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

FORM 10-Q

☒ QUARTERLY REPORT UNDER SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2016

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

For the transition period from _______ to ________

Commission File number 000-30262

VISUALANT, INCORPORATED

(Exact name of registrant as specified in charter)

Nevada	**90-0273142**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
500 Union Street, Suite 420, Seattle, Washington USA	**98101**
(Address of principal executive offices)	(Zip Code)

206-903-1351
(Registrant's telephone number, including area code)

N/A
(Former name, address, and fiscal year, if changed since last report)

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

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

Indicate by checkmark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer (See the definitions of “large accelerated filer,” “accelerated filer,” “non-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 ☒

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

The number of shares of common stock, $.001 par value, issued and outstanding as of May 5, 2016: 1,261,344 shares

TABLE OF CONTENTS

ITEM 1. FINANCIAL STATEMENTS

VISUALANT, INCORPORATED AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	March 31, 2016	September 30, 2015
ASSETS		(audited)
CURRENT ASSETS:		
Cash and cash equivalents	$ 520,281	$ 82,266
Accounts receivable, net of allowance of $40,000 and $40,000, respectively	810,484	619,849
Prepaid expenses	35,321	27,774
Inventories, net	253,963	217,824
Total current assets	1,620,049	947,713
EQUIPMENT, NET	344,244	366,250
OTHER ASSETS		
Intangible assets, net	86,750	158,000
Goodwill	983,645	983,645
Other assets	5,070	5,070
TOTAL ASSETS	$ 3,039,758	$ 2,460,678
LIABILITIES AND STOCKHOLDERS' (DEFICIT)		
CURRENT LIABILITIES:		
Accounts payable - trade	$ 2,557,359	$ 2,520,223
Accounts payable - related parties	30,480	73,455
Accrued expenses	71,517	4,068
Accrued expenses - related parties	1,250,415	1,256,861
Derivative liability	3,574,346	2,704,840
Convertible notes payable	868,749	109,000
Notes payable - current portion of long term debt	1,307,632	1,164,692
Deferred revenue	833	5,833
Total current liabilities	9,661,331	7,838,972
COMMITMENTS AND CONTINGENCIES	-	-
STOCKHOLDERS' DEFICIT		
Preferred stock - $0.001 par value, 5,000,000 shares authorized, 0 shares issued and outstanding at 3/31/2016 and 9/30/2015, respectively	-	-
Series A Convertible Preferred stock - $0.001 par value, 23,334 shares authorized, 23,334 and 11,667 issued and outstanding at 3/31/2016 and 9/30/2015, respectively	23	12
Series B Redeemable Convertible Preferred stock - $0.001 par value, 5,000 shares authorized, 255 and 0 shares issued and outstanding at 3/31/2016 and 9/30/2015, respectively	5	-
Common stock - $0.001 par value, 100,000,000 shares authorized, 1,259,644 and 1,155,991 shares issued and outstanding at 3/31/2016 and 9/30/2015, respectively	1,260	1,156
Additional paid in capital	19,850,314	18,786,694
Accumulated deficit	(26,473,175)	(24,166,156)
Total stockholders' deficit	(6,621,573)	(5,378,294)
TOTAL LIABILITIES AND STOCKHOLDERS' DEFICIT	$ 3,039,758	$ 2,460,678

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

VISUALANT, INCORPORATED AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended,		Six Months Ended,	
	March 31, 2016	March 31, 2015	March 31, 2016	March 31, 2015
REVENUE	$ 1,467,465	$ 1,435,097	$ 2,752,265	$ 3,278,310
COST OF SALES	1,252,275	1,204,705	2,338,953	2,750,154
GROSS PROFIT	215,190	230,392	413,312	528,156
RESEARCH AND DEVELOPMENT EXPENSES	81,765	77,143	173,727	196,530
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	817,778	875,022	1,553,985	1,528,225
OPERATING LOSS	(684,353)	(721,773)	(1,314,400)	(1,196,599)
OTHER INCOME (EXPENSE):				
Interest expense	(87,737)	(83,889)	(126,378)	(121,019)
Other income	945	12,131	3,265	18,448
Gain (loss) on change - derivative liability	476,454	3,032,030	(869,506)	381,023
Total other income (expense)	389,662	2,960,272	(992,619)	278,452
LOSS BEFORE INCOME TAXES	(294,691)	2,238,499	(2,307,019)	(918,147)
Income taxes - current provision	-	(3,752)	-	(3,089)
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NET (LOSS) INCOME	$ (294,691)	$ 2,242,251	$ (2,307,019)	$ (915,058)
Basic and diluted (loss) income per common share attributable to Visualant,				
Inc. and subsidiaries common shareholders-				
Basic and diluted l(oss) income per share	$ (0.24)	$ 1.99	$ (1.95)	$ (0.81)
Weighted average shares of common stock outstanding- basic and diluted	1,210,141	1,128,757	1,185,620	1,124,897

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

VISUALANT, INCORPORATED AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Six Months Ended,	
	March 31, 2016	March 31, 2015
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (2,307,019)	$ (915,058)
Adjustments to reconcile net loss to net cash (used in) operating activities		
Depreciation and amortization	94,546	209,882
Issuance of capital stock for services and expenses	184,827	137,500
Stock based compensation	23,674	40,150
(Gain) on sale of assets	(800)	(18,650)
Loss on change - derivative liability	869,506	(381,023)
Provision for losses on accounts receivable	649	3,036
Non-cash related to issuance of convertible notes payable	131,507	-
Changes in operating assets and liabilities:		
Accounts receivable	(191,284)	(52,882)
Prepaid expenses	(7,547)	(9,724)
Inventory	(36,139)	103,088
Accounts payable - trade and accrued expenses	55,164	760,980
Income tax receivable	-	(3,089)
Deferred revenue	(5,000)	-
CASH (USED IN) OPERATING ACTIVITIES	(1,187,916)	(125,790)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital expenditures	(1,290)	-
Proceeds from sale of equipment	800	20,060
NET CASH (USED IN) PROVIDED BY INVESTING ACTIVITIES:	(490)	20,060
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from line of credit	142,940	(88,799)
Proceeds from sale of preferred stock	505,000	350,000
Proeeds from warrant exercises	169,360	-
Proceeds from convertible notes payable	924,500	64,000
Repayments of convertible notes	(114,979)	(166,500)
Repayments of capital leases	-	(1,495)
NET CASH PROVIDED BY FINANCING ACTIVITIES	1,626,821	157,206
NET INCREASE IN CASH AND CASH EQUIVALENTS	438,415	51,476
CASH AND CASH EQUIVALENTS, beginning of period	82,266	70,386
CASH AND CASH EQUIVALENTS, end of period	$ 520,681	$ 121,862
Supplemental disclosures of cash flow information:		
Interest paid	$ 26,460	$ 81,257
Taxes paid	$ -	$ -
Gain (loss) on change - derivative liability warrants	$ -	$ 17,727
Issuance of common stock for debt conversion	$ -	$ 25,499

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

VISUALANT, INCORPORATED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. ORGANIZATION

Visualant, Incorporated (the "Company," "Visualant, Inc." or "Visualant") was incorporated under the laws of the State of Nevada in 1998. The Company has authorized 105,000,000 shares of capital stock, of which 100,000,000 are shares of voting common stock, par value $0.001 per share, and 5,000,000 are shares preferred stock, par value $0.001 per share. On July 21, 2015, the Company filed with the Secretary of State of Nevada an Amended and Restated Certificate of Designations, Preferences and Rights for our Series A Convertible Preferred Stock. On March 8, 2016, the Company received approval from the State of Nevada for the Certificate of Designations of Preferences, Powers, Rights and Limitations of Series B Redeemable Convertible Preferred Stock. The Certificate authorized 5,000 shares of Series B Preferred Stock at a par value of $.001 per share that is convertible into common stock at $7.50 per share, subject to certain adjustments as set forth in the Certificate.

Since 2007 the Company has been focused primarily on the development of a proprietary technology which is capable of uniquely identifying and authenticating almost any substance using light at the "photon" level to detect the unique digital "signature" of the substance. The Company calls this its "ChromaID™" technology.

In 2010, the Company acquired TransTech Systems, Inc. as an adjunct to its business. TransTech is a distributor of products for employee and personnel identification. TransTech currently provides substantially all of the Company's revenues.

The Company is in the process of commercializing its ChromaID™ technology. To date, the Company has entered into one License Agreement with Sumitomo Precision Products Co., Ltd. and has a strategic relationship with Invention Development Management Company, L.L.C. ("IDMC").

The Company believes that its commercialization success is dependent upon its ability to significantly increase the number of customers that are purchasing and using its products. To date the Company has generated minimal revenue from sales of its ChromaID products. The Company is currently not profitable. Even if the Company succeeds in introducing the ChromaID technology and related products to its target markets, the Company may not be able to generate sufficient revenue to achieve or sustain profitability.

ChromaID was invented by scientists from the University of Washington under contract with Visualant. The Company has pursued an aggressive intellectual property strategy and have been granted nine patents. The Company also has 21 patents pending. The Company possess all right, title and interest to the issued patents. Ten of the pending patents are licensed exclusively to the Company in perpetuity by the Company's strategic partner, Intellectual Ventures through its subsidiary IDMC.

On May 6, 2015, the Company's stockholders approved a reverse split of our common stock, in a ratio to be determined by the Company's Board of Directors, of not less than 1-for-50 nor more than 1-for-150. On June 9, 2015, the Company's Board of Directors determined that the ratio of the reverse split would be 1-for-150. All warrant, option, share and per share information in this Form 10-Q gives retroactive effect for a 1-for-150 split with all numbers rounded up to the nearest whole share.

2. GOING CONCERN

The accompanying financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. The Company incurred net losses of $ 2,307,019, $2,631,037 and $1,017,291 for the six months ended March 31, 2016 and the years ended September 30, 2015 and 2014, respectively. Net cash used in operating activities was $(1,187,916), $(239,877) and $(1,379,397) for the for the six months ended March 31, 2016 and the years ended September 30, 2015 and 2014, respectively.

The Company anticipates that it will record losses from operations for the foreseeable future. As of March 31, 2016, the Company's accumulated deficit was $26,473,175. The Company has limited capital resources, and operations to date have been funded with the proceeds from private equity and debt financings and loans from Ronald P. Erickson, our Chief Executive Officer, or entities with which he is affiliated. These conditions raise substantial doubt about our ability to continue as a going concern. The audit report prepared by the Company's independent registered public accounting firm relating to our financial statements for the year ended September 30, 2015 includes an explanatory paragraph expressing the substantial doubt about the Company's ability to continue as a going concern.

Continuation of the Company as a going concern is dependent upon obtaining additional working capital. The financial statements do not include any adjustments that might be necessary if we are unable to continue as a going concern.

3. SIGNIFICANT ACCOUNTING POLICIES: ADOPTION OF ACCOUNTING STANDARDS

Basis of Presentation – The accompanying unaudited consolidated financial statements include the accounts of the Company. Intercompany accounts and transactions have been eliminated. The preparation of these unaudited condensed consolidated financial statements were prepared in conformity with U.S. generally accepted accounting principles (“GAAP”).

The unaudited consolidated financial statements of the Company and the accompanying notes included in this Quarterly Report on Form 10-Q are unaudited. In the opinion of management, all adjustments necessary for a fair presentation of the Consolidated Financial Statements have been included. Such adjustments are of a normal, recurring nature. The Consolidated Financial Statements, and the accompanying notes, are prepared in accordance with generally accepted accounting principles in the United States ("GAAP") and do not contain certain information included in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2015. The interim Condensed Consolidated Financial Statements should be read in conjunction with that Annual Report on Form 10-K.

Principles of Consolidation – The consolidated financial statements include the accounts of the Company and its wholly owned and majority-owned subsidiaries, TransTech Systems, Inc. Inter-Company items and transactions have been eliminated in consolidation.

Cash and Cash Equivalents – The Company classifies highly liquid temporary investments with an original maturity of three months or less when purchased as cash equivalents. The Company maintains cash balances at various financial institutions. Balances at US banks are insured by the Federal Deposit Insurance Corporation up to $250,000. The Company has not experienced any losses in such accounts and believes it is not exposed to any significant risk for cash on deposit.

Accounts Receivable and Allowance for Doubtful Accounts – Accounts receivable consist primarily of amounts due to the Company from normal business activities. The Company maintains an allowance for doubtful accounts to reflect the expected non-collection of accounts receivable based on past collection history and specific risks identified within the portfolio. If the financial condition of the customers were to deteriorate resulting in an impairment of their ability to make payments, or if payments from customers are significantly delayed, additional allowances might be required.

Inventories – Inventories consist primarily of printers and consumable supplies, including ribbons and cards, badge accessories, capture devices, and access control components held for resale and are stated at the lower of cost or market on the first-in, first-out (“FIFO”) method. Inventories are considered available for resale when drop shipped and invoiced directly to a customer from a vendor, or when physically received by TransTech at a warehouse location. The Company records a provision for excess and obsolete inventory whenever an impairment has been identified. There is a $20,000 for impaired inventory as of March 31, 2016 and September 30, 2015, respectively.

Equipment – Equipment consists of machinery, leasehold improvements, furniture and fixtures and software, which are stated at cost less accumulated depreciation and amortization. Depreciation is computed by the straight-line method over the estimated useful lives or lease period of the relevant asset, generally 2-10 years, except for leasehold improvements which are depreciated over 5-20 years.

Intangible Assets/ Intellectual Property – The Company amortizes the intangible assets and intellectual property acquired in connection with the acquisition of TransTech, over sixty months on a straight - line basis, which was the time frame that the management of the Company was able to project forward for future revenue, either under agreement or through expected continued business activities. Intangible assets and intellectual property acquired from RATLab LLC and Javelin are recorded likewise. The Company performs annual assessments and has determined that no impairment is necessary. On June 7, 2011, the Company closed the acquisition of all Visualant related assets of the RATLab LLC, namely the rights to the medical field of use of the Chroma ID technology. On July 31, 2012, the Company closed the acquisition of all rights to the ChromaID technology in the environmental field of use from Javelin LLC.

Goodwill – Goodwill is the excess of cost of an acquired entity over the fair value of amounts assigned to assets acquired and liabilities assumed in a business combination. With the adoption of ASC 350, goodwill is not amortized, rather it is tested for impairment annually, and will be tested for impairment between annual tests if an event occurs or circumstances change that would indicate the carrying amount may be impaired. Impairment testing for goodwill is done at a reporting unit level. Reporting units are one level below the business segment level, but are combined when reporting units within the same segment have similar economic characteristics. Under the criteria set forth by ASC 350, the Company has one reporting unit based on the current structure. An impairment loss generally would be recognized when the carrying amount of the reporting unit’s net assets exceeds the estimated fair value of the reporting unit. The Company performs annual assessments and has determined that no impairment is necessary.

Long-Lived Assets – The Company reviews its long-lived assets for impairment annually or when changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Long-lived assets under certain circumstances are reported at the lower of carrying amount or fair value. Assets to be disposed of and assets not expected to provide any future service potential to the Company are recorded at the lower of carrying amount or fair value (less the projected cost associated with selling the asset). To the extent carrying values exceed fair values, an impairment loss is recognized in operating results.

Fair Value Measurements and Financial Instruments – ASC Topic 820, *Fair Value Measurement and Disclosures*, defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. This topic also establishes a fair value hierarchy, which requires classification based on observable and unobservable inputs when measuring fair value. The fair value hierarchy distinguishes between assumptions based on market data (observable inputs) and an entity's own assumptions (unobservable inputs). The hierarchy consists of three levels:

Level 1 – Quoted prices in active markets for identical assets and liabilities;

Level 2 – Inputs other than level one inputs that are either directly or indirectly observable; and.

Level 3 - Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The recorded value of other financial assets and liabilities, which consist primarily of cash and cash equivalents, accounts receivable, other current assets, and accounts payable and accrued expenses approximate the fair value of the respective assets and liabilities at March 31, 2016 and September 30, 2015 based upon the short-term nature of the assets and liabilities.

Derivative financial instruments -The Company evaluates all of its financial instruments to determine if such instruments are derivatives or contain features that qualify as embedded derivatives. For derivative financial instruments that are accounted for as liabilities, the derivative instrument is initially recorded at its fair value and is then re-valued at each reporting date, with changes in the fair value reported in the consolidated statements of operations. For stock-based derivative financial instruments, the Company uses a weighted average Black-Scholes-Merton option pricing model to value the derivative instruments at inception and on subsequent valuation dates. The classification of derivative instruments, including whether such instruments should be recorded as liabilities or as equity, is evaluated at the end of each reporting period. Derivative instrument liabilities are classified in the balance sheet as current or non-current based on whether or not net-cash settlement of the derivative instrument could be required within twelve months of the balance sheet date.

Revenue Recognition – Visualant and TransTech revenue are derived from products and services. Revenue is considered realized when the products or services have been provided to the customer, the work has been accepted by the customer and collectability is reasonably assured. Furthermore, if an actual measurement of revenue cannot be determined, the Company defers all revenue recognition until such time that an actual measurement can be determined. If during the course of a contract management determines that losses are expected to be incurred, such costs are charged to operations in the period such losses are determined. Revenues are deferred when cash has been received from the customer but the revenue has not been earned.

Stock Based Compensation – The Company has share-based compensation plans under which employees, consultants, suppliers and directors may be granted restricted stock, as well as options to purchase shares of Company common stock at the fair market value at the time of grant. Stock-based compensation cost is measured by the Company at the grant date, based on the fair value of the award, over the requisite service period. For options issued to employees, the Company recognizes stock compensation costs utilizing the fair value methodology over the related period of benefit. Grants of stock options and stock to non-employees and other parties are accounted for in accordance with the ASC 505.

Convertible Securities – Based upon ASC 815-15, we have adopted a sequencing approach regarding the application of ASC 815-40 to convertible securities issued subsequent to September 30, 2015. We will evaluate our contracts based upon the earliest issuance date. In the event partial reclassification of contracts subject to ASC 815-40-25 is necessary, due to our inability to demonstrate we have sufficient shares authorized and unissued, shares will be allocated on the basis of issuance date, with the earliest issuance date receiving first allocation of shares. If a reclassification of an instrument were required, it would result in the instrument issued latest being reclassified first

Income Taxes – Income taxes are calculated based upon the asset and liability method of accounting. Deferred income taxes are recorded to reflect the tax consequences in future years of differences between the tax basis of assets and liabilities and their financial reporting amounts at each year-end. A valuation allowance is recorded against deferred tax assets if management does not believe the Company has met the "more likely than not" standard to allow for recognition of such an asset. In addition, realization of an uncertain income tax position must be estimated as "more likely than not" (i.e., greater than 50% likelihood of receiving a benefit) before it can be recognized in the financial statements. Further, the recognition of tax benefits recorded in the financial statements, if any, is based on the amount most likely to be realized assuming a review by tax authorities having all relevant information.

Net Loss per Share – Under the provisions of ASC 260, "Earnings Per Share," basic loss per common share is computed by dividing net loss available to common shareholders by the weighted average number of shares of common stock outstanding for the periods presented. Diluted net loss per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that would then share in the income of the Company, subject to anti-dilution limitations. The common stock equivalents have not been included as they are anti-dilutive. As of March 31, 2016, there were (i) options outstanding for the purchase of 56,641 common shares; (ii) warrants for the purchase of 931,755 common shares; (iii) 23,334 shares of our common stock issuable upon the conversion of Series A Convertible Preferred Stock; (iv) up to 28,554 shares of our common stock issuable upon the exercise of placement agent warrants; (v) an unknown number of shares related to the conversion of $975,000 in convertible promissory notes and an unknown number of our common shares issuable upon the exercise of $719,000 of warrants related to Convertible Notes Payable; and (vi) and unknown number of shares related to the conversion of Series B Redeemable Preferred Stock which could potentially dilute future earnings per share. As of March 31, 2015, there were (i) options outstanding for the purchase of 72,433 common shares; (ii) warrants for the purchase of 899,702 common shares; (iii) preferred stock for the conversion of 23,334 common shares; and (iv) an unknown number of shares related to the conversion of a $64,000 Convertible Promissory Note which could potentially dilute future earnings per share.

Dividend Policy – The Company has never paid any cash dividends and intends, for the foreseeable future, to retain any future earnings for the development of our business. Our future dividend policy will be determined by the board of directors on the basis of various factors, including our results of operations, financial condition, capital requirements and investment opportunities.

Patent Policy—The Company expenses all costs incurred for patents applications and registered trademarks.

Use of Estimates – The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Recent Accounting Pronouncements

A variety of proposed or otherwise potential accounting standards are currently under study by standard setting organizations and various regulatory agencies. Due to the tentative and preliminary nature of those proposed standards, management has not determined whether implementation of such proposed standards would be material to our consolidated financial statements.

New Accounting Standards Issued But Not Yet Adopted

In July 2015, the FASB issued ASU 2015-11, *Inventory (Topic 330): Simplifying the Measurement of Inventory* ("ASU 2015-11"). This ASU requires inventories measured under any methods other than last-in, first-out ("LIFO") or the retail inventory method to be subsequently measured at the lower of cost or net realizable value, rather than at the lower of cost or market. Subsequent measurement of inventory using LIFO or the retail inventory method is unchanged by this ASU. ASU 2015-11 is effective for public companies for interim and annual periods beginning after December 15, 2016. The Company is currently evaluating the impact that this standard will have on the consolidated financial statements and does not anticipate a significant impact to the Company's financial position as a result of this change.

In February 2015, the FASB issued ASU No. 2015-02, *Consolidation (Topic 810): Amendments to the Consolidation Analysis* ("ASU 2015-02"). ASU 2015-02 affects reporting entities that are required to evaluate whether they should consolidate certain legal entities. ASU 2015-02 is effective for us on January 1, 2016, with early adoption permitted. The Company does not believe that this pronouncement had no impact on the Company's consolidated financial statements.

In April 2015, the FASB issued ASU No. 2015-03, *Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs ("ASU 2015-03")* The amendments in ASU 2015-03 require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in ASU 2015-03. ASU 2015-03 is effective for the Company on January 1, 2016, with early adoption permitted. The Company is currently evaluating the potential changes from this ASU to the Company's future financial reporting and disclosures.

4. DEVELOPMENT OF OUR CHROMAID™ TECHNOLOGY

The Company is focused primarily on the development of a proprietary technology which is capable of uniquely identifying and authenticating almost any substance using light to create, record and detect the unique digital "signature" of the substance. The Company calls this its "ChromaID™" technology.

The Company's ChromaID™ Technology

The Company has developed a proprietary technology to uniquely identify and authenticate almost any substance. This patented technology utilizes light at the photon (elementary particle of light) level through a series of emitters and detectors to generate a unique signature or "fingerprint" from a scan of almost any solid, liquid or gaseous material. This signature of reflected or transmitted light is digitized, creating a unique ChromaID signature. Each ChromaID signature is comprised of from hundreds or thousands of specific data points.

The ChromaID technology looks beyond visible light frequencies to areas of near infra-red and ultraviolet light that are outside the humanly visible light spectrum. The data obtained allows the Company to create a very specific and unique ChromaID signature of the substance for a myriad of authentication and verification applications.

Traditional light-based identification technology, called spectrophotometry, has relied upon a complex system of prisms, mirrors and visible light. Spectrophotometers typically have a higher cost and utilize a form factor more suited to a laboratory setting and require trained laboratory personnel to interpret the information. The ChromaID technology uses lower cost LEDs and photodiodes and specific frequencies of light resulting in a more accurate, portable and easy-to-use solution for a wide variety of applications. The ChromaID technology not only has significant cost advantages as compared to spectrophotometry, it is also completely flexible is size, shape and configuration. The ChromaID scan head can range in size from endoscopic to a scale that could be the size of a large ceiling-mounted florescent light fixture.

In normal operation, a ChromaID master or reference scan is generated and stored in a database. The Visualant scan head can then scan similar materials to identify, authenticate or diagnose them by comparing the new ChromaID digital signature scan to that of the original or reference ChromaID signature or scan result.

The following summarizes the Company's plans for its Company's proprietary ChromaID technology. Based on the Company's anticipated expenditures on this technology, the expected efforts of its management and its relationship with Intellectual Ventures and its subsidiary, IDMC, and the Company's other strategic partner, Sumitomo Precision Products, Ltd., the Company expects its ChromaID technology to provide an increasing portion of its revenues in future years from product sales, licenses, royalties and other revenue streams., as discussed further below.

ChromaID: A Foundational Platform Technology

The Company's ChromaID technology provides a platform upon which a myriad of applications can be developed. As a platform technology, it is analogous to a smartphone, upon which an enormous number of previously unforeseen applications have been developed. The ChromaID technology is an enabling technology that brings the science of light and photonics to low cost, real world commercialization opportunities across multiple industries. The technology is foundational and as such, the basis upon which the Company believes a significant business can be built.

As with other foundational technologies, a single application may reach across multiple industries. The ChromaID technology can, for example effectively differentiate and identify different brands of clear vodkas that appear identical to the human eye. By extension this same technology can identify pure water from water with contaminants present. It can provide real time detection of liquid medicines such as morphine that have been adulterated or compromised. It can detect if jet fuel has water contamination present. It could determine when it is time to change oil in a deep fat fryer. These are but a few of the potential applications of the ChromaID technology based upon extensions of its ability to identify different clear liquids.

The cornerstone of a company with a foundational platform technology is its intellectual property. ChromaID was invented by scientists from the University of Washington under contract with Visualant. The Company has pursued an aggressive intellectual property strategy and has been granted nine patents. The Company currently have 21 patents pending. The Company possesses all right, title and interest to the issued patents. Ten of the pending patents are licensed exclusively to us in perpetuity by our strategic partner, the IDMC subsidiary of Intellectual Ventures.

IDMC Relationship

In November 2013, the Company entered into a strategic relationship with IDMC, a subsidiary of Intellectual Ventures, a private intellectual property fund. IDMC has worked to expand the reach and the potential application of the ChromaID technology and has filed ten patents base on the ChromaID technology, which it has licensed to the Company. In connection with IDMC's work to expand the Company's intellectual property portfolio, the Company agreed to curtail outbound marketing activities of its technology through the fourth fiscal quarter of 2014.

Products

The Company first delivered product, the ChromaID Lab Kit, scans and identifies solid surfaces. The Company is marketing this product to customers who are considering licensing the technology. Target markets include, but are not limited to, commercial paint manufacturers, pharmaceutical equipment manufacturers, process control companies, currency paper and ink manufacturers, security cards, cosmetic companies, scanner manufactures and food processing companies.

The Company's second product, the ChromaID Liquid Lab Kit, scans and identifies liquids. This product is currently in prototype form. Similar to the Company's first product, it will be marketed to customers who are considering licensing the technology. Rather than use an LED emitter to reflect light off of a surface that is captured by a photodiode to generate a ChromaID signature the liquid analysis product shines light through the liquid (transmissive) with the LEDs positioned on one side of the liquid sample and the photo detectors on the opposite side. This device is in a functional state in our laboratory and the Company anticipates having a Liquid ChromaID Lab Kit available for customers by the Company during the fall of 2015. Target markets include, but are not limited to, water companies, petrochemical companies, pharmaceutical companies, and numerous consumer applications.

The ChromaID Lab Kits allows potential licensors of our technology to work with our technology and develop solutions for their particular application. Our contractual arrangements with IDMC are described in greater detail below.

The Company's next planned product should be an exemplar product is a prototype that will be produced to address several markets. The primary purpose of this prototype will be to demonstrate the technology to prospective business partners, and will consist of a small, hand held, battery powered, Bluetooth enabled scanning device. The scanner should wirelessly connect to a smart phone or tablet to transfer the scanned data. The smart phone application will include two or three industry specific but generic applications that allow for the demonstration of the scanning and matching of the ChromaID signatures. The applications will focus on drug identification, food safety and liquid detection. The prototype device will lend itself to consumer applications and can be a consumer product as well.

Research and Development

The Company's research and development efforts are primarily focused improving the core foundational ChromaID technology and developing new and unique applications for the technology. As part of this effort, the Company typically conduct testing to ensure that ChromaID application methods are compatible with the customer's requirements, and that they can be implemented in a cost effective manner. The Company is also actively involved in identifying new application methods. Visualant's team has considerable experience working with the application of light-based technologies and their application to various industries. The Company believes that its continued development of new and enhanced technologies relating to our core business is essential to its future success. The Company spent $362,661 and $670,742 during the years ended September 30, 2015 and 2014, respectively, on research and development activities. The Company's research and development efforts are supported internally, through its relationship with IDMC and through contractors led by Dr. Tom Furness and his team at RATLab LLC.

The Company's Patents

The Company believes that it's nine patents, 21 patent applications, and two registered trademarks, and our trade secrets, copyrights and other intellectual property rights are important assets. The Company's patents will expire at various times between 2027 and 2033. The duration of the Company's trademark registrations varies from country to country. However, trademarks are generally valid and may be renewed indefinitely as long as they are in use and/or their registrations are properly maintained.

The patents that have been granted to Visualant include:

On August 9, 2011, the Company was issued US Patent No. 7,996,173 B2 entitled "Method, Apparatus and Article to Facilitate Distributed Evaluation of Objects Using Electromagnetic Energy," by the United States Office of Patents and Trademarks. The patent expires August 24, 2029.

On December 13, 2011, the Company was issued US Patent No. 8,076,630 B2 entitled "System and Method of Evaluating an Object Using Electromagnetic Energy" by the United States Office of Patents and Trademarks. The patent expires November 7, 2028.

On December 20, 2011, the Company was issued US Patent No. 8,081,304 B2 entitled "Method, Apparatus and Article to Facilitate Evaluation of Objects Using Electromagnetic Energy" by the United States Office of Patents and Trademarks. The patent expires July 28, 2030.

On October 9, 2012, the Company was issued US Patent No. 8,285,510 B2 entitled "Method, Apparatus, and Article to Facilitate Distributed Evaluation of Objects Using Electromagnetic Energy" by the United States Office of Patents and Trademarks. The patent expires July 31, 2027.

On February 5, 2013, the Company was issued US Patent No. 8,368,878 B2 entitled "Method, Apparatus and Article to Facilitate Evaluation of Objects Using Electromagnetic Energy by the United States Office of Patents and Trademarks. The patent expires July 31, 2027.

On November 12, 2013, the Company was issued US Patent No. 8,583,394 B2 entitled "Method, Apparatus and Article to Facilitate Distributed Evaluation of Objects Using Electromagnetic Energy by the United States Office of Patents and Trademarks. The patent expires July 31, 2027.

On November 21, 2014, the Company was issued US Patent No. 8,888,207 B2 entitled "Systems, Methods, and Articles Related to Machine-Readable Indicia and Symbols" by the United States Office of Patents and Trademarks. The patent expires February 7, 2033.

On March 23, 2015, the Company was issued US Patent No. 8,988,666 B2 entitled "Method, Apparatus, and Article to Facilitate Evaluation of Objects Using Electromagnetic Energy" by the United States Office of Patents and Trademarks. The patent expires July 31, 2027.

On May 26, 2015, the Company was issued patent US Patent No. 9,041,920 B2 entitled "Device for Evaluation of Fluids using Electromagnetic Energy" by the United States Office of Patents and Trademarks. The patent expires March 12, 2033.

The Company pursues an aggressive patent strategy to expand its unique intellectual property in the United States and othercountries.

Services and License Agreement Invention Development Management Company, L.L.C.

In November 2013, the Company entered into a Services and License Agreement with IDMC. IDMC is affiliated with Intellectual Ventures, which collaborates with inventors and partners with pioneering companies and invests both expertise and capital in the process of invention. On November 19, 2014, the Company amended the Services and License Agreement with IDMC. This amendment exclusively licenses 10 filed patents to us.

The agreement requires IDMC to identify and engage inventors to develop new applications of Visualant's ChromaID™ technology, present the developments to us for approval, and file at least 10 patent applications to protect the developments. IDMC is responsible for the development and patent costs. The Company provided the Chroma ID Lab Kits to IDMC at no cost and are providing ongoing technical support. In addition, to provide time for this accelerated expansion of its intellectual property the Company delayed the selling of the ChromaID Lab Kits for 140 days except for certain select accounts. The Company continued its business development efforts during this period and have worked with IDMC and their global business development resources to secure potential customers and licensees for the ChromaID technology. The Company shipped 20 ChromaID Lab Kits to inventors in the IDMC network during December 2013 and January 2014. As part of the agreement with IDMC, the Company curtailed its ChromaID marketing efforts through the fourth calendar quarter of 2014 while IDMC worked to expand our intellectual property portfolio. Thereafter, the Company began to actively market the ChromaID Lab Kits to interested and qualified customers.

The Company has received a worldwide, nontransferable, exclusive license to the intellectual property developed under the IDMC agreement during the term of the agreement, and solely within the identification, authentication and diagnostics field of use, to (a) make, have made, use, import, sell and offer for sale products and services; (b) make improvements; and (c) grant sublicenses of any and all of the foregoing rights (including the right to grant further sublicenses).

The Company received a nonexclusive and nontransferable option to acquire a worldwide, nontransferable, nonexclusive license to the useful intellectual property held by IDMC within the identification, authentication and diagnostics field of use to (a) make, have made, use, import, sell and offer to sell products and services and (b) grant sublicenses to any and all of the foregoing rights. The option to acquire this license may be exercised for up to two years from the effective date of the Agreement.

IDMC is providing global business development services to us for geographies not being pursued by Visualant. Also, IDMC has introduced the Company to potential customers, licensees and distributors for the purpose of identifying and pursuing a license, sale or distribution arrangement or other monetization event.

The Company granted to IDMC a nonexclusive, worldwide, fully paid, nontransferable, sublicenseable, perpetual license to our intellectual property solely outside the identification, authentication and diagnostics field of use to (a) make, have made, use, import, sell and offer for sale products and services and (b) grant sublicenses of any and all of the foregoing rights (including the right to grant further sublicenses).

The Company granted to IDMC a nonexclusive, worldwide, fully paid up, royalty-free, nontransferable, non-sublicenseable, perpetual license to access and use the Company's technology solely for the purpose of marketing the aforementioned sublicenses of our intellectual property to third parties outside the designated fields of use.

In connection with the original license agreement, the Company issued a warrant to purchase 97,169 shares of common stock to IDMC as consideration for the exclusive intellectual property license and application development services. The warrant has a current exercise price of $2.50 per share and expires November 10, 2018. The per share price is subject to adjustment based on any issuances below $2.50 per share except as described in the warrant.

The Company agreed to pay IDMC a percentage of license revenue for the global development business services and a percentage of revenue received from any company introduced to us by IDMC. The Company also have also agreed to pay IDMC a royalty when the Company receives royalty product revenue from an IDMC-introduced company. IDMC has agreed to pay the Company a license fee for the nonexclusive license of the Company's intellectual property.

The term of both the exclusive intellectual property license and the nonexclusive intellectual property license commences on the effective date of November 11, 2013, and terminates when all claims of the patents expire or are held in valid or unenforceable by a court of competent jurisdiction from which no appeal can be taken.

The term of the Agreement commences on the effective date until either party terminates the Agreement at any time following the fifth anniversary of the effective date by providing at least ninety days' prior written notice to the other party.

5. AGREEMENTS WITH SUMITOMO PRECISION PRODUCTS CO., LTD.

In May 2012, the Company entered into a Joint Research and Product Development Agreement (the "Joint Development Agreement") with Sumitomo Precision Products Co., Ltd., a publicly-traded Japanese corporation, for the commercialization of our ChromaID technology. In March 2013, the Company entered into an amendment to this agreement, which extended the Joint Development Agreement from March 31, 2013 to December 31, 2013. The extension provided for continuing work between Sumitomo and Visualant focused on advancing the ChromaID technology and market research aimed at identifying the most significant markets for the ChromaID technology. This agreement expired December 31, 2013. This collaborative work supported the development of the ChromaID Lab Kit. The current version of the technology was introduced to the marketplace as a part of our ChromaID Lab Kit during the fourth quarter of 2013.

The Company also entered into a License Agreement with Sumitomo in May 2012 which provides for an exclusive license for the then-extant ChromaID technology. The territories covered by this license include Japan, China, Taiwan, Korea and the entirety of Southeast Asia (Burma, Indonesia, Thailand, Cambodia, Laos, Vietnam, Singapore and the Philippines). On May 21, 2015, the Company entered into an amendment to the License Agreement, which, effective as of June 18, 2014, which eliminated the Sumitomo exclusivity and provides that if the Company sells products in certain territories – Japan, China, Taiwan, Korea and the entirety of Southeast Asia (Burma, Indonesia, Thailand, Cambodia, Laos, Vietnam, Singapore and the Philippines) – the Company will pay Sumitomo a royalty rate of 2% of net sales (excluding non-recurring engineering revenues) over the remaining term of the five-year License Agreement (through May 2017).

6. ACCOUNTS RECEIVABLE/CUSTOMER CONCENTRATION

Accounts receivable were $810,484 and $619,849, net of allowance, as of March 31, 2016 and September 30, 2015, respectively. The Company had one customer (16.1%) in excess of 10% of our consolidated revenues for the six months ended March 31, 2016. The Company had two customers (35.3% and 12.4%) with accounts receivable in excess of 10% as of March 31, 2016. The Company does expect to have customers with consolidated revenues or accounts receivable balances of 10% of total accounts receivable in the foreseeable future.

7. INVENTORIES

Inventories were $253,963 and $217,824 as of March 31, 2016 and September 30, 2015, respectively. Inventories consist primarily of printers and consumable supplies, including ribbons and cards, badge accessories, capture devices, and access control components held for resale. There is a $20,000 reserve for impaired inventory as of March 31, 2016 and September 30, 2015, respectively.

8. FIXED ASSETS

Fixed assets, net of accumulated depreciation, was $344,244 and $366,250 as of March 31, 2016 and September 30, 2015, respectively. Accumulated depreciation was $788.472 and $803,705 as of March 31, 2016 and September 30, 2015, respectively. Total depreciation expense, was $36,278 and $40,357 for the three months ended March 31, 2016 and 2015, respectively. All equipment is used for selling, general and administrative purposes and accordingly all depreciation is classified in selling, general and administrative expenses.

Property and equipment as of March 31, 2016 was comprised of the following:

	Estimated	March 31, 2016		
	Useful Lives	Purchased	Capital Leases	Total
Machinery and equipment	2-10 years	$ 249,350	$ 69,581	$ 318,931
Leasehold improvements	5-20 years	603,612	-	603,612
Furniture and fixtures	3-10 years	73,977	101,260	175,237
Software and websites	3- 7 years	34,936	-	34,936
Less: accumulated depreciation		(617,631)	(170,841)	(788,472)
		$ 344,244	$ -	$ 344,244

Depreciation expense was $23,296 and $40,150 for the six months ended March 31, 2016 and 2015, respectively.

9. DERIVATIVE INSTRUMENTS

In April 2008, the FASB issued a pronouncement that provides guidance on determining what types of instruments or embedded features in an instrument held by a reporting entity can be considered indexed to its own stock for the purpose of evaluating the first criteria of the scope exception in the pronouncement on accounting for derivatives. This pronouncement was effective for financial statements issued for fiscal years beginning after December 15, 2008. The adoption of these requirements can affect the accounting for warrants and many convertible instruments with provisions that protect holders from a decline in the stock price (or "down-round" provisions). For example, warrants or conversion features with such provisions are no longer recorded in equity. Down-round provisions reduce the exercise price of a warrant or convertible instrument if a company either issues equity shares for a price that is lower than the exercise price of those instruments or issues new warrants or convertible instruments that have a lower exercise price.

Derivative liability as of March 31, 2016 is as follows:

Financial Instruments	Fair Value Measurements Using Inputs Level 1	Level 2	Level 3	Carrying Amount at March 31, 2016
Liabilities:				
Derivative Instruments	$ -	$ 3,574,346	$ -	$ 3,574,346
Total	$ -	$ 3,574,346	$ -	$ 3,574,346

Derivative liability as of September 30, 2015 is as follows:

Financial Instruments	Fair Value Measurements Using Inputs Level 1	Level 2	Level 3	Carrying Amount at September 30, 2015
Liabilities:				
Derivative Instruments	$ -	$ 2,704,840	$ -	$ 2,704,840
Total	$ -	$ 2,704,840	$ -	$ 2,704,840

The risk-free rate of return reflects the interest rate for the United States Treasury Note with similar time-to-maturity to that of the warrants.

Derivative Instruments – Warrants with the June 2013 Private Placement

The Company issued warrants to purchase 697,370 shares of common stock in connection with our June 2013 private placement of 348,685 shares of common stock. The exercise price of these warrants is $2.50 per share. These warrants were not issued with the intent of effectively hedging any future cash flow, fair value of any asset, liability or any net investment in a foreign operation. These warrants were issued with a down-round provision whereby the exercise price would be adjusted downward in the event that additional shares of our common stock or securities exercisable, convertible or exchangeable for the Company's common stock were issued at a price less than the exercise price. Therefore, the fair value of these warrants were recorded as a liability in the consolidated balance sheet and are marked to market each reporting period until they are exercised or expire or otherwise extinguished.

The proceeds from the private placement were allocated between the shares of common stock and the warrants issued in connection with the private placement based upon their estimated fair values as of the closing date at June 14, 2013, resulting in the aggregate amount of $2,494,710 allocated to stockholders' equity and $2,735,290 allocated to the warrant derivative. The Company recognized $1,448,710 of other expense resulting from the increase in the fair value of the warrant liability at September 30, 2013. During the year ended September 30, 2014, the Company recognized $2,092,000 of other income resulting from the decrease in the fair value of the warrant liability at September 30, 2014. During the year ended September 30, 2015, the Company recognized $104,716 of other expense resulting from the decrease in the fair value of the warrant liability at September 30, 2015. During the six months ended March 31, 2016, the Company recognized $668,194 of other expense resulting from the increase in the fair value of the warrant liability at March 31, 2016.

Derivative Instruments – Warrant with the November 2013 IDMC Services and License Agreement

The risk-free rate of return reflects the interest rate for the United States Treasury Note with similar time-to-maturity to that of the warrants.

The Company issued a warrant to purchase 97,169 shares of common stock in connection with the November 2013 IDMC Services and License Agreement. The warrant price of $30.00 per share expires November 10, 2018 and the per share price is subject to adjustment. In August 2015 the exercise price was reset to $2.50 per shares. This warrant was not issued with the intent of effectively hedging any future cash flow, fair value of any asset, liability or any net investment in a foreign operation. This warrant was issued with a down-round provision whereby the exercise price would be adjusted downward in the event that additional shares of our common stock or securities exercisable, convertible or exchangeable for our common stock were issued at a price less than the exercise price. Therefore, the fair value of these warrants was recorded as a liability in the consolidated balance sheet and are marked to market each reporting period until they are exercised or expire or otherwise extinguished. During the year ended September 30, 2014, the Company recognized $320,657 of other expense related to the IDMC warrant. During the year ended September 30, 2015, the Company recognized $14,574 of other income related to the IDMC warrant. During the six months ended March 31, 2016, the Company recognized $131,644 of other expense resulting from the increase in the fair value of the warrant liability at March 31, 2016.

Derivative Instrument – Series A Convertible Preferred Stock

The risk-free rate of return reflects the interest rate for the United States Treasury Note with similar time-to-maturity to that of the Series A Convertible Preferred Stock.

The Company issued 11,667 shares of Series A Convertible Preferred Stock with attached warrants during the year ended September 30, 2015. The Company allocated $233,322 to stockholder's equity and $116,678 to the derivative warrant liability. The warrants were issued with a down round provision. The warrants have a term of five years, 23,334 are exercisable at $30 per common share and 23,334 are exercisable at $45 per common share. On August 14, 2015 the exercise price was adjusted to $2.50 per share. During the year ended September 30, 2015, the Company recognized $30,338 of other expense related to the warrant liability. During the six months ended March 31, 2016, the Company recognized $63,235 of other expense resulting from the increase in the fair value of the warrant liability at March 31, 2016.

Derivative Instrument – Convertible Note Payable Vis Vires Group, Inc.

The Company entered into a Convertible Note Payable with Vis Vires Group, Inc. on August 10, 2015 for $84,000 to fund short-term working capital. The Vis Vires Note accrues interest at a rate of 8% per annum and becomes due on May 12, 2016 and is convertible into common stock on February 5, 2016. The Vis Vires Note is convertible at 65% of the average of the lowest three day trading price in the 10 days prior to conversion. The Company recorded accrued interest of $405 as of September 30, 2015. During the year ended September 30, 2015, the Company recognized $55,038 of other expense related to the Vis Vires Note. On February 6, 2016, we paid $114,979 to Vis Vires to repay the Note Payable in full. The Company recognized other income of $47,028 during the six months ended March 31, 2016.

Liabilities measured at fair value on a recurring basis for the above derivatives are summarized as follows:

	March 31, 2016
Market price and estimated fair value of common stock:	$ 7.00
Exercise price	2.50
Expected term (years)	0.25
Dividend yield	-
Expected volatility	85.8%
Risk-free interest rate	0.01%

Derivative Instrument – Convertible Note Payable Vis Vires Group, Inc.

The Company entered into a Convertible Note Payable with Vis Vires Group, Inc. on February 19, 2016 for $100,000 to fund short-term working capital. The Vis Vires Note accrues interest at a rate of 8% per annum and becomes due on November 22, 2016 and is convertible into common stock on August 19, 2016. The Vis Vires Note is convertible at 65% of the average of the lowest three day trading price in the 10 days prior to conversion. The Company recorded accrued interest of $921 as of March 31, 2016. During the three months ended March 31, 2016, the Company recognized a $65,278 debt discount resulting from the the fair value of the conversion option and a change in the fair value of the liability in the amount of $3,827 at March 31, 2016. The Company also recorded other financing expense in the amount of $14,000 as a debt discount to be amortized over the term of the note.

Liabilities measured at fair value on a recurring basis for the Vis Vires Convertible Note Payable are summarized as follows:

		March 31, 2016
Market price and estimated fair value of common stock:	$	7.00
Exercise price		4.55
Expected term (years)		0.75
Dividend yield		-
Expected volatility		113.0%
Risk-free interest rate		0.75%

10. INTANGIBLE ASSETS

Intangible assets as of March 31, 2016 and September 30, 2015 consisted of the following:

	Estimated Useful Lives		March 31, 2016		September 30, 2015
Customer contracts	5 years	$	983,645	$	983,645
Technology	5 years		712,500		712,500
Less: accumulated amortization			(1,609,395)		(1,538,145)
Intangible assets, net		$	86,750	$	158,000

Total amortization expense was $71,250 and $169,615 for the six months ended March 31, 2016 and 2015, respectively.

The fair value of the TransTech intellectual property acquired was $983,645, estimated by using a discounted cash flow approach based on future economic benefits associated with agreements with customers, or through expected continued business activities with its customers. In summary, the estimate was based on a projected income approach and related discounted cash flows over five years, with applicable risk factors assigned to assumptions in the forecasted results.

The fair value of the RATLab intellectual property associated with the assets acquired was $450,000 estimated by using a discounted cash flow approach based on future economic benefits. In summary, the estimate was based on a projected income approach and related discounted cash flows over five years, with applicable risk factors assigned to assumptions in the forecasted results.

The fair value of the Javelin intellectual property acquired was $262,500 estimated by using a discounted cash flow approach based on future economic benefits associated with the assets acquired. In summary, the estimate was based on a projected income approach and related discounted cash flows over five years, with applicable risk factors assigned to assumptions in the forecasted results.

11. ACCOUNTS PAYABLE

Accounts payable were $2,557,359 and $2,520,233 as of March 31, 2016 and September 30, 2015, respectively. Such liabilities consisted of amounts due to vendors for inventory purchases and technology development, external audit, legal and other expenses incurred by the Company. The Company had two vendors (16.0% and 10.6%) with accounts payable in excess of 10% of its accounts payable as of March 31, 2016. The Company does expect to have vendors with accounts payable balances of 10% of total accounts payable in the foreseeable future.

12. CONVERTIBLE NOTES PAYABLE

Convertible notes payable as of March 31, 2016 consisted of the following:

The Company entered into a Convertible Note Payable with Vis Vires Group, Inc. on August 10, 2015 for $84,000 to fund short-term working capital. The Vis Vires Note accrued interest at a rate of 8% per annum and becomes due on May 12, 2016 and was convertible into common stock on February 5, 2016. The Vis Vires Note was convertible at 65% of the average of the lowest three day trading price in the 10 days prior to conversion. On February 6, 2015, the Company paid $114,979 to Vis Vires to repay the Note Payable in full.

The Company entered into Convertible Promissory Notes totaling $710,000 with accredited investors during September 2015 to February 2016 to fund short-term working capital. The Notes accrue interest at a rate of 8% per annum and become due September 2016 to February 2017 and are convertible into common stock at the same price of our next financing. The Company recorded accrued interest of $17,113 as of March 31, 2016. The investors received $710,000 in warrants that are exercisable into common stock at the price equal to the price of the common stock sold in our next public financing.

The Company entered into 8%-10% Convertible Promissory Notes and Securities Purchase Agreements with three accredited investors on February 4, 2016, totaling $165,000 with an original issue discount of $15,000 to fund short-term working capital. The Notes become due on February 3, 2017 and are convertible into common stock after six months from issuance. The Notes are convertible at 60% of the average of the lowest trading price in the 25 days prior to conversion but not less than $0.001 per share. The Company issued a total of 10,500 shares of restricted common stock to the investors valued at $70,875 and paid $7,500 in legal fees and recorded a total debt discount of $165,000 during the six months ended March 31, 2016. The Company received $128,500 net of all fees.

On February 5, 2016, the Company valued the beneficial conversion feature of this senior secured convertible redeemable debenture at $110,000 and recorded additional paid in capital of $110,000. During the six months March 31, 2016, the Company recorded interest expense of $12,962, related to the amortization of the debt discount associated with the Convertible Promissory Notes.

The Company entered into a Convertible Note Payable with Vis Vires Group, Inc. on February 18, 2016 for $100,000 to fund short-term working capital. The Vis Vires Note accrues interest at a rate of 8% per annum, becomes due on November 22, 2016 and is convertible into common stock beginning on August 19, 2016. The Vis Vires Note is convertible at 65% of the average of the lowest three-day trading price in the 10 days prior to conversion and includes a down round provision. The Company recorded a debt discount of $79,278 related to the conversion option derivative and a discount of $14,000 for issuance fees. We received $86,000 from the sale of the Vis Vires Not, net of all fees. The Company recorded accrued interest of $921 and $6,098 related to the amortization of the debt discount as of March 31, 2016.

13. NOTES PAYABLE, CAPITALIZED LEASES AND LONG TERM DEBT

Notes payable, capitalized leases and long term debt as of March 31, 2016 and September 30, 2015 consisted of the following:

	March 31, 2016	September 30, 2015
Capital Source Business Finance Group	$ 507,697	$ 364,757
Note payable to Umpqua Bank	199,935	199,935
Secured note payable to J3E2A2Z LP - related party	600,000	600,000
Total debt	1,307,632	1,164,692
Less current portion of long term debt	(1,307,632)	(1,164,692)
Long term debt	$ -	$ -

Capital Source Business Finance Group Secured Credit Facility

The Company finances its TransTech operations from operations and a Secured Credit Facility with Capital Source Business Finance Group. On December 9, 2008, TransTech entered into a $1,000,000 secured credit facility with Capital Source to fund its operations. On December 12, 2015, the secured credit facility was renewed for an additional six months, with a floor for prime interest of 4.5% (currently 4.5%) plus 2.5%. The eligible borrowing is based on 80% of eligible trade accounts receivable, not to exceed $1,000,000. The secured credit facility is collateralized by the assets of TransTech, with a guarantee by Visualant, including a security interest in all assets of Visualant. Availability under this Secured Credit ranges from $0 to $175,000 ($49,045 as of March 31, 2016) on a daily basis. The remaining balance on the accounts receivable line of $507,697 as of March 31, 2016 must be repaid by the time the secured credit facility expires on June 12, 2016, or we renew by automatic extension for the next successive six-month term.

AMEX Merchant Services Financing Loan

TransTech entered into a one year Loan in the amount of $214,000 on November 25, 2015 with AMEX Merchant Financing. The loan fees were $25,680. The total Loan of $239,680 will be paid with monthly payments of 25% of Credit Card Receipts on Monthly Sales. The amount of the loan was based on historical usage of credit card processing. No prepayment penalty for accelerated payments and or the balance before the maturity date of November 24, 2016. The remaining balance on the loan is $0 as of March 31, 2016.

Note Payable to Umpqua Bank

The Company has a $199,935 Business Loan Agreement with Umpqua Bank (the “Umpqua Loan”), which matures on March 31, 2016 and provides for interest at 3.25% per year. On December 19, 2015, the Umpqua Loan maturity was extended to December 31, 2016 and provides for interest at 3.50% per year related to this Umpqua Loan, the Company entered into a demand promissory note for $200,000 on January 10, 2014 with an entity affiliated with Ronald P. Erickson, our Chief Executive Officer. This demand promissory note will be effective in case of a default by the Company under the Umpqua Loan. The Company recorded accrued interest of $13,348 as of March 31, 2016.

Note Payables to Ronald P. Erickson or J3E2A2Z LP

The Company also has two other demand promissory notes payable to entities affiliated with Mr. Erickson, totaling $600,000. Each of these notes were issued between January and July 2014, provide for interest of 3% per year and now mature on March 31, 2016. They also provide for a second lien on our assets if not repaid by March 31, 2016 or converted into convertible debentures or equity on terms acceptable to the Mr. Erickson. The Company recorded accrued interest of $31,192 as of March 31, 2016.

Aggregate maturities totaling $1,307,632 are all due within twelve months.

14. EQUITY

Authorized Capital Stock

The Company has authorized 105,000,000 shares of capital stock, of which 100,000,000 are shares of voting common stock, par value $0.001 per share, and 5,000,000 are shares of voting preferred stock, par value $0.001 per share.

Voting Preferred Stock

As of March 31, 2016, the Company is authorized to issue up to 5,000,000 shares of preferred stock with a par value of $0.001.

On July 21, 2015, the Company filed with the Nevada Secretary of State an Amended and Restated Certificate of Designations, Preferences and Rights for our Series A Convertible Preferred Stock. Among other things, the Amended and Restated Certificate changed the conversion price and the stated value of the Series A Preferred from $0.10 (pre reverse stock split) to $30.00 (post-reverse stock split), and added a provision adjusting the conversion price upon the occurrence of certain events.

Under the Amended and Restated Certificate, the Company had 11,667 shares of Series A Preferred authorized, all of which are outstanding. Each holder of outstanding shares of Series A Preferred is entitled to the number of votes equal to the number of whole shares of common stock into which the shares of Series A Preferred held by such holder are then convertible as of the applicable record date. The Company cannot amend, alter or repeal any preferences, rights, or other terms of the Series A Preferred so as to adversely affect the Series A Preferred, without the written consent or affirmative vote of the holders of at least 66% of the then outstanding shares of Series A Preferred, voting as a separate voting group, given by written consent or by vote at a meeting called for such purpose for which notice shall have been duly given to the holders of the Series A Preferred.

During the year ended September 30, 2015, the Company sold 11,667 Series A Preferred Stock to two investors totaling $350,000. These shares are expected to be convertible into 11,667 shares of common stock at $30.00 per share, subject to adjustment, for a period of five years. The Series A Preferred Stock has voting rights and may not be redeemed without the consent of the holder.

The Company also issued (i) a Series C five-year Warrant for 23,334 shares of common stock at an exercise price of $30.00 per share, which is callable at $60.00 per share; and (ii) a Series D five-year Warrant for 23,334 shares of common stock at an exercise price of $45.00 per share, which is callable at $90.00 per share. The Series A Preferred Stock and Series C and D Warrants have registration rights.

On July 20, 2015, the two investors entered into an Amendment to Series A Preferred Stock Terms whereby they agreed to the terms of the Amended and Restated Certificate of Designations, Preferences and Rights of Series A Convertible Preferred Stock and waived all registration rights.

On August 14, 2015, the warrant exercise price was adjusted to $2.50 per share due to the issuance of common stock at that price.

On March 8, 2016, the Company received approval from the State of Nevada for the Correction to the Company's Amended and Restated Certificate of Designations, Preferences and Rights of its Series A Convertible Preferred Stock. The Amended and Restated Certificate filed July 21, 2015 changed the conversion price and the stated value from $0.10 (pre reverse stock split) to $30.00 (post-reverse stock split), and adding a provision adjusting the conversion price upon the occurrence of certain events. On February 19, 2016, the holders of Series A Convertible Preferred Stock entered into Amendment 2 of Series A Preferred Stock Terms and increased the number of Preferred Stock Shares to properly account for the reverse stock split. We have 23,334 Series A Preferred Stock issued and outstanding.

Series B Redeemable Convertible Preferred Stock

On March 8, 2016, the Company received approval from the State of Nevada for the Certificate of Designations of Preferences, Powers, Rights and Limitations of Series B Redeemable Convertible Preferred Stock. The Certificate authorized 5,000 shares of Series B Preferred Stock at a par value of $.001 per share that is convertible into common stock at $7.50 per share, subject to certain adjustments as set forth in the Certificate.

The Company entered into a Stock Purchase Agreement with an institutional investor pursuant to which the Company issued 255 Shares of Series B Redeemable Preferred Shares ("Series B Preferred Shares") of the Company at $10,000 per share with a 5.0% original issue discount for the sum of $2,500,000.

At closing, the Company sold 51 Series B Preferred Shares in exchange for payment to the Company of $500,000 in cash and issued an additional 204 Series B Preferred Shares in exchange for delivery of a full recourse 1% Promissory Note ("Note") for $1,995,000 and payment to the Company of $5,000 in cash (paid). The Note is collateralized by the Series B Preferred Shares. Under the terms of the Note, the Company is to receive an additional $500,000 for each $5 million, or in certain cases a lower amount, in aggregate trading volume of the common stock, so long as it meets certain other requirements. Any remaining balance under the Note is payable at its maturity in seven years. Due to the uncertainty on the receipt of achieving future funding, the Company has not booked the full recourse 1% Promissory Note.

The Series B Preferred Shares are convertible into common stock at $7.50 per share; provided that the institutional investor may not convert any Series B Preferred Shares into common stock until that portion of the Note underlying the purchase of the converted portion of Series B Preferred Shares is paid in cash to Company.

The Company may issue, at our sole discretion in lieu of cash, as a conversion premium or in payment of dividends on such shares of Series B Preferred Shares. The number of additional common shares that we may issue as a conversion premium or in payment of dividends, is dependent on the dividend rate which can vary depending on our underlying stock price at the time of conversion and assuming no triggering event has occurred.

The Company has file a Registration Statement on Form S-1 to register the resale of all shares of common stock issuable upon conversion of the Series B Shares and to make reasonable best efforts to cause such Registration Statement to be declared effective under the Act as promptly as practicable.

Common Stock

All of the offerings and sales described below were deemed to be exempt under Rule 506 of Regulation D and/or Section 4(a)(2) of the Securities Act. No advertising or general solicitation was employed in offering the securities, the offerings and sales were made to a limited number of persons, all of whom were accredited investors and transfer was restricted by the company in accordance with the requirements of Regulation D and the Securities Act. All issuances to accredited and non-accredited investors were structured to comply with the requirements of the safe harbor afforded by Rule 506 of Regulation D, including limiting the number of non-accredited investors to no more than 35 investors who have sufficient knowledge and experience in financial and business matters to make them capable of evaluating the merits and risks of an investment in our securities.

The following equity issuances occurred during the six months ended March 31, 2016:

Nine investors exercised warrants at $2.50 per share and received 67,745 shares of common stock, for a total of $169,360 in proceeds to the Company.

On October 21, 2015, the Company entered into a Public Relations Agreement with Financial Genetics LLC for public relation services. Under the Agreement, Financial Genetics was awarded 21,696 shares of our common stock. The Company expensed $158,250 during the six months ended March 31, 2016.

On October 6, 2015, the Company entered into a Consulting Agreement with Joshua Conroy for business development services. Under the Agreement, Mr. Conroy was awarded 1,711 shares of our common stock. The Company expensed $11,977 during the three months ended December 31, 2015.

The Company entered into Convertible Promissory Notes totaling $710,000 with accredited investors during September 2015 to February 2016 to fund short-term working capital. The Notes accrue interest at a rate of 8% per annum and become due September 2016 to February 2017 and are convertible into common stock as part of our next financing. The investors received $710,000 in warrants that are exercisable into common stock at the price equal to the price of the common stock sold in our next public financing.

The Company entered into 8%-10% Convertible Promissory Notes and Securities Purchase Agreements with three accredited investors on February 4, 2016, totaling $165,000 with an original issue discount of $15,000 to fund short-term working capital. The Notes become due on February 3, 2017 and are convertible into common stock after six months from issuance. The Notes are convertible at 60% of the average of the lowest trading price in the 25 days prior to conversion but not less than $0.001 per share. The Company issued a total of 10,500 shares of restricted common stock to the investors valued at $70,875 and paid $7,500 in legal fees and recorded a total debt discount of $165,000 during the six months ended March 31, 2016. The Company received $128,500 net of all fees.

On February 23, 2016, the Company entered into a Consulting Agreement with David Markowski for business development services. On February 29, 2016, Mr. Markowski was awarded 2,000 shares of our common stock. The Company expensed $14,600 during the three months ended March 31, 2016.

On May 6, 2015, the Company's stockholders approved a reverse split of our common stock, in a ratio to be determined by the Company's Board of Directors, of not less than 1-for-50 nor more than 1-for-150. On June 9, 2015, the Company's Board of Directors determined that the ratio of the reverse split would be 1-for-150. All warrant, option, share and per share information in this Form 10-Q gives retroactive effect for a 1-for-150 split with all numbers rounded up to the nearest whole share.

Warrants to Purchase Common Stock

The following warrant exercises occurred during the six months ended March 31, 2016:

Nine investors exercised warrants at $2.50 per share and received 67,745 shares of common stock, for a total of $169,360 in proceeds to the Company.

A warrant to acquire 1,679 shares of common stock at $19.36 per share expired.

The Company entered into Convertible Promissory Notes totaling $710,000 with accredited investors during September 2015 to February 2016 to fund short-term working capital. The investors received $710,000 in warrants that are exercisable into common stock at the price equal to the price of the common stock sold in our next public financing. The number of warrants convertible into shares of common stock is not known at this time as the number of shares is determined by the price of the next up-lift offering by an investment banker.

A summary of the warrants issued as of March 31, 2016 were as follows:

	March 31, 2016	
	Shares	Weighted Average Exercise Price
Outstanding at beginning of period	899,750	$ 3.18
Issued	-	-
Exercised	(67,745)	(2.50)
Forfeited	-	-
Expired	(1,679)	19.36
Outstanding at end of period	830,326	$ 3.21
Exerciseable at end of period	830,326	

A summary of the status of the warrants outstanding as of March 31, 2016 is presented below:

March 31, 2016				
Number of Warrants	Weighted Average Remaining Life (In Years)	Weighted Average Exercise Price	Shares Exerciseable	Weighted Average Exercise Price
808,321	2.03	$ 2.50	808,321	$ 2.50
1,667	0.63	19.50-22.50	1,667	19.50-22.50
20,338	1.33	30.00	20,338	30.00
830,326	1.85	$ 3.21	830,326	$ 3.21

The significant weighted average assumptions relating to the valuation of the Company's warrants for the period ended March 31, 2016 were as follows:

Dividend yield	0%
Expected life	3
Expected volatility	90%
Risk free interest rate	0.7%

There were vested warrants of 808,321 as of March 31, 2016 with an aggregate intrinsic value of $3,637,445.

15. STOCK OPTIONS

Description of Stock Option Plan

On April 29, 2011, the Company's 2011 Stock Incentive Plan was approved at the Annual Stockholder Meeting. The Company was authorized to issue options for, and has reserved for issuance, up to 46,667 shares of common stock under the 2011 Stock Incentive Plan. On March 21, 2013, an amendment to the Stock Option Plan was approved by the stockholders of the Company, increasing the number of shares reserved for issuance under the Plan to 93,333 shares.

Determining Fair Value under ASC 505

The Company records compensation expense associated with stock options and other equity-based compensation using the Black-Scholes-Merton option valuation model for estimating fair value of stock options granted under our plan. The Company amortizes the fair value of stock options on a ratable basis over the requisite service periods, which are generally the vesting periods. The expected life of awards granted represents the period of time that they are expected to be outstanding. The Company estimates the volatility of our common stock based on the historical volatility of its own common stock over the most recent period corresponding with the estimated expected life of the award. The Company bases the risk-free interest rate used in the Black Scholes-Merton option valuation model on the implied yield currently available on U.S. Treasury zero-coupon issues with an equivalent remaining term equal to the expected life of the award. The Company has not paid any cash dividends on our common stock and does not anticipate paying any cash dividends in the foreseeable future. Consequently, the Company uses an expected dividend yield of zero in the Black-Scholes-Merton option valuation model and adjusts share-based compensation for changes to the estimate of expected equity award forfeitures based on actual forfeiture experience. The effect of adjusting the forfeiture rate is recognized in the period the forfeiture estimate is changed.

Stock Option Activity

The Company had the following stock option transactions during the six months ended March 31, 2016:

During the six months ended March 31, 2016, employees forfeited stock option grants for 766 shares of common stock at $36.03 per share.

There are currently 56,641 options to purchase common stock at an average exercise price of $18.19 per share outstanding as of March 31, 2016 under the 2011 Stock Incentive Plan. The Company recorded $23,674 and $40,150 of compensation expense, net of related tax effects, relative to stock options for the three months ended March 31, 2016 and 2014 in accordance with ASC 505. Net loss per share (basic and diluted) associated with this expense was approximately ($0.02) and ($0.04) per share, respectively. At March 31, 2016, there is approximately $161,537 of total unrecognized costs related to employee granted stock options that are not vested. These costs are expected to be recognized over a period of approximately 3.77 years.

Stock option activity for the three months ended March 31, 2016 and the years ended September 30, 2015 and 2014 was as follows:

	Options	Weighted Average Exercise Price	$
Outstanding as of September 30, 2013	84,900	$ 18.954	$ 1,609,200
Granted	2,633	15.002	39,500
Exercised	-	-	-
Forfeitures	(200)	(32.500)	(6,500)
Outstanding as of September 30, 2014	87,333	18.804	1,642,200
Granted	11,335	15.000	170,025
Exercised	-	-	-
Forfeitures	(41,261)	(18.286)	(754,500)
Outstanding as of September 30, 2015	57,407	18.43	1,057,725
Granted	-	-	-
Exercised	-	-	-
Forfeitures	(766)	(36.034)	(27,602)
Outstanding as of March 31, 2016	56,641	$ 18.187	$ 1,030,123

The following table summarizes information about stock options outstanding and exercisable as of March 31, 2016:

Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Life In Years	Weighted Average Exercise Price Exerciseable	Number Exerciseable	Weighted Average Exercise Price Exerciseable
13.500	3,334	2.13	$ 13.50	3,334	$ 13.50
15.000	20,970	3.33	15.00	8,331	15.00
19.500	19,003	4.09	19.50	19,002	19.50
22.500	13,334	4.13	22.50	13,334	22.50
	56,641	3.83	$ 18.19	44,001	$ 19.58

There were exercisable options of 44,001 as of March 31, 2016 with an aggregate intrinsic value of $0.

16. OTHER SIGNIFICANT TRANSACTIONS WITH RELATED PARTIES

Related Party Transactions with Ronald P. Erickson

See Note 13 for Notes Payable to Ronald P. Erickson, our Chief Executive Officer Chief and/or entities in which Mr. Erickson has a beneficial interest.

Note Payable to Umpqua Bank

The Company has a $199,935 Business Loan Agreement with Umpqua Bank (the "Umpqua Loan"), which matures on March 31, 2016 and provides for interest at 3.25% per year. On December 19, 2015, the Umpqua Loan maturity was extended to December 31, 2016 and provides for interest at 3.50% per year Related to this Umpqua Loan, the Company entered into a demand promissory note for $200,000 on January 10, 2014 with an entity affiliated with Ronald P. Erickson, our Chief Executive Officer. This demand promissory note will be effective in case of a default by the Company under the Umpqua Loan. The Company recorded accrued interest of $13,348 as of March 31, 2016.

Note Payables to Ronald P. Erickson or J3E2A2Z LP

The Company also has two other demand promissory notes payable to entities affiliated with Mr. Erickson, totaling $600,000. Each of these notes were issued between January and July 2014, provide for interest of 3% per year and now mature on March 31, 2016. They also provide for a second lien on our assets if not repaid by March 31, 2016 or converted into convertible debentures or equity on terms acceptable to the Mr. Erickson. The Company recorded accrued interest of $31,192 as of March 31, 2016.

17. COMMITMENTS, CONTINGENCIES AND LEGAL PROCEEDINGS

Legal Proceedings

The Company may from time to time become a party to various legal proceedings arising in the ordinary course of our business. The Company is currently not a party to any pending legal proceeding that is not ordinary routine litigation incidental to our business.

Properties and Operating Leases

The Company is obligated under various non-cancelable operating leases for its various facilities and certain equipment.

Corporate Offices

The Company's executive office is located at 500 Union Street, Suite 420, Seattle, Washington, USA, 98101. The Company leases 2,244 square feet and its net monthly payment is $2,535. The Company leases this office on a month to month basis.

TransTech Facilities

TransTech is located at 12142 NE Sky Lane, Suite 130, Aurora, OR 97002. TransTech leases a total of approximately 9,750 square feet of office and warehouse space for its administrative offices, product inventory and shipping operations. The Company leases this office until June 30, 2016 for $5,486 per month.

The aggregate future minimum lease payments under operating leases as of March 31, 2016 were $19,033.

18. SUBSEQUENT EVENTS

The Company evaluates subsequent events, for the purpose of adjustment or disclosure, up through the date the financial statements are available. Subsequent to March 31, 2016, there were no material transactions that require disclosure:

On April 29, 2016, the Company entered into amendments to two demand promissory notes, totaling $600,000, and a note payable for $200,000 related to the Umpqua Bank Business Loan Agreement with Mr. Erickson, our Chief Executive Officer and/or entities in which Mr. Erickson has a beneficial interest. The amendments extend the due date from March 31, 2016 to June 30, 2016 and continue to provide for interest of 3% per annum and a second lien on company assets if not repaid by June 30, 2016 or converted into convertible debentures or equity on terms acceptable to the Holder.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-looking statements in this report reflect the good-faith judgment of our management and the statements are based on facts and factors as we currently know them. Forward-looking statements are subject to risks and uncertainties and actual results and outcomes may differ materially from the results and outcomes discussed in the forward-looking statements. Factors that could cause or contribute to such differences in results and outcomes include, but are not limited to, those discussed below as well as those discussed elsewhere in this report (including in Part II, Item 1A (Risk Factors)). Readers are urged not to place undue reliance on these forward-looking statements because they speak only as of the date of this report. We undertake no obligation to revise or update any forward-looking statements in order to reflect any event or circumstance that may arise after the date of this report.

BUSINESS

We are focused primarily on the development of a proprietary technology which is capable of uniquely identifying and authenticating almost any substance using light to create, record and detect the unique digital "signature" of the substance. We call this our "ChromaID™" technology.

Our ChromaID™ Technology

We have developed a proprietary technology to uniquely identify and authenticate almost any substance. This patented technology utilizes light at the photon (elementary particle of light) level through a series of emitters and detectors to generate a unique signature or "fingerprint" from a scan of almost any solid, liquid or gaseous material. This signature of reflected or transmitted light is digitized, creating a unique ChromaID signature. Each ChromaID signature is comprised of from hundreds to thousands of specific data points.

The ChromaID technology looks beyond visible light frequencies to areas of near infra-red and ultraviolet light that are outside the humanly visible light spectrum. The data obtained allows us to create a very specific and unique ChromaID signature of the substance for a myriad of authentication and verification applications.

Traditional light-based identification technology, called spectrophotometry, has relied upon a complex system of prisms, mirrors and visible light. Spectrophotometers typically have a higher cost and utilize a form factor more suited to a laboratory setting and require trained laboratory personnel to interpret the information. The ChromaID technology uses lower cost LEDs and photodiodes and specific frequencies of light resulting in a more accurate, portable and easy-to-use solution for a wide variety of applications. The ChromaID technology not only has significant cost advantages as compared to spectrophotometry, it is also completely flexible is size, shape and configuration. The ChromaID scan head can range in size from endoscopic to a scale that could be the size of a large ceiling-mounted florescent light fixture.

In normal operation, a ChromaID master or reference scan is generated and stored in a database. The Visualant scan head can then scan similar materials to identify, authenticate or diagnose them by comparing the new ChromaID digital signature scan to that of the original or reference ChromaID signature or scan result.

ChromaID was invented by scientists from the University of Washington under contract with Visualant. We have pursued an aggressive intellectual property strategy and have been granted nine patents. We also have 21 patents pending. We possess all right, title and interest to the issued patents. Ten of the pending patents are licensed exclusively to us in perpetuity by our strategic partner, Intellectual Ventures through its subsidiary IDMC.

In 2010, we acquired TransTech Systems, Inc. (“TransTech”) as an adjunct to our business. TransTech is a distributor of products for employee and personnel identification. TransTech currently provides substantially all of our revenues. We intend, however, to further develop and market our ChromaID technology.

The following summarizes our plans for our proprietary ChromaID technology. Based on our anticipated expenditures on this technology, the expected efforts of our management and our relationship with Intellectual Ventures and its subsidiary, IDMC, and our other strategic partner, Sumitomo Precision Products, Ltd., we expect our ChromaID technology to provide an increasing portion of our revenues in future years from product sales, licenses, royalties and other revenue streams., as discussed further below.

ChromaID: A Foundational Platform Technology

Our ChromaID technology provides a platform upon which a myriad of applications can be developed. As a platform technology, it is analogous to a smartphone, upon which an enormous number of previously unforeseen applications have been developed. The ChromaID technology is an enabling technology that brings the science of light and photonics to low cost, real world commercialization opportunities across multiple industries. The technology is foundational and as such, the basis upon which we believe a significant business can be built.

As with other foundational technologies, a single application may reach across multiple industries. The ChromaID technology can, for example effectively differentiate and identify different brands of clear vodkas that appear identical to the human eye. By extension this same technology can identify pure water from water with contaminants present. It can provide real time detection of liquid medicines such as morphine that have been adulterated or compromised. It can detect if jet fuel has water contamination present. It could determine when it is time to change oil in a deep fat fryer. These are but a few of the potential applications of the ChromaID technology based upon extensions of its ability to identify different clear liquids.

The cornerstone of a company with a foundational platform technology is its intellectual property. ChromaID was invented by scientists from the University of Washington under contract with Visualant. We have pursued an aggressive intellectual property strategy and have been granted nine patents. We currently have 21 patents pending. We possess all right, title and interest to the issued patents. Ten of the pending patents are licensed exclusively to us in perpetuity by our strategic partner, the IDMC subsidiary of Intellectual Ventures.

At the Photonics West trade show held in San Francisco in February 2013, we were honored to receive a PRISM award from the Society of Photo-Optical Instrumentation Engineers International, better known as SPIE. The PRISM awards recognizes photonic products that break with conventional ideas, solve problems, and improve life through the application of light-based technologies.

IDMC Relationship

In November 2013, we entered into a strategic relationship with Invention Development Management Company, a subsidiary of Intellectual Ventures, a private intellectual property fund with over $5 billion under management. Intellectual Ventures owns over 40,000 IP assets and has broad global relationships for the invention of technology, the filing of patents and the licensing of intellectual property. IDMC has worked to expand the reach and the potential application of the ChromaID technology and has filed ten patents base on the ChromaID technology, which it has licensed to us. In connection with IDMC’s work to expand our intellectual property portfolio, we agreed to curtail outbound marketing activities of our technology through the fourth calendar quarter of 2014.

Initial testing in our laboratories and the work of the IDMC inventors have shown that the ChromaID technology has a number of broad and useful applications a few of which include:

- Milk identification for quality, protein and fat content and impurities
- Identification of liquids for counterfeits or contaminants
- Detecting adulterants in food and food products compromising its quality

- Color grading of diamonds
- Identifying real cosmetics versus counterfeit cosmetics
- Identifying counterfeit medications versus real medications
- Identifying regular flour versus gluten free flour
- Authenticating secure identification cards

Products

Our first delivered product, the ChromaID Lab Kit, scans and identifies solid surfaces. We are marketing this product to customers who are considering licensing the technology. Target markets include, but are not limited to, commercial paint manufacturers, pharmaceutical equipment manufacturers, process control companies, currency paper and ink manufacturers, security cards, cosmetic companies, scanner manufactures and food processing companies.

Our second product, the ChromaID Liquid Lab Kit, scans and identifies liquids. This product is currently in prototype form. Similar to our first product, it will be marketed to customers who are considering licensing the technology. Rather than use an LED emitter to reflect light off of a surface that is captured by a photodiode to generate a ChromaID signature the liquid analysis product shines light through the liquid (transmissive) with the LEDs positioned on one side of the liquid sample and the photo detectors on the opposite side. This device is in a functional state in our laboratory and we anticipate having a Liquid ChromaID Lab Kit available for customers by the Company during the fall of 2015. Target markets include, but are not limited to, water companies, petrochemical companies, pharmaceutical companies, and numerous consumer applications.

The ChromaID Lab Kits allows potential licensors of our technology to work with our technology and develop solutions for their particular application. Our contractual arrangements with IDMC are described in greater detail below.

Our next planned product should be an exemplar product is a prototype that will be produced to address several markets. The primary purpose of this prototype will be to demonstrate the technology to prospective business partners, and will consist of a small, hand held, battery powered, Bluetooth enabled scanning device. The scanner should wirelessly connect to a smart phone or tablet to transfer the scanned data. The smart phone application will include two or three industry specific but generic applications that allow for the demonstration of the scanning and matching of the ChromaID signatures. The applications will focus on drug identification, food safety and liquid detection. The prototype device will lend itself to consumer applications and can be a consumer product as well.

Our Commercialization Plans for the ChromaID Technology

We shipped our first ChromaID product, the ChromaID Lab Kits, to our strategic partner IDMC during the last calendar quarter of 2013 and first calendar quarter of 2014, after we completed final assembly and testing. As part of our agreement with IDMC, we curtailed our ChromaID marketing efforts through the fourth calendar quarter of 2014 while IDMC worked to expand our intellectual property portfolio. Thereafter, we began to actively market the ChromaID Lab Kits to interested and qualified customers. Some ChromaID Lab Kits are provided free of charge to potential customers. Others are sold for a modest price. To date, we have achieved limited revenue from the sale of our ChromaID Lab Kits.

The Lab Kit includes the following:

ChromaID Scanner. A small device made with electronic and optical components and firmware which pulses light onto a flat material and records and digitizes the light that is reflected back from that material. The device is the size of a typical flashlight (5.5” long and 1.25” diameter). However, the technology can be incorporated into almost any size, shape and configuration.

ChromaID Lab Software. A software application that runs on a Windows PC. The software allows for configuration of the scanner, controls the behavior of the ChromaID Scanner, displays a graph of the captured ChromaID signature profile, stores the ChromaID signature in a database and uses algorithms to compare the accuracy of the match of the unknown scan to the known ChromaID signature profile. This software is intended for lab and experimental use only and is not required for commercialized product applications.

Software Development Toolkit. A collection of software applications, API (an abbreviation of application program interface – a set of routines, protocols, and tools for building software applications) definitions and file descriptions that allow a customer to extract the raw data from the ChromaID signatures and run their own software routines against that raw data.

The ChromaID Lab Kit allows customers to experiment with and evaluate the ChromaID technology and determine if it is appropriate for their specific applications. The primary electronic and optical parts of the ChromaID scanner, called the “scan head,” could be supplied to customers to integrate into their own products. A set of ChromaID Developer Tools are also available. These allow customers to develop their own applications and products based on the ChromaID technology.

ChromaID signatures must be stored, managed, and readily accessible for comparison, matching and authentication purposes. Thedatabase can be owned and operated by the end customer, but in the case of thousands of ChromaID signatures, database management may be outsourced to us or a third party provider. These database services could be made available on a per-access transaction basis or on a monthly or annual subscription basis. The actual storage location of the database can be cloud-based, on a stand-alone scanning device or on a mobile device via a Bluetooth connection depending on the requirements of access, size of the database and security as defined by the customer. As a result, large databases can be accessed by cell phone or other mobile technologies using either local storage or cloud based storage.

Based on the commercialization plans outlined above, our business model anticipates deriving revenue from several sources:

- Sales of the ChromaID Lab Kit and ChromaID Liquid Lab Kit
- Non Recurring Engineering (NRE) fees to assist customers with scan integration into their products
- Licensing of the ChromaID technology
- Royalties per unit generated from the sales of scan heads
- Multi-unit sales of the above referenced exemplar product for as yet to be determined consumer product applications
- Per click transaction revenue from accessing the unique ChromaID signatures
- Developing custom product applications for customers
- ChromaID database administration and management services

Our Acceleration of Business Development in the United States and Around the World

We are coordinating our internal business development, sales and marketing efforts with those of our strategic partners IDMC, and Sumitomo Precision Products to leverage market data and information in order to focus on specific target vertical markets which have the greatest potential for early adoption. The ChromaID Lab Kit provides a means for us to demonstrate the technology to customers in these markets. It also allows customers to experiment with developing unique applications for their particular use. Our Business Development team is pursuing license opportunities with customers in our target markets. As an example, in March 2016 we entered into a Collaboration Agreement and License with Intellicheck Mobilisa. The agreement provides Intellicheck with exclusive rights to our ChromaID technology in the areas of homeland security, law enforcement and crime prevention.

There is no requirement for FDA or other government approval for the current applications of our ChromaID technology. Over time, as we explore the application of our ChromaID technology for medical diagnostics and other applications, we expect that there will be requirements for FDA and other government approvals before applications using the technology in medical and other regulated fields can enter the marketplace.

Research and Development

Our research and development efforts are primarily focused improving the core foundational ChromaID technology and developing new and unique applications for the technology. As part of this effort, we typically conduct testing to ensure that ChromaID application methods are compatible with the customer's requirements, and that they can be implemented in a cost effective manner. We are also actively involved in identifying new application methods. Our team has considerable experience working with the application of light-based technologies and their application to various industries. We believe that its continued development of new and enhanced technologies relating to our core business is essential to our future success. We spent $362,661 and $670,742 for the years ended September 30, 2015 and 2014, respectively, on development activities. Our research and development efforts are supported internally, through its relationship with IDMC and through contractors led by Dr. Tom Furness and his team at RATLab LLC.

Our Patents

We believe that our nine patents, 21 patent applications, and two registered trademarks, and our trade secrets, copyrights and other intellectual property rights are important assets for us. Our patents will expire at various times between 2027 and 2033. The duration of our trademark registrations varies from country to country. However, trademarks are generally valid and may be renewed indefinitely as long as they are in use and/or their registrations are properly maintained.

The patents that have been granted to Visualant include:

On August 9, 2011, we were issued US Patent No. 7,996,173 B2 entitled "Method, Apparatus and Article to Facilitate Distributed Evaluation of Objects Using Electromagnetic Energy," by the United States Office of Patents and Trademarks. The patent expires August 24, 2029.

On December 13, 2011, we were issued US Patent No. 8,076,630 B2 entitled "System and Method of Evaluating an Object Using Electromagnetic Energy" by the United States Office of Patents and Trademarks. The patent expires November 7, 2028.

On December 20, 2011, we were issued US Patent No. 8,081,304 B2 entitled "Method, Apparatus and Article to Facilitate Evaluation of Objects Using Electromagnetic Energy" by the United States Office of Patents and Trademarks. The patent expires July 28, 2030.

On October 9, 2012, we were issued US Patent No. 8,285,510 B2 entitled "Method, Apparatus, and Article to Facilitate Distributed Evaluation of Objects Using Electromagnetic Energy" by the United States Office of Patents and Trademarks. The patent expires July 31, 2027.

On February 5, 2013, we were issued US Patent No. 8,368,878 B2 entitled "Method, Apparatus and Article to Facilitate Evaluation of Objects Using Electromagnetic Energy by the United States Office of Patents and Trademarks. The patent expires July 31, 2027.

On November 12, 2013, we were issued US Patent No. 8,583,394 B2 entitled "Method, Apparatus and Article to Facilitate Distributed Evaluation of Objects Using Electromagnetic Energy by the United States Office of Patents and Trademarks. The patent expires July 31, 2027.

On November 21, 2014, we were issued US Patent No. 8,888,207 B2 entitled "Systems, Methods, and Articles Related to Machine-Readable Indicia and Symbols" by the United States Office of Patents and Trademarks. The patent expires February 7, 2033.

On March 23, 2015, we were issued US Patent No. 8,988,666 B2 entitled "Method, Apparatus, and Article to Facilitate Evaluation of Objects Using Electromagnetic Energy" by the United States Office of Patents and Trademarks. The patent expires July 31, 2027.

On May 26, 2015, we were patent US Patent No. 9,041,920 B2 entitled "Device for Evaluation of Fluids using Electromagnetic Energy" by the United States Office of Patents and Trademarks. The patent expires March 12, 2033.

We pursue an aggressive patent strategy to expand our unique intellectual property in the United States and other countries.

Services and License Agreement Invention Development Management Company, L.L.C.

In November 2013, we entered into a Services and License Agreement with Invention Development Management Company. IDMC is a subsidiary of Intellectual Ventures, which collaborates with inventors and partners with pioneering companies and invests both expertise and capital in the process of invention. On November 19, 2014, we amended the Services and License Agreement with IDMC. This amendment exclusively licenses 10 filed patents to us

The agreement requires IDMC to identify and engage inventors to develop new applications of our ChromaID™ technology, present the developments to us for approval, and file at least 10 patent applications to protect the developments. IDMC is responsible for the development and patent costs. We provided the Chroma ID Lab Kits to IDMC at no cost and are providing ongoing technical support. In addition, to provide time for this accelerated expansion of its intellectual property we delayed the selling of the ChromaID Lab Kits for 140 days except for certain select accounts. We have continued our business development efforts during this period and have worked with IDMC and their global business development resources to secure potential customers and licensees for the ChromaID technology. We shipped 20 ChromaID Lab Kits to inventors in the IDMC network during December 2013 and January 2014. As part of our agreement with IDMC, we curtailed our ChromaID marketing efforts through the fourth calendar quarter of 2014 while IDMC worked to expand our intellectual property portfolio. Thereafter, we began to actively market the ChromaID Lab Kits to interested and qualified customers.

We have received a worldwide, nontransferable, exclusive license to the intellectual property developed under the IDMC agreement during the term of the agreement, and solely within the identification, authentication and diagnostics field of use, to (a) make, have made, use, import, sell and offer for sale products and services; (b) make improvements; and (c) grant sublicenses of any and all of the foregoing rights (including the right to grant further sublicenses).

We received a nonexclusive and nontransferable option to acquire a worldwide, nontransferable, nonexclusive license to the useful intellectual property held by IDMC within the identification, authentication and diagnostics field of use to (a) make, have made, use, import, sell and offer to sell products and services and (b) grant sublicenses to any and all of the foregoing rights. The option to acquire this license may be exercised for up to two years from the effective date of the Agreement.

IDMC is providing global business development services to us for geographies not being pursued by Visualant. Also, IDMC has introduced us to potential customers, licensees and distributors for the purpose of identifying and pursuing a license, sale or distribution arrangement or other monetization event.

We granted to IDMC a nonexclusive, worldwide, fully paid, nontransferable, sublicenseable, perpetual license to our intellectual property solely outside the identification, authentication and diagnostics field of use to (a) make, have made, use, import, sell and offer for sale products and services and (b) grant sublicenses of any and all of the foregoing rights (including the right to grant further sublicenses).

We granted to IDMC a nonexclusive, worldwide, fully paid up, royalty-free, nontransferable, non-sublicenseable, perpetual license to access and use our technology solely for the purpose of marketing the aforementioned sublicenses of our intellectual property to third parties outside the designated fields of use.

In connection with the original license agreement, we issued a warrant to purchase 97,169 shares of common stock to IDMC as consideration for the exclusive intellectual property license and application development services. The warrant has a current exercise price of $2.50 per share and expires November 10, 2018. The per share price is subject to adjustment based on any issuances below $2.50 per share except as described in the warrant.

We agreed to pay IDMC a percentage of license revenue for the global development business services and a percentage of revenue received from any company introduce to us by IDMC. We also have also agreed to pay IDMC a royalty when we receive royalty product revenue from an IDMC-introduced company. IDMC has agreed to pay us a license fee for the nonexclusive license of our intellectual property.

The term of both the exclusive intellectual property license and the nonexclusive intellectual property license commences on the effective date of November 11, 2013, and terminates when all claims of the patents expire or are held in valid or unenforceable by a court of competent jurisdiction from which no appeal can be taken.

The term of the Agreement commences on the effective date until either party terminates the Agreement at any time following the fifth anniversary of the effective date by providing at least ninety days' prior written notice to the other party.

TransTech Systems, Inc.

Our wholly owned subsidiary, TransTech Systems, Inc., is a distributor of products, including systems solutions, components and consumables, for employee and personnel identification in government and the private sector, document authentication, access control, and radio frequency identification. TransTech provides these products and services, along with marketing and business development assistance to value-added resellers and system integrators throughout North America.

We expect our ownership of TransTech to accelerate our market entry and penetration through well-operated and positioned dealers of security and authentication systems, thus creating a natural distribution channel for products featuring our proprietary ChromaID technology. TransTech currently provides substantially all of our revenues. Its management team functions independently from Visualant's and its operations require a minimal commitment of our management time and other resources. Our acquisition of TransTech in June 2010 and its operations are described in greater detail below.

Agreements with Sumitomo Precision Products Co., Ltd.

In May 2012, we entered into a Joint Research and Product Development Agreement with SumitomoPrecision Products Co., Ltd., a publicly-traded Japanese corporation, for the commercialization of our ChromaID technology. In March 2013, we entered into an amendment to this agreement, which extended the Joint Development Agreement from March 31, 2013 to December 31, 2013. The extension provided for continuing work between Sumitomo and Visualant focused upon advancing the ChromaID technology and market research aimed at identifying the most significant markets for the ChromaID technology. This collaborative work supported the development of the ChromaID Lab Kit. This agreement expired December 31, 2013. The current version of the technology was introduced to the marketplace as a part of our ChromaID Lab Kit during the fourth quarter of 2013. Sumitomo invested $2,250,000 in exchange for 115,385 shares of restricted shares of common stock priced at $19.50 per share that was funded on June 21, 2012.

We also entered into a License Agreement with Sumitomo in May 2012, under which Sumitomo paid the Company an initial payment of $1 million. The License Agreement granted Sumitomo an exclusive license for the then extant ChromaID technology. The territories covered by this license include Japan, China, Taiwan, Korea and the entirety of Southeast Asia (Burma, Indonesia, Thailand, Cambodia, Laos, Vietnam, Singapore and the Philippines). The Sumitomo License fee was recorded as revenue over the life the Joint Research and Product Development Agreement and was fully recorded as of May 31, 2013. On May 21, 2015, we entered into an amendment to the License Agreement, which, effective as of June 18, 2014, eliminated the Sumitomo exclusivity and provides that if we sell products in certain territories – Japan, China, Taiwan, Korea and the entirety of Southeast Asia (Burma, Indonesia, Thailand, Cambodia, Laos, Vietnam, Singapore and the Philippines) – the Company will pay Sumitomo a royalty rate of 2% of net sales (excluding non-recurring engineering revenues) over the remaining term of the five-year License Agreement (through May 2017).

Potential Markets and Customers

Our plan is to develop markets and customers who have a need to authenticate, detect, identify, verify or diagnose materials or substances which may include, but are not limited to, commercial paint manufacturers, pharmaceutical equipment manufacturers, process control companies, water purification and quality companies, currency paper and ink manufacturers, security card manufacturers, cosmetic companies and food processing companies.

Market opportunities include identification, detection, or diagnosis of:

- Pharmaceuticals – pill counting and verification
- Food safety – testing for contaminants and quality
- Gemstones – diamond color grading
- Liquid analysis – water purity
- Law enforcement - illicit drug identification for law enforcement applications
- Paint – color matching
- ID badges – counterfeit ID detection
- Secure packaging - Container seals and packaging materials with invisible markings
- Cosmetics – matching skin tones to correct products
- Documents and Currency– detect counterfeit paper and inks
- Medical - Noninvasive skin analysis for discovery of diseases or medical conditions

Our Strategy

To date, the substantial portion of our non-TransTech revenue has been generated from the development license with Sumitomo Precision Products and sales of our ChromaID Lab Kits. We expect to continue to grow revenues from sales of our Lab Kits, non-recurring engineering fees, licenses, per unit royalties and subscriptions, as well as “per click” revenues. Key aspects of our strategy include:

Customize and Refine our Solutions to Meet Potential Customers’ Needs

We are continuously improving and expanding our potential product offerings by testing the incorporation of our technologies into different media, such as the new ChromaID Liquid Lab Kit that is in the prototype stage. Each vertical market has specific requirements for their potential product application that will involve determining the range of LEDs and photodiodes that will provide optimum performance and the associated form factor required for their product. Our goal is to develop a cost-effective scanning system for each potential industry and customer that can be incorporated into that potential customer’s products that they will then take to market.

Continue to Expand Applications for ChromaID Technology

While we have basic proof of concepts for applications in several large markets to date, we plan to continue our ongoing effort to expand proof-of-concept testing in other vertical markets that have yet to be tested. We have also identified and are further examining opportunities to collaborate with companies and universities to develop new applications for the ChromaID technology. We believe the strength of our solutions is based on the unique and proprietary ChromaID signature that is created from every scan.

Target Potential High-Volume Markets

We will continue to focus our efforts on target vertical markets that are characterized by a high level of vulnerability to counterfeiting, product tampering, piracy, fraud, identity theft, contamination and adulteration. We believe the ChromaID technology can be a lower cost, real time, flexible form factor solution in the following areas: access control, quality and process control, food safety, water quality, law enforcement support, standardization and medical diagnostics. Our current target markets include pharmaceuticals, food quality and safety, gemstone grading, water purity, law enforcement, paint color matching, identity cards, chemical identification, cosmetics, currency, process control and healthcare. If and when we have significantly penetrated these markets, we intend to expand into additional related high volume markets.

Pursue Strategic Acquisitions and Alliances

We intend to pursue strategic acquisitions of companies and technologies that strengthen and complement our core technologies, improve our competitive positioning, allow us to penetrate new markets, and grow our customer base. We also intend to work in collaboration with potential strategic partners in order to continue to market and sell new product lines derived from, but not limited to, ChromaID technology.

Target Additional Markets

In fourth fiscal quarter of 2014, we began introducing our technology and services in Europe, the United States and Asia. Several potential customers are currently analyzing our technology. At the present time, we are focusing our efforts on the pharmaceutical industry, the food safety industry, law enforcement and homeland security. In the future, we plan to expand our focus to include identification cards and other secure documents, industrial materials, agrochemicals, pharmaceuticals, consumer products, cosmetics, currency and medical diagnostics.

Industry Background

Visualant's ChromaID is a part of the broad industry built upon photonics or light-based technology. Photonics science includes the generation, emission, transmission, modulation, signal processing, switching, amplification, and detection/sensing of light. Though covering all light's technical applications over the whole spectrum, most photonic applications are in the range of visible and near-infrared light. The term photonics developed as an outgrowth of the first practical semiconductor light emitters invented in the early 1960s and optical fibers developed in the 1970s.

Photonics came into common use in the 1980s as fiber-optic data transmission was adopted by telecommunications network operators. At that time, the term was used widely at Bell Laboratories. Its use was confirmed when the IEEE Lasers and Electro-Optics Society established an archival journal named Photonics Technology Letters at the end of the 1980s.

Photonics covers a huge range of science and technology applications, including laser manufacturing, biological and chemical sensing, medical diagnostics and therapy, display technology, and optical computing.

Applications of photonics includes all areas from everyday life to the most advanced science, e.g. light detection, telecommunications, information processing, lighting, metrology, spectroscopy, holography, medicine (surgery, vision correction, endoscopy, health monitoring), military technology, laser material processing, visual art, biophotonics, agriculture and robotics.

The world photonics market, according to the *World Photonics Report of 2013* was a $350 billion market and will grow to a $650 billion market by 2020.

Our business model is focused on the use of structured light - a disruptive conceptual breakthrough in photonics. Light-emitting diodes (LEDs) shine a single wavelength of pulsed light in increasing steps of intensity onto a subject. Photodiodes capture the light that is returned via reflection or re emission of that light. The photodiode produces an analog signal that is then converted into a 24 bit digital data point for each pulse of light. A typical scan is comprised of hundreds of pulses of light across a number of specific frequency LED's creating a unique ChromaID signature for the subject being scanned. In a typical application a "reference" or "master" ChromaID signature is captured and stored in a database for that specific subject. When an unknown substance is scanned to produce its own ChromaID signature, (the "discovery scan"), the unknown substance's ChromaID signature is compared to that of the known (or "reference") ChromaID signature. Algorithms are used to compare the two sets of data and determine if the "discovery" signature is the same as the "reference" ChromaID signature. This accuracy threshold can be adjusted from 51 % to 99.995 % accuracy based on the requirements for each specific application of the ChromaID technology. Historically, a number of the applications for ChromaID technology were performed by spectrophotometers. The sales of spectrophotometers by companies such as Ocean Optics, Perkin Elmer, Fisher Thermo Scientific and Agilent are multibillion dollar businesses. Spectrophotometers combine broad-spectrum light; a diffraction grating to split it; and a linear array for graphical presentation in software. They tend to be bulky, fragile, and expensive; scanning and analysis are complex. We believe our ChromaID technology uses lower cost components, provides more accurate data, has a very flexible form factor and the information it provides can be easily understood. The use of structured light by our ChromaID technology provides a platform for the development of a myriad of applications in the categories of identification, authentication and diagnostics.

We believe that the ChromaID technology is analogous to a smartphone, upon which an enormous number of previously unforeseen applications have been developed. The ChromaID technology may be considered an enabling technology that brings the science of light and photonics to low cost, real world commercialization opportunities across multiple industries. ChromaID is a sensor technology which, with its low cost, small form factor, and ease of connectivity can be an enabling technology for the broad Internet of Things and integrated into many aspects of everyday life providing useful information relating health, life and safety. The technology is foundational and as such, the basis upon which we believe a significant business can be built.

THE COMPANY'S COMMON STOCK

Our common stock trades on the OTCQB Exchange under the symbol "VSUL."

PRIMARY RISKS AND UNCERTAINTIES

We are exposed to various risks related to our need for additional financing, the sale of significant numbers of our shares and a volatile market price for our common stock. These risks and uncertainties are discussed in more detail below in Part II, Item 1A.

RESULTS OF OPERATIONS

The following table presents certain consolidated statement of operations information and presentation of that data as a percentage of change from period-to-period.

(dollars in thousands)

	Three Months Ended March 31,			
	2016	2015	$ Variance	% Variance
Revenue	$ 1,467	$ 1,435	$ 32	2.2%
Cost of sales	1,252	1,205	47	-3.9%
Gross profit	215	230	(15)	-6.5%
Research and development expenses	82	77	5	-6.5%
Selling, general and administrative expenses	817	875	(58)	6.6%
Operating loss	(684)	(722)	38	5.3%
Other income (expense):				
Interest expense	(88)	(84)	(4)	-4.8%
Other income	1	12	(11)	-91.7%
Gain on change - derivative liability	476	3,032	(2,556)	-84.3%
Total other income	389	2,960	(2,571)	-86.9%
Loss before income taxes	(295)	2,238	(2,533)	-113.2%
Income taxes - current (benefit)	-	(4)	4	100.0%
Net loss	$ (295)	$ 2,242	$ (2,537)	-113.2%

THREE MONTHS ENDED MARCH 31, 2016 COMPARED TO THE THREE MONTHS ENDED MARCH 31, 2015

Sales

Net revenue for the three months ended March 31, 2016 increased $32,000 to $1,467,000 as compared to $1,435,000 for the three months ended March 31, 2015. The increase was due to higher sales at TransTech of $1,465,000.

Cost of Sales

Cost of sales for the three months ended March 31, 2016 increased $47,000 to $1,252,000 as compared to $1,205,000 for the three months ended March 31, 2015. The increase was due to higher sales, offset by slightly lower gross margins at TransTech.

Gross profit was $215,000 for the three months ended March 31, 2016 as compared to $230,000 for the three months ended March 31, 2015. Gross profit was 14.5% for the three ended March 31, 2016 as compared to 16.0% for the three months ended March 31, 2015. The gross profit increase related to lower sales prices at TransTech.

Research and Development Expenses

Research and development expenses for the three months ended March 31, 2016 increased $5,000 to $82,000 as compared to $77,000 for the three months ended March 31, 2015. The increase was due to increased expenditures for suppliers related to the commercialization of our ChromaID technology.

Selling, General and Administrative Expenses

Selling, general and administrative expenses for the three months ended March 31, 2016 decreased $58,000 to $817,000 as compared to $875,000 for the three months ended March 31, 2015. The decrease primarily was due to decrease in business development expenses of $45,000 and consulting expenses of $18,000, offset by a decrease in all other expenses of $5,000 As part of the selling, general and administrative expenses for the three months ended March 31, 2016, we incurred investor relation expenses of $4,000 and business development expenses of $238,000.

Other Income/Expense

Other income for the three months ended March 31, 2016 was $389,000 as compared to $2,960,000 for the three months ended March 31, 2015. The other income for the three months ended March 31, 2016 included other income of $1,000 and change - derivative liability of $476,000, offset by interest expense of $88,000. The gain on change derivative liability related to derivative instruments included in the June 2013 private placement, the November 2013 IDMC Services and License Agreement, our convertible notes payable and the issuance of Series A Convertible Preferred Stock and Series B Redeemable Preferred Stock.

The other income for the three months ended March 31, 2015 included other income of $12,000 and gain on change - derivative liability of $3,032,000, offset by interest expense of $84,000. The gain on change derivative liability warrants related to derivative instruments included in the June 2013 private placement, the November 2013 IDMC Services and License Agreement, our convertible notes payable and the issuance of Series A Convertible Preferred Stock.

Net (Loss) Income

Net loss for the three months ended March 31, 2016 was $295,000 as compared to net income of $2,242,000 for the three months ended March 31, 2015. Net loss for the three months ended March 31, 2016 was net of change – derivative liability of $476,000, offset by included non-cash other expense of $222,000 including (i) depreciation and amortization of $49,000; (ii) issuance of capital stock for services and expenses of $80,000; (iii) stock based compensation of $11,000; and (iv) other expense of $82,000. TransTech's net loss from operations was $41,000 for the three months ended March 31, 2016 as compared net loss of $44,000 for the three months ended March 31, 2015.

The net loss for the three months ended March 31, 2015, included non-cash income of $2,790,000, including (i) gain on change- derivative liability of $3,032,000, (ii) other of $21,000, offset by (iii) depreciation and amortization of $106,000; (iv) stock based compensation of $19,000; and (v) share and warrant issuances of $138,000.

We expect losses to continue as we commercialize our ChromaID technology.

(dollars in thousands)

	Six Months Ended March 31,			
	2016	2015	$ Variance	% Variance
Revenue	$ 2,752	$ 3,278	$ (526)	-16.0%
Cost of sales	2,339	2,750	(411)	14.9%
Gross profit	413	528	(115)	-21.8%
Research and development expenses	174	197	(23)	11.7%
Selling, general and administrative expenses	1,553	1,528	25	-1.6%
Operating loss	(1,314)	(1,197)	(117)	-9.8%
Other income (expense):				
Interest expense	(126)	(121)	(5)	-4.1%
Other income	3	19	(16)	-84.2%
(Loss) gain on change - derivative liability	(870)	381	(1,251)	-328.3%
Total other (expense) income	(993)	279	(1,272)	-455.9%
Loss before income taxes	(2,307)	(918)	(1,389)	-151.3%
Income taxes - current (benefit)	-	(3)	3	-100.0%
Net loss	$ (2,307)	$ (915)	$ (1,392)	-152.1%

SIX MONTHS ENDED MARCH 31, 2016 COMPARED TO THE SIX MONTHS ENDED MARCH 31, 2015

Sales

Net revenue for the six months ended March 31, 2016 decreased $526,000 to $2,752,000 as compared to $3,278,000 for the six months ended March 31, 2015. The decrease was due to lower sales at TransTech of $1,282,000 resulting from a reduction in sales from the products of one large vendor.

Cost of Sales

Cost of sales for the six months ended March 31, 2016 decreased $411,000 to $2,339,000 as compared to $2,750,000 for the six months ended March 31, 2015. The decrease was due to lower sales and gross margins at TransTech.

Gross profit was $413,000 for the six months ended March 31, 2016 as compared to $528,000 for the six months ended March 31, 2015. Gross profit was 15.0% for the six ended March 31, 2016 as compared to 16.1% for the six months ended March 31, 2015. The gross profit increase related to lower sales prices at TransTech.

Research and Development Expenses

Research and development expenses for the six months ended March 31, 2016 decreased $23,000 to $174,000 as compared to $197,000 for the six months ended March 31, 2015. The decrease was due to reduced expenditures for suppliers related to the commercialization of our ChromaID technology.

Selling, General and Administrative Expenses

Selling, general and administrative expenses for the six months ended March 31, 2016 increased $25,000 to $1,553,000 as compared to $1,528,000 for the six months ended March 31, 2015. The increase primarily was due to increase in investor relations expenses of $82,000, consulting expenses of $62,000, and other expense of $21,000, offset by a decrease in amortization expense of $98,000. As part of the selling, general and administrative expenses for the six months ended March 31, 2016, we incurred investor relation expenses of $100,000 and business development expenses of $246,000.

Other Income/Expense

Other expense for the six months ended March 31, 2016 was $993,000 as compared to $279,000 for the six months ended March 31, 2015. The other expense for the six months ended March 31, 2016 included other income of $3,000, offset by loss on change - derivative liability of $870.000, and interest expense of $126,000. The loss on change derivative liability related to derivative instruments included in the June 2013 private placement, the November 2013 IDMC Services and License Agreement, our convertible notes payable and the issuance of Series A Convertible Preferred Stock and Series B Redeemable Preferred Stock.

The other income for the six months ended March 31, 2015 included other income of $19,000 and gain on change - derivative liability of $381,000, offset by interest expense of $121,000. The gain on change derivative liability warrants related to derivative instruments included in the June 2013 private placement, the November 2013 IDMC Services and License Agreement, our convertible notes payable and the issuance of Series A Convertible Preferred Stock.

Net Loss

Net loss for the six months ended March 31, 2016 was $2,307,000 as compared to $915,000 for the six months ended March 31, 2015. Net loss for the six months ended March 31, 2016 included non-cash other expense of $1,304,000 including (i) depreciation and amortization of $94,000; (ii) issuance of capital stock for services and expenses of $185,000; (iii) stock based compensation of $24,000; (iv) change – derivative liability of $870,000; and (v)expenses related to the issuance of convertible notes payable of $131,000. TransTech's net loss from operations was $127,000 for the six months ended March 31, 2016 as compared net loss of $36,000 for the six months ended March 31, 2015.

The net loss for the six months ended March 31, 2015, included non-cash expense of $9,000, including (i) gain on change- derivative liability warrants of $381,000, (ii) other of $16,000, offset by (iii) depreciation and amortization of $210,000; (iv) stock based compensation of $40,000; and (v) share and warrant issuances of $138,000.

We expect losses to continue as we commercialize our ChromaID technology.

LIQUIDITY AND CAPITAL RESOURCES

Liquidity is the ability of a company to generate funds to support its current and future operations, satisfy its obligations, and otherwise operate on an ongoing basis. Significant factors in the management of liquidity are funds generated by operations, levels of accounts receivable and accounts payable and capital expenditures.

We had cash of $521,000 and net working capital deficit of approximately $4,467,000 (excluding the derivative liability- warrants of $3,574,000) as of March 31, 2016. We expect losses to continue as we commercialize our ChromaID™ technology. Our cash used in operations for the six months ended March 31, 2016 and the years ended September 30, 2015 and 2014 was $(1,188,000) ($240,000) and $(1,379,000), respectively. We believe that our cash on hand will be sufficient to fund our operations through June 30, 2016.

The opinion of our independent registered public accounting firm on our audited financial statements as of and for the year ended September 30, 2015 contains an explanatory paragraph regarding substantial doubt about our ability to continue as a going concern. Our ability to continue as a going concern is dependent upon raising capital from financing transactions.

We need additional financing to implement our business plan and to service our ongoing operations and pay our current debts. There can be no assurance that we will be able to secure any needed funding, or that if such funding is available, the terms or conditions would be acceptable to us. If we are unable to obtain additional financing when it is needed, we will need to restructure our operations, and divest all or a portion of our business. We may seek additional capital through a combination of private and public equity offerings, debt financings and strategic collaborations. Debt financing, if obtained, may involve agreements that include covenants limiting or restricting our ability to take specific actions, such as incurring additional debt, and could increase our expenses and require that our assets secure such debt. Equity financing, if obtained, could result in dilution to our then-existing stockholders and/or require such stockholders to waive certain rights and preferences. If such financing is not available on satisfactory terms, or is not available at all, we may be required to delay, scale back or eliminate the development of business opportunities and our operations and financial condition may be materially adversely affected.

As of November 3, 2015, we received commitments from debtors to convert $1,000,000 into our common stock as part of our proposed listing on The NASDAQ Capital Market. These conversions are expected to increase stockholder's equity by $1,000,000.

We have outstanding Series A Warrants to purchase a total of 316,223 shares of common stock with a current exercise price of $2.50 per share, and Series B Warrants to purchase a total of 319,717 shares of common stock with a current exercise price of $2.50 per share, the IDMC warrant to purchase 97,169 shares of common stock with a current exercise price of $2.50 per share, placement warrants to purchase 28,554 shares of common stock with a current exercise price of $2.50 per share and Series C and D Warrants to purchase 23,334 shares of common stock at an exercise price of current exercise price of $2.50 per share. The above Warrants contain an adjustment provision that would require an adjustment in the exercise price of the above Warrants if we issue common stock, warrants or equity below the price that is reflected in the above Warrants. If we issue any additional shares of common stock, warrants or other equity securities at a price below the exercise prices of the above Warrants, it would result in a reduction in the exercise price of the above Warrants.

We issued convertible notes payable to investors totaling $710,000 to fund short-term working capital. These notes accrue interest at a rate of 8% per annum, become due during September 2016 to February 2017 and are convertible into common stock as part of our next public financing, at a conversion price equal to the price of the common stock sold in our next public financing. The investors received $710,000 in warrants that are exercisable into common stock at the price equal to the price of the common stock sold in our next public financing.

We entered into 10% Convertible Promissory Notes and Securities Purchase Agreements with three accredited investors on February 4, 2016, totaling $165,000, to fund short-term working capital. The Notes become due on February 3, 2017 and are convertible into common stock after six months from issuance. The Notes are convertible at 60% of the average of the lowest trading price in the 25 days prior to conversion. We issued a total of 10,500 shares of restricted common stock to the investors, and received $128,500 net of all fees.

We entered into a Convertible Note Payable with Vis Vires Group, Inc. on February 18, 2016 for $100,000 to fund short-term working capital. The Vis Vires Note accrued interest at a rate of 8% per annum, becomes due on November 22, 2016 and is convertible into common stock beginning on August 19, 2016. The Vis Vires Note is convertible at 65% of the average of the lowest three-day trading price in the 10 days prior to conversion. We received $86,000 from the sale of the Vis Vires Not, net of all fees.

On March 8, 2016, we received approval from the State of Nevada for the Certificate of Designations of Preferences, Powers, Rights and Limitations of Series B Redeemable Convertible Preferred Stock. The Certificate authorized 5,000 shares of Series B Preferred Stock at a par value of $.001 per share that is convertible into common stock at $7.50 per share, subject to certain adjustments as set forth in the Certificate.

We entered into a Stock Purchase Agreement with the selling stockholder pursuant to which the Company issued 255 Shares of Series B Redeemable Preferred Shares ("Series B Preferred Shares") of the Company at $10,000 per share with a 5.0% original issue discount for the sum of $2,500,000.

At closing, the Company sold 51 Series B Preferred Shares in exchange for payment to the Company of $500,000 in cash and issued an additional 204 Series B Preferred Shares in exchange for delivery of a full recourse 1% Promissory Note ("Note") for $1,995,000 and payment to the Company of $5,000 in cash. The Note is collateralized by the Series B Preferred Shares. Under the terms of the Note, the Company is to receive an additional $500,000 for each $5 million, or in certain cases a lower amount, in aggregate trading volume of the common stock, so long as it meets certain other requirements. Any remaining balance under the Note is payable at its maturity in seven years.

The Series B Preferred Shares are convertible into common stock at $7.50 per share; provided that the investor may not convert any Series B Preferred Shares into common stock until that portion of the Note underlying the purchase of the converted portion of Series B Preferred Shares is paid in cash to Company.

We have financed our corporate operations and our technology development through the issuance of convertible debentures, the issuance of preferred stock, the sale common stock, issuance of common stock in conjunction with an equity line of credit, loans by our Chief Executive Officer and the exercise of warrants.

We finance our TransTech operations from operations and a Secured Credit Facility with Capital Source Business Finance Group. On December 9, 2008, TransTech entered into a $1,000,000 secured credit facility with Capital Source to fund its operations. On December 12, 2015, the secured credit facility was renewed for an additional six months, with a floor for prime interest of 4.5% (currently 4.5%) plus 2.5%. The eligible borrowing is based on 80% of eligible trade accounts receivable, not to exceed $1,000,000. The secured credit facility is collateralized by the assets of TransTech, with a guarantee by Visualant, including a security interest in all assets of Visualant. Availability under this Secured Credit ranges from $0 to $175,000 ($49,000 as of March 31, 2016) on a daily basis. The remaining balance on the accounts receivable line of $508,000 as of March 31, 2016 must be repaid by the time the secured credit facility expires on June 12, 2016, or we renew by automatic extension for the next successive six-month term.

Operating Activities

Net cash used in operating activities for the three months ended March 31, 2016 was $1,188,000. This amount was primarily related to a net loss of $2,307,000 and an increase in accounts receivable of $191,000 offset by non-cash other expense of $1,304,000 and other of $6,000. The non-cash other expense of $1,244,000 includes (i) depreciation and amortization of $94,000; (ii) issuance of capital stock for services and expenses of $185,000; (iii) stock based compensation of $24,000; (iv) change – derivative liability of $870,000; and (v)expenses related to the issuance of convertible notes payable of $131,000.

Financing Activities

Net cash provided by financing activities for the three months ended March 31, 2016 was $1,629,000. This amount was primarily related to (i) proceeds from the exercise of warrants of $169,000; (ii) proceeds from convertible notes of $925,000; (iii) proceeds from line of credit of $143,000; and (iv) proceeds from the issuance of Series B Redeemable Preferred Stock of $505,000, offset by the repayment of convertible notes of $115,000.

Our contractual cash obligations as of March 31, 2016 are summarized in the table below:

Contractual Cash Obligations	Total	Less Than 1 Year	1-3 Years	3-5 Years	Greater Than 5 Years
Operating leases	$ 19,033	$ 19,033	$ -	$ -	$ -
Convertible notes payable	975,000	975,000	-	-	-
Notes payable	1,307,632	1,307,632	-	-	-
Capital expenditures	100,000	20,000	40,000	40,000	-
	$ 2,401,665	$ 2,321,665	$ 40,000	$ 40,000	$ -

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements (as that term is defined in Item 303 of Regulation S-K) that are reasonably likely to have a current or future material effect on our financial condition, revenue or expenses, results of operations, liquidity, capital expenditures or capital resources.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

This item is not applicable.

ITEM 4. CONTROLS AND PROCEDURES

a) Evaluation of Disclosure Controls and Procedures

We conducted an evaluation under the supervision and with the participation of our management, of the effectiveness of the design and operation of our disclosure controls and procedures. The term "disclosure controls and procedures," as defined in Rules 13a-15(e) and 15d-15(e) under the Securities and Exchange Act of 1934, as amended ("Exchange Act"), means controls and other procedures of a company that are designed to ensure that information required to be disclosed by the company in the reports it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures also include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate, to allow timely decisions regarding required disclosure. Based on this evaluation, our principal executive and principal financial officers concluded as of March 31, 2016 that our disclosure controls and procedures were not effective at the reasonable assurance level due to the material weaknesses in our internal controls over financial reporting discussed immediately below.

Identified Material Weakness

A material weakness in our internal control over financial reporting is a control deficiency, or combination of control deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected.

Management identified the following material weakness during its assessment of internal controls over financial reporting:

Audit Committee: While we have an audit committee, we lack a financial expert. During 2016, the Board expects to appoint an additional independent Director to serve as Audit Committee Chairman who is an "audit committee financial expert" as defined by the Securities and Exchange Commission ("SEC") and as adopted under the Sarbanes-Oxley Act of 2002. In addition, this Director is expected to strengthen our governance processes. We are using external service providers to ensure compliance with the Securities and Exchange Commission requirements until we appoint the Audit Committee Chairman.

b) Changes in Internal Control over Financial Reporting

During the quarter ended March 31, 2016, there were no changes in our internal controls over financial reporting during this fiscal quarter that materially affected, or is reasonably likely to have a materially affect, on our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1A. RISK FACTORS

There are certain inherent risks which will have an effect on the Company's development in the future and the most significant risks and uncertainties known and identified by our management are described below.

Risks Relating to the Commercialization of Our Products

We may not be able to generate sufficient revenue from the commercialization of our ChromaID technology and related products to achieve or sustain profitability.

We are in the process of commercializing our ChromaID™ technology. To date, we have entered into one License Agreement with Sumitomo Precision Products Co., Ltd. and have a strategic relationship with IDMC. Failure to sell our ChromaID products, grant additional licenses and obtain royalties or develop other revenue streams will have a material adverse effect on our business, financial condition and results of operations.

We believe that our commercialization success is dependent upon our ability to significantly increase the number of customers that are using our products To date, we have generated minimal revenue from sales of our ChromaID products. In addition, demand for our ChromaID products may not increase as quickly as planned and we may be unable to increase our revenue levels as expected. We are currently not profitable. Even if we succeed in introducing the ChromaID technology and related products to our target markets, we may not be able to generate sufficient revenue to achieve or sustain profitability.

We are in the early stages of commercialization and our ChromaID technology and related products may never achieve significant commercial market acceptance.

Our success depends on our ability to develop and market products that are recognized as accurate and cost-effective. Many of our potential customers may be reluctant to use our new technology. Market acceptance will depend on many factors, including our ability to convince potential customers that our ChromaID technology and related products are an attractive alternative to existing light-based technologies. We will need to demonstrate that our products provide accurate and cost-effective alternatives to existing light-based authentication technologies. Compared to most competing technologies, our technology is relatively new, and most potential customers have limited knowledge of, or experience with, our products. Prior to implementing our ChromaID technology and related products, potential customers are required to devote significant time and effort to testing and validating our products. In addition, during the implementation phase, customers may be required to devote significant time and effort to training their personnel on appropriate practices to ensure accurate results from our technology and products. Any failure of our ChromaID technology or related products to meet customer expectations could result in customers choosing to retain their existing testing methods or to adopt systems other than ours.

Many factors influence the perception of a system including its use by leaders in the industry. If we are unable to induce industry leaders in our target markets to implement and use our ChromaID technology and related products, acceptance and adoption of our products could be slowed. In addition, if our products fail to gain significant acceptance in the marketplace and we are unable to expand our customer base, we may never generate sufficient revenue to achieve or sustain profitability.

We may be unable to manage our future growth effectively, which could make it difficult to execute our business strategy.

We commenced our formal commercial launch in the fourth fiscal quarter of 2014 and anticipate growth in our business operations. Since our inception in 1998, we have increased our number of employees to 16 as of March 31, 2016 and we expect to increase our number of employees further as our business grows. This future growth could create strain on our organizational, administrative and operational infrastructure, including quality control, customer service and sales and marketing. Our ability to manage our growth properly will require us to continue to improve our operational, financial, and management controls, as well as our reporting systems and procedures. If our current infrastructure is unable to handle our growth, we may need to expand our infrastructure and staff and implement new reporting systems. The time and resources required to implement such expansion and systems could adversely affect our operations. Our expected future growth will impose significant added responsibilities on members of management, including the need to identify, recruit, maintain, and integrate additional employees. Our future financial performance and our ability to commercialize our products and to compete effectively will depend, in part, on our ability to manage this potential future growth effectively, without compromising quality.

Risks Relating to our Business and Financial Condition

We have a history of operating losses and there can be no assurance that we can achieve or maintain profitability.

We have experienced net losses since inception. As of March 31, 2016, we had an accumulated deficit of $26.5 million and net losses in the amount of $2,335.000, $2,631,000 and $1,017,000 for the six months ended March 31, 2016 and the years ended September 30, 2015 and 2014, respectively. There can be no assurance that we will achieve or maintain profitability. If we achieve profitability in the future, we may not be able to sustain profitability in subsequent periods. Failure to become and remain profitable would impair our ability to sustain operations and adversely affect the price of our common stock and our ability to raise capital. Our operating expenses may increase as we spend resources on growing our business, and if our revenue does not correspondingly increase, our operating results and financial condition will suffer. Our ChromaID business has produced limited revenues, and may not produce significant revenues in the near term, or at all, which would harm our ability to continue our operations or obtain additional financing and require us to reduce or discontinue our operations. You must consider our business and prospects in light of the risks and difficulties we will encounter as business with an early-stage technology in a new and rapidly evolving industry. We may not be able to successfully address these risks and difficulties, which could significantly harm our business, operating results and financial condition.

We need additional financing to support our technology development and ongoing operations, pay our debts and maintain ownership of our intellectual properties; we will not receive any of the proceeds from the sale of the common stock by the selling stockholder.

We are currently operating at a loss. We believe that our cash on hand will be sufficient to fund our operations through June 30, 2016. We need additional financing to implement our business plan and to service our ongoing operations, pay our current debts (described below) and maintain ownership of our intellectual property. There can be no assurance that we will be able to secure any needed funding, or that if such funding is available, the terms or conditions would be acceptable to us. If we are unable to obtain additional financing when it is needed, we will need to restructure our operations and/or divest all or a portion of our business. We may seek additional capital through a combination of private and public equity offerings, debt financings and strategic collaborations. Debt financing, if obtained, may involve agreements that include covenants limiting or restricting our ability to take specific actions, such as incurring additional debt, and could increase our expenses and require that our assets secure such debt. Equity financing, if obtained, could result in dilution to our then-existing stockholders and/or require such stockholders to waive certain rights and preferences. If such financing is not available on satisfactory terms, or is not available at all, we may be required to delay, scale back or eliminate the development of business opportunities and our operations and financial condition may be materially adversely affected.

Our services and license agreement with Invention Development Management Company, LLC is important to our business strategy and operations.

In November 2013, we entered into a Services and License Agreement with Invention Development Management Company. IDMC is a subsidiary of Intellectual Ventures, which collaborates with inventors, partners with companies and invests both expertise and capital in the process of invention. This agreement was amended in November 2014 to license ten patents filed by IDMC related to the ChromaID technology to us.

The amended agreement with IDMC covers a number of areas that are important to our operations, including the following:

- The agreement requires IDMC to identify and engage inventors to develop new applications of our ChromaID technology, present the developments to us for approval, and file at least ten patent applications to protect the developments;
- We received a worldwide, nontransferable, exclusive license to the licensed intellectual property developed under this agreement within the identification, authentication and diagnostics field of use;
- We received a nonexclusive and nontransferable option to acquire a worldwide, nontransferable, nonexclusive license to intellectual property held by IDMC within that same field of use; and
- We granted to IDMC certain licenses to our intellectual property outside the identification, authentication and diagnostics field of use.

Failure to operate in accordance with the IDMC agreement, or an early termination or cancellation of this agreement for any reason, would have a material adverse effect on ability to execute our business strategy and on our results of operations and business.

We need to continue as a going concern if our business is to succeed.

Because of our recurring losses and negative cash flows from operations, the audit report of our independent registered public accountants on our consolidated financial statements for the year ended September 30, 2015 contains an explanatory paragraph stating that there is substantial doubt about our ability to continue as a going concern. Factors identified in the report include our historical net losses, negative working capital, and the need for additional financing to implement our business plan and service our debt repayments. If we are not able to attain profitability in the near future our financial condition could deteriorate further, which would have a material adverse impact on our business and prospects and result in a significant or complete loss of your investment. Further, we may be unable to pay our debt obligations as they become due, which include obligations to secured creditors. If we are unable to continue as a going concern, we might have to liquidate our assets and the values we receive for our assets in liquidation or dissolution could be significantly lower than the values reflected in our financial statements. Additionally, we are subject to customary operational covenants, including limitations on our ability to incur liens or additional debt, pay dividends, redeem stock, make specified investments and engage in merger, consolidation or asset sale transactions, among other restrictions. In addition, the inclusion of an explanatory paragraph regarding substantial doubt about our ability to continue as a going concern and our lack of cash resources may materially adversely affect our share price and our ability to raise new capital or to enter into critical contractual relations with third parties.

We have obligations to repay approximately $2,849,935 in various loans in the near future, and if we do not satisfy these obligations, the lenders may have the right to demand payment in full or exercise other remedies.

We have a $199,935 Business Loan Agreement with Umpqua Bank (the "Umpqua Loan"), which currently matures on December 31, 2016 and provides for interest at 3.25% per year. Related to the Umpqua Loan, we entered into a demand promissory note for $200,000 on January 10, 2014 with an entity with which Ronald P. Erickson, our Chief Executive Officer, is affiliated. This demand promissory note will be effective in case of a default by us under the Umpqua Loan.

We also have two other demand promissory notes payable to entities affiliated with Mr. Erickson, totaling $600,000. Each of these notes were issued between January and July 2014, provide for interest of 3% per year and now mature on March 31, 2016. They also provide for a second lien on our assets if not repaid by March 31, 2016 or converted into convertible debentures or equity on terms acceptable to the Mr. Erickson. Mr. Erickson and/or entities with which he is affiliated also have advanced $668,500 and have unreimbursed expenses and compensation of approximately $386,500. We owe Mr. Erickson, or entities with which he is affiliated, $1,675,000 as of March 31, 2016.

We also have convertible notes payable to investors totaling $710,000 to fund short-term working capital. These notes accrue interest at a rate of 8% per annum, become due during September 2016 and February 2017 and are convertible into common stock as part of our next financing, at a conversion price equal to the price of the common stock sold in our next public financing. The investors received $710,000 in warrants that are exercisable into common stock at the price equal to the price of the common stock sold in our next public financing.

We entered into 10% Convertible Promissory Notes and Securities Purchase Agreements with three accredited investors on February 4, 2016 totaling $165,000 to fund short-term working capital. The Notes become due on February 3, 2017 and are convertible into common stock after six months from issuance. The Notes are convertible at 60% of the average of the lowest trading price in the 25 days prior to conversion. We issued a total of 10,500 shares of restricted common stock to the investors. We received $128,500 net of all fees.

We entered into a Convertible Note Payable with Vis Vires Group, Inc. on February 18, 2016 for $100,000 to fund short-term working capital. The Vis Vires Note accrued interest at a rate of 8% per annum and becomes due on November 22, 2016 and was convertible into common stock on August 19, 2016. The Vis Vires Note was convertible at 65% of the average of the lowest three day trading price in the 10 days prior to conversion. We received $86,000 net of all fees.

We require additional financing, to service and/or repay these debt obligations. If we raise additional capital through borrowing or other debt financing, we may incur substantial interest expense. If and when we raise more equity capital in the future, it will result in substantial dilution to our current stockholders.

Our management has concluded that we have material weaknesses in our internal controls over financial reporting and that our disclosure controls and procedures are not effective.

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of a company's annual or interim financial statements will not be prevented or detected on a timely basis. During the audit of our financial statements for the year ended September 30, 2015, our management identified material weaknesses in our internal control over financial reporting. If these weaknesses continue, investors could lose confidence in the accuracy and completeness of our financial reports and other disclosures.

In addition, our management has concluded that our disclosure controls and procedures were not effective due to the lack of an audit committee "financial expert."These material weaknesses, if not remediated, create an increased risk of misstatement of the Company's financial results, which, if material, may require future restatement thereof. A failure to implement improved internal controls, or difficulties encountered in their implementation or execution, could cause future delays in our reporting obligations and could have a negative effect on us and the trading price of our common stock.

If the company were to dissolve or wind-up, holders of our common stock would not receive a liquidation preference.

If we were to wind-up or dissolve our company and liquidate and distribute our assets, our common stockholders would share in our assets only after we satisfy any amounts we owe to our creditors and preferred equity holders. If our liquidation or dissolution were attributable to our inability to profitably operate our business, then it is likely that we would have material liabilities at the time of liquidation or dissolution. Accordingly, it is very unlikely that sufficient assets will remain available after the payment of our creditors and preferred equity holders to enable you to receive any liquidation distribution with respect to any common stock you hold.

If components used in our finished products become unavailable, or third-party manufacturers otherwise experience delays, we may incur delays in shipment to our customers, which would damage our business.

We depend on third-party suppliers for substantially all of our components and products. We purchase these products and components from third-party suppliers that serve the advanced lighting systems market and we believe that alternative sources of supply are readily available for most products and components. However, consolidation could result in one or more current suppliers being acquired by a competitor, rendering us unable to continue purchasing necessary amounts of key components at competitive prices. In addition, for certain of our customized components, arrangements for additional or replacement suppliers will take time and result in delays. We purchase products and components pursuant to purchase orders placed from time to time in the ordinary course of business. This means we are vulnerable to unanticipated price increases and product shortages. Any interruption or delay in the supply of components and products, or our inability to obtain components and products from alternate sources at acceptable prices in a timely manner, could harm our business, financial condition and results of operations.

While we believe alternative manufacturers for these products are available, we have selected these particular manufacturers based on their ability to consistently produce these products per our specifications ensuring the best quality product at the most cost effective price. We depend on our third-party manufacturers to satisfy performance and quality specifications and to dedicate sufficient production capacity within scheduled delivery times. Accordingly, the loss of all or one of these manufacturers or delays in obtaining shipments could have a material adverse effect on our operations until such time as an alternative manufacturer could be found.

We are dependent on key personnel.

Our success depends to a significant degree upon the continued contributions of key management and other personnel, some of whom could be difficult to replace, including Ronald P. Erickson, our Chief Executive Officer. We do not maintain key person life insurance covering any of our officers. Our success will depend on the performance of our officers, our ability to retain and motivate our officers, our ability to integrate new officers into our operations, and the ability of all personnel to work together effectively as a team. Our officers do not currently have employment agreements. Our failure to retain and recruit officers and other key personnel could have a material adverse effect on our business, financial condition and results of operations. Our success also depends on our continued ability to identify, attract, hire, train, retain and motivate highly skilled technical, managerial, manufacturing, administrative and sales and marketing personnel. Competition for these individuals is intense, and we may not be able to successfully recruit, assimilate or retain sufficiently qualified personnel. In particular, we may encounter difficulties in recruiting and retaining a sufficient number of qualified technical personnel, which could harm our ability to develop new products and adversely impact our relationships with existing and future customers. The inability to attract and retain necessary technical, managerial, manufacturing, administrative and sales and marketing personnel could harm our ability to obtain new customers and develop new products and could adversely affect our business and operating results.

We have limited insurance which may not cover claims by third parties against us or our officers and directors.

We have limited directors' and officers' liability insurance and commercial liability insurance policies. Claims by third parties against us may exceed policy amounts and we may not have amounts to cover these claims. Any significant claims would have a material adverse effect on our business, financial condition and results of operations. In addition, our limited directors' and officers' liability insurance may affect our ability to attract and retain directors and officers.

Our inability to effectively protect our intellectual property would adversely affect our ability to compete effectively, our revenue, our financial condition and our results of operations.

We rely on a combination of patent, trademark, and trade secret laws, confidentiality procedures and licensing arrangements to protect our intellectual property rights. Obtaining and maintaining a strong patent position is important to our business. Patent law relating to the scope of claims in the technology fields in which we operate is complex and uncertain, so we cannot be assured that we will be able to obtain or maintain patent rights, or that the patent rights we may obtain will be valuable, provide an effective barrier to competitors or otherwise provide competitive advantages. Others have filed, and in the future are likely to file, patent applications that are similar or identical to ours or those of our licensors. To determine the priority of inventions, or demonstrate that we did not derive our invention from another, we may have to participate in interference or derivation proceedings in the USPTO or in court that could result in substantial costs in legal fees and could substantially affect the scope of our patent protection. We cannot be assured our patent applications will prevail over those filed by others. Also, our intellectual property rights may be subject to other challenges by third parties. Patents we obtain could be challenged in litigation or in administrative proceedings such as *ex parte* reexam, *inter partes* review, or post grant review in the United States or opposition proceedings in Europe or other jurisdictions.

There can be no assurance that:

- any of our existing patents will continue to be held valid, if challenged;
- patents will be issued for any of our pending applications;
- any claims allowed from existing or pending patents will have sufficient scope or strength to protect us;
- our patents will be issued in the primary countries where our products are sold in order to protect our rightsand potential commercial advantage; or
- any of our products or technologies will not infringe on the patents of other companies.

If we are enjoined from selling our products, or if we are required to develop new technologies or pay significant monetary damages or are required to make substantial royalty payments, our business and results of operations would be harmed.

Obtaining and maintaining a patent portfolio entails significant expense and resources. Part of the expense includes periodic maintenance fees, renewal fees, annuity fees, various other governmental fees on patents and/or applications due in several stages over the lifetime of patents and/or applications, as well as the cost associated with complying with numerous procedural provisions during the patent application process. We may or may not choose to pursue or maintain protection for particular inventions. In addition, there are situations in which failure to make certain payments or noncompliance with certain requirements in the patent process can result in abandonment or lapse of a patent or patent application, resulting in partial or complete loss of patent rights in the relevant jurisdiction. If we choose to forgo patent protection or allow a patent application or patent to lapse purposefully or inadvertently, our competitive position could suffer.

Legal actions to enforce our patent rights can be expensive and may involve the diversion of significant management time. In addition, these legal actions could be unsuccessful and could also result in the invalidation of our patents or a finding that they are unenforceable. We may or may not choose to pursue litigation or interferences against those that have infringed on our patents, or used them without authorization, due to the associated expense and time commitment of monitoring these activities. If we fail to protect or to enforce our intellectual property rights successfully, our competitive position could suffer, which could have a material adverse effect on our results of operations and business.

Claims by others that our products infringe their patents or other intellectual property rights could prevent us from manufacturing and selling some of our products or require us to pay royalties or incur substantial costs from litigation or development of non-infringing technology.

In recent years, there has been significant litigation in the United States involving patents and other intellectual property rights. We may receive notices that claim we have infringed upon the intellectual property of others. Even if these claims are not valid, they could subject us to significant costs. Any such claims, with or without merit, could be time-consuming to defend, result in costly litigation, divert our attention and resources, cause product shipment delays or require us to enter into royalty or licensing agreements. Such royalty or licensing agreements, if required, may not be available on terms acceptable to us or at all. We have engaged in litigation and litigation may be necessary in the future to enforce our intellectual property rights or to determine the validity and scope of the proprietary rights of others. Litigation may also be necessary to defend against claims of infringement or invalidity by others. A successful claim of intellectual property infringement against us and our failure or inability to license the infringed technology or develop or license technology with comparable functionality could have a material adverse effect on our business, financial condition and operating results.

Our TransTech vendor base is concentrated.

Evolis, Fargo, Ultra Electronics - Magicard Division and NiSCA, are major vendors of TransTech whose products account for approximately 73% of TransTech's revenue. TransTech buys, packages and distributes products from these vendors after issuing purchase orders. Any loss of any of these vendors would have a material adverse effect on our business, financial condition and results of operations.

We currently have a very small sales and marketing organization. If we are unable to secure a sales and marketing partner or establish satisfactory sales and marketing capabilities, we may not be able to successfully commercialize our ChromaID technology.

We currently have one full-time sales and business development manager for the ChromaID technology. This individual oversees sales of our products and IP licensing and manages critical customer and partner relationships. In addition, he manages and coordinates the business development resources at our strategic partners IDMC and Sumitomo Precision Products as they relate to our ChromaID technology. We also work with third party entities that are focused in specific market verticals where they have business relationships that can be leveraged. Our subsidiary, TransTech Systems, has six sales and marketing employees on staff to support the ongoing sales efforts of that business. In order to commercialize products that are approved for commercial sales, we sell directly to our customers, collaborate with third parties that have such commercial infrastructure and work with our strategic business partners to generate sales. If we are not successful entering into appropriate collaboration arrangements, or recruiting sales and marketing personnel or in building a sales and marketing infrastructure, we will have difficulty successfully commercializing our ChromaID technology, which would adversely affect our business, operating results and financial condition.

We may not be able to enter into collaboration agreements on terms acceptable to us or at all. In addition, even if we enter into such relationships, we may have limited or no control over the sales, marketing and distribution activities of these third parties. Our future revenues may depend heavily on the success of the efforts of these third parties. If we elect to establish a sales and marketing infrastructure we may not realize a positive return on this investment. In addition, we will have to compete with established and well-funded pharmaceutical and biotechnology companies to recruit, hire, train and retain sales and marketing personnel. Factors that may inhibit our efforts to commercialize ChromaID without strategic partners or licensees include:

- our inability to recruit and retain adequate numbers of effective sales and marketing personnel;
- the lack of complementary products to be offered by sales personnel, which may put us at a competitive disadvantage relative to companies with more extensive product lines; and
- unforeseen costs and expenses associated with creating an independent sales and marketing organization.

Government regulatory approval may be necessary before some of our products can be sold and there is no assurance such approval will be granted.

Although we do not need regulatory approval for our current applications, our ChromaID technology may have a number of potential applications in fields of use which will require prior governmental regulatory approval before the technology can be introduced to the marketplace. For example, we are exploring the use of our ChromaID technology for certain medical diagnostic applications. There is no assurance that we will be successful in developing medical applications for our ChromaID technology. If we were to be successful in developing medical applications of our technology, prior approval by the FDA and other governmental regulatory bodies may be required before the technology could be introduced into the marketplace. There is no assurance that such regulatory approval would be obtained for a medical diagnostic or other applications requiring such approval.

We may engage in acquisitions, mergers, strategic alliances, joint ventures and divestures that could result in final results that are different than expected

In the normal course of business, we engage in discussions relating to possible acquisitions, equity investments, mergers, strategic alliances, joint ventures and divestitures. Such transactions are accompanied by a number of risks, including the use of significant amounts of cash, potentially dilutive issuances of equity securities, incurrence of debt on potentially unfavorable terms as well as impairment expenses related to goodwill and amortization expenses related to other intangible assets, the possibility that we may pay too much cash or issue too many of our shares as the purchase price for an acquisition relative to the economic benefits that we ultimately derive from such acquisition, and various potential difficulties involved in integrating acquired businesses into our operations.

From time to time, we have also engaged in discussions with candidates regarding the potential acquisitions of our product lines, technologies and businesses. If a divestiture such as this does occur, we cannot be certain that our business, operating results and financial condition will not be materially and adversely affected. A successful divestiture depends on various factors, including our ability to effectively transfer liabilities, contracts, facilities and employees to any purchaser; identify and separate the intellectual property to be divested from the intellectual property that we wish to retain; reduce fixed costs previously associated with the divested assets or business; and collect the proceeds from any divestitures.

If we do not realize the expected benefits of any acquisition or divestiture transaction, our financial position, results of operations, cash flows and stock price could be negatively impacted.

Our growth strategy depends in part on our ability to execute successful strategic acquisitions. We have made strategic acquisitions in the past and may do so in the future, and if the acquired companies do not perform as expected, this could adversely affect our operating results, financial condition and existing business.

We may continue to expand our business through strategic acquisitions. The success of any acquisition will depend on, among other things:

- the availability of suitable candidates;
- higher than anticipated acquisition costs and expenses;
- competition from other companies for the purchase of available candidates;
- our ability to value those candidates accurately and negotiate favorable terms for those acquisitions;
- the availability of funds to finance acquisitions and obtaining any consents necessary under our credit facility;
- the ability to establish new informational, operational and financial systems to meet the needs of our business;
- the ability to achieve anticipated synergies, including with respect to complementary products or services; and
- the availability of management resources to oversee the integration and operation of the acquired businesses.

We may not be successful in effectively integrating acquired businesses and completing acquisitions in the future. We also may incur substantial expenses and devote significant management time and resources in seeking to complete acquisitions. Acquired businesses may fail to meet our performance expectations. If we do not achieve the anticipated benefits of an acquisition as rapidly as expected, or at all, investors or analysts may not perceive the same benefits of the acquisition as we do. If these risks materialize, our stock price could be materially adversely affected.

We are subject to corporate governance and internal control requirements, and our costs related to compliance with, or our failure to comply with existing and future requirements could adversely affect our business.

We must comply with corporate governance requirements under the Sarbanes-Oxley Act of 2002 and the Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010, as well as additional rules and regulations currently in place and that may be subsequently adopted by the SEC and the Public Company Accounting Oversight Board. These laws, rules, and regulations continue to evolve and may become increasingly stringent in the future. The financial cost of compliance with these laws, rules, and regulations is expected to remain substantial.

Our management has concluded that our disclosure controls and procedures were not effective due to the lack of an audit committee "financial expert." We expect to appoint an additional independent director to serve as Audit Committee Chairman. This director will be an "audit committee financial expert" as defined by the SEC. However, we cannot assure you that we will be able to fully comply with these laws, rules, and regulations that address corporate governance, internal control reporting, and similar matters in the future. Failure to comply with these laws, rules and regulations could materially adversely affect our reputation, financial condition, and the value of our securities.

The Capital Source credit facility contains covenants that may limit our flexibility in operating our business and failure to comply with any of these covenants could have a material adverse effect on our business.

In December 8, 2009, we entered into the Capital Source credit facility. These Capital Source credit facility contains covenants that limit our ability to engage in specified types of transactions. These covenants limit our ability to, among other things:

- sell, transfer, lease or dispose of certain assets;
- engage in certain mergers and consolidations;
- incur debt or encumber or permit liens on certain assets, except in the limited circumstances permitted under the loan and security agreements;
- make certain restricted payments, including paying dividends on, or repurchasing or making distributions with respect to, our common stock; and
- enter into certain transactions with affiliates.

A breach of any of the covenants under the Capital Source credit facility could result in a default under the Capital Source credit facility. Upon the occurrence of an event of default under the Capital Source credit facility, the lenders could elect to declare all amounts outstanding to be immediately due and payable and terminate all commitments to extend further credit. If we are unable to repay those amounts, the lenders could proceed against the collateral granted to them to secure such indebtedness.

The exercise prices of the IDMC warrant, Series A, B, C and D placement agent warrants and the Series B Redeemable Preferred Shares may require further adjustment.

In connection with the June 2013 Special Situations financing described below under "Liquidity and Capital Resources", we have outstanding Series A Warrants to purchase a total of 316,223 shares of common stock with a current exercise price of $2.50 per share, and Series B Warrants to purchase a total of 319.717 shares of common stock with a current exercise price of $2.50 per share, the IDMC warrant to purchase 97,169 shares of common stock with a current exercise price of $2.50 per share, Series C and D Warrants to purchase 23,334 shares of common stock with a current exercise price of $2.50 per share and placement agent warrants to purchase 28,554 shares of common stock at an exercise price of current exercise price of $2.50 per share (collectively, the "Special Situations Warrants"). The Special Situations Warrants contain an adjustment provision that would require an adjustment in the exercise price of the Special Situations Warrants if we issue common stock, warrants or equity below the price that is reflected in the Special Situations Warrants (currently $2.50 per share). If we issue any additional shares of common stock, warrants or other equity securities at a price below the exercise prices of the Special Situations Warrants, it would result in a reduction in the exercise price of the Special Situations Warrants. A downward adjustment in the exercise price of the Special Situations Warrants could also affect the market price of the common stock. The Series B Redeemable Preferred Stock convert into common shares at an assumed exercise price of $7.50 per share, subject to certain adjustments.

Risks Relating to Our Stock

The price of our common stock is volatile, which may cause investment losses for our stockholders

The market price of our common stock has been and is likely in the future to be volatile. Our common stock price may fluctuate in response to factors such as:

- Announcements by us regarding liquidity, significant acquisitions, equity investments and divestitures,strategic relationships, addition or loss of significant customers and contracts, capital expenditure commitments and litigation;
- Issuance of convertible or equity securities and related warrants for general or merger and acquisition purposes;
- Issuance or repayment of debt, accounts payable or convertible debt for general or merger and acquisitionpurposes;
- Sale of a significant number of shares of our common stock by stockholders;
- General market and economic conditions;
- Quarterly variations in our operating results;
- Investor and public relation activities;
- Announcements of technological innovations;
- New product introductions by us or our competitors;
- Competitive activities; and
- Additions or departures of key personnel.

These broad market and industry factors may have a material adverse effect on the market price of our common stock, regardless of our actual operating performance. These factors could have a material adverse effect on our business, financial condition and results of operations.

Transfers of our securities may be restricted by virtue of state securities "blue sky" laws, which prohibit trading absent compliance with individual state laws. These restrictions may make it difficult or impossible to sell shares in those states.

Transfers of our common stock may be restricted under the securities or securities regulations laws promulgated by various states and foreign jurisdictions, commonly referred to as "blue sky" laws. Absent compliance with such individual state laws, our common stock may not be traded in such jurisdictions. Because the securities held by many of our stockholders have not been registered for resale under the blue sky laws of any state, the holders of such shares and persons who desire to purchase them should be aware that there may be significant state blue sky law restrictions upon the ability of investors to sell the securities and of purchasers to purchase the securities. These restrictions may prohibit the secondary trading of our common stock. Investors should consider the secondary market for our securities to be a limited one.

The sale of a significant number of our shares of common stock could depress the price of our common stock.

Sales or issuances of a large number of shares of common stock in the public market or the perception that sales may occur could cause the market price of our common stock to decline. As of March 31, 2016, there were 1,259,644 shares of our common stock issued and outstanding, outstanding stock options grants for the purchase of 56,641 shares of common stock at an $18.19 average exercise price and outstanding warrants for the purchase of 830,326 shares of common stock at a $3.21 average exercise price. We may be obligated to issue up to 28,554 additional placement agent warrants at $2.50 per share related to the funding which closed June 14, 2013 which have the potential to add additional shares to the total number of shares of common stock issued and outstanding.

In addition, there are 23,334 shares of common stock reserved for issuance upon conversion of Series A Convertible Preferred stock and an unknown number of shares related to the conversion of notes payable.

There are an unknown number of shares of our common stock issuable upon the conversion of $975,000 of Convertible Notes Payable.

There are an unknown number shares of our common stock issuable upon the conversion of Series B Redeemable Preferred Stock at an assumed exercise price of $7.50 per share, subject to certain adjustments.

Significant shares of common stock are held by our principal stockholders, other company insiders and other large stockholders. As "affiliates" of Visualant, as defined under Securities and Exchange Commission Rule 144 under the Securities Act of 1933, our principal stockholders, other of our insiders and other large stockholders may only sell their shares of common stock in the public market pursuant to an effective registration statement or in compliance with Rule 144.

These options, warrants, convertible notes payable and convertible preferred stock could result in further dilution to common stock holders and may affect the market price of the common stock.

Future issuance of additional shares of common stock and/or preferred stock could dilute existing stockholders.We have and may issue preferred stock that could have rights that are preferential to the rights of common stock that could discourage potentially beneficially transactions to our common stockholders.

Pursuant to our certificate of incorporation, we currently have authorized 100,000,000 shares of common stock and 5,000,000 shares of preferred stock. To the extent that common shares are available for issuance, subject to compliance with applicable stock exchange listing rules, our board of directors has the ability to issue additional shares of common stock in the future for such consideration as the board of directors may consider sufficient. The issuance of any additional securities could, among other things, result in substantial dilution of the percentage ownership of our stockholders at the time of issuance, result in substantial dilution of our earnings per share and adversely affect the prevailing market price for our common stock.

An issuance of additional shares of preferred stock could result in a class of outstanding securities that would have preferences with respect to voting rights and dividends and in liquidation over our common stock and could, upon conversion or otherwise, have all of the rights of our common stock. Our Board of Directors' authority to issue preferred stock could discourage potential takeover attempts or could delay or prevent a change in control through merger, tender offer, proxy contest or otherwise by making these attempts more difficult or costly to achieve. The issuance of preferred stock could impair the voting, dividend and liquidation rights of common stockholders without their approval.

Future capital raises may dilute our existing stockholders' ownership and/or have other adverse effects on our operations.

If we raise additional capital by issuing equity securities, our existing stockholders' percentage ownership will be reduced and these stockholders may experience substantial dilution. We may also issue equity securities that provide for rights, preferences and privileges senior to those of our common stock. If we raise additional funds by issuing debt securities, these debt securities would have rights senior to those of our common stock and the terms of the debt securities issued could impose significant restrictions on our operations, including liens on our assets. If we raise additional funds through collaborations and licensing arrangements, we may be required to relinquish some rights to our technologies or candidate products, or to grant licenses on terms that are not favorable to us.

We do not anticipate paying any cash dividends on our capital stock in the foreseeable future.

We have never declared or paid cash dividends on our capital stock. We currently intend to retain all of our future earnings, if any, to finance the growth and development of our business, and we do not anticipate paying any cash dividends on our capital stock in the foreseeable future. In addition, the terms of any future debt agreements may preclude us from paying dividends. As a result, capital appreciation, if any, of our common stock will be your sole source of gain for the foreseeable future.

Anti-takeover provisions may limit the ability of another party to acquire our company, which could cause our stock price to decline.

Our certificate of incorporation, as amended, our bylaws and Nevada law contain provisions that could discourage, delay or prevent a third party from acquiring our company, even if doing so may be beneficial to our stockholders. In addition, these provisions could limit the price investors would be willing to pay in the future for shares of our common stock.

Our articles of incorporation allow for our board to create new series of preferred stock without further approval by our stockholders, which could adversely affect the rights of the holders of our common stock; our Series A Preferred Stock contains provisions that restrict our ability to take certain actions without the consent of at least 66% of the Series A Preferred Stock then outstanding.

Our Board of Directors has the authority to fix and determine the relative rights and preferences of preferred stock. Our Board of Directors also has the authority to issue preferred stock without further stockholder approval. As a result, our Board of Directors could authorize the issuance of a series of preferred stock that would grant to holders the preferred right to our assets upon liquidation, the right to receive dividend payments before dividends are distributed to the holders of common stock and the right to the redemption of the shares, together with a premium, prior to the redemption of our common stock. In addition, our Board of Directors could authorize the issuance of a series of preferred stock that has greater voting power than our common stock or that is convertible into our common stock, which could decrease the relative voting power of our common stock or result in dilution to our existing stockholders.

In addition, our articles of incorporation restrict our ability to take certain actions without the approval of at least 66% of the Series A Preferred Stock then outstanding. These actions include, among other things;

• authorizing, creating, designating, establishing or issuing an increased number of shares of Series A Preferred Stock or any other class or series of capital stock ranking senior to or on a parity with the Series A Preferred Stock;

• adopting a plan for the liquidation, dissolution or winding up the affairs of our company or any recapitalization plan (whether by merger, consolidation or otherwise);

• amending, altering or repealing, whether by merger, consolidation or otherwise, our articles of incorporation or bylaws in a manner that would adversely affect any right, preference, privilege or voting power of the Series A Preferred Stock; and

• declaring or paying any dividend (with certain exceptions) or directly or indirectly purchase, redeem, repurchase or otherwise acquire any shares of our capital stock, stock options or convertible securities (with certain exceptions).

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

During the three months ended March 31, 2016, we had the following issuances of unregistered sales of equity securities:

Seven investors converted warrants into 61,240 shares of common stock at $2.50 per share or $153,100.

On October 21, 2015, we entered into a Public Relations Agreement with Financial Genetics LLC for public relation services. On January 6, 2016 Financial Genetics was issued 9,196 shares of our common stock. We expensed $65,791 during the three months ended March 31, 2016.

On February 23, 2016, we entered into a Consulting Agreement with David Markowski for business development services. On February 29, 2016, Mr. Markowski was awarded 2,000 shares of our common stock. We expensed $14,600 during the three months ended March 31, 2016.

We issued convertible notes payable to investors totaling $315,000 to fund short-term working capital. These notes accrue interest at a rate of 8% per annum, become due during February 2017 and are convertible into common stock as part of our next public financing, at a conversion price equal to the price of the common stock sold in our next public financing. The investors received $315,000 in warrants that are exercisable into common stock at the price equal to the price of the common stock sold in our next public financing.

We entered into 8%-10% Convertible Promissory Notes and Securities Purchase Agreements with three accredited investors on February 4, 2016, totaling $165,000 with an original issue discount of $15,000 to fund short-term working capital. The Notes become due on February 3, 2017 and are convertible into common stock after six months from issuance. The Notes are convertible at 60% of the average of the lowest trading price in the 25 days prior to conversion but not less than $0.001 per share. We issued a total of 10,500 shares of restricted common stock to the investors valued at $70,875 and paid $7,500 in legal fees and recorded a total debt discount of $165,000 during the six months ended March 31, 2016. The Company received $128,500 net of all fees.

We entered into a Convertible Note Payable with Vis Vires Group, Inc. on February 18, 2016 for $100,000 to fund short-term working capital. The Vis Vires Note accrues interest at a rate of 8% per annum, becomes due on November 22, 2016 and is convertible into common stock beginning on August 19, 2016. The Vis Vires Note is convertible at 65% of the average of the lowest three-day trading price in the 10 days prior to conversion and includes a down round provision. The Company recorded a debt discount of $79,278 related to the conversion option derivative and a discount of $14,000 for issuance fees. We received $86,000 from the sale of the Vis Vires Not, net of all fees.

On March 8, 2016, we entered into a Stock Purchase Agreement with an institutional investor pursuant to which the Company issued 255 Shares of Series B Redeemable Preferred Shares ("Series B Preferred Shares") of the Company at $10,000.00 per share with a 5.0% original issue discount for the sum of $2,500,000.

At closing, the Company sold 51 Series B Preferred Shares in exchange for payment to the Company of $500,000 in cash and issued an additional 204 Series B Preferred Shares in exchange for delivery of a full recourse 1% Promissory Note ("Note") for $1,995,000 and payment to the Company of $5,000 in cash. The Note is collateralized by the Series B Preferred Shares. Under the terms of the Note, the Company is to receive an additional $500,000 for each $5 million, or in certain cases a lower amount, in aggregate trading volume of the common stock, so long as it meets certain other requirements. Any remaining balance under the Note is payable at its maturity in seven years.

The Series B Preferred Shares are convertible into common stock at $7.50 per share; provided that the investor may not convert any Series B Preferred Shares into common stock until that portion of the Note underlying the purchase of the converted portion of Series B Preferred Shares is paid in cash to Company.

ITEM 5. OTHER INFORMATION

This item is not applicable.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

The exhibits required to be filed herewith by Item 601 of Regulation S-K, as described in the following index of exhibits, are attached hereto unless otherwise indicated as being incorporated by reference, as follows:

(a) Exhibits

3.1	Correction to Amended and Restated Certificate of Designations, Preferences and Rights of its Series A Convertible Preferred Stock dated March 8, 2016 (incorporated by reference to the Company's Current Report on Form 8-K, filed March 15, 2016).

3.2	Amendment 2 of Series A Preferred Stock Terms dated February 19, 2016 (incorporated by reference to the Company's Current Report on Form 8-K, filed March 15, 2016).
3.3	Certificate of Designations of Preferences, Powers, Rights and Limitations of Series B Redeemable Convertible Preferred Stock dated March 8, 2016 (incorporated by reference to the Company's Current Report on Form 8-K, filed March 15, 2016).
10.1	Amendment 5 to Demand Promissory Note dated December 31, 2015 by and between Visualant, Incorporated and J3E2A2Z LP (incorporated by reference to the Company's Current Report on Form 8-K, filed January 4, 2016).
10.2	Amendment 6 to Demand Promissory Note dated December 31, 2015 by and between Visualant, Incorporated and J3E2A2Z LP (incorporated by reference to the Company's Current Report on Form 8-K, filed January 4, 2016).
10.3	Amendment 7 to Demand Promissory Note dated December 31, 2015 by and between Visualant, Incorporated and J3E2A2Z LP (incorporated by reference to the Company's Current Report on Form 8-K, filed January 4, 2016).
10.4	Stock Purchase Agreement dated March 8, 2016 by and between Visualant, Incorporated and an institutional investor (incorporated by reference to the Company's Current Report on Form 8-K, filed March 10, 2016).
31.1	Rule 13a-14(a)/15d-14(a) Certification of Principal Executive Officer. Attached herewith.
31.2	Rule 13a-14(a)/15d-14(a) Certification of Principal Financial Officer. Attached herewith.
32.1	Section 906 Certifications. Attached herewith.
32.2	Section 906 Certifications. Attached herewith.
101	Interactive data files pursuant to Rule 405 of Regulation S-T. (1)

Pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933 or Section 18 of the Securities Exchange Act of 1934 and otherwise are not subject to liability.

SIGNATURES

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

VISUALANT, INCORPORATED

(Registrant)

Date: May 5, 2016	By: /s/ Ronald P. Erickson Ronald P. Erickson Chief Executive Officer, President, and Director (Principal Executive Officer)
Date: May 5, 2016	By: /s/ Mark Scott Mark Scott Chief Financial Officer, Secretary and Treasurer (Principal Financial and Accounting Officer)

EXHIBIT 31.1

SECTION 302 CERTIFICATIONS

I, Ronald P. Erickson, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Visualant, Incorporated;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant’s other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant’s other certifying officer(a) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 5, 2016

/s/ Ronald P. Erickson
Ronald P. Erickson
Chief Executive Officer

EXHIBIT 31.2

SECTION 302 CERTIFICATIONS

I, Mark Scott, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Visualant, Incorporated;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(a) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 5, 2016

/s/ Mark Scott
Mark Scott
Chief Financial Officer

EXHIBIT 32.1

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Visualant, Incorporated (the "Company") on Form 10-Q for the quarter ended March 31, 2016 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Ronald P. Erickson, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to the best of my knowledge, that:

1.The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

2.The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company for the dates and periods covered by the Report.

This certificate is being made for the exclusive purpose of compliance by the Chief Executive and Financial and Accounting Officer of the Company with the requirements of Section 906 of the Sarbanes-Oxley Act of 2002, and may not be disclosed, distributed or used by any person or for any reason other than as specifically required by law.

/s/ Ronald P. Erickson
Ronald P. Erickson
Chief Executive Officer
May 5, 2016

EXHIBIT 32.2

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Visualant, Incorporated (the "Company") on Form 10-Q for the quarter ended March 31, 2016 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Mark Scott, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to the best of my knowledge, that:

1.The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

2.The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company for the dates and periods covered by the Report.

This certificate is being made for the exclusive purpose of compliance by the Chief Executive and Financial and Accounting Officer of the Company with the requirements of Section 906 of the Sarbanes-Oxley Act of 2002, and may not be disclosed, distributed or used by any person or for any reason other than as specifically required by law.

/s/ Mark Scott
Mark Scott
Chief Financial Officer
May 5, 2016