internal operations, products and documentation as proprietary, and relies and plans to rely on a combination of copyright and trademark laws, trade secrets, software security measures, license agreements and nondisclosure agreements to protect proprietary information. The Company does not currently hold any patents.

We cannot guarantee that our protections will be adequate, or that our competitors will not independently develop technologies that are substantially equivalent or superior to our system. Nonetheless, the Company intends to vigorously defend its proprietary technologies, trademarks, and trade secrets. The Company has generally and will in the future require existing and future members of management, employees and consultants to sign non-disclosure and invention assignment agreements for work performed on the Company's behalf.

We also intend to secure appropriate national and international trademark protections with the intention of prosecuting any infringements, although we have not historically sought any patent protection, but have solely relied on trade secrets, software security measures and nondisclosure agreements. Iveda has trademark registrations for "Iveda Solutions," "Iveda," the Company's logo, and "SafeCiti" from the U.S. Patent and Trademark Office. We are also seeking to trademark for our product names.

Iveda has developed Cerebro, a proprietary software product used internally by Iveda. Cerebro allows Iveda to manage and track all aspects of its remote monitoring service and generate reports on such items as daily monitoring, reported events, property and contact data, major incident tracking, intervention specialist performance tracking and service performance statistics. It also allows employees to participate in internal message board communications. Iveda has historically relied on trade secret protection for Cerebro, but management may consider applying for patent or copyright protection for this database or related processes in the future.

In November 2012, Iveda signed a cooperation agreement with Industrial Technology Research Institute (ITRI). ITRI is a research and development organization based in Taiwan. Iveda and ITRI have been co-developing cloud-video services. ITRI has given Iveda license to some of their patents being used in the development. Iveda will have exclusive rights to the products and services being co-developed. Some of these products will be shown at the ISC West Show in April 2013.

We do not believe that our proprietary rights infringe the intellectual property rights of third parties. However, we cannot guarantee that third parties will not assert infringement claims against us with respect to current or future technology or that any such assertion may not require us to enter into royalty arrangements or result in costly litigation. Furthermore, our proposed future products and services may not be proprietary and other companies may already be providing these products and services.

**Government Regulation** . Various states within the United States require companies performing low voltage equipment installation to be licensed. Iveda maintains active licenses in Arizona and California. Iveda transitioned all installation activities to its security integrator partners with required licenses to install equipment in the states they cover.

**Employees** . As of the date of this report, Iveda has 32 employees in the US and 15 in Taiwan. The Company's future success will depend, in part, on its ability to attract, retain, and motivate highly qualified security, sales, marketing, technical and management personnel. From time to time, the Company employs independent consultants or contractors to support its development, marketing, sales and support and administrative needs. The Company's employees are not represented by any collective bargaining unit.

Part of our business is labor intensive and, as a result, is affected by the availability of qualified personnel and the cost of labor. Although the security services industry is generally characterized by high turnover, we believe our experience compares favorably with that of the industry. We have not experienced any material difficulty in employing suitable numbers of qualified personnel, and employee turnover is low.

We believe that the quality of our intervention specialists is essential to our ability to offer effective and reliable real-time remote surveillance service, and we believe diligence in their selection and training produces the level of performance required to maintain customer satisfaction and internal growth. Our policy requires that all selected applicants for an intervention position with us undergo a detailed pre-employment interview and a background investigation. We also run a criminal background check, conducted by a third party. Personnel are selected based upon maturity, experience, personality, stability and reliability.

Our comprehensive training programs for our intervention specialists include initial training, on-the-job training and refresher training. Initial training explains the duties of an intervention specialist, report preparation, emergency procedures, ethics and professionalism, grounds for discharge, and basic post responsibilities. On-the-job training covers specific duties as required. A quarterly meeting is held with all intervention specialists to discuss any problem areas, go over new techniques, and discuss tips for effective monitoring, providing further ongoing training. The remote surveillance department's management team also conducts a monthly meeting. Ongoing refresher training is given on an annual basis as the need arises as determined by the employee's supervisor or quality control personnel.

**Insurance.** We maintain insurance, including comprehensive general liability coverage, key man, and directors' and officers' coverage in amounts and with types of coverage that management believes to be customary in our industry. Special coverage is sometimes added in response to unique customer requirements. We also maintain compliance with applicable state workers' compensation laws. A certificate of insurance, which meets individual contract specifications, is made available to every customer.



## **Competition**

### **Video Hosting Service**

Iveda offers cloud-based enterprise-class and consumer-class video hosting services. Consumer-class video hosting normally provides proprietary cameras and software. Typically, only one streaming video access is allowed at one time. This kind of solution is generally not robust enough for commercial or enterprise-level video hosting solution. Iveda has direct competitors with our consumer-class video hosting service (IvedaXpress) including Securei, MyCamServer, Byremote, Envysion, Icontrol and IVR Controls . Iveda differentiates its products and services by using its enterprise-class IP infrastructure, which allows us to manage a large number of cameras, in our consumer service offerings. Our infrastructure features high availability and redundancy. We manage our own datacenter and we have end-to-end level of security from the servers hosting our video to edge devices (i.e., cameras and video encoders).

The Company's enterprise-class video hosting service, IvedaEnterprise, allows centralized management of multiple cameras located anywhere in the world, regardless of camera type. Our open-source IP infrastructure, utilizing world-class data centers, allows hosting of unlimited number of cameras, allowing multiple, simultaneous access by users via a web browser on any Internet-accessible device. Iveda can also centrally host and manage mobile video streams from police cars, delivery trucks, and school buses. Access to remote video recording and extended storage can also be accomplished through a web browser. Iveda's video hosting and surveillance solution reduces capital expenditure for companies by allowing companies to avoid installing servers and software, and hiring IT personnel to maintain the necessary infrastructure. Although the Company is not aware of other companies offering similar cloud-based services, the competitors identified above offer similar services based on proprietary cameras and software to enterprise-class customers.

### **Real-Time Surveillance Service (IvedaSentry)**

Iveda's services are based on its IP network infrastructure and utilize world-class data centers. Management believes the Company's surveillance facility is a competitive strength, as it is capable of performing real-time video surveillance for customers without the need of an electronic alarm that prompts an alarm company to log into a specific camera to view the potential breach.

Management believes that Iveda is the only company providing enterprise-class **real-time** remote video surveillance in the United States as of the date of this report. The majority of monitoring companies review camera monitors after an electronic alarm has been triggered. Iveda uses specialized software analytics that allow intervention specialists to monitor customer properties and respond to incidents in real time. This technology offers configurable view-zones,

programmable movement direction, and pattern-recognition to a particular user. The Company also has an in-house database management system that allows interventions specialists to record every event. This system generates a Daily Surveillance Report (DSR), emailed to the customer at the end of the surveillance shift.

Integrators and central monitoring companies, the Company's closest competitors, provide monitoring services based on electronic alarm triggers. Examples of companies providing these competing services include Westec Interactive, Iverify, Xtreme Surveillance, Viewpoint, byRemote, and Monitoring Partners.

Some of Iveda's current and future competitors may conduct more extensive promotional activities and may offer lower prices to customers than Iveda, which could allow them to gain greater market share or prevent Iveda from increasing its market share. In the future, Iveda may need to decrease its prices if Iveda's competitors lower their prices. Iveda's competitors may be able to respond more quickly to new or changing opportunities, technologies and customer requirements. To be successful, Iveda must carry out its business plan, establish and strengthen its brand awareness through marketing, effectively differentiate its services from those of its competitors and build its reseller network, while maintaining superior levels of service, which management believes is what will ultimately differentiate Iveda's services from any similar services its competitors may develop in the future.

## Available Information

The Company electronically files its Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and all amendments to these reports and other information with the Securities and Exchange Commission (the “SEC”). These reports can be obtained by accessing the SEC’s website at [www.sec.gov](http://www.sec.gov). The public can also obtain copies by visiting the SEC’s Public Reference Room at 100 F Street NE, Washington, DC 20549 on official business days during the hours of 10:00 am to 3:00 pm or by calling the SEC at 1-800-SEC-0330. The Company has two websites located at [www.ivedasolutions.com](http://www.ivedasolutions.com) and [www.ivedaexpress.com](http://www.ivedaexpress.com). Information contained on the Company’s website is not a part of this report.

## ITEM 1A – RISK FACTORS

*An investment in our securities is highly speculative and involves a high degree of economic risk. You should carefully consider the following risk factors along with the other matters described in this Annual Report in making an investment decision to buy our securities. If you decide to buy our securities, you should be able to afford the possibility of a complete loss of your investment.*

### *Risk Factors Involving Our Business*

*Iveda’s Financial Statements Contain A Going Concern Opinion.*

Iveda’s financial statements included with this report were prepared on a “going concern basis” and the audit report contains a “going concern qualification” (see the Audit Report on the Financial Statements for the year ended December 31, 2012 and Note 1 to those Financial Statements). Our financial statements assume we will continue as a going concern, but to be able to do so we will need to raise additional capital to fund our operations until positive operating cash flow is achieved. There can be no assurance that we will be able to raise sufficient additional capital to continue our operations.

*Iveda Needs to Raise Significant Additional Funding.*

At Iveda’s current estimated burn rate, Iveda has sufficient capital to continue its operations for only a short period of time. Accordingly, Iveda must raise capital to continue as a going concern. The Board of Directors approved the

Company to engage with an investment banker to act as the Company's financial and capital markets advisor to seek to raise up to \$30 million in long term financing. The board also approved the Company to raise up to \$3 million in bridge financing in advance of the long term financing. There can be no assurance that Iveda can raise sufficient funding to continue as a going concern or to even operate profitably. Any inability to obtain additional financing when needed could require Iveda to significantly curtail operations or delay its expansion plans.

Even if funding is available to the Company, Iveda cannot assure investors that additional financing will be available on terms that are favorable to the Company's existing shareholders. Additional funding may be accomplished through the issuance of equity or debt securities that could be significantly dilutive to the percentage ownership of Iveda's existing shareholders. In addition, these newly issued securities may have rights, preferences or privileges senior to those of existing shareholders. Accordingly, such a financing transaction could materially and adversely impact the price of our Common Stock.

*Iveda Depends On Certain Key Personnel.*

Iveda's future success will be dependent on the efforts of key management personnel, particularly David Ly, Iveda's President and CEO, Luz Berg, Iveda's COO and CMO, Alex Kuo, Chief Strategy Officer, Richard Gibson, SVP of Global Sales & Support, and Brian Duling, Iveda's CFO, each of whom is employed at will by Iveda. Mr. Ly's relationships within Iveda's industry are vital to Iveda's continued operations, and if Mr. Ly was no longer actively involved with Iveda, Iveda would likely be unable to continue its operations. Iveda has obtained key man insurance on Mr. Ly in the amount of \$1 million. The loss of one or more of Iveda's other key employees could also have a material adverse effect on Iveda's business, results of operations and financial condition.

Iveda also believes that Iveda's future success will be largely dependent on Iveda's ability to attract and retain highly qualified management, sales and marketing personnel. Iveda cannot assure investors that the Company will be able to attract and retain such personnel. Iveda's inability to retain such personnel or to train them rapidly enough to meet Iveda's expanding needs could cause a decrease in the overall quality and efficiency of Iveda's staff, which could have a material adverse effect on Iveda's business, results of operations and financial condition.

*Rapid Growth May Strain Iveda's Resources.*

As Iveda continues the commercialization of its security and surveillance products and services, it expects to experience significant and rapid growth in the scope and complexity of its business, which may place a significant strain on the senior management team and Iveda's financial and other resources. The proposed acceleration will expose us to greater overhead, marketing and support costs and other risks associated with growth and expansion. Iveda will need to add staff to monitor additional cameras, market its products and services, manage operations, handle sales and marketing efforts and perform finance and accounting functions. Iveda will be required to hire a broad range of additional personnel in order to successfully advance its operations.

Management has implemented strategies to handle projected growth, including increasing our leased space within Iveda's existing building. Iveda's existing leased space can accommodate up to 15 monitoring stations, with four employees required to monitor each station around the clock and other additional key employees. While maintaining two existing data centers, located in Phoenix and Scottsdale, Arizona, we also leased a new less expensive facility with comparable features. Iveda's ability to manage its rapid growth effectively will require Iveda to continue to improve its operations, to improve its financial and management information systems and to train, motivate and manage its employees.

This growth may place a strain on Iveda's management and operational resources. The failure to develop and implement effective systems, or to hire and retain sufficient personnel for the performance of all of the functions necessary to effectively service and manage Iveda's business, or the failure to manage growth effectively, could have a materially adverse effect on Iveda's business and financial condition. In addition, difficulties in effectively managing the budgeting, forecasting and other process control issues presented by such a rapid expansion could harm Iveda's business, prospects, results of operations and financial condition.

*Demand For Iveda's Security And Surveillance Products And Services May Be Lower Than Iveda Anticipates.*

Iveda has limited resources to undertake extensive marketing activities. Iveda cannot predict with certainty the potential consumer demand for its security and surveillance products or services or the degree to which Iveda will meet that demand. If demand for its security and surveillance products and services does not develop to the extent or

as quickly as expected, Iveda might not be able to generate revenue to become profitable.

Iveda is targeting the sale of its security and surveillance products and services to the following primary customer groups: commercial entities, educational facilities, golf courses, gated residential communities, automotive lot, small unattended businesses, construction sites, municipalities, government, and law enforcement. Iveda has based its strategy to target these consumers on a number of assumptions, some or all of which could prove to be incorrect.

Even if markets for its products and services develop, Iveda could achieve a smaller share of these markets than Iveda currently anticipates. Achieving market share will require substantial marketing efforts and expenditure of significant funds to inform customers of the distinctive characteristics and benefits of using Iveda's products and services. Iveda cannot assure investors that its marketing efforts will result in the attainment of sufficient market share to become profitable.

*Iveda Believes Industry Trends Support Its Open Source Systems, But If Trends Reverse, Iveda May Experience Decreased Demand.*

The security and surveillance industry is characterized by rapid changes in technology and customer demands. Management believes that the existing market preference for open source systems (systems capable of integrating a wide range of products and services through community and private based cooperation, such as the Internet, Linux, and certain cameras used in Iveda's business) is strong and will continue for the foreseeable future.

While Iveda is able to convert CCTV and analog systems for use with Iveda's monitoring services, certain systems may not be convertible in the future, and to the extent that customers prefer to install these systems, it would be more difficult to sell Iveda's services since customers would be required to spend additional funds to acquire new cameras that Iveda would be able to monitor.

***Risks Associated with the Surveillance and Remote Security Industry***

As a result of providing its products and services, Iveda is exposed to risks associated with participation in the security and surveillance industry. These risks are summarized below.

*Iveda Depends On Third Party Manufacturers And Suppliers For The Products It Sells.*

Iveda has relationships with a number of third party manufacturers and suppliers, including Axis Communications, Milestone, Scansource, Anixter, and Dotworkz for cameras, accessories, and software and Dell for servers and network equipment, for the supply of all of the hardware components of Iveda's products. Iveda has signed reseller and development partner agreements with Axis Communications and Milestone. For customers in Taiwan, its subsidiary purchased equipment locally and software from their partner company in Hong Kong. Risks associated with Iveda's dependence upon third party manufacturing relationships include: (i) reduced control over delivery schedules; (ii) lack of control over quality assurance; (iii) poor manufacturing yields and high costs; (iv) potential lack of adequate capacity during periods of excess demand; and (v) potential misappropriation of Iveda's intellectual property. Although

Iveda depends on third party manufacturers and suppliers for products it sells, risks are minimized because it does not depend on one manufacturer and supplier. It utilizes an open platform, which means that in order to deliver its services, it does not discriminate based on camera brand or manufacturer and its services can be used with a wide array of products.



Iveda does not know if it will be able to maintain third party manufacturing and supply contracts on favorable terms, if at all, or that its current or future third party manufacturers and suppliers will meet its requirements for quality, quantity or timeliness. Iveda's success depends in part on whether its manufacturers are able to fill the orders it places with them in a timely manner. If Iveda's manufacturers fail to satisfactorily perform their contractual obligations or fill purchase orders Iveda places with them, Iveda may be required to pursue replacement manufacturer relationships.

If Iveda is unable to find replacements on a timely basis, or at all, Iveda may be forced to either temporarily or permanently discontinue the sale of certain products and associated services, which could expose it to legal liability, loss of reputation and risk of loss or reduced profit. Management believes that Iveda's present suppliers offer products that are superior to comparable products available from other suppliers. In addition, Iveda has development partner relationships with many of its present suppliers, which provides it with greater control over future enhancements to the off-the-shelf products Iveda sells. Iveda's business, results of operation and reputation would be adversely impacted if Iveda is unable to provide quality products to its customers in a timely manner.

Iveda could also be adversely affected by an increase in its manufacturers' prices for its product components or a significant decline in Iveda's manufacturers' financial condition. If Iveda's relationship with any one of its manufacturers is terminated and Iveda is not successful in establishing a relationship with an alternative manufacturer who offers similar services at similar prices, Iveda's costs could increase, adversely affecting its operations.

*Iveda Operates In A Highly-Competitive Industry And its Failure To Compete Effectively May Adversely Affect Its Ability To Generate Revenue.*

Although management believes that there is, at this time, no competitor that offers a similar package of services to the package offered by Iveda, management is aware of similar products and services which compete indirectly with Iveda's products and services. In management's opinion, companies providing indirect competition include Westec Interactive, Iverify, Xtreme Surveillance, Viewpoint, byRemote, and Monitoring Partners. Some companies may also be developing similar products and services, including companies that may have significantly greater financial, technical and marketing resources, larger distribution networks, and generate greater revenue and have greater name recognition than Iveda. These companies may develop security products and services that are superior to those offered by Iveda. Such competition may potentially affect Iveda's chances of achieving profitability.

Some of Iveda's current and future competitors may conduct more extensive promotional activities and may offer lower prices to customers than Iveda, which could allow them to gain greater market share or prevent Iveda from increasing its market share. In the future, Iveda may need to decrease its prices if Iveda's competitors lower their prices. Iveda's competitors may be able to respond more quickly to new or changing opportunities, technologies and customer requirements. To be successful, Iveda must carry out its business plan, establish and strengthen its brand awareness through marketing, effectively differentiate its services from those of its competitors and build its reseller network, while maintaining superior levels of service, which management believes is what will ultimately differentiate

Iveda's services from any similar services its competitors may develop in the future. To achieve this Iveda may have to substantially increase marketing and development activities in order to compete effectively.

*Future Legislation Or Governmental Regulations Or Policies Could Have A Significant Impact On Iveda's Operations.*

While Iveda is presently subject only to licensing requirements related to its contracting activities, for which it holds low voltage contractors' licenses in California and Arizona, the security and surveillance industry as a whole is subject to regulation. Iveda may be subject to additional regulation in the future. Future changes in laws or regulations could require Iveda to change the way it operates, which could increase costs or otherwise disrupt operations. In addition, failure to comply with any applicable laws or regulations could result in substantial fines or revocation of any required operating permits and licenses. If laws and regulations change or it fails to comply in the future, Iveda's financial condition, results of operations and cash flows could be materially and adversely affected.

*Regulation Of The Telecommunications Industry And The Internet May Impact Iveda's Operations*

Aspects of Iveda's operations may be, or become, subject to regulations governing the Internet. There can be no assurance that government agencies will not increasingly regulate Internet-related services. Increased regulation may slow Iveda's growth, and legislation could be enacted that would prohibit certain forms of telecommunication critical to Iveda's operations. Such regulation may also negatively impact the cost of doing business and materially adversely affect Iveda's business, financial condition and results of operations.

*The Failure Of Iveda's Systems Could Result In A Material Adverse Effect.*

Iveda utilizes third party data centers in Arizona. These data centers are designed to meet the most stringent requirements established by the Telecommunications Industry Association's Telecommunications Infrastructure Standards for Data Centers, or TIA-942. The data centers transmit data to Iveda's monitoring system via a dedicated fiber connection, and offers the greatest reliability provided by the industry always-on service level and offers a 100% uptime Service Level Agreement, due to a number of back-up measures. Iveda's operations are dependent upon its ability to support a complex network infrastructure and avoid damage to both its monitoring center and the data center from fires, earthquakes, floods, hurricanes, power losses, war, terrorist acts, telecommunications failures, computer viruses, physical and electronic break-ins, and similar natural or manmade events. The occurrence of a natural disaster, intentional or unintentional human error or actions, or other unanticipated problem could cause interruptions in the services provided by Iveda, and resulting losses by Iveda's customers. The property and business interruption insurance Iveda carries may not have coverage adequate to compensate it fully for losses that may occur. Any damage or failure that causes interruptions in the service provided by Iveda could have a material adverse effect on its business, operating results and financial condition.

Iveda has experienced individual camera failures or outages in the past, and will likely experience future individual camera failures or outages that disrupt the monitoring of those cameras. Iveda's revenue depends in large part on maintaining the operability of its surveillance systems. Accordingly, the performance, reliability and availability of Iveda's network, servers for Iveda's corporate operations and infrastructure are critical to Iveda's reputation and Iveda's ability to attract and retain customers.

Iveda is continually expanding and enhancing its technology and network infrastructure and other technologies to accommodate substantial increases in the volume of traffic on its network and the overall size of its customer base. Iveda may be unsuccessful in these efforts or Iveda may be unable to project accurately the rate or timing of these increases. The data centers that Iveda currently use have significant additional bandwidth available should Iveda need it for expanding its operations. Approximately three to four weeks elapses between signing a new customer and commencing hosting and/or surveillance of that customer's cameras, which provides Iveda with what management believes to be sufficient time to acquire additional bandwidth if needed. However, Iveda's failure, or Iveda's suppliers' failure, to achieve or maintain high data transmission capacity could significantly reduce consumer demand for Iveda's services.

*If Iveda's Security Measures Are Breached And Unauthorized Access Is Obtained, Existing And Potential Customers Might Not Perceive Iveda's Services As Being Secure And Might Terminate Or Fail To Purchase Iveda's Services.*

Iveda's business involves the monitoring of cameras that may be recording sensitive areas of its customers' facilities, and as a result, Iveda utilizes security measures that are comparable to those used by banks in providing online banking services. Iveda has also partnered with a company in India that specializes in cloud security, adding a layer of security on the actual devices such cameras and video encoders. No security measures are completely secure, however, and, for example, hackers or individuals who attempt to breach its network security could, if successful, cause interruptions in Iveda's services. If Iveda experiences any breaches of its network security or sabotage, Iveda might be required to expend significant capital and resources to protect against or alleviate these problems. Iveda may not be able to remedy any problems caused by hackers or saboteurs in a timely manner, or at all. Because techniques used to obtain unauthorized access or to sabotage systems change frequently and generally are not recognized until launched against a target, Iveda may be unable to anticipate these techniques or to implement adequate preventative measures. If an actual or perceived breach of Iveda's security occurs, the perception of the effectiveness of Iveda's security measures and Iveda's reputation could be harmed and Iveda could lose current and potential customers.

*The Timing Of Iveda's Revenues Can Vary Depending On How Long Customers Take To Evaluate Iveda's Services.*

It is difficult to forecast the timing of revenues in the security industry because the development period for a customized system or solution may be lengthy, larger customers may need a significant amount of time to evaluate products before purchasing them and, in the case of governmental customers, sales are dependent on budgetary and other bureaucratic processes. The period between initial customer contact and a purchase by a customer varies greatly depending on the customer, and historically has ranged from days to weeks. During the evaluation period, customers may defer or scale down proposed orders of products or systems for various reasons, including (i) changes in budgets and purchasing priorities; (ii) a reduced need to upgrade existing systems; (iii) deferrals in anticipation of enhancements or new products; (iv) introduction of products by competitors; and (v) lower prices offered by competitors.

*Iveda Will Rely On Both Iveda's Internal Sales Force And Resellers To Distribute Its Security Products And Services To Customers.*

Iveda relies on both Iveda's internal sales force and resellers to distribute its security products and services to its customers. As of the date of this report, Iveda has signed many resellers and independent agents, and anticipates adding more as Iveda implements its business plan. Iveda plans to continue its internal sales activity for the foreseeable future to market its products and services until its resellers are completely trained and mobilized. If Iveda's relationship with any of its larger resellers is terminated and Iveda is not successful in establishing a relationship with an alternative reseller who offers similar services at similar prices, Iveda's business could decline depending on the level of revenue generated by that reseller.

*Government Contracts Generally Contain Rights And Remedies Which Could Reduce The Value Of Such Contracts, Or Result In Losses.*

Iveda presently provides its products and services for certain state and local government customers, and obtained certification of SAFETY Act Designation by the Department of Homeland Security under the Support Anti-terrorism by Fostering Effective Technologies Act, or SAFETY Act, in April 2009. Although not significant sources of revenue at this time, government contracts often contain provisions that give the governments that are party to those contracts certain rights and remedies not typically found in private commercial contracts, including provisions enabling the governments to: (i) terminate or cancel existing contracts for convenience; (ii) in the case of the U.S. government, suspend the contracting company from doing business with a foreign government or prevent the company from selling its products in certain countries; (iii) audit and object to the company's contract-related costs and expenses, including allocated indirect costs; and (iv) change specific terms and conditions in the company's contracts, including changes that would reduce the value of its contracts.

In addition, many jurisdictions have laws and regulations that deem government contracts in those jurisdictions to include these types of provisions, even if the contract itself does not contain them. If a government terminates a contract with Iveda for convenience, Iveda may not be able to recover its incurred or committed costs, any settlement expenses or profit on work completed prior to the termination. If a government terminates a contract for default, Iveda may not recover those amounts and, in addition, Iveda may be liable for any costs incurred by a government in procuring undelivered items and services from another source. Further, an agency within a government may share information regarding Iveda's termination with other government agencies. As a result, Iveda's on-going or prospective relationships with such other government agencies could be impaired.

*There Is A Shortage Of Qualified Electricians. Since The Majority Of Iveda's Work Is Performed By Electricians, This Shortage May Negatively Impact Iveda's Business, Including Its Ability To Grow.*

There is a shortage of qualified electricians in the United States. In order to conduct some of Iveda's business, it is necessary for Iveda or Iveda's resellers to employ electricians and have those electricians qualified in the states where they do business. Iveda's ability to increase productivity and profitability may be limited by its and its resellers' ability to employ, train and retain skilled electricians required to meet Iveda's customers' needs. Accordingly there can be no assurance, among other things, that:

- Iveda or Iveda's resellers will be able to maintain the skilled labor force necessary to operate efficiently;
- Iveda's or Iveda's resellers' labor expenses will not increase as a result of a shortage in the skilled labor supply; and
- Iveda or Iveda's resellers will be able to maintain the skilled labor force necessary to implement Iveda's planned growth.

*The Estimates Iveda Uses In Placing Bids Could Be Materially Incorrect, Resulting In Possible Losses.*

Iveda currently generates, and expects to continue to generate, a significant portion of its revenues for product sales and installation under fixed price contracts. The cost of labor and materials, however, may vary significantly from the costs Iveda originally estimates. Variations from estimated contract costs along with other risks inherent in performing fixed price contracts may result in actual revenue and gross profits for a project differing from those Iveda originally estimated and could result in losses on projects. Depending upon the size of a particular project, variations from estimated contract costs can have a significant impact on Iveda's operating results.





### ***Risks Related to Iveda's Intellectual Property***

#### ***Iveda Depends On its Intellectual Property.***

Iveda's success and ability to compete depends in part on Iveda's proprietary database, Cerebro, the security information and reporting web service developed and used by Iveda internally, and on the process by which Iveda integrates existing third party products into a video hosting and monitoring solution. If any of Iveda's competitors copy or otherwise gain access to Iveda's proprietary technology or develop similar technologies independently, Iveda may not be able to compete as effectively. Iveda considers its proprietary database invaluable to its ability to continue to develop and maintain the goodwill and recognition associated with its brand. Iveda does not currently hold any patents. The measures Iveda takes to protect its technologies, and other intellectual property rights, which presently are based upon trade secrets, may not be adequate to prevent their unauthorized use.

If Iveda is unable to protect its intellectual property, Iveda's competitors could use Iveda's intellectual property to market products, services and technologies similar to Iveda's, which could reduce demand for Iveda's products, services and technologies. Iveda may be unable to prevent unauthorized parties from attempting to copy or otherwise obtain and use its products or technology. Policing unauthorized use of Iveda's technology is difficult, and Iveda may not be able to prevent misappropriation of its technology, particularly in foreign countries where the laws may not protect its intellectual property as fully as those in the United States. Others may circumvent the trade secrets, trademarks and copyrights that Iveda currently or in the future owns. Iveda does not have patent protection with respect to its software or systems, although management is considering seeking such protection.

Iveda seeks to protect its proprietary intellectual property, which includes intellectual property that may only be protectable as a trade secret, in part by confidentiality agreements with its employees, consultants and business partners. These agreements afford only limited protection and may not provide us with adequate remedies for any breach or prevent other persons or institutions from asserting rights to intellectual property arising out of these relationships. See "Business – Other Information – Proprietary Rights."

#### ***Iveda Could Incur Substantial Costs Defending its Intellectual Property From Infringement By Others.***

Unauthorized parties may attempt to copy aspects of Iveda's proprietary software or to obtain and use its other proprietary information. Litigation may be necessary to enforce Iveda's intellectual property rights, to protect its trade secrets and to determine the validity and scope of the proprietary rights of others. Iveda may not have the financial resources to prosecute any infringement claims that it may have. Any litigation could result in substantial costs and diversion of resources with no assurance of success.

*Iveda Could Incur Substantial Costs Defending Against Claims That Its Products Infringe On The Proprietary Rights Of Others.*

The scope of any intellectual property rights that Iveda has is uncertain and may not be sufficient to prevent infringement claims against Iveda or claims that Iveda has violated the intellectual property rights of third parties. Iveda was named as a defendant in two patent-related lawsuits, one of which has been settled. See “Item 3. Legal Proceedings” below for details.

Competitors may have filed applications for or may have been issued patents and may obtain additional patents and proprietary rights relating to products or processes that compete with or are related to Iveda’s products and services. The scope and viability of these patents, the extent to which Iveda may be required to obtain licenses under these patents or under other proprietary rights and the cost and availability of licenses are unknown, but these factors may limit Iveda’s ability to market its products and services.

Third parties could claim infringement by us with respect to any patents or other proprietary rights that they hold, and Iveda cannot assure investors that Iveda would prevail in any such proceeding as the intellectual property status of its current and future competitors’ products and services is uncertain. Any infringement claim against Iveda, whether meritorious or not, could be time-consuming, result in costly litigation or arbitration and diversion of technical and management personnel, or require Iveda to develop non-infringing technology or to enter into royalty or licensing agreements.

Iveda might not be successful in developing or otherwise acquiring rights to non-infringing technologies. Royalty or licensing agreements, if required, may not be available on terms acceptable to Iveda, or at all, and could significantly harm Iveda's business and operating results. A successful claim of infringement against Iveda or Iveda's failure or inability to license the infringed or similar technology could require it to pay substantial damages and could harm its business because Iveda would not be able to continue operating its surveillance products without incurring significant additional expense.

In addition, to the extent Iveda agrees to indemnify customers or other third parties against infringement of the intellectual property rights of others, a claim of infringement could require Iveda to incur substantial time, effort and expense to indemnify these customers and third parties and could disrupt or terminate their ability to use, market or sell Iveda's products. Furthermore, Iveda's suppliers may not provide it with indemnification in the event that their products are found to infringe upon the intellectual property rights of any third parties, and if they do not, Iveda would be forced to bear any resulting expense.

### ***Risk Factors Involved In Being a Public Company***

#### *Our Shares Are "Penny Stock."*

In general, "penny stock" includes securities of companies which are not listed on the principal stock exchanges and have a bid price in the market of less than \$5.00; and companies with net tangible assets of less than \$2 million (\$5 million if the issuer has been in continuous operation for less than three years), or which has recorded revenues of less than \$6 million in the last three years. As "penny stock," Iveda's stock therefore is subject to Rule 15c-2, which imposes additional sales practice requirements on broker-dealers which sell such securities to persons other than established customers and "accredited investors" (generally, individuals with net worth in excess of \$1 million or annual incomes exceeding \$200,000, or \$300,000 together with their spouses, or individuals who are the officers or directors of the issuer of the securities). For transactions covered by Rule 15c-2, a broker-dealer must make a special suitability determination for the purchaser and have received the purchaser's written consent to the transaction prior to sale. Consequently, this rule may adversely affect the ability of broker-dealers to sell Iveda's stock, and therefore may adversely affect Iveda stockholders' ability to sell the stock in the public market.

#### *There Is A Limited Market For Our Common Stock.*

Only a very limited trading market currently exists for Iveda's common stock. As a result, any broker-dealer that makes a market in our stock or other person that buys or sells our stock could have a significant influence over its price at any given time. The Company cannot assure its shareholders that a market for its stock will be sustained. There is no assurance that our shares will have any greater liquidity than shares which do not trade on a public market.

*Our Reporting Obligations as a Public Company Are Costly.*

Operating a public company involves substantial costs to comply with reporting obligations under federal securities laws. These reporting obligations will increase Iveda's operating costs significantly from historical norms prior to becoming a public company. Iveda may not reach sufficient size to justify its public reporting status. If it were forced to become a private company, then its shareholders may lose their ability to sell their shares and there would be substantial costs associated with becoming a private company.

## **ITEM 1B. UNRESOLVED STAFF COMMENTS**

As a smaller reporting company, the Company is not required to provide Item 1B disclosure in this Annual Report.

## **ITEM 2. PROPERTIES**

Iveda's executive offices are located at 1201 S. Alma School Rd., Suite 8500, Mesa, Arizona 85210, where the Company currently leases approximately 5,779 square feet of office space for \$8,668.50 per month from Mesa Financial Plaza Investors, LLC. The lease expires in October of 2016. The Company is not affiliated with its lessor. Although the Company believes that its current facilities are adequate for the foreseeable future, additional office space may be needed as additional employees are hired. The Company's current building has the fiber necessary for the Company's projected bandwidth requirements and it has significant additional space available for additional employees and remote monitoring stations.

The Company has a three-year data center services agreement with i/o Data Center datacenter (highest industry rating) in Phoenix and Scottsdale, Arizona with a 100% uptime guarantee. The agreement commenced on October 1, 2011. Iveda is not affiliated with i/o Data Center.

The Company also signed a three-year data center services agreement with Phoenix NAP, LLC on March 22, 2012 in Phoenix, Arizona. This data center also has 100% uptime guarantee. The Company's management believes that all facilities occupied by the Company are adequate for present requirements and that the Company's current equipment is in good condition and is suitable for the operations involved.

MegaSys's executive offices are located at 2F, -15, No. 14, Lane 609, Sec. 5 Chongxin Rd., Sanchong City, Taipei, County 241, Taiwan (R.O.C.), where the Company currently leases two suites totaling approximately 4,838 square feet of office space for \$2,378 per month. The leases expire in June and July 2013. The Company is not affiliated with its lessor. Although the Company believes that its current facilities are adequate for the foreseeable future, additional office space may be needed as additional employees are hired.

## **ITEM 3. LEGAL PROCEEDINGS**

On April 11, 2011, Iveda was named as a defendant in a lawsuit filed in United States District Court for the District of Delaware. The complaint alleges that Iveda's Real Time Remote Video Surveillance System infringes patents licensed by the plaintiff and seeks an adjudication that the specified patent has been infringed, awards of unspecified damages and permanent injunctions enjoining further acts of infringement. *See Walker Digital, LLC v. Arrow Security, Inc.*, No. 10-CV-00310 (D. Del.) (April 11, 2011). On March 20, 2013, the parties entered into a Settlement and License Agreement (the "WD Settlement Agreement") resolving this dispute. Under the terms of the WD Settlement Agreement, Iveda received a fully paid up license to use the patents that are the subject of the litigation in exchange for payment of a one-time fee. The plaintiff also agreed to release Iveda from all claims of infringement of the subject patents and to dismiss with prejudice all claims and counter claims in the pending litigation within 5 days of receipt of the specified consideration. We do not expect this proceeding or the WD Settlement Agreement to have any material adverse effect on the Company's financial condition or results of operations.

#### **ITEM 4. MINE SAFETY DISCLOSURES.**

Not applicable.

**PART II****ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES****Market Information**

Iveda shares trade on the OTC Bulletin Board under the symbol "IVDA".

Set forth in the table below is information with respect to the high and low bid quotations of our common stock for the periods indicated, as reported by the OTC Bulletin Board. The quotations represent inter-dealer prices without retail mark-ups, mark-downs or commissions, and may not necessarily represent actual transactions. The quotations may be rounded for presentation. There is an absence of an established trading market for Iveda's common stock, as the market is limited, sporadic, and highly volatile, all of which may affect the prices listed below.

| 2013  | High<br>Bid | Low<br>Bid |
|---|-------------|------------|
| Quarter Ended March 31, 2013 (through March 18, 2013) | \$2.00      | \$1.30     |

| 2012                             | High<br>Bid | Low<br>Bid |
|----------------------------------|-------------|------------|
| Quarter Ended December 31, 2012  | \$1.25      | \$1.00     |
| Quarter Ended September 30, 2012 | \$1.20      | \$.95      |
| Quarter Ended June 30, 2012      | \$1.25      | \$.99      |
| Quarter Ended March 31, 2012     | \$1.50      | \$.97      |

| 2011                             | High<br>Bid | Low<br>Bid |
|----------------------------------|-------------|------------|
| Quarter Ended December 31, 2011  | \$1.05      | \$.90      |
| Quarter Ended September 30, 2011 | \$1.11      | \$.85      |
| Quarter Ended June 30, 2011      | \$1.10      | \$.90      |
| Quarter Ended March 31, 2011     | \$1.05      | \$.85      |

There is limited trading activity in Iveda's securities, and there can be no assurance that a regular trading market for our common stock will be sustained.

### **Security Holders**

As of March 15, 2013, we had 22,611,048 shares of our common stock outstanding held by 224 shareholders of record, exclusive of shares held in street name. We have no preferred stock outstanding.

### **Dividends**

Iveda has never paid cash dividends on its capital stock. Iveda currently intends to retain all earnings, if any, to finance the growth and development of its business. Iveda does not anticipate paying any cash dividends in the foreseeable future.



**Equity Compensation Plans (As of December 31, 2012)**

On January 18, 2010, the Company adopted the 2010 Stock Option Plan (the “2010 Option Plan”), which allows the Board to grant options to purchase up to 1,000,000 shares of common stock to directors, officers, key employees, and service providers of the Company. In 2011, the 2010 Option Plan was amended to increase the number of shares issuable under the 2010 Option Plan to 3,000,000 shares. The shares under the 2010 Option Plan are registered with the SEC under Forms S-8 filed on February 2, 2010 and June 24, 2011. As of December 31, 2012, options to purchase 3,877,783 shares were outstanding under the 2010 Option Plan.

The Company has also periodically issued warrants to purchase shares of common stock as equity compensation to officers, directors, employees, and consultants. As of December 31, 2012, warrants to purchase 2,797,219 shares of common stock were outstanding, all of which were issued as equity compensation. Terms of these warrants are comparable to the terms of the outstanding options.

| Plan Category  | Number of securities to be issued upon exercise of outstanding options, warrants and rights | Weighted-average exercise price of outstanding options, warrants and rights | Number of securities remaining available for future issuance under equity compensation plans |
|--|---|---|--|
| Equity compensation plans approved by shareholders     | 5,038,512   | \$ 0.91   | 9,138,217  |
| Equity compensation plans not approved by shareholders | 2,797,219   | \$ 1.33   | -  |
| Total  | 7,835,731   | \$ 1.06   | 9,138,217  |

**Recent Sales of Unregistered Securities**

All sales of unregistered securities during the year ended December 31, 2012 were previously disclosed.

**ITEM 6. SELECTED FINANCIAL DATA**

As a smaller reporting company, the Company is not required to provide Item 6 disclosure in this Annual Report.

## ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

*The following discussion should be read in conjunction with our audited and unaudited financial statements and associated notes appearing elsewhere in this report.*

### Overview

Iveda Solutions, Inc. began operations on January 24, 2005 under the name of IntelaSight, Inc. On October 15, 2009, IntelaSight became a wholly-owned subsidiary of Charmed Homes, Inc., which changed its name to Iveda Corporation. All Company operations were conducted through IntelaSight until December 31, 2010, at which time IntelaSight merged with and into Iveda Corporation and changed its name to Iveda Solutions. On April 30, 2011, the Company completed its acquisition of MegaSys. See "Item 1. Business – General." Unless otherwise noted, all references to "Iveda," "Company," "we," "us" and "our" hereafter in this section refer to the current business of Iveda Solutions, Inc.

Iveda installs video surveillance equipment, primarily for security purposes, and provides video hosting, archiving and real-time remote surveillance services to a variety of businesses and organizations. The accompanying financial statements have been prepared assuming that Iveda will continue as a going concern. Iveda generated accumulated losses of approximately \$15 million through December 31, 2012.

A multi-step plan was adopted by management to enable the Company to continue to operate and begin to report operating profits. The highlights of that plan are as follows:

The Board of Directors approved the Company to engage with a financial capital markets advisor in connection with a potential capital financial transaction to raise up to \$30 million in long-term financing.

The Board of Directors also approved the Company to raise up to an aggregate amount of \$3 million in bridge financing in advance of the long-term financing.

The Company established reseller distribution channels to increase the scope of the Company's marketing activities with low cost to the Company.

The Company signed a cooperation agreement with an R&D organization in Taiwan to develop new products and services.

The Company may evaluate and consider merger and/or acquisition activities.

### ***Application of Critical Accounting Policies***

We have identified the policies below as critical to our business operations and the understanding of our results of operations. The impact and any associated risks related to these policies on our business operations are discussed throughout Management's Discussion and Analysis of Financial Condition and Results of Operations when such policies affect our reported or expected financial results.

In the ordinary course of business, we have made a number of estimates and assumptions relating to the reporting of results of operations and financial condition in the preparation of our financial statements in conformity with accounting principles generally accepted in the United States. We base our estimates on historical experience and on various other assumptions that we believe are reasonable under the circumstances. The results form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results could differ significantly from those estimates under different assumptions and conditions. We believe that the following discussion addresses our most critical accounting policies, which are those that are most important to the portrayal of our financial condition and results of operations and require our most difficult, subjective, and complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain.

The material estimates for Iveda are that of the stock based compensation recorded for options and warrants issued and the income tax valuation allowance recorded for deferred tax assets. The fair values of options and warrants are determined using the Black-Scholes option-pricing model. Iveda has no historical data on the accuracy of these estimates. The estimated sensitivity to change is related to the various variables of the Black-Scholes option-pricing model stated below. The specific quantitative variables are included in the Notes to the Financial Statements. The estimated fair value of options and warrants is recognized as expense on the straight-line basis over the options' and warrants' vesting periods. The fair value of each option and warrant granted is estimated on the date of grant using the Black-Scholes option-pricing model with the expected life, dividend yield, expected volatility, and risk free interest rate weighted-average assumptions used for options and warrants granted. Expected volatility for 2011 and 2012 was estimated by using the Dow Jones U.S. Industry indexes sector classification methodology for industries similar to the Company. The risk-free rate for periods within the contractual life of the option and warrant is based on the U.S. Treasury yield curve in effect at the grant date. The expected life of options and warrants is based on the average of three public companies offering services similar to Iveda.

### **Impairment of Long-Lived Assets**

We have a significant amount of property and equipment primarily consisting of leased equipment. The Company reviews the recoverability of the carrying value of long-lived assets using the methodology prescribed in ASC 360 "Property, Plant and Equipment." Recoverability of long-lived assets to be held and used is measured by a comparison of the carrying amount of an asset to the undiscounted future net operating cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured as the amount by which the carrying value of the assets exceeds their fair value.

### **Basis of Accounting and Going Concern**

Iveda's financial statements have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America. In addition, the accompanying financial statements have been prepared assuming that the Company will continue as a going concern, which contemplates the realization of assets and the liquidation of liabilities in the normal course of business. The Company generated accumulated losses of approximately \$15 million through December 31, 2012 and has insufficient working capital and cash flows to support operations. These factors raise substantial doubt about the Company's ability to continue as a going concern. The financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amounts and classification of liabilities that might result from this uncertainty.

### **Revenue and Expense Recognition**

The Company recognizes revenue when persuasive evidence of an arrangement exists, title transfer has occurred, the price is fixed or readily determinable, and collectability is reasonably assured. The Company recognizes revenue in accordance with ASC 60, "Revenue Recognition." Sales are recorded net of sales returns and discounts, which are estimated at the time of shipment based upon historical data. Revenues from monitoring services are recognized when the services are provided. Expenses are recognized as incurred.

Revenues from fixed-price equipment installation contracts are recognized on the percentage-of-completion method. The percentage completed is measured by the percentage of costs incurred to date to estimated total costs for each contract. This method is used because management considers expended costs to be the best available measure of progress on these contracts. Because of inherent uncertainties in estimating costs and revenues, it is at least reasonably possible that the estimates used will change.

Contract costs include all direct material, subcontractors, labor costs, and equipment costs and those indirect costs related to contract performance. General and administrative costs are charged to expense as incurred. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are determined. Changes in job performance, job conditions, and estimated profitability may result in revisions to costs and income and are recognized in the period in which the revisions are determined. Changes in estimated job profitability resulting from job performance, job conditions, contract penalty provisions, claims, change orders, and settlements are accounted for as changes in estimates in the current period. Profit incentives are included in revenues when their realization is reasonably assured. Claims are included in revenues when realization is probable and the amount can be reliably estimated.

The liability, "Billings in excess of costs and estimated earnings on uncompleted contracts," represents billings in excess of revenues recognized.

### **Stock-Based Compensation**

On January 1, 2006, the Company adopted the fair value recognition provisions of ASC 718, *Share-Based Payment*, which requires the recognition of an expense related to the fair value of stock-based compensation awards. The Company elected the modified prospective transition method as permitted by ASC 718. Under this transition method, stock-based compensation expense for the years ended December 31, 2011 and 2010 includes compensation expense for stock-based compensation granted on or after the date ASC 718 was adopted based on the grant-date fair value estimated in accordance with the provisions of ASC 718. The Company recognizes compensation expense on a straight-line basis over the requisite service period of the award. The fair value of stock-based compensation awards granted prior to, but not yet vested as of December 31, 2010 and 2009, were estimated using the "minimum value method" as prescribed by original provisions of ASC 718, *Accounting for Stock-Based Compensation*, therefore, no compensation expense is recognized for these awards in accordance with ASC 718. The Company recognized \$248,072 and \$515,419 of stock-based compensation expense for the years ended December 31, 2012 and 2011, respectively.

## Acquisition of MegaSys

On April 30, 2011, the Company acquired Sole-Vision Technologies, Inc. (doing business as MegaSys), a corporation organized under the laws of the Republic of China (“MegaSys”), pursuant to the share exchange agreement (the “Agreement”) dated March 21, 2011 and a related side agreement of even date (the “Side Agreement”), by and among the Company, MegaSys, and the shareholders of MegaSys (the “MegaSys Shareholders”). Pursuant to the Agreement (i) the Company acquired 100% of the issued and outstanding shares of MegaSys Common Stock in exchange for the issuance to the MegaSys Shareholders of 1,700,000 shares of Common Stock of the Company (the “Exchange”), and (ii) MegaSys became a wholly owned subsidiary of Iveda. The Side Agreement provides that the MegaSys Shareholders are entitled to receive up to an additional 2,000,000 shares of Common Stock of the Company upon achievement by MegaSys of certain financial milestones set forth therein. The Exchange was approved by Taiwan’s Foreign Investment Commission Agency.

MegaSys is a Taiwanese company specializing in deploying video surveillance systems for airports, commercial buildings, government customers, data centers, shopping centers, hotels, banks, and Safe City initiatives in Taiwan and other neighboring countries. MegaSys integrates security surveillance products, software and services to provide integrated security solutions to the end user. Most of MegaSys’s revenues are derived from one-time sales, which differs from Iveda’s business model of on-going monitoring revenues. MegaSys does not own any proprietary technology or intellectual property other than certain trademarks in China and Taiwan used in its business.

Management believes that the acquisition of MegaSys provides the following potential benefits to the Company’s business:

• MegaSys has an established presence and credibility in, and provides the Company with access to, the Asian market.

• Management believes that the Company will be able to leverage MegaSys’s relationships in Asia for cost-effective research and development of new product offerings and cost reduction of current product offerings.

• Management expects to be able to source products directly using MegaSys’s product sourcing expertise to enhance the Company’s custom integration capabilities.

• Management expects the Company will benefit from cost reductions for infrastructure equipment (servers, storage devices, network switches, and Super Wifi technologies) through a direct OEM relationship.

- Management believes that MegaSys enhances the global distribution potential for Iveda’s products and services.

MegaSys is expected to benefit from the Company's expertise in cloud-based video surveillance and access to the U.S. markets for its products.



The company does not expect to derive significant revenues from prior MegaSys customer installations. However, the prior MegaSys customer base helps to establish credibility for the Company to market its products and services in the Taiwanese and other Asian marketplaces. There can be no assurance that the Company will generate material future revenue from MegaSys's customers at the time of the Exchange.

### **Results of Operations for the Year Ended December 31, 2012 Compared to the Year Ended December 31, 2011**

**Net Revenue.** We recorded net consolidated revenue of \$3,608,998 for the year ended December 31, 2012, compared to \$2,818,729 for the year ended December 31, 2011, an increase of \$790,269 or 28%. In fiscal 2012, our recurring service revenue was \$605,840 or 17% of consolidated net revenue, and our equipment sales and installation revenue was \$2,815,150 or 78% of net revenue, compared to 617,437 or 22% of net revenue for recurring service and \$2,081,923 or 74% of net revenue for equipment sales and installation revenue in 2011. Revenues in our U.S. operations were primarily derived from our recurring monthly service revenue, which represents 79% of U.S. net income. This material increase in total revenue in 2012 compared to the same period in 2011 is attributable primarily to increased equipment sales from our MegaSys subsidiary.

**Cost of Revenue.** Total cost of revenue was \$3,230,495 (89% of revenues; gross margin of 11%) for the year ended December 31, 2012, compared to \$2,154,221 (76% of revenues; 24% gross margin) for the year ended December 31, 2011, an increase of \$1,076,274 or 50%. The increase in cost of revenue and decrease of gross margin was primarily due to the increase of equipment sales and installation, which normally garner lower gross margin, combined with a \$267,087 delay penalty for late completion of a project with New Taipei Police Station in Taiwan. This delay penalty was a reduction to revenue and in turn negatively impacted the gross margin percentage. This delay penalty is being contested with New Taipei Police Station and may be recouped during 2013, though currently there is no certainty of this outcome. Approximately 95% of MegaSys' revenue, with lower gross margin, was derived from equipment sales and installation.

**Operating Expenses.** Operating expenses were \$4,223,455 for the year ended December 31, 2012, compared to \$5,049,966 for the year ended December 31, 2011, a decrease of \$826,511 or 16%. The significant decrease in operating expenses was largely due to an impairment charge to goodwill during 2011 of \$955,710. Without the goodwill charge in 2012 compared to 2011, operating expenses increased by \$129,199, or 3%. The insignificant increase was attributable to professional fees associated with capital raises, general staffing expenses, and international travel expenses.

**Loss from Operations.** Loss from operations decreased to \$3,844,952 for the year ended December 31, 2012, compared to \$4,385,458 for the year ended December 31, 2011, a decrease of \$540,506 or 12%. The majority of this decrease was due to the one-time goodwill impairment charge in 2011. The majority of the loss, \$3,416,026, was from our U.S. operations and the remaining \$425,901 was from our operations in Taiwan.



**Other Expense-Net.** Other expense-net was \$79,477 for the year ended December 31, 2012, compared to \$30,566 for the year ended December 31, 2011, an increase of \$48,911 or 160%. The expense-net increase is primarily in interest expense which relates to \$79,759, offset by interest income of \$806 and loss on foreign currency exchange of \$524.

**Net Loss.** Net loss was \$3,841,927 for the year ended December 31, 2012, compared to \$4,463,051 for the year ended December 31, 2011. The decrease of \$ 621,124 or 14% in net loss was caused by a decrease of \$955,710 in impairment goodwill charges, off-set by the insignificant increase in other operating expenses and the lower gross margin from MegaSys Taiwan equipment sales.

### **Liquidity and Capital Resources**

As of December 31, 2012, we had cash and cash equivalents of \$42,920 in our domestic business and \$71,542 in our foreign business, compared to \$341,570 in our domestic business and \$508,794 in our foreign business as of December 31, 2011. This decrease in our cash and cash equivalents is primarily a result of timing differences in collections of accounts receivable, which were collectively \$1,051,920 higher as of December 31, 2012 compared to December 31, 2011. There are no legal or economic factors that materially impact our ability to transfer funds between our domestic and foreign businesses.

Net cash used in operating activities during the year ended December 31, 2012 was \$3,327,703 and during the year ended December 31, 2011 was \$2,108,913. Cash used in operating activities for the year ended December 31, 2012 consisted primarily of the net loss offset by approximately \$248,072 in non-cash stock compensation and \$123,940 in non-cash compensation. Our receivables increased significantly with our foreign entity recording their largest sales in the fourth quarter. Cash used in operating activities for the year ended December 31, 2011 consisted primarily of the net loss offset by approximately \$515,419 in non-cash stock compensation and \$518,000 in non-cash compensation.

Net cash used by investing activities for the year ended December 31, 2012 was \$338,825. Net cash provided by investing activities during the year ended December 31, 2011 was \$586,993. Our net cash used by investing activities consisted for the year ended December 31, 2012 of increased capital expenditures to expand our infrastructure for a new major customer.

Net cash provided by financing activities for the year ended December 31, 2012 was \$2,918,602 and during the year ended December 31, 2011 was \$2,039,922. Net cash provided in both periods consisted primarily of net proceeds from the sale of stock and proceeds from short-term borrowings, which were partially offset by principal payments on short term debt note obligations.

At December 31, 2012, we had approximately \$11,453,000 in net operating loss carryforwards available for federal and state income tax purposes. We did not recognize any benefit from these operating loss carryforwards, which federal operating loss carryforwards will expire beginning in 2025 through 2032. State net operating loss carryforwards will begin to expire in 2013.

We have experienced significant operating losses since our inception. Our capital expenditures and working capital requirements will increase and other adjustments to our operating plan will be needed to respond to changes in competition or unexpected events.

We believe that our cash on hand is not sufficient to meet our anticipated needs for working capital and capital expenditures. At December 31, 2012, we had cash and other current assets to meet working capital needs for only a limited period of time. We intend to seek to obtain additional working capital through debt and equity offerings. There can be no assurance that additional funds will be available on acceptable terms or on terms that do not adversely impact our existing shareholders or the price of our Common Stock. In the event that additional funds are not available on acceptable terms, we could be required to reduce the scope of, or cease, operations.

One customer in 2012 represented approximately 69% of total revenue and three customers in 2011 represented approximately 50% (26%, 14% and 10%) of total revenue. The accounts receivable from this customer was approximately 76% of total accounts receivable as of December 31, 2012. No other customers represented greater than 10% of total revenues in 2012 and 2011.

Our U.S. operation has 47% of gross accounts receivable aged over 120 days at the year ended December 31, 2012. The terms for payment for our U.S. operations are “due upon receipt”. Therefore, we have established an allowance for doubtful accounts of \$22,554 to be recorded with respect to our U.S. operations.

Our Taiwan operations, through MegaSys, have 21% of gross accounts receivables aged over 180 days at December 31, 2012. The payment terms vary based on the timing of the completion of the project. In general, payment takes place within one year of commencing the project, except that 5% of the total payment is retained and released one year after the completion of the project. Excluding such retained amounts, MegaSys provides an allowance for doubtful accounts for any receivables that will not be paid within one year. Management has set up a 5%, or \$117,732, allowance for doubtful accounts as of the year ended December 31, 2012. Management deems the rest to be collectible based on the nature of the customer contracts and past experience with similar customers.

Substantially all cash is deposited in two financial institutions, one in the United States and one in Taiwan. At times, amounts on deposit in the United States may be in excess of the FDIC insurance limit. Deposits in Taiwan financial institutions are insured by CDIC (Central Deposit Insurance Corporation) with maximum coverage of NTD 3 million. At times, amounts on deposit in Taiwan may be in excess of the CDIC insurance limit.

The Company leases its office facilities under a non-cancelable operating lease expiring October 2016 that requires minimum monthly payments ranging from \$8,669 to \$10,836. Rent expense was \$107,885 and \$95,635 for the years ended December 31, 2012 and 2011, respectively. The Company also has two non-cancellable data center service agreements for approximately \$7,298 and \$2,575 per month, expiring September 2014. The company has a third non-cancellable data center service agreement for approximately \$5,826, expiring March 2015. Data center services expense was \$170,776 and \$126,626 for the years ended December 31, 2012 and 2011, respectively, and is included as a component of Cost of Revenue in the Statement of Operations.

Future minimum lease payments under these leases are as follows:

|      |           |
|------|-----------|
| 2013 | \$309,211 |
| 2014 | \$268,194 |
| 2015 | \$135,169 |
| 2016 | \$108,356 |

The Company has no off-balance sheet arrangements.

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## **Inflation**

Management does not believe that the current levels of inflation in the United States have had a significant impact on the operations of the Company. Likewise, management does not believe that the current levels of inflation in Taiwan have had a significant impact on the operations of MegaSys.

## **Recent Accounting Standards**

In October 2012, FASB has issued Accounting Standards Update (ASU) No. 2012-04, Technical Corrections and Improvements. This ASU make technical corrections, clarifications, and limited-scope improvements to various Topics throughout the Codification. The amendments in this ASU that will not have transition guidance will be effective upon issuance for both public entities and nonpublic entities. For public entities, the amendments that are subject to the transition guidance will be effective for fiscal periods beginning after December 15, 2012. For nonpublic entities, the amendments that are subject to the transition guidance will be effective for fiscal periods beginning after December 15, 2013. The Company does not expect the adoption of this guidance to have a material impact on its consolidated financial statements.

In August 2012, FASB has issued Accounting Standards Update (ASU) No. 2012-03, Technical Amendments and Corrections to SEC Sections. This ASU amends various SEC paragraphs pursuant to SAB 114, SEC Release No. 33-9250, and ASU 2010-22, which amend or rescind portions of certain SAB Topics. The Company does not expect the adoption of this guidance to have a material impact on its consolidated financial statements.

In July 2012, the FASB issued ASU 2012-02, Intangibles—Goodwill and Other (Topic 350): Testing Indefinite-Lived Intangible Assets for Impairment. The objective of the measure is to reduce the cost and complexity associated with performing an impairment test for indefinite-lived intangible assets and to make the impairment test similar to the recent changes for testing goodwill for impairment (ASU 2011-08). ASU 2012-02 is effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012 and early adoption is permitted. The Company does not expect the adoption of this guidance to have a material impact on its consolidated financial statements.

In December 2011, the Financial Accounting Standards Board ("FASB") issued ASU 2011-11, Balance Sheet (Topic 210) Disclosures about Offsetting Assets and Liabilities. The amendments in this update will enhance disclosures required by U.S. GAAP by requiring improved information about financial instruments and derivative instruments that are either (1) offset in accordance with either ASC 210-20-45 or ASC 815-10-45 or (2) subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset in accordance with either ASC 210-20-45 or ASC 815-10-45. This information will enable users of an entity's financial statements to evaluate

the effect or potential effect of netting arrangements on an entity's financial position, including the effect or potential effect of rights of setoff associated with certain financial instruments and derivative instruments in the scope of this Update. The amendments in this Update are effective for annual periods for fiscal years beginning on or after January 1, 2013. The Company does not expect the adoption of this guidance to have a material impact on its consolidated financial statements.

In September 2011, the FASB has issued Accounting Standards Update (ASU) No. 2011-08, Intangibles—Goodwill and Other (Topic 350): Testing Goodwill for Impairment. ASU 2011-08 is intended to simplify how entities, both public and nonpublic, test goodwill for impairment. ASU 2011-08 permits an entity to first assess qualitative factors to determine whether it is "more likely than not" that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test described in Topic 350, Intangibles-Goodwill and Other. The more-likely-than-not threshold is defined as having a likelihood of more than 50%. ASU 2011-08 is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted, including for annual and interim goodwill impairment tests performed as of a date before September 15, 2011, if an entity's financial statements for the most recent annual or interim period have not yet been issued or, for nonpublic entities, have not yet been made available for issuance.

#### **ITEM 7A . QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

As a smaller reporting company, Iveda is not required to provide Item 7A disclosure in this Annual Report.

#### **ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

The required accompanying financial statements begin on page F-1 of this Annual Report.



## **ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

Not applicable.

## **ITEM 9A. CONTROLS AND PROCEDURES**

### **Evaluation of Disclosure Controls and Procedures**

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the design and operation 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 (the “Exchange Act”), as of December 31, 2012. Based on our evaluation, our management has concluded that our disclosure controls and procedures are effective to ensure that the reports that we file or submit under the Exchange Act are recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms and that the information required to be disclosed by us in such reports is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

### **Management’s Report on Internal Control over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act. Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our evaluation under the framework in *Internal Control – Integrated Framework*, our management concluded that our internal control over financial reporting was not effective as of December 31, 2012.

This annual report does not include an attestation report of our registered public accounting firm regarding internal control over financial reporting. In July 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”) was enacted into law. The Dodd-Frank Act provides non-accelerated filers with a permanent exemption from the requirement to obtain an external audit on the effectiveness of internal financial reporting controls provided in Section 404(b) of the Sarbanes-Oxley Act.

### **Changes in Internal Control over Financial Reporting**

In August 2012, we hired a CFO who has experience in SEC reporting and disclosures. The Company now has two employees knowledgeable in SEC accounting and reporting. The Company has plans for hiring additional financial personnel and implementing additional controls and processes involving both our financial personnel in order to ensure all transactions are accounted for and disclosed in an accurate and timely manner. There have not been any other changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act) during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect our internal control over financial reporting for our business operations.

### **Limitations on the Effectiveness of Controls**

Our management, including our principal executive officer and principal financial officer, does not expect that our disclosure controls and internal controls will prevent all errors and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within Iveda have been detected. These inherent limitations include the realities that judgments in decision making can be faulty, and that breakdowns can occur because of a simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management or Board override of the control.

The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

### **Identified Material Weakness**

*Oversight of Subsidiary Operations:* As of December 31, 2012, the Company needs to hire additional staff at MegaSys that are knowledgeable in SEC accounting and reporting. Increased staffing at the subsidiary level will provide daily oversight of MegaSys operations and minimize the likelihood of any material error in reporting the subsidiary's results. Action plans are in place to address this staffing need during 2013.

### **Management's Remediation Initiatives**

As our resources allow, we plan to add financial personnel at the subsidiary level to properly provide accurate and timely financial reporting.

## **ITEM 9B. OTHER INFORMATION**

During 2012, the Company raised \$2,426,319 in a private placement of shares at \$1.00 per share. Costs associated with this raise totaled \$317,465. The mix of investors include 21 individuals, 3 trusts and 4 corporations.

These issuances were made pursuant to Section 4(2) of the Securities Act of 1933, as amended, Regulation D, and Rule 506 promulgated thereunder. The facts relied upon by the Company to use this exemption were the following: (a) the Company did not use general solicitation or advertising to market the securities; (b) the issuances were only made to accredited investors; and (c) the Company informed the investors that they would receive only "restricted" securities.

There were no other items required to be disclosed in a report on Form 8-K during the fourth quarter of the fiscal year ended December 31, 2012 that have not been already disclosed on a Form 8-K filed with the SEC.



## **PART III**

### **ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

Each member of the Company's Board serves a one-year term and is subject to reelection at the Company's Annual Meeting of Shareholders held each year.

#### *Board Committees*

The Board has established an Audit Committee consisting of James Staudohar (Chairman), Joseph Farnsworth and Robert Gillen; a Compensation Committee consisting of Joseph Farnsworth (Chairman), James Staudohar, Greg Omi, Alex Kuo and Alejandro Franco; and a Nominating Committee consisting of Gregory Omi (Chairman), Joseph Farnsworth, Alex Kuo and Alejandro Franco. No other committees have been formed.

#### *Audit Committee*

The Audit Committee was established on February 18, 2010, although the Board had previously adopted a Charter which was amended on April 13, 2010. The Audit Committee Charter lists the purposes of the Audit Committee as overseeing the accounting and financial reporting processes of the Company and audits of the financial statements of the Company, and providing assistance to the Board in monitoring the (i) integrity of the Company's financial statements; (ii) Company's compliance with legal and regulatory requirements; (iii) independent auditor's qualifications and independence; and (4) performance of the Company's internal audit function, if any, and independent auditor.

The Board has determined that Mr. Staudohar is an "audit committee financial expert" as defined in Item 407(d)(5) of Regulation S-K promulgated by the SEC. The Board's conclusions regarding the qualifications of Mr. Staudohar as an audit committee financial expert were based on his service as a chief financial officer of numerous companies in various industries, his experience as a certified public accountant, and his degree in accounting.

*Directors, Executive Officers and Key Employees* . The executive officers, directors and other key employees serving the Company as of the date of this report were as follows:

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| <b>Name</b>        | <b>Age</b> | <b>Position</b>                              |
|--------------------|------------|--|
| David Ly           | 37         | CEO, President, Chairman of the Board        |
| Luz Berg           | 50         | Secretary, COO, CMO                          |
| Brian Duling       | 55         | CFO  |
| Richard Gibson     | 60         | Sr. Vice President of Global Sales & Support |
| Chen-Ho (Alex) Kuo | 49         | Director                                     |
| Joseph Farnsworth  | 53         | Director                                     |
| Gregory Omi        | 51         | Director                                     |
| James D. Staudohar | 75         | DiDirector                                   |
| Robert D. Gillen   | 58         | DDirector                                    |
| Alejandro Franco   | 60         | DiDirector                                   |

*David Ly* – Mr. Ly founded Iveda and has served as a director and as the President and Chief Executive Officer since inception. He has held positions with several major corporations, including Applications Engineer at Metricom, Inc. (from 1998 to 2001), Corporate Sales at Nextel Communications (from 2001 to 2002), Market Manager at Door To Door Storage (from 2001 to 2002), and B2B Sales Manager at T-Mobile USA (from 2002 to 2004). While at T-Mobile, his last position before founding Iveda Solutions, he was awarded the prestigious sales award of President’s Club Top Salesman. Mr. Ly received his B.S. in Civil Engineering, with a minor in International Business, from San Francisco State University. Mr. Ly’s day-to-day leadership as our Chief Executive Officer provides him with detailed knowledge of our business and operations. Among other professional experiences, qualifications, and skills, Mr. Ly brings in depth knowledge and understanding of the video surveillance industry, as well as business and engineering expertise and management skills that have been critical to formulating the Company’s short and long-term strategies.

*Luz Berg* – Luz Berg joined Iveda Solutions in 2004, prior to its incorporation as the VP of Marketing. She was promoted to Senior VP of Operations & Marketing in 2007, and was further promoted to Chief Operating Officer and Chief Marketing Officer in 2009. Ms. Berg also serves as the Corporate Secretary. Ms. Berg has over 20 years of business experience in a variety of industries, with proven track record in building a startup company from the ground up. She has been working alongside the CEO since inception, making sure that the Company remains focused on its goals and the founder's vision realized. Ms. Berg manages the Company's day-to-day operation, formulating policies and procedures. Ms. Berg has extensive experience in developing and implementing results-driven marketing communications plans for lead/sales generation, building brand, brand revitalization, and customer retention in a wide-range of industries. She has been instrumental in the Company's messaging and image building. Ms. Berg served as the Director of Marketing at Cygnus Business Media from 2003 to 2004 and at Penton Media from 2001 to 2003. She has also worked in the high-tech industry at Metricom, serving as Marketing Programs/Channel Marketing Manager from 1999 to 2001, and Spectra-Physics Lasers, serving as Marketing Communications Specialist from 1991 to 1999. Ms. Berg received her B.A. in Management from St. Mary's College in California.

*Brian Duling* - Brian Duling joined the company in 2012 as Chief Financial Officer and Corporate Treasurer. He has over 25 years' experience as a chief financial officer in high tech companies, for both private and publicly-held companies. Prior to joining the Company, Mr. Duling served as Chief Financial Officer and Chief Operating Officer at PSS, Inc., from 2009 to 2012. PSS, Inc. is a private company that assists businesses improve their customer service and communications systems by transitioning customer contact centers into integrated multi-media centers. Also during this time, from 2009 to 2012, Mr. Duling worked as Chief Financial Officer at Global Profit Technologies, Inc. (GLPT:PK). This publicly-traded company provides proprietary foreign exchange trading software, which enables traders to trade foreign exchange currencies in an automated manner. Prior to this, from 2006 to 2009, Mr. Duling served as Executive Vice President of Administration and Chief Financial Officer of Cology, Inc., a private company that provides student loan origination technology and services to lenders. From 2002 to 2005, Mr. Duling served as Chief Financial Officer of Trimble Mobile Solutions, a wholly-owned subsidiary of Trimble Navigation (NASDAQ: TRMB), an integrator of wireless, GPS, and web-based software information technology. From 1998 to 2002, Mr. Duling served as Chief Financial Officer of Tiros Corporation, an international developer of high-tech equipment for semiconductor manufacturers. Prior to Tiros, from 1992 to 1998, Mr. Duling was the Chief Financial Officer and Chief Operations Officer at Wordlink, Inc., a provider of IT consulting, software development, and Internet services. From 1986 to 1992, Mr. Duling worked as Chief Financial Officer at Cellular One, a wholly owned subsidiary of SBC Communications (NYSE:T).

Currently, Mr. Duling serves on the Board of Directors of Global Profit Technologies, Inc. (from 2008 to present); and on the advisory board of directors of eResourcePlanner (from 2005 to present), a private company that provides workforce management applications and services. Mr. Duling has a Bachelor of Business degree from Western Illinois University, a Master of Business Administration degree from the Keller Graduate School of Management in Chicago, IL, and is a member of the Institute of Internal Auditors.

*Richard Gibson* - Richard Gibson joined Iveda in October 2011 as Senior Vice President of Global Sales & Support. Mr. Gibson comes to Iveda with 30 years' experience in IT, networks, and security. He has held leadership positions in large companies such as IBM and Motorola, as well as in several smaller companies. From 2008 up to just before Mr. Gibson joined Iveda in October 2011, he was Senior Vice President of Sales and Service at SEER Technology, Inc.

From 2005 to 2008, Mr. Gibson provided consulting services in sales, marketing, start-up funding, and business plan development to small technology companies. Mr. Gibson worked at CYBERAIR Technologies, Inc. from 2003 to 2005 as Senior Vice President of Sales and Marketing. From 1999 to 2003, he worked for Motorola Global Infrastructure Solutions as Director of Business Development. From 1997 to 1999, Mr. Gibson worked for NETSAFE and INTERCELL in sales and marketing executive roles. Mr. Gibson held sales and marketing management positions at Motorola Government Electronics from 1992 to 1997. He started his professional career at IBM as Senior Market Representative from 1988 to 1992 and Systems Engineer from 1979 to 1988. Mr. Gibson is managing the company's sales organization, including direct, resellers, and distribution channels. He is also managing Iveda's strategic sales initiatives in the U.S. and overseas. Mr. Gibson is in charge of establishing and enhancing new sales and customer service methodologies, systems, and organization. Mr. Gibson received his MBA degree at Thunderbird School of International Management in Glendale, Arizona, specializing in the Asia region. He earned his undergraduate Bachelor of Science in International Relations degree from the University of Minnesota in Minneapolis, Minnesota, graduating summa cum laude. He also completed IBM's Internal Graduate School program at IBM Systems Research Institute.



*Joseph Farnsworth* – Mr. Farnsworth was appointed to Iveda’s Board in January 2010. Mr. Farnsworth has over 25 years of experience in the real estate industry. Since 1995, Mr. Farnsworth has served as President and a director of Farnsworth Realty & Management Co., an Arizona based privately held real estate company. He has also served on the Board of Farnsworth Development, a closely held real estate developer, since 1995, and on the Board of Farnsworth Companies since 2008. From 1987 to 1991, Mr. Farnsworth served as President of Farnsworth International, a real estate investment company based in Taipei, Taiwan, and from 1990 to 1995, Mr. Farnsworth served as President of Alfred’s International, a company with operations in China and Korea. He serves on the Board of Directors of Arizona Brain Food, an organization providing food to lower income school children, and is actively involved with the La Masita, a homeless shelter. He has previously served on the Board of Adjustment for the City of Mesa, Arizona, and also previously served on the City Planning and Zoning Board for the City of Mesa, Arizona. Mr. Farnsworth is a graduate of Brigham Young University with a B.S. in real estate finance and is a licensed Arizona real estate broker. Among other professional experiences, qualifications, and skills, Mr. Farnsworth has substantial knowledge of the usefulness of the Company’s services in the real estate industry and has extensive contacts in the industry. In addition, Mr. Farnsworth has extensive experience in managing companies, as well as a strong background in finance, all of which are vital to the overall success of the Company.

*Gregory Omi* – Mr. Omi has been a director since 2005. Mr. Omi has been working as a senior programmer for Zynga since November 2009, writing online games in Flash for Facebook. From January 2009 to November 2009, Mr. Omi worked at Monkey Gods, LLC, a video game provider, designing Facebook applications as a programmer. From October 2006 to January 2009, Mr. Omi worked at Flektor, Inc., focused on Flash 9 / Flex 2 / Action Script 3, C, XML and Ruby programming for a web application, including video and image processing. Flektor was acquired by FOX Interactive Media in 2007. From October 1996 to June 2006, Greg held the position of Senior Programmer with Naughty Dog, a computer game company, which was acquired by Sony. He has also held programming positions with 3DO (from 1992 to 1996), TekMagic (during 1992), Epyx (from 1986 to 1992), Atari (during 1991), Nexa (from 1982 to 1983 and 1985 to 1986) and HES (during 1983). Mr. Omi assists the Company in overseeing all software development activities and improvements to its technologies including development of a web-based executive dashboard to gather information and functionalities for cameras, video services, digital video recorders and access control. Mr. Omi attended DeVry Institute in Phoenix, Arizona from 1979 to 1980 where he studied industrial electronics engineering. Among other professional experiences, qualifications, and skills, Mr. Omi’s expertise and skills in computer programming, software development, and writing code are instrumental to the development of our products.

*James D. Staudohar* - Mr. Staudohar was appointed to Iveda’s Board in January 2010. Since 2003, Mr. Staudohar has served as President of Lakeview Enterprises, LLC, providing business advisory and consulting services to companies throughout the Phoenix metropolitan area. From 2007 to 2009, Mr. Staudohar served as the Chief Financial Officer and as a director of Veritest International Corporation, a startup company that raised approximately \$2.8 million dollars for the development of a drug screening device. From 1994 to 2002, Mr. Staudohar served as Vice Chairman and Chief Financial Officer of RSI Enterprises, Inc., a multi-million dollar profitable asset recovery business located in Phoenix, Arizona. Prior to 1994, Mr. Staudohar held a number of financial positions, including serving as Vice President and Corporate Controller of Modern Merchandising, Inc. from 1981 until its acquisition by Best Products, Inc. in 1983, when Mr. Staudohar was promoted to Chief Financial Officer and Senior Vice President of Best Products, a \$3 billion retail organization, positions he held until 1989. Mr. Staudohar also served from 1973-1981 as Vice President and Controller of B. Dalton Bookseller during a period when the retail chain grew from 66 to 650 stores.

In addition to his financial experience, Mr. Staudohar previously served on the Board of Directors of Smith & Wesson Holding Corporation, the publicly traded parent company of the gun manufacturer from 2002 to 2004. He also served as the Chair of Smith & Wesson's Audit Committee and as a member of the Nominating Committee. Mr. Staudohar presently serves on the Board of Directors and on multiple committees of the Phoenix Sister Cities Commission, a not for profit company. Mr. Staudohar holds a B.A. from the University of Minnesota. Among other professional experiences, qualifications and skills, Mr. Staudohar's knowledge and understanding of the capital markets and his in-depth experience in corporate finance and business management will provide valuable assistance to the Company in oversight of financial management, internal controls, and strategic planning. Mr. Staudohar also serves as Chairman of the Company's Audit Committee.

*Robert D. Gillen* – Mr. Gillen was appointed to Iveda’s Board in November 2011. Mr. Gillen is the president of the Law Offices of Robert D. Gillen, Ltd., a law firm assisting clients with domestic and international planning, with offices located in Scottsdale, Arizona and Naperville, Illinois. Mr. Gillen is an international speaker and has extensive experience in advising businesses and professionals on tax and legal matters. Mr. Gillen graduated from the University of Illinois in 1976 with a Bachelor of Science in Business Administration and from IIT Chicago Kent College of Law in 1979 with a Juris Doctor Degree with Honors. Mr. Gillen has been active in the cellular industry since its inception and has assisted in the development of the cellular network. Mr. Gillen has served on various boards of directors and advisory committees for growing companies, as well as donating his time and expertise on not-for-profit boards. Mr. Gillen has also authored many articles on business, tax and legal matters.

*Chen-Ho (Alex) Kuo* - Mr. Kuo was appointed to Iveda’s Board in November 2011. In 2009, Alex Kuo was hired by Iveda as a consultant to facilitate the acquisition of MEGAsys—Taiwan. Shortly after the completion of the acquisition, in May 2011, Iveda hired Mr. Kuo as Senior Vice President of Global Strategies—Asia, and he was recently promoted to Chief Strategy Officer. Mr. Kuo has 20 years of executive experience at Acer Group. Prior to Acer, he was General Manager at Servex/Anextek from 2001 to 2007. He also held Vice President and Senior Vice President positions at China Security and Surveillance Technology (NYSE:CSR), FalconStor Software (NASDAQ: FALC), and Global Data Solutions Limited from 2007 to 2010. Mr. Kuo also serves as an instructor at the Cloud Computing Industry Association of Taiwan. Mr. Kuo received his Masters of Science and Technology Innovation Management from George Washington University and his undergraduate degree from National Taiwan University.

*Alejandro Franco* – Mr. Franco was appointed to Iveda’s Board in November 2011. Mr. Franco has been serving Iveda as a consultant for over a year, with respect to business development and strategic partnership opportunities in Mexico. He has been advising and facilitating the Company’s negotiations with a telecommunications company in Mexico. Mr. Franco has 26 years of cross-industry experience and accomplishment with leading start-up and high-growth companies. He is known for delivering strong and sustainable revenue and profit gain in highly competitive markets throughout China, Taiwan, USA, Mexico, and Brazil. He has extensive experience in leading large-scale, complex, global operations in China, Taiwan, Latin America, and the U.S. Mr. Franco is the president and founder of Amextel in Mexico. He also founded and was president of TVM, Inc., in Mexico from 1985 to 1988 and Bela Corp. in the U.S. from 1988 to 2000. Mr. Franco has a degree in Economics from UNAM University, Mexico, a degree in Industrial Design from IBERO University, Mexico, and Masters in Theology from Oblate University, San Antonio Texas.

Iveda's directors, as named above, will serve until the next annual meeting of Iveda's shareholders or until their successors are duly elected and qualified. Directors will be elected for one-year terms at the annual shareholders meeting. There is no arrangement or understanding between any of the directors or officers of Iveda and any other person pursuant to which any director or officer was or is to be selected as a director or officer, and there is no arrangement, plan or understanding as to whether non-management shareholders will exercise their voting rights to continue to elect the current directors to Iveda's board. There are also no arrangements, agreements or understandings between non-management shareholders that may directly or indirectly participate in or influence the management of Iveda's affairs.

There are no agreements or understandings for any officer or director to resign at the request of another person, and none of the officers or directors are acting on behalf of, or will act at the direction of, any other person. There are no family relationships among our executive officers and directors.

#### Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Exchange Act requires Iveda's directors and executive officers, and persons who beneficially own more than ten percent of a registered class of our equity securities, to file with the SEC initial reports of beneficial ownership and reports of changes in beneficial ownership of our common stock. The rules promulgated by the SEC under Section 16(a) of the Exchange Act require those persons to furnish us with copies of all reports filed with the SEC pursuant to Section 16(a). The information in this section is based solely upon a review of Forms 3, 4, and 5 received by us.

We believe that Iveda's executive officers, directors and 10% shareholders timely complied with their filing requirements during the year ended December 31, 2012, with the following exceptions: 1) on June 20, 2012, Mr. Joe Farnsworth filed an untimely Form 4 with respect to gifts made during 2011; and 2) on September 5, 2012, Mr. Brian Duling filed an untimely Form 4 with respect to options granted on October 31, 2012

#### Code of Ethics

We have adopted a Code of Ethics, which was amended and restated on April 13, 2010. We adopted a Code of Conduct and Ethics (filed as Exhibit 14.1 to Form 10-K, filed on April 15, 2010) that applies to all of our officers, directors, and employees, and a separate Code of Ethics (filed as Exhibit 14.2 to Form 10-K, filed on April 15, 2010) for our Chief Executive Officer and Senior Financial Officers that supplements our Code of Conduct and Ethics. Each of these policies comprises written standards that are reasonably designed to deter wrongdoing and to promote the behavior described in Item 406 of Regulation S-K promulgated by the SEC.



### Nominating Procedures

There have been no material changes to the procedures by which our shareholders may recommend nominees to the Board of Directors during our last fiscal year.

## **ITEM 11. EXECUTIVE COMPENSATION**

### Compensation Philosophy and Overview

The Company believes that it is important to design a compensation program that supports the Company's business strategy. As a result, our compensation program emphasizes performance-based compensation and is designed to support the Company's business goals, promote short- and long-term growth, and attract, retain, and motivate key talent. The compensation program has three components:

(1) base salary;

(2) bonus awards; and

(3) long-term performance incentives.

The Company believes that our executive officers and other key employees should have a portion of their potential annual compensation tied to our profitability and other Company goals. Additionally, we seek to align the ability to earn long-term incentives directly with the interests of our shareholders through the use of equity-based incentives. The Company strives to ensure compensation is competitive with companies similar to Company; however, the Company acknowledges that base salaries are currently below market.

### **SUMMARY COMPENSATION TABLE**

The following summary compensation table sets forth information concerning compensation for services rendered in all capacities during our past two fiscal years awarded to, earned by, or paid to each of the individuals listed in the Summary Compensation Table below. Salary and other compensation for these officers and former officers were set by the Board. Iveda has historically suffered severe shortages in cash and has structured its compensation policies to minimize salaries and focus instead on reward of equity.

| Name and Principal Position             | Year | Salary     | Bonus     | Option Awards  | Total          |
|---|------|------------|-----------|----------------|----------------|
| David Ly<br>Chairman,<br>CEO, President | 2012 | \$ 135,225 | \$ 60,000 | (1) \$ 13,491  | (2) \$ 208,716 |
|   | 2011 | \$ 118,654 | \$ 41,981 | (3) \$ 115,500 | (2) \$ 276,135 |
| Luz Berg<br>COO, CMO, Secretary         | 2012 | \$ 130,225 | \$ 45,000 | (1) \$ 6,746   | (2) \$ 181,971 |
|   | 2011 | \$ 116,923 | \$ 23,174 | (4) \$ 192,500 | (2) \$ 332,597 |
| Brian Duling<br>CFO, Treasurer(5)       | 2012 | \$ 38,827  | \$ 15,000 | (1) \$ 52,560  | (2) \$ 106,387 |

(1) Gross bonuses accrued in 2012 financial statements, to be paid in 2013

(2) See Note 7 of the Notes to Consolidated Financial Statements in our Annual Report on Form 10-K, filed in this report, for information regarding assumptions underlying the valuation of equity awards.

(3) Net bonus of \$25,000 was grossed up for taxes.

(4) Net bonus of \$15,000 was grossed up for taxes.

(5) Mr. Duling was hired as the Company's CFO and Treasurer on August 31, 2012. Mr. Duling receives an annual salary of \$115,000 and received options to purchase 200,000 shares of the Company's common stock.

## OUTSTANDING EQUITY AWARDS AT FISCAL YEAR-END

| Name                            | Number of Securities Underlying Unexercised Options/Warrants (#) Exercisable | Number of Securities Underlying Unexercised Options (#) Unexercisable | Equity Incentive Plan Awards: Number of Securities Underlying Unexercised Unearned Options (#) | Option Exercise Price (\$) | Option Expiration Date |
|---------------------------------|--|---|--|----------------------------|------------------------|
| David Ly, Chairman, CEO & Pres. | 300,000 <sup>(5)</sup><br>(options)  | -   | -  | \$ 1.00                    | 6/20/21                |
| Luz Berg, COO, CMO, & Secretary | 50,000 <sup>(7)</sup><br>(options)   | -   | -  | \$ 1.10                    | 12/18/22               |
|                                 | 256,140 <sup>(1)</sup><br>(warrants)   | -   | -  | \$ 0.10                    | 12/30/16               |
|                                 | 240,331 <sup>(2)</sup><br>(warrants)   | -   | -  | \$ 0.10                    | 9/10/17                |
|                                 | 425,712 <sup>(3)</sup><br>(options)  | -   | -  | \$ 0.10                    | 4/01/18                |
|                                 | 500,000 <sup>(4)</sup><br>(options)  | -   | -  | \$ 1.00                    | 6/20/21                |
| Brian Duling, CFO & Treasurer   | 25,000 <sup>(7)</sup><br>(options)   | -   | -  | \$ 1.10                    | 12/18/22               |
|                                 | 200,000 <sup>(6)</sup>   | -   | -  | \$ 1.10                    | 8/31/22                |

(1) The warrants became fully vested on December 30, 2006.

(2) The warrants became fully vested on September 10, 2007.

(3) The options became fully vested on April 10, 2008.

(4) The options became fully vested on June 20, 2011.

(5) 300,000 options were canceled as of December 31, 2011 for failing to exercise options as indicated on the 2010 Option Plan.

(6) The options become fully vested on August 31, 2015

(7) The options became fully vested on December 18, 2012



**Director Compensation**

Directors have received stock compensation for their service on the Board, and are reimbursed for attendance of meetings for all non-employee directors. For the year ended December 31, 2012, all directors listed below received stock awards in the forms of options. Joseph Farnsworth, James Staudohar, Gregory Omi, Robert Gillen, Alex Kuo and Alejandro Franco received 50,000 options each.

| Name              | Fees earned or paid in cash (\$) | Stock Awards (\$) | Options Awards (\$) <sup>(7)</sup> | Non-Equity Incentive Plan Compensation | Nonqualified deferred compensation earnings (\$) | All Other Compensation (\$) | Total (\$) |
|-------------------|----------------------------------|-------------------|------------------------------------|--|--|-----------------------------|------------|
| Joseph Farnsworth | -                                | -                 | \$ 13,491                          | (1) -                                  | -  | -                           | \$13,491   |
| James Staudohar   | -                                | -                 | \$ 13,491                          | (2) -                                  | -  | -                           | \$13,491   |
| Gregory Omi       | -                                | -                 | \$ 13,491                          | (3) -                                  | -  | -                           | \$13,491   |
| Alex Kuo          | -                                | -                 | \$ 13,491                          | (4) -                                  | -  | -                           | \$13,491   |
| Robert Gillen     | -                                | -                 | \$ 13,491                          | (5) -                                  | -  | -                           | \$13,491   |
| Alejandro Franco  | -                                | -                 | \$ 13,491                          | (6) -                                  | -  | -                           | \$13,491   |

(1) As of December 31, 2012, Mr. Farnsworth had 230,000 options outstanding.

(2) As of December 31, 2012, Mr. Staudohar had 155,000 options outstanding.

(3) As of December 31, 2012, Mr. Omi had 230,000 options outstanding.

(4) As of December 31, 2012, Mr. Kuo had 200,000 options outstanding.

(5) As of December 31, 2012, Mr. Gillen had 100,000 options outstanding.

(6) As of December 31, 2012, Mr. Franco had 100,000 options outstanding.

(7) See Note 7 of the Notes to Consolidated Financial Statements in our Annual Report on Form 10-K, filed in this report, for information regarding assumptions underlying the valuation of equity awards.

Compensation Policies and Risk Management

The Board has reviewed the Company's compensation policies and practices for all of its employees and has determined that such policies and practices do not encourage risk taking to a degree that is reasonably likely to have a material adverse effect on the Company.

**ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

The following table sets forth certain information regarding the beneficial ownership of Iveda's common stock as of March 23, 2012, for (i) each person known by Iveda to be a beneficial owner of five percent or more of the outstanding common stock of Iveda; (ii) each executive officer and director; and (iii) all directors and executive officers of Iveda as a group. As of March 15, 2013 Iveda had 22,594,503 shares of common stock outstanding, options to purchase 5,038,512 shares of common stock outstanding, and warrants to purchase 2,797,219 shares of common stock outstanding.

| Name of Beneficial Owner              | Position                 | Amount of Shares of Common Stock | Options or Warrants to Purchase Common Stock | Total Beneficial Ownership <sup>(1)</sup> | Percent of Class <sup>(1)</sup> |   |
|---------------------------------------|--------------------------|----------------------------------|--|---|---------------------------------|---|
| David Ly <sup>(2)</sup>               | CEO, Director, President | 3,185,181                        | 350,000                                      | 3,535,181                                 | 12.5                            | % |
| Luz Berg <sup>(2)</sup>               | COO, CMO & Secretary     | -                                | 1,447,183                                    | 1,447,183                                 | 5.1                             | % |
| Brian Duling <sup>(2)</sup>           | CFO & Treasurer          | -                                | 200,000                                      | 200,000                                   | 0.7                             | % |
| Joseph Farnsworth <sup>(2)</sup>      | Director                 | 79,958                           | 277,500                                      | 357,458                                   | 1.3                             | % |
| Gregory Omi <sup>(2)</sup>            | Director                 | 903,859                          | 250,000                                      | 1,153,859                                 | 4.1                             | % |
| James D. Staudohar <sup>(2)</sup>     | Director                 | 0                                | 155,000                                      | 155,000                                   | 0.6                             | % |
| Robert Gillen <sup>(2)</sup>          | Director                 | 1,301,140                        | 175,000                                      | 1,476,140                                 | 5.2                             | % |
| Chen-Ho (Alex) Kuo <sup>(2)</sup>     | Director                 | 300,000                          | 200,000                                      | 500,000                                   | 1.8                             | % |
| Alejandro Franco <sup>(2)</sup>       | Director                 | -                                | 100,000                                      | 100,000                                   | .4                              | % |
| All directors and officers as a group |                          | 5,770,138                        | 3,154,683                                    | 8,924,821                                 | 26.7                            | % |
| William A. Walsh <sup>(3)</sup>       |                          | 2,100,000                        | 0  | 2,100,000                                 | 7.4                             | % |

(1) Reflects ownership of securities of Iveda on a fully-diluted basis.

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(2) The address for each of these individuals is c/o Iveda Solutions, 1201 S. Alma School Road, Suite 8500, Mesa, AZ 85210.

(3) The address for Mr. Walsh is 117 North 2<sup>nd</sup> Avenue, Sterling, Colorado 80751.

### **ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE**

The Company has provided surveillance services since 2005 at a pre-established rate to entities owned by Ross Farnsworth, either through a family partnership or through his majority owned limited liability company, and subsequently Ross Farnsworth became a shareholder of the Company in 2006. Mr. Farnsworth's holdings have always been less than 5% of the Company's outstanding stock, but the revenue for the year ended December 31, 2012 and the year ending 2011 was \$71,350 and \$68,119, respectively, and there was a trade accounts receivable balance of \$0 and \$5,859 at December 31, 2012 and December 31, 2011, respectively.

On June 7, 2012, the Company entered into a debenture agreement with one of its Board Members for \$200,000. Interest is payable at 10% per annum, payable on the maturity date of July 6, 2012. The Company issued warrants to purchase 20,000 shares of the company stock, at an exercise price of \$1.10. Accordingly, the Company recognized a discount of \$15,179 on the principal value of the \$200,000 and this discount is fully amortized by June 30, 2012.

On June 20, 2012, the Company entered into a separate debenture agreement with a different Board Member for \$200,000. Interest is payable at 12% per annum, payable on the maturity date of June 20, 2013. The Company issued warrants to purchase 20,000 shares of the company stock, at an exercise price of \$1.00. Accordingly, the Company recognized a discount of \$16,789 on the principal value of the \$200,000 and is amortizing the discount over the 12 month term of the debenture.

#### Director Independence

Using the standards of the NYSE Amex (to which rules and regulations Iveda is not subject), Iveda's Board has determined that Mr. Farnsworth, Mr. Omi, Mr. Staudohar, Mr. Gillen, and Mr. Franco each qualify as an independent director and as a member of the Audit Committee, Nominating and Compensation Committees, as applicable. No other directors are independent under these standards. Iveda did not consider any relationship or transaction between itself and these independent directors not already disclosed in this report in making this determination.

### **ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

On October 17, 2011, Iveda Solutions, Inc. ("Iveda"), with the approval of the Audit Committee of the Board of Directors, appointed Albert Wong & Co. ("AW") as Iveda's principal accounting firm. Since 2008, AW has served as the principal accounting firm for Sole Vision Technologies ("MegaSys"), a Taiwanese corporation acquired by Iveda

in April 2011. Due to the larger business comprised by the MegaSys subsidiary, Iveda decided to replace its former principal accounting firm, Farber Hass Hurley LLP (“FHH”), with AW in order to increase efficiencies and reduce costs in its auditing procedures. FHH continues to assist AW on the audit of Iveda’s U.S. based operations.

The Company paid or accrued the following fees in each of the prior two fiscal years to its principal accountant Albert Wong & Co. and its former principal accountant Farber Hass Hurley LLP:

|                    | Year ended<br>December 31,<br>2012 | Year ended<br>December 31,<br>2011 |
|--------------------|------------------------------------|------------------------------------|
| Audit fees         | \$ 66,000                          | \$ 56,000                          |
| Audit-related fees | \$ 15,448                          | \$ 11,550                          |
| Tax fees           | \$ 0                               | \$ 0                               |
| All other fees     | \$ 0                               | \$ 0                               |

Audit fees include fees for the audit of our annual financial statements, reviews of our quarterly financial statements, and related consents for documents filed with the SEC.

As part of its responsibility for oversight of the independent registered public accountants, the Audit Committee has established a pre-approval policy for engaging audit and permitted non-audit services provided by our independent registered public accountants, Farber Hass Hurley LLP and Albert Wong & Company. In accordance with this policy, each type of audit, audit-related, tax and other permitted service to be provided by the independent auditors is specifically described and each such service, together with a fee level or budgeted amount for such service, is pre-approved by the Audit Committee. The Audit Committee has delegated authority to its Chairman to pre-approve additional non-audit services (provided such services are not prohibited by applicable law) up to a pre-established aggregate dollar limit. All services pre-approved by the Chairman of the Audit Committee must be presented at the next Audit Committee meeting for review and ratification. All of the services provided by Albert Wong & Company and Farber Hass Hurley LLP described above were approved by the Audit Committee for 2011.

Iveda's principal accountant, Albert Wong & Company, and former accountant Farber Hass Hurley LLP, did not engage any other persons or firms other than the principal accountant's full-time, permanent employees .

## ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

**(Except as otherwise indicated, all exhibits were previously filed)**

| <b>Exhibit Number</b> | <b>Description of Exhibits</b>  |
|-----------------------|---|
| 2.1                   | Agreement and Plan of Merger, dated March 21, 2011, by and among Iveda Solutions, Inc., a Nevada corporation, Sole-Vision Technologies, Inc. (doing business as MegaSys), a corporation organized under the laws of the Republic of China, and the shareholders of MegaSys (Incorporated by reference to the Form 10-K/A filed on 2/9/2012) |
| 3.1                   | Articles of Incorporation of Charmed Homes Inc. (Incorporated by reference to the Form SB-2 filed on 4/27/2007)   |
| 3.2                   | Bylaws of Charmed Homes Inc. (Incorporated by reference to the Form SB-2 filed on 4/27/2007)  |
| 3.3                   | Amendment to Bylaws of Charmed Homes Inc. (Incorporated by reference to the Form 8-K filed on 12/15/2008)   |
| 3.4                   | Amendment to Articles of Incorporation, filed with the Nevada Secretary of State on September 9, 2009 (Incorporated by reference to the Form 8-K filed on 10/21/2009)   |
| 3.5                   | Articles of Merger filed with the Secretary of State of Nevada on December 28, 2010, and dated effective December 31, 2010 (Incorporated by reference to the Form 8-K filed on January 4, 2010)   |

4.1 Specimen Stock Certificate (Incorporated by reference to the Form SB-2 filed on 4/27/2007)

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- 4.2 Form of Stock Option Agreement under the Intelasight, Inc. 2008 Stock Option Plan (Incorporated by reference to the Form S-4/A1 filed on 7/10/2009)
- 4.3 Form of Common Stock Purchase Warrant issued by Intelasight, Inc. (Incorporated by reference to the Form S-4/A1 filed on 7/10/2009)
- 4.4 2009 Stock Option Plan, dated October 15, 2009 (Incorporated by reference to the Form 8-K filed on 10/21/2009)
- 4.5 Form of Common Stock Purchase Warrant issued by Iveda Corporation in conjunction with the Merger (Incorporated by reference to the Form 8-K filed on 10/21/2009)
- 4.6 2010 Stock Option Plan, dated January 18, 2010 (Incorporated by reference to the Form S-8 filed on 2/4/2010)
- 4.7 Form of Notice of Grant of Stock Option under the Iveda Solutions, Inc. 2010 Stock Option Plan, as amended (Incorporated by reference to Form S-8 filed on 6/24/2011)
- 4.8 Form of Stock Option Agreement under the Iveda Solutions, Inc. 2010 Stock Option Plan, as amended (Incorporated by reference to Form S-8 filed on 6/24/2011)
- 4.9 Form of Stock Option Exercise Notice under the Iveda Solutions, Inc. 2010 Stock Option Plan, as amended (Incorporated by reference to Form S-8 filed on 6/24/2011)
- 10.1 Application Development Service Agreement dated July 14, 2006 by and between Axis Communications AB and Intelasight, Inc. (Incorporated by reference to the Form S-4/A2 filed on 8/2/2009)
- 10.2 Partner Agreement dated January 30, 2007 by and between Milestone Systems, Inc. and Intelasight, Inc. (Incorporated by reference to the Form S-4/A1 filed on 7/10/2009)
- 10.3 Solution Partner Agreement dated March 13, 2008 by and between Milestone Systems A/S and Intelasight, Inc. (Incorporated by reference to the Form S-4/A1 filed on 7/10/2009)
- 10.4 Channel Partner Program Membership Agreement – Gold Solution Partner Level – dated June 23, 2009 by and between Axis Communications Inc. and Intelasight, Inc. (Incorporated by reference to the Form S-4/A1 filed on 7/10/2009)
- 10.5 Stock Purchase Agreement, dated October 15, 2009, by and among Iveda Corporation, Intelasight, Inc., Ian Quinn and Kevin Liggins (Incorporated by reference to the Form 8-K filed on 10/21/2009)
- 10.6 Subscription Agreement, dated July 26, 2010 (Incorporated by reference to Form 10-Q filed on November 12, 2010)
- 10.7 Line of Credit Promissory Note, dated September 15, 2010 (Incorporated by reference to Form 10-Q filed on November 12, 2010)
- 10.8 Agreement for Service, dated October 20, 2010 (Incorporated by reference to Form 10-Q filed on November 12, 2010)
- 10.9 Consulting Agreement, dated October 25, 2010 (Incorporated by reference to Form 10-Q filed on November 12, 2010)
- 10.10 Operating Level Agreement, dated October 25, 2010 (Incorporated by reference to Form 10-Q filed on November 12, 2010)
- 10.11 Side Letter, dated March 21, 2011, by and among Iveda Solutions, Inc., a Nevada corporation, Sole-Vision Technologies, Inc. (doing business as MegaSys), a corporation organized under the laws of the Republic of China, and the shareholders of MegaSys (Incorporated by reference to Form 10-K filed on 3/30/2011)



- 10.12 Non-Exclusive Strategic Collaboration Agreement between Iveda Solutions, Inc. and Telmex, U.S.A., LLC, dated October 28, 2011 (Incorporated by reference to Form 10-Q/A filed on 3/7/2012)
- 10.13 2010 Digital Video Remote Monitoring Recording System Procurement Contract between Sole-Vision Technology, Inc. and New Taipei City Police Department Purchasing Authority, dated January 9, 2012 (Incorporated by reference to Form 10-K filed on 3/30/2012).
- 10.14 Consulting Agreement between Iveda Solutions, inc. and Amextel S.A. de C.V. dated November 2, 2011 (Incorporated by reference to Form 10-K/A filed on 5/11/2012).
- 14.1 Code of Conduct and Ethics (Incorporated by reference to the Form 10-K filed on 4/15/2010)
- 14.2 Code of Ethics for Chief Executive Officer and Senior Financial Officers (Incorporated by reference to the Form 10-K filed on 4/15/2010)
- 21 Subsidiaries of the Registrant (Incorporated by reference to Form 10-K filed on 3/30/2012).
- 31.1\* Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 – Chief Executive Officer
- 31.2\* Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 – Chief Financial Officer
- 32.1\*\* Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002  
The following financial information from the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2012, formatted in XBRL (eXtensible Business Reporting Language): (i) Condensed Consolidated Balance Sheets as of December 31, 2012 and December 31, 2011, (ii) Condensed Consolidated
- 101.1\*\* Statements of Operations for the years ended December 31, 2012 and 2011, (iii) Condensed Consolidated Statements of Stockholders’ Equity for the years ended December 31, 2012 and 2011, (iv) Condensed Consolidated Statements of Cash Flows for the years ended December 31, 2012 and 2011, and (iv) the Notes to Condensed Consolidated Financial Statements.

\*  
\*\*

Filed herewith  
Furnished herewith

**IVEDA SOLUTIONS, INC.**

**CONSOLIDATED FINANCIAL STATEMENTS**

**YEARS ENDED DECEMBER 31, 2012 AND 2011**

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|   |                   |
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ALBERT WONG & CO.

CERTIFIED PUBLIC ACCOUNTANTS

Room 701, 7th Floor, Nan Dao Commercial Building

359-361 Queen's Road Central

Hong Kong

Tel : 2851 7954

Fax: 2545 4086

ALBERT WONG

B.Soc., Sc., ACA., LL.B., CPA(Practising)

To: The board of directors and stockholders of  
Iveda Solutions, Inc. ("the Company")

**Report of Independent Registered Public Accounting Firm**

We have audited the accompanying consolidated balance sheet of Iveda Solutions, Inc. and subsidiaries as of December 31, 2012 and 2011, and the related consolidated statements of income, stockholders' equity and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

We were not engaged to examine management's assertion about the effectiveness of the Company's internal control over financial reporting as of December 31, 2012 and 2011 included in the Company's Item 9A "Controls and

Procedures” in the Annual Report on Form 10-K and, accordingly, we do not express an opinion thereon.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Iveda Solutions, Inc. as of December 31, 2012 and 2011, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1 to the consolidated financial statements, the Company has suffered recurring losses from operations and has a significant accumulated deficit. In addition, the Company continues to experience negative cash flows from operations. These factors raise substantial doubt about the Company's ability to continue as a going concern. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Hong Kong      Albert Wong & Co.  
March 29, 2013 Certified Public Accountants

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**IVEDA SOLUTIONS, INC.****CONSOLIDATED BALANCE SHEETS****DECEMBER 31, 2012 AND 2011**

|  | 2012         | 2011         |
|--|--------------|--------------|
| <b>ASSETS</b>  |              |              |
| <b>CURRENT ASSETS</b>  |              |              |
| Cash and Cash Equivalents  | \$ 114,462   | \$ 850,364   |
| Restricted Cash  | 447,206      | 53,806       |
| Accounts Receivable, Net   | 1,958,799    | 942,879      |
| Inventory  | 123,021      | 80,033       |
| Other Current Assets   | 645,728      | 535,631      |
| Total Current Assets   | 3,289,216    | 2,462,713    |
| <b>PROPERTY AND EQUIPMENT, Net</b>   | 516,981      | 375,520      |
| <b>OTHER ASSETS</b>  |              |              |
| Intangible Assets, Net   | 166,666      | 186,667      |
| Goodwill   | 841,000      | 841,000      |
| Other Assets   | 105,621      | 15,474       |
| Total Other Assets   | 1,113,287    | 1,043,141    |
| Total Assets   | \$4,919,484  | \$3,881,374  |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>  |              |              |
| <b>CURRENT LIABILITIES</b>   |              |              |
| Accounts and Other Payables  | \$2,456,788  | \$1,095,269  |
| Due to Related Parties, net of debt discount   | 336,605      | 76,424       |
| Short Term Debt  | 802,122      | 248,319      |
| Current Portion of Long-Term Debt  | 75,707       | 11,882       |
| Total Current Liabilities  | 3,671,222    | 1,431,894    |
| <b>LONG TERM DEBT</b>  | 67,695       | 10,464       |
| <b>STOCKHOLDERS' EQUITY</b>  |              |              |
| Preferred Stock, \$0.00001 par value; 100,000,000 shares   | -            | -            |
| Common Stock, \$0.00001 par value; 200,000,000 shares Authorized; 20,458,048 and 18,031,729 shares issued And outstanding as of December 31, 2012 and 2011, respectively | 204          | 180          |
| Additional Paid-In Capital   | 16,204,068   | 13,642,892   |
| Accumulated Comprehensive Income (Loss)  | (23,629 )    | (45,907 )    |
| Accumulated Deficit  | (15,000,076) | (11,158,149) |

|  |             |             |
|--|-------------|-------------|
| Total Stockholders' Equity                 | 1,180,567   | 2,439,016   |
| Total Liabilities and Stockholders' Equity | \$4,919,484 | \$3,881,374 |

*See accompanying Notes to Financial Statements.*

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**IVEDA SOLUTIONS, INC.****CONSOLIDATED STATEMENTS OF OPERATIONS****YEARS ENDED DECEMBER 31, 2012 AND 2011**

|   | 2012             | 2011             |
|---|------------------|------------------|
| <b>REVENUE</b>                              |                  |                  |
| Equipment Sales                             | \$2,815,150      | \$2,081,923      |
| Service Revenue                             | 731,908          | 726,630          |
| Other Revenue                               | 61,940           | 10,176           |
| <b>Total Revenue</b>                        | <b>3,608,998</b> | <b>2,818,729</b> |
| <b>COST OF REVENUE</b>                      |                  |                  |
|   | 3,230,495        | 2,154,221        |
| <b>GROSS PROFIT</b>                         |                  |                  |
|   | 378,503          | 664,508          |
| <b>OPERATING EXPENSES:</b>                  |                  |                  |
| General & Administrative                    | 4,223,455        | 4,094,256        |
| Impairment of Goodwill                      | -                | 955,710          |
| <b>LOSS FROM OPERATIONS</b>                 |                  |                  |
|   | (3,844,952 )     | (4,385,458 )     |
| <b>OTHER INCOME (EXPENSE)</b>               |                  |                  |
| Foreign Currency Gain (Loss)                | (524 )           | -                |
| Interest Income                             | 806              | 996              |
| Interest Expense                            | (79,759 )        | (31,562 )        |
| <b>Total Other Income (Expense)</b>         | <b>(79,477 )</b> | <b>(30,566 )</b> |
| <b>LOSS BEFORE INCOME TAXES</b>             |                  |                  |
|   | (3,924,429 )     | (4,416,024 )     |
| <b>BENEFIT (PROVISION) FOR INCOME TAXES</b> | <b>82,502</b>    | <b>(47,027 )</b> |
| <b>NET LOSS</b>                             |                  |                  |
|   | \$(3,841,927 )   | \$(4,463,051 )   |
| <b>BASIC AND DILUTED LOSS PER SHARE</b>     |                  |                  |
|   | \$(0.20 )        | \$(0.28 )        |
| <b>WEIGHTED AVERAGE SHARES</b>              |                  |                  |
|   | 19,077,341       | 15,845,268       |

*See accompanying Notes to Financial Statements.*





**IVEDA SOLUTIONS, INC.****CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY****YEARS ENDED DECEMBER 31, 2012 AND 2011**

|                                     | Shares     | Amount | Additional<br>Paid-in-Capital | Accumulated<br>Deficit | Accumulated<br>other<br>Comprehensive<br>Income (loss) | Total<br>Stockholder's<br>Equity (Deficit) |
|-------------------------------------|------------|--------|-------------------------------|------------------------|--|--|
| BALANCE AT DECEMBER<br>31, 2010     | 13,664,257 | 137    | 7,212,914                     | (6,695,098 )           | -  | 517,953                                    |
| Common Stock Issued for<br>Cash     | 2,117,472  | 21     | 2,179,998                     |                        |  | 2,180,019                                  |
| Costs of Capital                    |            |        | (103,500 )                    |                        |  | (103,500 )                                 |
| Stock Based Compensation            |            |        | 515,419                       |                        |  | 515,419                                    |
| Stock Value of MEGAsys              | 1,700,000  | 17     | 1,665,983                     |                        |  | 1,666,000                                  |
| Contingent Consideration            |            |        | 1,635,980                     |                        |  | 1,635,980                                  |
| Debt Discount                       |            |        | 18,103                        |                        |  | 18,103                                     |
| Common Stock Issued for<br>Services | 550,000    | 5      | 517,995                       |                        |  | 518,000                                    |
| Net Loss                            |            |        |                               | (4,463,051 )           |  | (4,463,051 )                               |
| Comprehensive Loss                  |            |        |                               |                        | (45,907 )  | (45,907 )                                  |
| Total Comprehensive Loss            |            |        |                               |                        |  | (4,508,958 )                               |
| BALANCE AT DECEMBER<br>31, 2011     | 18,031,729 | \$ 180 | \$ 13,642,892                 | \$(11,158,149)         | \$ (45,907 )   | \$ 2,439,016                               |
| Common Stock Issued for<br>Cash     | 2,426,319  | 24     | 2,426,295                     |                        |  | 2,426,319                                  |
| Costs of Capital                    |            |        | (317,465 )                    |                        |  | (317,465 )                                 |
| Stock Based Compensation            |            |        | 248,072                       |                        |  | 248,072                                    |
| Debt Discount                       |            |        | 40,200                        |                        |  | 40,200                                     |
| Common Stock Issued for<br>Services | -          | -      | 164,074                       |                        |  | 164,074                                    |
| Net Loss                            |            |        |                               | (3,841,927 )           |  | (3,841,927 )                               |
| Comprehensive Loss                  |            |        |                               |                        | 22,278   | 22,278                                     |
| Total Comprehensive Loss            |            |        |                               |                        |  | (3,819,649 )                               |
| BALANCE AT DECEMBER<br>31, 2012     | 20,458,048 | \$ 204 | \$ 16,204,068                 | \$(15,000,076)         | \$ (23,629 )   | \$ 1,180,567                               |

*See accompanying Notes to Financial Statements.*

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**IVEDA SOLUTIONS, INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS****YEARS ENDED DECEMBER 31, 2012 AND 2011**

|   | 2012          | 2011          |
|---|---------------|---------------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>                                   |               |               |
| Net Loss  | \$(3,841,927) | \$(4,463,051) |
| Adjustments to Reconcile Net Loss to Net Cash<br>Used by Operating Activities |               |               |
| Depreciation and Amortization   | 218,229       | 255,692       |
| Stock Compensation  | 248,072       | 515,419       |
| Common stock issued for services  | 123,940       | 518,000       |
| Impairment of Goodwill  | -             | 955,710       |
| Provision for obsolete inventory  | 28,480        | 20,584        |
| (Increase) Decrease in Operating Assets:                                      |               |               |
| Accounts Receivable   | (970,337 )    | (29,998 )     |
| Inventory   | (68,375 )     | 20,527        |
| Other Current Assets  | (516,905 )    | (237,772 )    |
| Accounts and Other Payables   | 1,451,120     | 335,976       |
| Net cash used in operating activities   | (3,327,703)   | (2,108,913)   |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>                                   |               |               |
| Cash Acquired in Acquisition  | -             | 740,561       |
| Purchase of Property and Equipment  | (338,825 )    | (153,568 )    |
| Net cash provided by (used in) investing activities                           | (338,825 )    | 586,993       |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>                                   |               |               |
| Changes in Restricted Cash  | (385,112 )    | (41,720 )     |
| Proceeds from (Payments on) Short-term Notes Payable/Debt                     | 604,856       | (45,200 )     |
| Proceeds from (Payments to) Related Parties                                   | 456,989       | 90,000        |
| Proceeds from (Payments on) Long-term Debt                                    | 52,680        | (39,658 )     |
| Common Stock Issued, net of Costs of Capital                                  | 2,189,189     | 2,076,500     |
| Net cash provided by financing activities                                     | 2,918,602     | 2,039,922     |
| <b>EFFECT OF EXCHANGE RATE CHANGES ON CASH</b>                                | 12,024        | (22,981 )     |
| <b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>                   | (735,902 )    | 495,021       |
| Cash and Cash Equivalents - Beginning of Year                                 | 850,364       | 355,343       |
| <b>CASH AND CASH EQUIVALENTS - END OF YEAR</b>                                | \$114,462     | \$850,364     |

**SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION**

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|  |          |          |
|--|----------|----------|
| Debt Converted to Stock                            | \$0      | \$0      |
| Interest Paid                                      | \$79,758 | \$31,562 |
| Property and Equipment Purchased via Capital Lease | \$-      | \$9,374  |

*See accompanying Notes to Financial Statements.*

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**IVEDA SOLUTIONS, INC.**

**NOTES TO FINANCIAL STATEMENTS**

**YEARS ENDED DECEMBER 31, 2012 AND 2011**

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

Nature of Operations

Iveda Solutions, Inc. (formerly Iveda Corporation) (the “Company”) began operations on January 24, 2005, under the name IntelaSight, Inc., a Washington corporation doing business as Iveda Solutions (“IntelaSight”). On October 15, 2009, IntelaSight completed a reverse merger with Charmed Homes, Inc., a Nevada corporation (“Charmed”) pursuant to which IntelaSight became a wholly-owned subsidiary of Charmed and Charmed changed its name to Iveda Corporation. Prior to the reverse merger, Charmed was a shell company and did not have any operations.

All Company operations were conducted through IntelaSight until December 31, 2010, at which time IntelaSight merged with and into Iveda Corporation and Iveda Corporation changed its name to Iveda Solutions, Inc.

The Company installs video surveillance equipment, primarily for security purposes, and provides video hosting, archiving and real-time remote surveillance services to a variety of businesses and organizations throughout the United States.

On April 30, 2011, the Company completed its acquisition of Sole-Vision Technologies, Inc (doing business as MegaSys) (“MegaSys”). MegaSys was incorporated in the Republic of China (Taiwan) on July 5, 1999. MegaSys designs and integrates electronic security and surveillance products, software, and services.

**Consolidation**

The consolidated financial statements include the accounts of the Company and MegaSys through December 31, 2012. All intercompany balances and transactions have been eliminated in consolidation. See Note 11.

## Going Concern

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern, which contemplates the realization of assets and the liquidation of liabilities in the normal course of business. The Company generated accumulated losses of approximately \$15 million from January 2005 through December 31, 2012 and has insufficient working capital and cash flows to support operations. These factors raise substantial doubt about the Company's ability to continue as a going concern. The financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amounts and classification of liabilities that might result from this uncertainty.

A multi-step plan was adopted by management to enable the Company to continue to operate and begin to report operating profits. The highlights of that plan are:

- The Company successfully raised \$2,153,000 through March 15, 2013 in common stock at a purchase price of \$1.00 per share in a private placement memorandum offering and will continue efforts of this nature during 2013 as deemed necessary.

- The Board of Directors approved the Company to engage with a financial capital markets advisor in connection with a potential capital financial transaction to raise up to \$30 million (“Long Term Financing”).

The Board of Directors also approved the Company to raise up to an aggregate amount of \$3 million in bridge financing in advance of the Long Term Financing.

The Company plans to establish distributor networks with existing companies to create a reseller network to increase the scope of the Company’s marketing activities with low cost to the Company.

- The Company may evaluate and consider merger and/or acquisition activities.

- The Company completed the acquisition of MegaSys.

**IVEDA SOLUTIONS, INC.**

**NOTES TO FINANCIAL STATEMENTS**

**YEARS ENDED DECEMBER 31, 2012 AND 2011**

**Impairment of Long-Lived Assets**

The Company has a significant amount of property and equipment primarily consisting of leased equipment. The Company reviews the recoverability of the carrying value of long-lived assets using the methodology prescribed in ASC 360 "Property, Plant and Equipment." The Company reviews our long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset or asset group may not be recoverable. Recoverability of long-lived assets to be held and used is measured by a comparison of the carrying amount of an asset to the undiscounted future net operating cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured as the amount by which the carrying value of the assets exceeds their fair value. The Company did not make any impairment for the years ended December 31, 2012 and 2011.

**Basis of Accounting**

The Company's financial statements have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America.

**Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from these estimates.

**Revenue and Expense Recognition**



Company recognizes revenue when persuasive evidence of an arrangement exists, title transfer has occurred, the price is fixed or readily determinable, and collectability is reasonably assured. The Company recognizes revenue in accordance with ASC 605, "Revenue Recognition." Sales are recorded net of sales returns and discounts, which are estimated at the time of shipment based upon historical data.

Revenues from services are recognized when the services are provided. Expenses are recognized as incurred.

Revenues from fixed-price equipment installation contracts are recognized on the percentage-of-completion method. The percentage completed is measured by the percentage of costs incurred to date to estimated total costs for each contract. This method is used because management considers expended costs to be the best available measure of progress on these contracts. Because of inherent uncertainties in estimating costs and revenues, it is at least reasonably possible that the estimates used will change.

**IVEDA SOLUTIONS, INC.**

**NOTES TO FINANCIAL STATEMENTS**

**YEARS ENDED DECEMBER 31, 2012 AND 2011**

Contract costs include all direct material, subcontractors, labor costs, and equipment costs and those indirect costs related to contract performance. General and administrative costs are charged to expense as incurred. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are determined. Changes in job performance, job conditions, and estimated profitability may result in revisions to costs and income and are recognized in the period in which the revisions are determined. Changes in estimated job profitability resulting from job performance, job conditions, contract penalty provisions, claims, change orders, and settlements are accounted for as changes in estimates in the current period. Profit incentives are included in revenues when their realization is reasonably assured. Claims are included in revenues when realization is probable and the amount can be reliably estimated.

**Comprehensive loss**

Comprehensive loss is defined to include all changes in equity except those resulting from investments by owners and distributions to owners. Among other disclosures, all items that are required to be recognized under current accounting standards as components of comprehensive income are required to be reported in a financial statement that is presented with the same prominence as other financial statements. The Company's current component of other comprehensive income is the foreign currency translation adjustment.

**Concentrations**

Financial instruments, which potentially subject the Company to concentrations of credit risk, consist principally of cash and cash equivalents and trade accounts receivable.

Substantially all cash is deposited in two financial institutions, one in the United States and one in Taiwan. At times, amounts on deposit in the United States may be in excess of the FDIC insurance limit. Deposits in Taiwan financial institutions are insured by CDIC (Central Deposit Insurance Corporation) with maximum coverage of NTD 3 million. At times, amounts on deposit in Taiwan may be in excess of the CDIC Insurance limit.

Accounts receivable are unsecured and the Company is at risk to the extent such amount becomes uncollectible. The Company performs periodic credit evaluations of its customers' financial condition and generally does not require collateral. One customer in 2012 represented approximately 69% of total revenues and three customers in 2011 represented approximately 50% (26%, 14% and 10%) of total revenues. The net accounts receivable from this customer was approximately 76% of total accounts receivable as of December 31, 2012. No other customers represented greater than 10% of total revenues in 2012 and 2011.

### **Cash and Cash Equivalents**

For purposes of the statement of cash flows, the Company considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents.

### **Restricted cash**

Restricted cash represents time deposits on account to secure short-term bank loans in our foreign operation.

**IVEDA SOLUTIONS, INC.****NOTES TO FINANCIAL STATEMENTS****YEARS ENDED DECEMBER 31, 2012 AND 2011****Accounts Receivable**

The Company provides an allowance for doubtful collections which is based upon a review of outstanding receivables, historical collection information and existing economic conditions. For our US operation, receivables past due more than 120 days are considered delinquent. For our Taiwan operation, receivables over one year are considered delinquent. Delinquent receivables are written off based on individual credit valuation and specific circumstances of the customer. As of December 31, 2012, an allowance for uncollectible accounts of \$22,554 was deemed necessary for our US Operation. No allowance was deemed necessary as of December 31, 2011 for our US Operation. As of December 31, 2012 and 2011, respectively, an allowance of \$116,315 and \$100,703 was established against the receivables in our foreign corporation. The Company does not generally charge interest on past due receivables.

Trade receivables, net are comprised of the following:

|                                 | 2012        | 2011        |
|---------------------------------|-------------|-------------|
| Trade receivables, gross        | \$2,097,668 | \$1,043,582 |
| Allowance for doubtful accounts | (138,869 )  | (100,703 )  |
| Trade receivables, net          | \$1,958,799 | \$942,879   |

**Other Current Assets**

Other current assets are comprised of the following:

|                   | 2012    | 2011      |
|-------------------|---------|-----------|
| Notes receivables | \$6,255 | \$102,092 |
| Deposits-current  | 415,108 | 388,652   |

|   |           |           |
|---|-----------|-----------|
| Prepaid expenses and other current assets | 224,365   | 44,887    |
| Other current assets                      | \$645,728 | \$535,631 |

### **Notes Receivable**

Notes receivable represents post-dated checks collected from customers in Taiwan. The Company provides an allowance for doubtful accounts which is based upon a review of outstanding receivables, historical collection information and existing economic conditions. For our Taiwan operation, notes receivables over 90 days are considered delinquent. Delinquent receivables are written off based on individual credit valuation and specific circumstances of the customer. As of December 31, 2012 and 2011, no allowance for doubtful accounts was deemed necessary for our Taiwan operation. The company does not generally charge interest on notes receivable.

### **Deposits – Current**

The Company's current deposits represent tender deposits placed with local governments and major customers in Taiwan during the bidding process for new proposed projects.

### **Prepaid Expenses and Other Current Assets**

Prepaid expenses and other current assets represent cash paid in advance to insurance companies and vendors for service coverage extending into 2013. It also includes some other receivables as the result of travel advances due from employees.

### **Inventories**

Inventories consists of equipment purchased for installation projects and is recorded at the lower of cost (first-in, first-out) or market.

### **Property and Equipment**

Property and equipment are stated at cost. Depreciation is computed primarily using the straight-line method over the estimated useful lives of three to seven years. Expenditures for routine maintenance and repairs are charged to expense

as incurred. Depreciation expense for the years ended December 31, 2012 and 2011 was \$197,557 and \$107,833, respectively.

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**IVEDA SOLUTIONS, INC.**

**NOTES TO FINANCIAL STATEMENTS**

**YEARS ENDED DECEMBER 31, 2012 AND 2011**

**Intangible Assets and Goodwill**

Intangible assets consist of trademarks and other intangible assets associated with the purchase price allocation of MegaSys. Such assets are being amortized over their estimated useful lives of six months to ten years. Other intangible assets are fully amortized at December 31, 2012. Future amortization of Trademarks is as follows:

Trademarks

|            |          |
|------------|----------|
| 2013       | \$20,000 |
| 2014       | \$20,000 |
| 2015       | \$20,000 |
| 2016       | \$20,000 |
| 2017       | \$20,000 |
| Thereafter | \$66,667 |

Goodwill represents the excess of the purchase price of MegaSys over the net assets acquired.

We allocate goodwill to reporting units based on the reporting unit expected to benefit from the business combination. We evaluate our reporting units on an annual basis and, if necessary, reassign goodwill using a relative fair value allocation approach. Goodwill is tested for impairment at the reporting unit level on an annual basis and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying value. These events or circumstances could include a significant change in the business climate, legal factors, operating performance indicators, competition, or sale or disposition of a significant portion of a reporting unit.

Application of the goodwill impairment test requires judgment. We first assess qualitative factors to determine whether it is more likely than not that goodwill is impaired. If the more likely than not threshold is met, we perform a quantitative impairment test. At December 31, 2012, the Company determined that goodwill was not impaired.

**Other Assets**

Other assets are comprised of the following:

|                     | 2012      | 2011     |
|---------------------|-----------|----------|
| Deposits- long-term | \$10,836  | \$10,836 |
| Deferred tax assets | 94,785    | 4,638    |
| Other assets        | \$105,621 | \$15,474 |

**Deposits- long-term**

Long-term deposits consists of our security deposit held by Landlord under the First Amendment to Lease effective July 1, 2011 for our domestic office space.



**IVEDA SOLUTIONS, INC.****NOTES TO FINANCIAL STATEMENTS****YEARS ENDED DECEMBER 31, 2012 AND 2011****Income Taxes**

Deferred income taxes are recognized in the financial statements for the tax consequences in future years of differences between the tax bases of assets and liabilities and their financial reporting amounts based on enacted tax laws and statutory tax rates. Temporary differences arise from sales cut-off, depreciation, deferred rent expense, and net operating losses. Valuation allowances are established when necessary to reduce deferred tax assets to the amount that represents the Company's best estimate of such deferred tax assets that, more likely than not, will be realized. Income tax expense is the tax payable for the year and the change during the year in deferred tax assets and liabilities. During 2012, the Company reevaluated the valuation allowance for deferred tax assets and determined that no current benefits should be recognized for the year ended December 31, 2012 for our U.S. operation. However, a benefit of \$82,502 is recorded on the balance sheet for our Taiwan business. See Note 9 for more information.

The Company is subject to U.S. federal income tax as well as state income tax.

The Company's income tax returns are subject to review and examination by federal, state, and local authorities. The tax returns for the years 2006 to 2011 are open to examination by federal, local, and state authorities.

**Accounts and Other Payables**

Accounts and other payables are comprised of the following:

|                    | 2012      | 2011      |
|--------------------|-----------|-----------|
| Accounts Payable   | \$673,173 | \$499,640 |
| Accrued Expenses   | 1,674,258 | 393,612   |
| Income Tax Payable | 53,784    | 103,204   |
| Deferred Revenue   | 55,573    | 98,813    |

Accounts and Other Payables \$2,456,788 \$1,095,269

**Deferred Revenue**

Deposits received from customers on future installation projects are recorded as deferred revenue.

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**IVEDA SOLUTIONS, INC.**

**NOTES TO FINANCIAL STATEMENTS**

**YEARS ENDED DECEMBER 31, 2012 AND 2011**

**Stock-Based Compensation**

On January 1, 2006, the Company adopted the fair value recognition provisions of ASC 718, *Share-Based Payment*, which requires the recognition of an expense related to the fair value of stock-based compensation awards. The Company elected the modified prospective transition method as permitted by ASC 718. Under this transition method, stock-based compensation expense for the years ended December 31, 2012 and 2011 includes compensation expense for stock-based compensation granted on or after the date ASC 718 was adopted based on the grant-date fair value estimated in accordance with the provisions of ASC 718. The Company recognizes compensation expense on a straight-line basis over the requisite service period of the award. The fair value of stock-based compensation awards granted prior to, but not yet vested as of December 31, 2011 and 2010, were estimated using the “minimum value method” as prescribed by original provisions of ASC 718, *Accounting for Stock-Based Compensation*, therefore, no compensation expense is recognized for these awards in accordance with ASC 718. The Company recognized \$248,072 and \$515,419 of stock-based compensation expense for the years ended December 31, 2012 and 2011, respectively.

**Fair Value of Financial Instruments**

Fair value estimates discussed herein are based upon certain market assumptions and pertinent information available to management as of December 31, 2012 and 2011. The respective carrying value of certain on-balance-sheet financial instruments, approximate their fair values. These financial instruments include cash, accounts receivable, accounts payable, accrued expenses, and amounts due to related parties. Fair values were assumed to approximate carrying values for these financial instruments because they are short term in nature and their carrying amounts approximate fair values or they are receivable or payable on demand.

**Segment Information**

The Company conducts operations in various geographic regions outside the United States. The operations and the customer base conducted in the foreign countries are similar to the United States operations. The net revenues and net assets (liabilities) for other significant geographic regions outside the United States are as follows:

|               | Net Revenues | Net Assets |
|---------------|--------------|------------|
| United States | \$ 491,040   | \$ 814,845 |
| Asia          | \$ 2,841,157 | \$ 365,722 |
| Mexico        | \$ 276,801   | \$ -       |

Furthermore, due to operations in various geographic locations, the Company is susceptible to changes in national, regional and local economic conditions, demographic trends, consumer confidence in the economy and discretionary spending priorities that may have a material adverse effect on the Company's future operations and results.

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**IVEDA SOLUTIONS, INC.****NOTES TO FINANCIAL STATEMENTS****YEARS ENDED DECEMBER 31, 2012 AND 2011**

The Company is required to collect certain taxes and fees from customers on behalf of government agencies and remit these back to the applicable governmental agencies on a periodic basis. These taxes and fees are legal assessments to the customer, for which the Company has a legal obligation to act as a collection agent. Because the Company does not retain these taxes and fees, the Company does not include such amounts in revenue. The Company records a liability when the amounts are collected and relieves the liability when payments are made to the applicable governmental agencies.

The company operates as two reportable business segments as defined in ASC 280. "Segment Reporting." Each company has a chief operating decision maker and management personnel which review their company's performance as it relates to revenue, operating profit and operating expenses.

|                              | Twelve Months<br>Ending Dec. 31,<br>2012<br>Iveda Solutions,<br>Inc. | Twelve Months<br>Ending Dec. 31,<br>2012<br>MegaSys | Condensed<br>Consolidated<br>Total |
|------------------------------|--|---|------------------------------------|
| Revenue                      | \$ 765,109   | \$ 2,843,889  | \$3,608,998                        |
| Cost of Revenue              | 601,840  | 2,628,655   | 3,230,495                          |
| Gross Profit                 | 163,269  | 215,234   | 378,503                            |
| Depreciation and Amort.      | 209,521  | 8,708   | 218,229                            |
| General & Administrative     | 3,302,871  | 702,356   | 4,005,227                          |
| (Loss) from Operations       | (3,349,123 )   | (495,830 )  | (3,844,953 )                       |
| Interest Income              | -  | 806   | 806                                |
| (Loss) from Foreign Currency | (524 )   | -   | (524 )                             |
| Interest Expense             | (67,051 )  | (12,707 )   | (79,758 )                          |
| (Loss) Before Income Taxes   | (3,416,698 )   | (507,731 )  | (3,924,429 )                       |
| Benefit For Income Taxes     | -  | 82,502  | 82,502                             |
| Net Loss                     | \$ (3,416,698 )  | \$ (425,229 )                                       | \$ (3,841,927 )                    |

Revenues as shown below represent sales to external customers for each segment. Intercompany revenues have been eliminated and are immaterial for separate disclosure.

Additions to long-lived assets as presented in the following table represent capital expenditures.

Inventories, property and equipment for operating segments are regularly reviewed by management and are therefore provided below.

|                                      | December 31, |             |
|--------------------------------------|--------------|-------------|
|                                      | 2012         | 2011        |
| Revenues                             |              |             |
| United States                        | \$767,841    | \$1,054,354 |
| Republic of China (Taiwan)           | 2,843,889    | 1,823,087   |
| Elimination of intersegment revenues | (2,732 )     | (58,712 )   |
|                                      | \$3,608,998  | \$2,818,729 |

|                                    | December 31,  |               |
|------------------------------------|---------------|---------------|
|                                    | 2012          | 2011          |
| Operating earnings (loss)          |               |               |
| United States                      | \$(3,348,419) | \$(4,067,453) |
| Republic of China (Taiwan)         | (495,830 )    | (327,660 )    |
| Elimination of intersegment profit | (703 )        | 9,655         |
|                                    | \$(3,844,952) | \$(4,385,458) |

|                            | December 31, |           |
|----------------------------|--------------|-----------|
|                            | 2012         | 2011      |
| Property and equipment     |              |           |
| United States              | \$488,648    | \$365,964 |
| Republic of China (Taiwan) | 28,333       | 9,556     |
|                            | \$516,981    | \$375,520 |

December 31,

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|                                | 2012      | 2011      |
|--------------------------------|-----------|-----------|
| Additions to long-lived assets |           |           |
| United States                  | \$338,432 | \$150,029 |
| Republic of China (Taiwan)     | 5,395     | 3,539     |
|                                | \$343,827 | \$153,568 |

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|                            | December 31, |          |
|----------------------------|--------------|----------|
|                            | 2012         | 2011     |
| Inventory                  |              |          |
| United States              | \$26,794     | \$7,236  |
| Republic of China (Taiwan) | 96,227       | 72,797   |
|                            | \$123,021    | \$80,033 |

|                            | December 31, |             |
|----------------------------|--------------|-------------|
|                            | 2012         | 2011        |
| Total Assets               |              |             |
| United States              | \$1,727,017  | \$2,021,637 |
| Republic of China (Taiwan) | 3,192,467    | 1,859,737   |
|                            | \$4,919,484  | \$3,881,374 |

### Reclassification

Certain amounts in 2011 have been reclassified to conform to the 2012 presentation.

### New Accounting Standards

In October 2012, FASB has issued Accounting Standards Update (ASU) No. 2012-04, Technical Corrections and Improvements. This ASU make technical corrections, clarifications, and limited-scope improvements to various Topics throughout the Codification. The amendments in this ASU that will not have transition guidance will be effective upon issuance for both public entities and nonpublic entities. For public entities, the amendments that are subject to the transition guidance will be effective for fiscal periods beginning after December 15, 2012. For nonpublic entities, the amendments that are subject to the transition guidance will be effective for fiscal periods beginning after December 15, 2013. The Company does not expect the adoption of this guidance to have a material impact on its consolidated financial statements.

In August 2012, FASB has issued Accounting Standards Update (ASU) No. 2012-03, Technical Amendments and Corrections to SEC Sections. This ASU amends various SEC paragraphs pursuant to SAB 114, SEC Release No. 33-9250, and ASU 2010-22, which amend or rescind portions of certain SAB Topics. The Company does not expect the adoption of this guidance to have a material impact on its consolidated financial statements.



In July 2012, the FASB issued ASU 2012-02, Intangibles—Goodwill and Other (Topic 350): Testing Indefinite-Lived Intangible Assets for Impairment. The objective of the measure is to reduce the cost and complexity associated with performing an impairment test for indefinite-lived intangible assets and to make the impairment test similar to the recent changes for testing goodwill for impairment (ASU 2011-08). ASU 2012-02 is effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012 and early adoption is permitted. The Company does not expect the adoption of this guidance to have a material impact on its consolidated financial statements.

In December 2011, the Financial Accounting Standards Board ("FASB") issued ASU 2011-11, Balance Sheet (Topic 210) Disclosures about Offsetting Assets and Liabilities. The amendments in this update will enhance disclosures required by U.S. GAAP by requiring improved information about financial instruments and derivative instruments that are either (1) offset in accordance with either ASC 210-20-45 or ASC 815-10-45 or (2) subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset in accordance with either ASC 210-20-45 or ASC 815-10-45. This information will enable users of an entity's financial statements to evaluate the effect or potential effect of netting arrangements on an entity's financial position, including the effect or potential effect of rights of setoff associated with certain financial instruments and derivative instruments in the scope of this Update. The amendments in this Update are effective for annual periods for fiscal years beginning on or after January 1, 2013. The Company does not expect the adoption of this guidance to have a material impact on its consolidated financial statements.

In September 2011, the FASB has issued Accounting Standards Update (ASU) No. 2011-08, Intangibles—Goodwill and Other (Topic 350): Testing Goodwill for Impairment. ASU 2011-08 is intended to simplify how entities, both public and nonpublic, test goodwill for impairment. ASU 2011-08 permits an entity to first assess qualitative factors to determine whether it is "more likely than not" that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test described in Topic 350, Intangibles-Goodwill and Other. The more-likely-than-not threshold is defined as having a likelihood of more than 50%. ASU 2011-08 is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted, including for annual and interim goodwill impairment tests performed as of a date before September 15, 2011, if an entity's financial statements for the most recent annual or interim period have not yet been issued or, for nonpublic entities, have not yet been made available for issuance.

**IVEDA SOLUTIONS, INC.**

**NOTES TO FINANCIAL STATEMENTS**

**YEARS ENDED DECEMBER 31, 2012 AND 2011**

**NOTE 2 RELATED PARTIES**

The Company has provided surveillance services since 2005 to entities owned by Ross Farnsworth, either through a family partnership or through his majority owned LLC, and subsequently Mr. Farnsworth became a shareholder of the Company in 2006. Mr. Farnsworth's holdings are less than 5% of the Company but the revenue for years ending 2012 and 2011 \$71,350 and \$68,119, respectively, and there was a trade accounts receivable balance of \$0 and \$5,859 at December 31, 2012 and 2011.

On June 20, 2012, the Company entered into a convertible debenture agreement with a Board Member for \$200,000. Interest is payable at 12% per annum, payable on the maturity date of June 20, 2013. The Company issued warrants to purchase 20,000 shares of the Company Stock, at an exercise price of \$ 1.00. Accordingly, the Company recognized a discount of \$16,789 on the principal value of the \$200,000 and is amortizing the discount over the 12 month term of the debenture. The debenture is convertible into shares of Company Common Stock on or before the Maturity Date, at a conversion rate of \$1.00 per share. \$ 200,000

On September 26, 2011, the Company entered into a \$45,000 promissory note agreement with one of its shareholders. Interest on the note will be payable in 45,000 warrants at a \$1.10 exercise price, exercisable within three years of issuance. On October 24, 2011, the Board of Directors approved the issuance of the warrants. Accordingly, the Company recognized a discount of \$16,909 on the principal value of the \$45,000 note payable and is amortizing the discount over the 12 month life of the note. On September 25, 2012 a Promissory Note Extension Agreement was signed to extend the maturity date of one of the \$45,000 notes to March 25, 2013. 45,000

On November 19, 2012, the Company entered into a separate convertible debenture agreement with a different Board Member for \$100,000. Interest is payable at 10% per annum, payable on the maturity date of May 19, 2013. The Company issued warrants to purchase 10,000 shares of the Company Stock, at an exercise price of \$ 1.10. The debenture is convertible into shares of Company Common Stock on or before the Maturity Date, at a conversion rate of \$1.10 per share. 100,000

Less: Debt Discount (8,395 )

Total Due to Related Parties, net of debt discount \$ 336,605

**NOTE 3 SHORT-TERM DEBT**

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Two short-term bank loans were initiated on September 28, 2012 and November 26, 2012, due and payable on April 30, 2013 and November 26, 2013 respectively. The short-term debt balances were as follows:

|   | 2012       | 2011       |
|---|------------|------------|
| Loan from Sovereign Bank at an interest rate at 5.8% per annum, due on November 26, 2013 (2011: 3.26% per annum, due on May 21, 2012)                         | \$ 132,097 | \$ 99,600  |
| Loan from Bank of Shanghai at various interest rates ranging from 1% per annum to 3.24%. Due on April 30, 2013 (2011: 1% per annum, due on February 29, 2012) | 488,025    | 112,880    |
| Notes Payable, non-interest-bearing, maturing Jan. 2012 to August 2012  | -          | 35,839     |
| Note Payable, 10% interest per annum, maturing on December 7, 2013  | 77,000     | -          |
| Note Payable, 10% interest per annum, maturing on December 20, 2013   | 10,000     | -          |
| Note Payable, maturing on January 29, 2013  | 50,000     | -          |
| Note Payable, 12% interest per annum, maturing on March 25, 2013  | 45,000     | -          |
| Balance at end of year  | \$ 802,122 | \$ 248,319 |

The holder of the \$77,000 note is entitled to subscribe for a purchase 7,000 warrant shares at an exercise price of \$1.50 per share. The holder of the \$10,000 note is entitled to subscribe for a purchase 909 warrant shares at an exercise price of \$1.50 per share. The holder of the 50,000 note was issued 50,000 warrant shares in lieu of interest on August 2, 2012. The holder of this note may choose to convert this note into shares of Company Common Stock on or before the maturity date, at a conversion rate of \$1.10 per share.

**NOTE 4 OBLIGATIONS UNDER CAPITAL LEASES AND LONG-TERM DEBT**

The Company is the lessee of certain computer equipment under capital leases extending through 2014. The assets and liabilities under the capital leases are recorded at the lower of the present value of the minimum lease payments or the fair value of the assets. The assets are depreciated over their estimated useful lives. The computer equipment has been recorded in the accompanying financial statements in office equipment of \$257,166 and \$257,166 and accumulated depreciation of \$207,590 and \$158,163 at December 31, 2012 and 2011, respectively. The leases have imputed interest rates between 8% and 22% and monthly payments between \$53 and \$361.

Future minimum lease payments under the capital leases as of December 31, 2012 for each of the remaining years are as follows:

|                              |         |
|------------------------------|---------|
| Year Ending December 31,     |         |
| 2013                         | \$9,630 |
| 2014                         | 2,468   |
| Total Minimum Lease Payments | 12,098  |
| Less: Interest               | 1,090   |

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|                         |         |
|-------------------------|---------|
| Total Principal         | 11,008  |
| Less: Current Portion   | 8,370   |
| Long-Term Capital Lease | \$2,638 |

Our Taiwan subsidiary has \$65,057 in Long-Term debt relating to a bank loan. Total Long-Term Debt for the Company is \$67,695.

As of December 31, 2012, the long-term bank balance was as follows:

|   | 2012      | 2011 |
|---|-----------|------|
| Loan from Taipei Fubon Bank with an interest rate at 5.5% per annum, due on November 26, 2014 | \$140,764 | \$ - |
| Current Portion of Long-Term Debt   | (75,707)  | -    |
| Balance at end of year  | \$65,057  | \$ - |

The future principal payments under the bank loans are as follows:

| For the year ended December 31, |           |
|---------------------------------|-----------|
| 2013                            | \$75,707  |
| 2014                            | 65,057    |
| Total                           | \$140,764 |

**IVEDA SOLUTIONS, INC.**

**NOTES TO FINANCIAL STATEMENTS**

**YEARS ENDED DECEMBER 31, 2012 AND 2011**

**NOTE 5 OPERATING LEASES**

The Company leases its office facilities under a non-cancelable operating lease expiring October 2016 that requires minimum monthly payments ranging from \$8,669 to \$10,836. Rent expense was \$107,885 and \$95,635 for the years ended December 31, 2012 and 2011, respectively. The Company also has two non-cancellable data center service agreements for approximately \$7,298 and \$2,575 per month, expiring September 2014. The company has a third non-cancellable data center service agreement for approximately \$5,826, expiring March 2015. Data center services expense was \$170,776 and \$126,626 for the years ended December 31, 2012 and 2011, respectively, and is included as a component of Cost of Revenue in the Statement of Operations.

Future minimum lease payments under these leases are as follows:

|       |            |
|-------|------------|
| 2013  | \$ 309,211 |
| 2014  | 268,194    |
| 2015  | 135,169    |
| 2016  | 108,356    |
| Total | \$820,930  |

**NOTE6 PREFERRED STOCK**

The Company has the authority to issue 100 million shares of preferred stock with a par value of \$0.00001 per share and may be divided into and issued in series. The Board of Directors is authorized, within any limitations prescribed by law and the Company's Article of Incorporation to fix and determine the designations, rights, qualifications, preferences, limitations and terms of the shares of any series of Preferred Stock.

**NOTE 7 EQUITY**

**Common Stock**

During 2011, the Company raised \$2,180,019 in a private placement of shares at prices ranging from \$.80 at \$1.00 per share. Costs associated with this raise totaled \$103,500. In the second quarter of 2011, there were 675,000 shares issued at a price of \$.80 per share in two private placement transactions with two corporations. In the same quarter, there were 22,472 shares issued at a price of \$.89 per share to a trust. All remaining shares were issued at \$1.00 per share in approximately 36 private placement transactions with a mix of investors including 14 individuals, 16 trusts and 6 corporations.

During 2012, the Company raised \$2,426,319 in a private placement of shares at \$1.00 per share. Costs associated with this raise totaled \$317,465. The mix of investors include 21 individuals, 3 trusts and 4 corporations.

**IVEDA SOLUTIONS, INC.**

**NOTES TO FINANCIAL STATEMENTS**

**YEARS ENDED DECEMBER 31, 2012 AND 2011**

**NOTE 8 STOCK OPTION PLAN AND WARRANTS**

**Stock Options**

On October 15, 2009, the Company adopted the 2009 Stock Option Plan (the "2009 Option Plan"), pursuant to which it may grant equity awards to eligible persons. The 2009 Option Plan allows the Company's Board of Directors (the "Board") to grant options to purchase up to 1,500,000 shares of common stock to directors, officers, key employees, and service providers of the Company. As of December 31, 2011, options to purchase 1,166,729 shares were outstanding under the 2009 Option Plan.

On January 18, 2010, the Company adopted the 2010 Stock Option Plan (the "2010 Option Plan"), which allows the Board to grant options to purchase up to 1,000,000 shares of common stock to directors, officers, key employees, and service providers of the Company. In 2011, the 2010 Option Plan was amended to increase the number of shares issuable under the 2010 Option Plan to 3,000,000 shares. The shares under the 2010 Option Plan are registered with the SEC under Forms S-8 filed on February 2, 2010 and June 24, 2011. As of December 31, 2011, options to purchase 2,496,450 shares were outstanding under the 2010 Option Plan.

Stock options may be granted as either incentive stock options intended to qualify under Section 422 of the Internal Revenue Code of 1986, as amended (the "Code"), or as options not qualified under Section 422 of the Code. All options are issued with an exercise price at or above the fair market value of the common stock on the date of the grant as determined by the Company's Board of Directors. Incentive stock option plan awards of restricted stock are intended to qualify as deductible performance-based compensation under Section 162(m) of the Code. Incentive Stock Option awards of unrestricted stock are not designed to be deductible to the Company under Section 162(m). Under the Plan, stock options will terminate on the tenth anniversary date of the grant or earlier if provided in the grant.

**IVEDA SOLUTIONS, INC.****NOTES TO FINANCIAL STATEMENTS****YEARS ENDED DECEMBER 31, 2012 AND 2011**

The Company has also granted non-qualified stock options to employees and contractors. All non-qualified options are generally issued with an exercise price that may not be less than the fair value of the common stock on the date of the grant as determined by the Company's Board of Directors. Options may be exercised up to ten years following the date of the grant, with vesting schedules determined by the Company upon grant. Vesting periods range from 100% fully vested upon grant to a range of up to four years. Vested options may be exercised up to three months following date of termination of the relationship. The fair values of options are determined using the Black-Scholes option-pricing model. The estimated fair value of options is recognized as expense on the straight-line basis over the options' vesting periods. The Company has unrecognized stock-based compensation with a weighted-average term of approximately 3 years of \$416,021 at December 31, 2012.

Stock option transactions during 2012 and 2011 were as follows:

|  | 2012       | Weighted -<br>Average<br>Exercise<br>Price | 2011       | Weighted -<br>Average<br>Exercise<br>Price |
|--|------------|--|------------|--|
|  | Shares     |  | Shares     |  |
| Outstanding at Beginning of Year                               | 3,663,179  | \$ 0.81                                    | 1,959,979  | \$ 0.73                                    |
| Granted  | 1,529,333  | 1.16                                       | 2,053,200  | 0.99                                       |
| Exercised  | -          | -  | -          | -  |
| Forfeited or Canceled  | (154,000 ) | 1.01                                       | (350,000 ) | 1.06                                       |
| Outstanding at End of Year                                     | 5,038,512  | 0.91                                       | 3,663,179  | 0.81                                       |
| Options Exercisable at Year-End                                | 3,748,003  | 1.22                                       | 3,024,029  | 0.85                                       |
| Weighted-Average Fair Value of Options Granted During the Year | \$0.28     |  | \$0.35     |  |

Information with respect to stock options outstanding and exercisable at December 31, 2012 is as follows:

| Options Outstanding<br>Number | Weighted -<br>Average | Weighted - | Options Exercisable<br>Number | Weighted -<br>Exercisable |
|-------------------------------|-----------------------|------------|-------------------------------|---------------------------|
|-------------------------------|-----------------------|------------|-------------------------------|---------------------------|



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| Range of<br>Exercise<br>Prices | at<br>December 31<br>2012 | Remaining<br>Contractual<br>Life | Average<br>Exercise<br>Price | At<br>December 31,<br>2012 | Average<br>Exercise<br>Price |
|--------------------------------|---------------------------|----------------------------------|------------------------------|----------------------------|------------------------------|
| \$0.10 - \$1.40                | 5,038,512                 | 7.9 Years                        | \$ 0.91                      | 3,748,003                  | \$ 1.22                      |

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**IVEDA SOLUTIONS, INC.****NOTES TO FINANCIAL STATEMENTS****YEARS ENDED DECEMBER 31, 2012 AND 2011**

The fair value of each option granted is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions used for options granted.

|                         |         |   |         |   |
|-------------------------|---------|---|---------|---|
|                         | 2012    |   | 2011    |   |
| Expected Life           | 5 Years |   | 5 Years |   |
| Dividend Yield          | 0       | % | 0       | % |
| Expected Volatility     | 26      | % | 38      | % |
| Risk-Free Interest Rate | .80     | % | 1.53    | % |

Expected volatility for 2012 and 2011 was estimated by using the Dow Jones U.S. Industry indexes sector classification methodology for industries similar to the Company. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the grant date. The expected life of the options is based on the average of three public companies offering services similar to the Company.

**Warrants**

The Company has also periodically issued warrants to purchase shares of common stock as equity compensation to officers, directors, employees, and consultants. On October 24, 2011 the Company authorized the issuance of warrants to purchase 47,500 of Common Stock at an exercise price of \$1.10 per share, exercisable within three years of grant date, to one of its Board Members for his help in raising funds without compensation.

As of December 31, 2012, warrants to purchase 2,797,219 shares of common stock were outstanding, all of which were issued either as equity compensation or in connection with financing transactions. Warrants may be exercised between a range of two to ten years following the date of the grant, with vesting schedules determined by the Company upon issue. Vesting periods range from 100% fully vested upon grant to four years. The fair value of warrants is determined using the Black-Scholes option-pricing model. The estimated fair value of warrants is recognized as expense on the straight-line basis over the warrants' vesting periods.

**IVEDA SOLUTIONS, INC.****NOTES TO FINANCIAL STATEMENTS****YEARS ENDED DECEMBER 31, 2012 AND 2011**

Stock warrant transactions for 2012 and 2011 were as follows:

|  | 2012       |   | 2011      |   |
|--|------------|---|-----------|---|
|  | Shares     | Weighted -<br>Average<br>Exercise Price | Shares    | Weighted -<br>Average<br>Exercise Price |
| Outstanding at Beginning of year                               | 1,612,778  | \$ 0.77                                 | 1,064,778 | \$ 0.59                                 |
| Granted  | 1,434,441  | 1.07                                    | 548,000   | 1.10                                    |
| Exercised  | -          | 0.00                                    | -         | 0.00                                    |
| Forfeited or Canceled  | (250,000 ) | 1.00                                    | -         | 0.00                                    |
| Outstanding at end of Year                                     | 2,797,219  | 0.90                                    | 1,612,778 | 0.77                                    |
| Warrants Redeemable at End of Year                             | 2,797,219  | 0.90                                    | 1,600,278 | 0.77                                    |
| Weighted-Average Fair Value of Warrants Issued During the Year | \$0.31     |   | \$0.34    |   |

Information with respect to warrants outstanding and exercisable at December 31, 2012 is as follows:

| Range of<br>Exercise<br>Prices | Warrants Outstanding                                |   |  | Warrants Redeemable                                |  |
|--------------------------------|---|---|--|--|--|
|                                | Number<br>Outstanding<br>at<br>December 31,<br>2012 | Weighted -<br>Average<br>Remaining<br>Contractual<br>Life | Weighted -<br>Average<br>Redemption<br>Price | Number<br>Redeemable<br>at<br>December 31,<br>2012 | Weighted -<br>Average<br>Redemption<br>Price |
| \$0.10 - \$1.10                | 2,797,219   | 3.6 Years   | \$ 0.90                                      | 2,797,219  | \$ 0.90                                      |

The fair value of each warrant issued is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions used for warrants issued.

|                         | 2012   | 2011   |
|-------------------------|--------|--------|
| Expected Life           | 3.8    | 3.8    |
| Dividend Yield          | 0 %    | 0 %    |
| Expected Volatility     | 24 %   | 32 %   |
| Risk-Free Interest Rate | 1.65 % | 2.17 % |

Expected volatility was estimated by using the Dow Jones U.S. Industry indexes sector classification methodology for industries similar to the Company. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the grant date. The expected life of warrants is based on the actual expiration date of the grant.

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**IVEDA SOLUTIONS, INC.****NOTES TO FINANCIAL STATEMENTS****YEARS ENDED DECEMBER 31, 2012 AND 2011****NOTE 9 INCOME TAXES****U.S. FEDERAL CORPORATE INCOME TAX**

Temporary differences between financial statement carrying amounts and the tax basis of assets and liabilities and tax credit and operating loss carryforwards that create deferred tax assets and liabilities are as follows:

|                                       | 2012        | 2011        |
|---------------------------------------|-------------|-------------|
| Tax Operating Loss Carryforward - USA | \$4,665,000 | \$3,539,000 |
| Accelerated Depreciation – USA        | (57,900 )   | (59,500 )   |
| Valuation Allowance - USA             | (4,607,100) | (3,479,500) |
|                                       | \$-         | \$-         |

The valuation allowance increased approximately \$1,127,600, primarily as a result of the increased net operating losses of the operation in the USA.

As of December 31, 2012, the Company has federal net operating loss carryforwards for income tax purposes of approximately \$11,453,000 which will begin to expire in 2025. The Company also has Arizona, California and Minnesota net operating loss carryforwards for income tax purposes of approximately \$9,379,000, \$1,870,000 and \$105,000 which will begin to expire in 2013. These carryforwards have been utilized in the determination of the deferred income taxes for financial statement purposes. The following table accounts for federal net operating loss carryforwards only.

| Year Ending<br>December 31, | Net Operating<br>Loss: | Year of<br>Expiration: |
|-----------------------------|------------------------|------------------------|
| 2012                        | \$ 2,850,000           | 2032                   |
| 2011                        | 2,427,000              | 2031                   |

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|      |               |      |
|------|---------------|------|
| 2010 | 1,799,000     | 2030 |
| 2009 | 1,750,000     | 2029 |
| 2008 | 1,308,000     | 2028 |
| 2007 | 429,000       | 2027 |
| 2006 | 476,000       | 2026 |
| 2005 | 414,000       | 2025 |
|      | \$ 11,453,000 |      |

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**IVEDA SOLUTIONS, INC.****NOTES TO FINANCIAL STATEMENTS****YEARS ENDED DECEMBER 31, 2012 AND 2011**

The tax provision differs from the expense that would result from applying Federal statutory rates to income before income taxes due to the effect of state income taxes and because certain expenses are deducted for financial reporting that are not deductible for tax purposes.

|   | 2012          | 2011          |
|---|---------------|---------------|
| Tax Benefit of 34%                                  | \$(1,148,400) | \$(1,391,513) |
| Increase (Decrease) in Income Taxes Resulting from: |               |               |
| State Income Tax Benefit, Net of Federal Tax        | (134,458 )    | (112,253 )    |
| Nondeductible Expenses                              | 175,851       | 217,297       |
| Valuation Allowance                                 | 1,107,007     | 1,286,469     |
| Total   | \$-           | \$-           |

**TAIWAN (REPUBLIC OF CHINA) CORPORATE TAX**

Sole-Vision Technologies, Inc. is a subsidiary of the Company which is operating in Taiwan as a profit-seeking enterprise. Its applicable corporate income tax rate is 17%. In addition, Taiwan's corporate tax system allows the government to levy a 10% profit retention tax on undistributed earnings for the prior year. This tax will not be provided if the company distributed the earnings before the ended of the fiscal year.

According to the Taiwan corporate income tax ("TCIT") reporting system, the TCIT sales cut-off base is concurrent with the business tax classified as value-added type ("VAT") which will be reported to the Ministry of Finance ("MOF") on a bi-monthly basis. Since the VAT and TCIT are accounted for on a VAT tax basis that recorded all sales on business tax on a VAT tax reporting system, the Company is bound to report the TCIT according to the MOF prescribed tax reporting rules. Under the VAT tax reporting system, sales cut-off did not take the accrual base but rather on a VAT taxable reporting basis. Therefore, when the company adopted US GAAP on accrual basis, the sales cut-off TCIT timing difference which derived from the VAT reporting system will create a temporary sales cut-off timing difference and this difference is reflected in the deferred tax assets or liabilities calculations on the income tax estimation reported in the Form 10-K.

**IVEDA SOLUTIONS, INC.****NOTES TO FINANCIAL STATEMENTS****YEARS ENDED DECEMBER 31, 2012 AND 2011**

Temporary differences between financial statement carrying amounts and the tax basis of assets and liabilities and VAT tax reporting system and operating loss carryforwards that create deferred tax assets and liabilities are as follows:

|  | December 31, 2012 |           |
|--|-------------------|-----------|
|  | US Dollar         |           |
| Tax Operating Income – Taiwan                  | \$                | 7,957     |
| Temporary Difference:                          |                   |           |
| VAT reporting system – Sales cut-off           | (201,571          | )         |
| VAT reporting system – Cost & expenses cut-off | (221,542          | )         |
| Provision of Bad Debt                          | (11,598           | )         |
| Accelerated Depreciation – Taiwan              | 1,198             |           |
| Permanent Difference:                          |                   |           |
| Inventory written-off                          | 5,343             |           |
| Non-deductible expenses                        | (103,690          | )         |
| Miscellaneous income                           | 16,172            |           |
| Adjusted Net Loss Before Tax – Taiwan          | \$                | (507,731) |

Income tax expense (benefits) for the years ended December 31, 2012 and 2011 is summarized as followings:

|   | 2012       | 2011     |
|---|------------|----------|
| Current:  |            |          |
| Provision for Federal Income Tax (34%)              | \$—        | \$—      |
| Provision for TCIT (17%)                            | 6,007      | 16,850   |
| Provision for Undistributed Earnings Tax (10%)      | —          | 89,176   |
| Increase (Decrease) in Income Taxes Resulting from: |            |          |
| Pre-acquisition TCIT                                | —          | (4,811)  |
| Temporary Difference                                | (88,509)   | (54,188) |
| Income Tax Expenses (Benefit)                       | \$(82,502) | \$47,207 |

**RECONCILIATION OF DEFERRED TAX ASSET/(LIABILITIES)**



|                              |          |
|------------------------------|----------|
| Deferred Tax Assets          | 2012     |
| Balance at Beginning of Year | \$4,638  |
| Temporary Difference         | 88,509   |
| Foreign currency difference  | 1,638    |
| Balance at End of Year       | \$94,785 |

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**IVEDA SOLUTIONS, INC.****NOTES TO FINANCIAL STATEMENTS****YEARS ENDED DECEMBER 31, 2012 AND 2011****NOTE 10 EARNINGS (LOSS) PER SHARE**

The following table provides a reconciliation of the numerators and denominators reflected in the basic and diluted earnings per share computations, as required by ASC No. 260, "Earnings Per Share" ("EPS").

Basic EPS is computed by dividing reported earnings available to stockholders by the weighted average shares outstanding. The Company had net losses for the years ended December 31, 2012 and 2011 and the effect of including dilutive securities in the earnings per common share would have been anti-dilutive. Accordingly, all options to purchase common shares were excluded from the calculation of diluted earnings per share for the years ended December 31, 2012 and 2011. Total common stock equivalents that could be convertible into common stock were 7,835,731 and 5,275,957 for 2012 and 2011, respectively.

|                         | 2012           | 2011           |
|-------------------------|----------------|----------------|
| Basic EPS               |                |                |
| Net Loss                | \$(3,841,927 ) | \$(4,463,051 ) |
| Weighted Average Shares | 19,077,341     | 15,845,268     |
| Basic Loss Per Share    | \$(0.20 )      | \$(0.28 )      |

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**IVEDA SOLUTIONS, INC.**

**NOTES TO FINANCIAL STATEMENTS**

**YEARS ENDED DECEMBER 31, 2012 AND 2011**

**NOTE 11 BUSINESS COMBINATION**

On April 30, 2011, the Company completed its acquisition of MegaSys. The Company issued 1,700,000 shares of its common stock, which was valued at \$0.98 per share (market value on the date of acquisition). In addition, the Company is committed to the issuance of an additional 2,000,000 shares of its common stock (valued at \$1,636,000) if certain financial milestones are obtained by MegaSys. MegaSys must achieve at least \$300,000 post tax income for the year ended December 31, 2011. For 2012, MegaSys must achieve \$300,000 post tax income and increase net revenues by \$1,300,000 related to the SafeCiti project from July 1, 2010 to December 31, 2012. If these milestones are not achieved, the additional 2,000,000 shares will not be issued.

The preliminary purchase price allocation based on qualified independent valuation is as follows:

|                        |             |
|------------------------|-------------|
| Cash                   | \$740,561   |
| Accounts Receivable    | 588,726     |
| Property and Equipment | 20,678      |
| Other Assets           | 458,523     |
| Intangible Assets      | 330,000     |
| Goodwill               | 1,796,710   |
| Liabilities Assumed    | (633,198 )  |
| Total Purchase Price   | \$3,302,000 |

In connection with the acquisition, the Company also issued 250,000 shares of common stock to a consultant who advised the Company on its acquisition. The value of the shares issued (\$245,000) is reflected in the Statement of Operations for the periods ended December 31, 2011.

The following is the unaudited pro forma condensed consolidated financial statement of the combined entity as though the business combination had been as of the beginning of the comparable annual reporting period for the twelve-month period ended December 31, 2012 and the twelve-month period ended December 31, 2011 for comparability purposes.

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|   | Twelve Months Ended December 31, |                 |
|---|----------------------------------|-----------------|
|   | 2012                             | 2011            |
| Total revenues                                  | \$ 3,608,998                     | \$ 3,349,003    |
| Total net expenses                              | 7,533,427                        | 6,641,482       |
| Income (loss) before income taxes               | (3,924,429 )                     | (3,292,479 )    |
| Income tax benefit (provision)                  | 82,502                           | (51,838 )       |
| Net income (loss)                               | \$ (3,841,927 )                  | \$ (3,344,317 ) |
| Net income (loss) per share — basic and diluted | \$ (0.20 )                       | \$ (0.18 )      |

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**IVEDA SOLUTIONS, INC.**

**NOTES TO FINANCIAL STATEMENTS**

**YEARS ENDED DECEMBER 31, 2012 AND 2011**

**NOTE 12 CONTINGENT LIABILITIES**

As part of the terms of contracts with New Taipei City for projects performed during 2012, MegaSys is required to provide after-project services in accordance with the contract terms. If MegaSys were to fail provide these after-project services in the future, other parties of the related contract would have recourse. The financial exposure to MegaSys in the event of failure to provide after-project services in the future total \$1,802,542.

**NOTE 13 SUBSEQUENT EVENTS (UNAUDITED)**

Since January 1, 2013 through March 15, 2013 the Company has sold 2,153,000 shares of Company Common Stock at a purchase price of \$1.00 per share in 49 private placement transactions with 27 individuals, 6 trusts and 4 corporations.

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## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on April 1, 2013.

IVEDA SOLUTIONS, INC.

By: /s/ David Ly  
David Ly  
Chief Executive Officer, President  
(Principal Executive Officer)

Pursuant to the requirements of Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated on April 1, 2013.

|  |   |
|--|---|
| /s/ David Ly<br>David Ly                     | Chief Executive Officer and Director<br>(Principal Executive Officer)                 |
| /s/ Brian Duling<br>Lynne Phillis            | Chief Financial Officer and Treasurer<br>(Principal Financial and Accounting Officer) |
| /s/ Joseph Farnsworth<br>Joseph Farnsworth   | Director  |
| /s/ Gregory Omi<br>Gregory Omi               | Director  |
| /s/ James D. Staudohar<br>James D. Staudohar | Director  |
| /s/ Chen-Ho (Alex) Kuo<br>Chen-Ho (Alex) Kuo | Director  |
| /s/ Robert Gillen<br>Robert Gillen           | Director  |
| /s/ Alejandro Franco<br>Alejandro Franco     | Director  |

