

ID SYSTEMS INC  
Form 10-K  
March 14, 2008

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

FORM 10-K

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934 for the fiscal year ended December 31, 2007.

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934 for the transition period from \_\_\_\_\_ to \_\_\_\_\_.

Commission File Number: **1-15087**

**I.D. SYSTEMS, INC.**

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of  
incorporation or organization)

**22-3270799**

(IRS Employer  
identification No.)

**One University Plaza, Hackensack, New Jersey**

(Address of principal executive offices)

**07601**

(Zip Code)

**(201) 996-9000**

(Registrant's telephone number, including area code)

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

Securities registered pursuant to Section 12(g) of the Act:

**Common Stock, par value \$0.01 per share**

(Title of class)

Indicate by checkmark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act of 1933. Yes  or No

Indicate by checkmark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

Yes  or No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  or No

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

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of “accelerated filer”, “large accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Securities Exchange Act of 1934.

Large accelerated filer  Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Securities Exchange Act of 1934). Yes  or No

The aggregate market value of the registrant’s common stock, par value \$0.01 per share (“Common Stock”), held by non-affiliates is \$133.4 million, computed by reference to the price at which the Common Stock was last sold on June 29, 2007, as reported on the Nasdaq National Market.

The number of shares of Common Stock outstanding as of March 3, 2008 was 10,855,000 shares.

#### **DOCUMENTS INCORPORATED BY REFERENCE**

|   |                   |
|---|-------------------|
| Document  | Part of Form 10-K |
| Proxy Statement For 2007 Annual Meeting of Stockholders | Part III          |

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## PART I.

In addition to historical information, this Annual Report on Form 10-K contains “forward-looking statements” (within the meaning of Section 27A of the Securities Act of 1933, as amended (the “Securities Act”), and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”)) that involve risks and uncertainties. See “Risk Factors - Cautionary Note Regarding Forward-Looking Statements.” I.D. Systems, Inc. has, or has applied for, trademark protection for I.D. Systems, Inc.®, Intelli-Listening®, MAC™, Vehicle Asset Communicator®, Battery ChaMP™, ChaMP™, Wireless Asset Net®, AvRamp™, Opti-Kan™, Line Asset Communicator™ and WiFree™.

### Item 1. Business

#### Overview

We develop, market and sell wireless solutions for managing and securing high-value enterprise assets. These assets include industrial vehicles, such as forklifts and airport ground support equipment, and rental vehicles. Our patented Wireless Asset Net system, which utilizes radio frequency identification, or RFID, technology, addresses the needs of organizations to control, track, monitor and analyze their assets. Our solutions enable customers to achieve tangible economic benefits by making timely, informed decisions that increase the security, productivity and efficiency of their operations.

We have focused our business activities on two primary applications - industrial fleet management and security, and rental fleet management. Our solution for industrial fleet management and security allows our customers to reduce operating costs and capital expenditures and to comply with certain safety regulations by accurately and reliably measuring and controlling fleet activity. This solution also enhances security at industrial facilities and areas of critical infrastructure, such as airports, by controlling access to, and restricting the use of, vehicles and equipment. Our solution for rental fleet management allows rental car companies to generate higher revenue by more accurately tracking vehicle data, such as fuel consumption and odometer readings, and improve customer service by expediting the rental and return processes. In addition to focusing on these core applications, we have adapted, and intend to continue to adapt, our solutions to meet our customers’ broader asset management needs.

We market and sell our solutions to a wide range of customers in the commercial and government sectors. Our customers operate in diverse markets, such as automotive manufacturing, heavy industry, retail and wholesale distribution, aerospace and defense, homeland security and vehicle rental. Based on revenues for 2007, our top customers are:

- U.S. Postal Service;
- Wal-Mart Stores, Inc.
- Ford Motor Company;

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We were incorporated in the State of Delaware in 1993.

### **Our Solution**

We design and implement solutions that focus primarily on the closed-loop asset management and security segment of the market for RFID and other wireless-based technologies. In this segment, RFID-based devices that provide on-board control, location tracking and data processing are integrated with enterprise assets to provide real-time visibility of, and two-way communications with, such assets. Our Wireless Asset Net system provides architectural and functional advantages that differentiate it from systems used for inventory and logistics tracking. For example, while inventory tracking systems rely on consistent radio frequency, or RF, connectivity to perform core functions, our system requires only periodic RF communications, and our on-asset devices perform their core functions autonomously. Unlike logistics tracking systems, which typically require substantial monthly expenditures for cellular or satellite communications, our system does not require customers to incur wireless communications costs and can track mobile assets indoors, where global positioning systems, or GPS, receivers typically do not work and cellular coverage can be sporadic.

Our Wireless Asset Net tracking and management system consists of three principal elements:

- miniature wireless programmable computers attached to assets;
- fixed-position communication infrastructure consisting of network computers with two-way RF capabilities, RF-based location-emitting beacons and application-specific network servers; and
- proprietary software, which is a user-friendly, Windows-based graphical user interface that utilizes client-server architecture and a database.

Each of these system elements processes and stores information independently to create a unique, patented system of “distributed intelligence,” which mitigates the risk that a single point of failure could compromise system integrity or data and asset security. Our on-asset hardware stores information locally so that it can autonomously and automatically control the asset and monitor asset activity regardless of the status or availability of other system components. Our on-asset hardware performs its functions even when outside the RF range of any other system component or if the facility computer network is unavailable. Our communication infrastructure independently processes data and executes programmable application logic, in addition to linking monitored mobile asset data automatically to our system’s database. Our server software populates the database and is designed to mitigate the effects of any computer outages that could affect real-time availability of the database. Finally, our client software interfaces only with the database, not directly with our communication infrastructure or on-asset hardware, which restricts access to, and limits corruption of, system information and minimizes network bandwidth usage.

We have focused our business activities on two primary applications - industrial fleet management and security and rental fleet management. In addition to focusing on these core applications, we have adapted, and intend to continue to adapt, our wireless solutions to meet our customers’ broader asset management needs.

### ***Industrial Fleet Management and Security***

Our solution for industrial fleet management and security allows fleet operators to reduce operating costs and capital expenditures, comply with certain safety regulations and enhance security.

To analyze and benchmark vehicle utilization and operator productivity, our system automatically records a wide range of activity and enables detailed performance comparisons to help management make informed decisions about vehicle and manpower allocations. This can lead to fleet and personnel reductions as well as increases in productivity from existing fleets. The system also provides real-time and historical visibility of vehicle movements.

To help reduce fleet maintenance costs, our system can automate and enforce preventative maintenance scheduling by:

- wirelessly uploading usage data from each vehicle;
- automatically prioritizing maintenance events based on weighted, user-defined variables;
- automatically sending reminders to individual vehicles or operators via the system's text messaging module;
- enabling remote lock-out of vehicles overdue for maintenance; and
- allowing maintenance personnel to locate and retrieve vehicles due for service via the system's graphical viewer software.

To help improve fleet safety and security, our system provides, among other things:

- compatibility with a variety of technologies that verify driver identity;
- wireless vehicle access control to ensure that only trained and authorized personnel use equipment as required by the Occupational Safety and Health Administration, or OSHA;
- electronic vehicle inspection checklists for paperless proof of OSHA compliance;
- automatic reporting of emerging vehicle safety issues;
- automatic on-vehicle intervention, such as alarms and the disabling of equipment, in response to user-definable safety and security parameters;
- remote vehicle deactivation capabilities, allowing a vehicle to be shut down manually or automatically under defined conditions;
- impact sensing to assign responsibility for abusive driving;
- geo-fencing to restrict vehicles from operating in prohibited areas or issue alerts upon unauthorized entry to such areas; and
- a graphical, icon-based view of vehicle safety/security/operational status on a facility map, filterable by a variety of conditions, both historically and in real time.

A specialized application of our solution in the industrial fleet management and security market is vehicle security, particularly at airports, seaports and other areas of critical infrastructure. The Transportation Security Act of 2001 mandates security for aircraft servicing equipment, including aircraft tow tractors, baggage tugs, cargo loaders, catering vehicles and fuel trucks.





### ***Rental Fleet Management***

Our solution for rental fleet management is designed both to enhance the consumer's rental experience and benefit the rental company by providing information that can be used to increase revenues, reduce costs and improve customer service. Our system automatically uploads vehicle identification number, mileage and fuel data as a vehicle enters and exits the rental lot, which can significantly expedite the rental and return processes for travelers and provide the rental company with more timely inventory status, more accurate billing data that can generate higher fuel-related revenue, and an opportunity to utilize customer service personnel for more productive activities, such as inspecting vehicles for damage and helping customers with luggage.

### **Growth Strategy**

Our objective is to become the leading global provider of wireless solutions for managing and securing enterprise assets. To achieve this goal, we intend to:

#### ***Increase sales to existing customers and pursue opportunities with new customers by:***

- maintaining a sales and marketing team that is focused on identifying, seizing and managing revenue opportunities, with the primary goal of expanding our customer base and achieving wider market penetration;
- utilizing a performance services team to (a) shorten our initial sales cycles by helping prospective customers identify and quantify benefits expected from our system, (b) accelerate transitions from initial implementation to roll-out programs by helping customers achieve and prove expected system benefits, and (c) build service revenue through long-term consultative engagements that help customers use our system to attain continuous improvements in their operations;
- utilizing a business development team to establish and manage value-added channel partners that provide (a) new sales, marketing, distribution and support networks, (b) opportunities for system integration and development of unique, integrated value propositions, and (c) software development opportunities to expand our product and application offerings;
- utilizing a strategic markets team to identify opportunities for and expand sales in key vertical markets—such as automotive, aviation, civilian government, defense, and rental cars—where our solutions can be effectively branded and marketed with specific functionality and subject matter expertise; and
- expanding our resources and activities internationally, especially in Europe, where re-packaging, promoting and supporting our products represents a large, untapped growth opportunity.

#### ***Expand into new applications and markets for our technology by:***

- pursuing opportunities to integrate our system with computer hardware and software vendors, including original equipment manufacturers;
- establishing relationships with global distributors to market and sell our system internationally; and
- pursuing acquisitions of companies that we believe will enhance the functionality and broaden the applicability of our solutions.

### **Products and Services**

We offer our customers integrated wireless solutions to control, monitor, track and analyze their enterprise assets. Our solutions are comprised of hardware and software, as well as maintenance, support and consulting services.

***Principal Products***

*On-Asset Hardware.* With a variety of mounting and user-interface options, our on-asset hardware is designed to be installed quickly and easily and provide an autonomous means of asset control and monitoring. Our on-asset hardware:

- contains an integrated computer, programmed with a product-specific application, and an advanced wireless transceiver with a communication range of up to one-half mile;
- controls equipment access with a variety of electronic interface options;

- is compatible with most existing facility access security systems;
- generates paperless electronic safety checklists via a built-in display and keypad;
- wirelessly and automatically uploads and downloads data to and from other system components;
- performs monitoring and control functions at all times, independent of RF or network connectivity; and
- incorporates a multi-voltage power supply designed to control electrical anomalies.

*Wireless Asset Managers.* Each of our Wireless Asset Net system deployments requires at least one fixed-position communication device, referred to as a Wireless Asset Manager, to link the mobile assets being monitored with the customer's computer network. Our Wireless Asset Managers conduct two-way RF communications with the assets being monitored and can communicate on either a local or wide area network. The Wireless Asset Managers solution offers flexible configuration options and scalability. A single Wireless Asset Manager is enough to operate an entire asset management system. For expanded, real-time data communication and location tracking, Wireless Asset Managers can be added incrementally as needed. They also allow system settings and on-asset functionality to be changed without physically interfacing with on-asset hardware, which can save significant time and money.

Each of our Wireless Asset Managers:

- incorporates an integrated computer, programmed with a product specific application, and an advanced wireless transceiver with a communication range of up to one-half mile;
- accommodates an unlimited number of on-asset hardware devices;
- automatically uploads and downloads data to and from other system components;
- employs built-in self-diagnostic capabilities; and
- is configurable to achieve a wide range of asset management goals.

*Server Software.* Each of our Wireless Asset Net system deployments requires at least one installation of our server software, which automatically manages data communications between the system's database and the Wireless Asset Managers. Our server software:

- is a set of Windows services;
- automatically processes data between our Wireless Asset Managers and system databases;
- actively polls Wireless Asset Managers to retrieve data on demand;
- passively listens to allow remote systems to initiate data communications for data download;
- automates event scheduling, including data downloads, database archiving and diagnostic notifications;
- interfaces with certain existing external systems, including maintenance and training systems;
- supports remote control/management of event processes;
- automatically performs diagnostics on system components; and
- automatically e-mails event alerts and customizable reports.

*Client Software .* Our client software, referred to as the Wireless Asset Net Console, provides an intuitive, easy-to-use, Windows-based interface. The console is deployed in a standard client-server network architecture or as a thin-client. The console interfaces only with the database, not directly with our communication infrastructure or on-asset hardware, which restricts access to, and limits corruption of, system information and minimizes network bandwidth usage. An unlimited number of consoles can be used on a network at any given time.

The Wireless Asset Net console:

- shows the location, status and inventory of vehicles - in real time and historically - in each area of a facility;
- allows real-time, two-way text communications, including broadcast text paging to all operators simultaneously;



- searches, sorts and analyzes assets by drive time, idle time, location, status, group, maintenance condition and other parameters;
- displays and prints predefined and ad hoc reports; and
- allows remote access by management, customers and vendors through the Internet.

***Additional Products***

*Battery ChaMP.* Our Battery Charger Monitoring Point, which we refer to as Battery ChaMP, tracks data on industrial battery fast-charge and battery swap systems. The Battery ChaMP provides automatic data uploads, real-time system visibility and data collection for electric vehicle batteries and chargers. The Battery ChaMP:

- tracks vehicle operator compliance with battery charging requirements;
- enforces critical equalization charging schedules;
- monitors data necessary for battery warranty compliance; and
- simplifies battery life management.

*Line Asset Communicator.* Our Line Asset Communicator is a wireless messaging device that triggers automatic, real-time task requests via radio frequency. Our Line Asset Communicator is designed to automatically forward requests to the material handling resource that:

- has been designated as capable of performing the work requested;
- is available for work at the moment of request; and

is physically closest to the site where the work must be performed.

The Line Asset Communicator is a key component of our OptiKan system, an optimized, wireless, electronic "kanban" system. "Kanban" refers to a method of signaling for parts replenishment on an assembly line, popularized by Japanese automobile manufacturers to achieve "just in time" production efficiencies. Our OptiKan system is designed to (i) eliminate dependence on line-of-sight parts replenishment calls, which can optimize material handling efficiency by reducing vehicle travel and eliminating unnecessary down time and (ii) provide a more dynamic, intelligent allocation of tasks to the material handling workforce that feeds the assembly line, which can both increase the timeliness and accuracy of parts replenishment and significantly reduce indirect labor costs.

### **Services**

*Maintenance Services* . We provide a warranty on all hardware and software components of our system. During the warranty period, we either replace or repair defective hardware. We also make extended maintenance contracts available to customers and offer ongoing maintenance and support on a time and materials basis. Pricing for our extended maintenance and support contracts is dependent upon the level of service we expect to provide. Our maintenance and support services typically include remote system monitoring, help desk technical support, escalation procedure development and routine diagnostic data analysis.

*Customer Support and Consulting Services* . We have developed a framework for the various phases of system training and support that offers our customers both structure and flexibility. Major training phases include hardware installation and troubleshooting, software installation and troubleshooting, train-the-trainer training on asset hardware operation, preliminary software user training, system administrator training, information technology issue training, ad hoc training during system launch and advanced software user training. These services are priced based on the extent of training that the customer requests.

Following system launch and advanced training, we make additional, refresher training available for a fee, either at the customer's site or at our offices. The customer may also elect to purchase additional training as part of a larger extended maintenance contract.

To help our customers derive the most benefit from our system, we supply a broad range of support documentation and provide initial post-launch data consulting. Our support documentation includes hardware user guides, software manuals, vehicle installation overviews, troubleshooting guides and issue escalation procedures. Our initial data consulting is intended to help the customer determine which reports and charts are most meaningful to different system users and which specific data may represent cost-saving or productivity-enhancing opportunities.

We have provided our consulting services on a limited basis, both as a stand-alone service to study the potential benefits of implementing a wireless fleet management system, and as part of the system implementation itself.

### **Sales and Marketing**

Our sales and marketing objective is to achieve broad market penetration, with an emphasis both on expanding business opportunities with existing customers and on securing new customers. As of March 3, 2008, we had 26 employees, including two based in Germany, devoted to sales and marketing.

We primarily market our systems directly to commercial and government organizations. To market to government organizations, we also pursue contract solicitations, capitalizing on tools such as our U.S. General Services Administration contract, which enables us to sell our products on an off-the-shelf basis to federal governmental agencies without further competitive bidding. To complement our direct sales activities, we recently began to sell through indirect sales channels, such as industrial equipment dealers. In addition, we are actively pursuing strategic relationships with key companies in our target markets — including original equipment manufacturers, complementary hardware and software vendors, and service providers — to further penetrate these markets by embedding our products in the assets our systems monitor and integrating our solutions with other systems.

We sell our systems to both executive and division-level management. Typically, our initial system deployment serves as a basis for potential expansion across the customer's organization. Ford, Walgreens, the U.S. Postal Service, Target and Wal-Mart Stores, Inc. are all examples of this progression.

- Ford initially implemented our system at one plant in 1999, which led to a blanket purchase order to deploy our system across its North American operations. As of December 31, 2007, we had deployed our system at 38 Ford facilities.
- Walgreens initially deployed our system at a single distribution center in 2003. As of December 31, 2007, we had deployed our system at 8 distribution centers.
- The U.S. Postal Service used the implementation of our system at one of its facilities to form the basis of a solicitation for competitive bids for a powered vehicle management system. Based on our proposal for that program, the U.S. Postal Service awarded us a national contract in 2004 to deploy our system at up to 460 U.S. Postal Service facilities nationwide. As of December 31, 2007, we had deployed our system at 80 facilities.
- Beginning in 2003, Target utilized our system on a limited number of vehicles at one of its facilities. As of December 31, 2007, we had deployed our system at 31 facilities.
- Wal-Mart initially deployed our system at a single distribution center in 2005. After testing our system, Wal-Mart deployed our system in 20 additional facilities.

We work closely with customers like these to help maximize the utilization and benefits of our system and demonstrate the value of enterprise-wide deployments.

## **Customers**

We market and sell our wireless solutions to a wide range of customers in the commercial and government sectors. Our customers operate in diverse markets, such as automotive manufacturing, heavy industry, retail and wholesale distribution, aerospace and defense, homeland security and vehicle rental. Customers that have implemented our system include:



|                                     |  |
|-------------------------------------|--|
| 3M Company                          | Nissan North America, Inc.                   |
| Advanced Technology Institute       | Northrop Grumman Corporation                 |
| AeroVironment, Inc.                 | Nucor Company                                |
| American Axle & Manufacturing, Inc. | Premier Manufacturing Support Services, Inc. |
| Archer Daniels Midland Company      | Rite Aid Corporation                         |
| Avis Rent A Car System, Inc.        | Target Corporation                           |
| Canadian Tire Corporation, Limited  | Toyota Motor Manufacturing Kentucky, Inc.    |
| DaimlerChrysler Corp.               | Tyler Pipe Company                           |
| Deere & Company                     | U.S. Department of Defense                   |
| FMC Technologies                    | U.S. Department of Homeland Security         |
| Ford Motor Company                  | U.S. Navy                                    |
| Kellogg Company                     | U.S. Postal Service                          |
| General Dynamics Corporation        | Walgreen Co.                                 |
| Golub Corporation                   | Wal-Mart Stores, Inc.                        |
| Longview Fibre Company              | Weyerhaeuser Company                         |
| Meijer, Inc.                        | WinCo Foods, Inc.                            |

During the year ended December 31, 2007, the U.S. Postal Service, Wal-Mart Stores, Inc. and Ford Motor Company accounted for 37%, 32% and 10% of our revenues, respectively. During the year ended December 31, 2006, the U.S. Postal Service and Wal-Mart Stores, Inc. accounted for 61% and 14% of our revenues, respectively. No other customer accounted for greater than 10% of our net revenues during these periods.

We strive to establish long-term relationships with our customers in order to maximize opportunities for new application development and increased sales. Our relationship with the U.S. Postal Service, summarized below, illustrates this effort.

- In 1995, under a U.S. Postal Service research and development contract, we finalized the development of our patented RFID-based asset tracking system and created a product called the FlexTag designed to track test packages through the U.S. mail distribution system.
- In 1997, we deployed the FlexTag test mail tracking system across several U.S. Postal Service facilities and, at the same time, began developing a related system for tracking and managing the industrial trucks that operate in those facilities.
- In 1998 and 1999, we deployed early versions of our Wireless Asset Net industrial vehicle management system at certain U.S. Postal Service facilities.
- In 2003, we introduced an upgraded version of the Wireless Asset Net system at a U.S. Postal Service facility in Buffalo, New York.
- In 2004, the U.S. Postal Service solicited bids for deployment of an enterprise-wide Powered Industrial Vehicle Management System (“PIVMS”), and subsequently awarded us a national contract to deploy our Wireless Asset Net technology as its PIVMS at up to 460 U.S. Postal Service facilities across the United States. As of December 31, 2007, we had implemented the PIVMS in 80 U.S. Postal Service facilities.

In 2006, the U.S. Postal Service awarded us a development contract to integrate automated material flow management and human resource planning capabilities into the PIVMS.

## **Competition**

The market for RFID solutions is rapidly evolving, highly competitive and fragmented. Our target markets are also subject to quickly changing product technologies, shifting customer needs, regulatory requirements and frequent introductions of new products and services. A significant number of companies have developed or are developing and marketing software and hardware for RFID-based and other wireless products that currently compete or will compete directly with our solutions. We compete with organizations varying in size, including many small, start-up companies as well as large, well capitalized organizations. While some of our competitors focus exclusively on providing RFID solutions, many are involved in RFID technology as an extension of a more expansive business strategy. Many of our larger competitors are able to dedicate extensive financial resources to the research and development and deployment of RFID solutions. As government and commercial entities expand the use of RFID technologies, we expect that competition will continue to increase within our target markets.

We distinguish ourselves from our competitors by focusing on two distinct applications - industrial fleet management and security, and rental fleet management. This focus has enabled us to direct product development efforts specifically suited for our target markets. Our on-asset device for industrial fleet management and security is designed to operate independently of other system components, allowing for continuous asset control and data gathering even when the vehicle is out of RF communication range. We believe that our proprietary technology as well as our experience in designing and developing products for our target markets distinguishes us within these markets.

In each of our markets, we encounter different competitors due to the competitive dynamics of each segment. In the industrial fleet management and security market, the wireless control, tracking and management of enterprise assets is relatively new. Although we are not aware of any current competitors that provide the precise capabilities of our systems, we are aware of competitors that offer subsets of our system capabilities or alternate approaches to the needs our products address. Those companies include both emerging companies with limited operating histories, such as ShockWatch, a division of Media Recovery Inc., and Access Control Group, and companies with longer operating histories, greater name recognition and/or significantly greater financial, technical and marketing resources than ours, such as Savi Technology, which was acquired by Lockheed Martin Company in June 2006, Symbol Technologies, which was acquired by Motorola, Inc. in January 2007, Intermec, Inc. and WhereNet Corp., which was acquired by Zebra Technologies Corporation in January 2007.

In the rental fleet management market, we compete primarily against handheld device companies that currently provide the solutions used by vehicle rental companies. Currently, our principal competitors in this market are handheld device providers, such as Motorola, and other RFID-focused companies, such as WhereNet. Although handheld device providers currently control the majority of the rental fleet market, we believe a shift to RFID represents a compelling opportunity for vehicle rental companies, given the potential for increased customer satisfaction and efficiency resulting from the use of an RFID system. Because of these potential benefits, we believe our focused RFID product development strategy, portfolio of intellectual property and proven system efficacy are key competitive advantages in this market.

## **Research and Development**

As of March 3, 2008, including our executive vice president of engineering, our research and development group was comprised of 17 full-time employees. These employees have expertise in areas such as software and hardware design, wireless communications and mechanical and electrical engineering.

We have focused our research and development efforts on the evolution of our Wireless Asset Net system as a “universal system” to promote more widespread use of our technology for a broader range of equipment, with easier installations, maintenance and support, and with fewer configuration concerns. Using our universal platform, we have adapted our technology to meet the needs of several emerging markets, including rental fleet management, airport vehicle security, industrial battery charging management and remote automated machine monitoring. As a result of what we believe to be the end-user benefits inherent in these developments, including the important security implications of our technology in the airport environment, we have received funding from our customers, including the U.S. Department of Homeland Security, for programs that required adaptations of our system.

In our effort to expand our product beyond North America, we achieved product compliance certification, including European Telecommunications Standard Institutes and European Conformity certification, for our primary product line. In addition, we have completed our conversion of those products to meet the requirements of the European Union’s Restriction of certain Hazardous Substances Directive (RoHS) and its Waste Electrical and Electronic Equipment (WEEE) regulations. These efforts included redesign of circuitry, replacement of components and materials, and new marking and documentation. This has permitted us to market and sell our integrated wireless solutions in the European Union.

Our current research and development efforts are focused on:

- enhancing productivity by continuing to add to the functionality and reduce the costs of our system;
- expanding our system to meet the needs of potential markets and to provide new solutions to our customers; and
- improving our core products by utilizing continuing advances in technology.

We spent \$2.8 million, \$2.6 million and \$1.6 million for research and development during years ended December 31, 2007, 2006 and 2005, respectively.

## **Intellectual Property**

### ***Patents***

We attempt to protect our technology and products through the pursuit of patent protection in the United States and certain foreign jurisdictions. We have built a portfolio of patents and patent applications relating to aspects of our technology and products. We have four U.S. patents and twenty-four pending U.S. patent applications. With the timely payment of all maintenance fees, our U.S. patent that covers our Wireless Asset Net system (U.S. Patent Number 5,682,142) expires on October 28, 2014, our U.S. patent that covers our rental car fleet management system (U.S. Patent Number 6,898,493) expires on April 6, 2020, our U.S. patent that covers our Wireless Asset Net system (U.S. Patent Number 7,165,040) expires on April 28, 2023), and our U.S. patent that covers our Wireless Asset Net system (U.S. Patent Number 7,171,381) expires on December 20, 2019.

U.S. Patent Number 5,682,142, entitled “Electronic Control System/Network,” is directed toward a network of programmable, location marking and processing, movable tag nodes and a fixed position tag node. The movable and fixed tag nodes communicate directly and are capable of location identification and logical control of environmental conditions without requiring a central processor.

U.S. Patent Number 6,898,493, entitled “Fully Automated Vehicle Rental System,” is directed toward an automated vehicle rental system. The system uses vehicle monitors mounted in each rental vehicle for keeping track of vehicle

data, such as mileage, fuel level and location of the vehicle. The system transmits the vehicle data to a central database for automatically completing the checkout of the vehicle.

U.S. Patent Number 7,165,040 and U.S. Patent Number 7,171,381, entitled “System and Method for Managing Remotely and Distantly Located Assets” and “System Architecture and Communications for an Asset Management System,” respectively, are directed toward protection for wireless, bi-directional communications between intelligent asset monitoring devices and central data processing nodes. The patented systems enable monitoring and control of remote assets in environments where wireless communication networks are overburdened or not reliable. We have foreign patents in China, South Korea, Australia and Mexico covering our Wireless Asset Net system. We also have patent applications for our Wireless Asset Net system pending in Japan and Canada and patent applications for our mobile RFID portal pending in Canada, China, Mexico, Europe and Australia. Because of the differences in patent laws and laws concerning proprietary rights, the extent of protection provided by U.S. patents or proprietary rights owned by us may differ from that of their foreign counterparts.

### ***Trademarks***

We have, or have applied for, trademark protection for I.D. Systems, Inc.®, Intelli-Listening®, MAC™, Vehicle Asset Communicator®, Battery ChaMP™, ChaMP™, Wireless Asset Net®, AvRamp™, Opti-Kan™, Line Asset Communicator™ and WiFree™.

We attempt to avoid infringing known proprietary rights of third parties in our product development and sales efforts. However, it is difficult to proceed with certainty in a rapidly evolving technological environment in which there may be numerous patent applications pending, many of which are confidential at the time of the application filing, with regard to similar technologies. If we were to discover that our products violate third-party proprietary rights, we may not be able to:

- obtain licenses to continue offering such products without substantial reengineering;
- reengineer our products successfully to avoid infringement;
- obtain licenses on commercially reasonable terms, if at all; or
- litigate an alleged infringement successfully or settle without substantial expense and damage awards.

Any claims against us relating to the infringement of third-party proprietary rights, even if without merit, could result in the expenditure of significant financial and managerial resources or in injunctions preventing us from distributing certain products. Such claims could materially adversely affect our business, financial condition and results of operations.

Our software products are susceptible to unauthorized copying and uses that may go undetected, and policing such unauthorized use is difficult. In general, our efforts to protect our intellectual property rights through patent, copyright, trademark and trade secret laws and contractual safeguards may not be effective to prevent misappropriation of the technology, or to prevent the development and design by others of products or technologies similar to or competitive with those developed by us. Our failure or inability to protect our proprietary rights could materially adversely affect our business, financial condition and results of operations.

## **Manufacturing**

We outsource our hardware manufacturing operations to leading contract manufacturers, such as Flextronics International Ltd. This strategy enables us to focus on our core competencies — designing hardware and software systems and delivering solutions to customers — and avoid investing in capital-intensive electronics manufacturing infrastructure. Outsourcing also provides us with the ability to ramp up deliveries to meet increases in demand without increasing fixed expenses.

Our manufacturers are responsible for obtaining the necessary components and supplies to manufacture our products. While components and supplies are generally available from a variety of sources, manufacturers generally depend on a limited number of suppliers. In the past, unexpected demand for communication products caused worldwide shortages of certain electronic parts and allocation of such parts by suppliers that had an adverse impact on the ability of manufacturers to deliver products as well as on the cost of producing such products.

Due to the general availability of manufacturers for our products, we do not believe that the loss of any of our manufacturers would have a long-term material adverse effect on our business, although there could be a short-term adverse effect on our business.

We generally attempt to maintain sufficient inventory to meet customer demand for products, as well as to meet anticipated sales levels. If our product mix changes in unanticipated ways, or if sales for particular products do not materialize as anticipated, we may have excess inventory or inventory that becomes obsolete. In such cases, our operating results could be negatively affected.

## **Government Regulations**

The use of radio emissions are subject to regulation in the United States by various federal agencies including the FCC and OSHA. Various state agencies also have promulgated regulations which concern the use of lasers and radio/electromagnetic emissions standards.

Regulatory changes in the United States and other countries in which we may operate in the future could require modifications to some of our products for us to continue manufacturing and marketing our products.

Our products intentionally transmit radio signals, including narrow band and spread spectrum signals, as part of their normal operation. We have obtained certification from the FCC for our products that require certification. Users of these products in the United States do not require any license from the FCC to use or operate our products. To market and sell our integrated wireless solutions in the European Union, we also utilize unlicensed radio spectra, and have obtained the required European Norm (EN) certifications.

In addition, some of our operations use substances regulated under various federal, state and local laws governing the environment and worker health and safety, including those governing the discharge of pollutants into the ground, air and water, the management and disposal of hazardous substances and wastes and the cleanup of contaminated sites. Certain of our products are subject to various federal, state and local laws governing chemical substances in electronic products.

The adoption of unfavorable regulations, or unfavorable interpretations of existing regulations by courts or regulatory bodies, could require us to incur significant compliance costs, cause the development of the affected markets to become impractical or otherwise adversely affect our ability to produce or market our products.

## Employees

As of March 3, 2008, we had 99 full-time employees, of which 33 are engaged in customer service, 17 in product development (which includes engineering), 9 in operations, 26 in sales and marketing, and 14 in finance and administration. None of our employees are represented by union or collective bargaining agreements. We believe that our relationships with our employees are good.

## Available Information

Our website is “www.id-systems.com.” We make available on this website free of charge, our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after we electronically file such material with, or furnish such information to, the Securities and Exchange Commission (“SEC”). We also make available on this website, free of charge, our Code of Ethics for Senior Financial Officers, which applies to our principal executive officer, principal financial officer and principal accounting officer.

## Item 1A. Risk Factors

**We have incurred significant losses and have a substantial accumulated deficit. If we cannot achieve profitability, the market price of our common stock could decline significantly.**

Although we generated net income of \$851,000 for the year ended December 31, 2005, we incurred net losses of approximately \$1.6 million and \$7.3 million for the years ended December 31, 2006, and 2007, respectively, and have incurred additional net losses since inception. At December 31, 2007, we had an accumulated deficit of approximately \$19.5 million. During 2007, our revenues decreased and our expenses increased, primarily as a result of an increase in payroll and related expenses due to the hiring of additional staff within our sales and customer service departments. Our ability to increase our revenues from the sale of our products will depend on our ability to successfully implement our growth strategy and the continued expansion of our markets. During 2007, the market price of our common stock declined significantly. If our revenues do not grow or if our operating expenses continue to increase, we may not be able to become profitable as we were in 2005 and the market price of our common stock could decline further.

**We are highly dependent upon sales of our Wireless Asset Net system to a few customers. The loss of any of these customers, or any material reduction in the amount of our products they purchase, could materially and adversely affect our financial condition and results of operations.**

During the year ended December 31, 2007, the U.S. Postal Service, Wal-Mart Stores, Inc. and Ford Motor Company accounted for 37%, 32% and 10% of our revenues, respectively. During the year ended December 31, 2006, the U.S. Postal Service and Wal-Mart Stores, Inc. accounted for 61% and 14% of our revenues, respectively. Some of these and other customers operate in markets that have suffered business downturns in the past few years or may so suffer in the future. The loss of or any material reduction in the amount of our products that these customers purchase, or any material adverse change in the financial condition of such customers, could materially and adversely affect our financial condition and results of operations. If we are unable to replace such revenue from existing or new customers, the market price of our common stock could decline significantly.



**If the market for our technology does not develop or become sustainable, expands more slowly than we expect or becomes saturated, our revenues will continue to decline and our financial condition and results of operations could be materially and adversely affected.**

Our success is highly dependent on the continued market acceptance of our Wireless Asset Net system. The market for our wireless products and services is new and rapidly evolving. During the fiscal year ended December 31, 2007, our revenues declined by 30.9% from the prior year. If the market for our products and services does not redevelop or become sustainable, or becomes saturated with competing products or services, our revenues will continue to decline and our financial condition and results of operations could be materially and adversely affected.

**If we are unable to keep up with rapid technological change, we may be unable to meet the needs of our customers, which could materially and adversely affect our financial condition and results of operations and reduce our ability to grow our market share.**

Our market is characterized by rapid technological change and frequent new product announcements. Significant technological changes could render our existing technology obsolete. We are active in the research and development of new products and technologies and in enhancing our current products. However, research and development in our industry is complex and filled with uncertainty. For example, it is common for research and development projects to encounter delays due to unforeseen problems, resulting in low initial volume production, fewer product features than originally considered desirable and higher production costs than initially budgeted, any of which may result in lost market opportunities. In addition, these new products may not adequately meet the requirements of the marketplace and may not achieve any significant degree of market acceptance. If our efforts do not lead to the successful development, marketing and release of new products that respond to technological developments or changing customer needs and preferences, our revenues and market share could be materially and adversely affected. We may expend a significant amount of resources in unsuccessful research and development efforts. In addition, new products or enhancements by our competitors may cause customers to defer or forego purchases of our products. Any of the foregoing could materially and adversely affect our financial condition and results of operations and reduce our ability to grow our market share.

**If we are unable to effectively manage our growth, our business may become inefficient and we may not be able to effectively compete, increase our revenues or control our expenses.**

We have grown our business rapidly over the past few years. Between the fiscal years ended December 31, 2001 and 2006, our revenues increased at a compounded annual growth rate of 93%, and between fiscal years ended December 31, 2006 and 2007, our revenues decreased by 30.9%. During 2007, we increased our operating expenses to expand our sales and marketing capabilities and broadened our customer support capabilities and fund greater levels of research and development. Our rapid growth from 2001 to 2006 has placed, and is expected to continue to place, a significant strain on our managerial, technical, operational and financial resources. To manage our growth, we will have to:

- retain existing personnel;
- hire, train, manage and retain additional qualified personnel, including sales and marketing and research and development personnel;
- implement additional operational controls, reporting and financial systems and procedures; and
- effectively manage and expand our relationships with customers, subcontractors and other third parties responsible for manufacturing and delivering our products.



**The long and variable sales cycles for our solutions may cause our revenues and operating results to vary significantly from quarter to quarter, which could adversely affect the market price of our common stock.**

We expect that customers who utilize our solutions will do so as part of a large-scale deployment of these solutions across multiple or all divisions of their organizations. A customer's decision to deploy our solutions throughout its organization will involve a significant commitment of its resources. Accordingly, initial implementations may precede any decision to deploy our solutions enterprise-wide. Throughout this sales cycle, we may spend considerable time and expense educating and providing information to prospective customers about the benefits of our solutions.

The timing of the deployment of our solutions may vary widely and will depend on the specific deployment plan of each customer, the complexity of the customer's organization and the difficulty of such deployment. Customers with substantial or complex organizations may deploy our solutions in large increments on a periodic basis. Accordingly, we may receive purchase orders for significant dollar amounts on an irregular and unpredictable basis. Because of our limited operating history and the nature of our business, we cannot predict the timing or size of these sales and deployment cycles. Long sales cycles, as well as our expectation that customers will tend to place large orders sporadically with short lead times, may cause our revenue and results of operations to vary significantly and unexpectedly from quarter to quarter. These variations could materially and adversely affect the market price of our common stock.

**If we are unable to protect our intellectual property rights, our financial condition and results of operations could be materially and adversely affected.**

We rely on a combination of patents, copyrights, trademarks, trade secrets and contractual measures to protect our intellectual property rights. Third parties may seek to challenge, invalidate, circumvent or render unenforceable any patents or proprietary rights owned by us. If such challenges are successful, our business will be materially and adversely affected.

Our employees, consultants and advisors enter into confidentiality agreements with us that prohibit the disclosure or use of our confidential information. We also have entered into confidentiality agreements to protect our confidential information delivered to third parties for research and other purposes. Despite these efforts, we cannot assure you that we will be able to effectively enforce these agreements or our confidential information will not be disclosed, that others will not independently develop substantially equivalent confidential information and techniques or otherwise gain access to our confidential information or that we can meaningfully protect our confidential information.

Disputes may arise in the future with respect to the ownership of rights to any technology developed with advisors or collaborators. These and other possible disagreements could lead to delays in the collaborative research, development or commercialization of our systems, or could require or result in costly and time-consuming litigation that may not be decided in our favor. Any such event could materially and adversely affect our financial condition and results of operations.

Policing the unauthorized use of our intellectual property is difficult, and we cannot assure you that the steps we have taken will prevent unauthorized use of our technology or other intellectual property, particularly in foreign countries where the laws may not protect our proprietary rights as fully as in the United States. Accordingly, we may not be able to protect our proprietary rights against unauthorized third party copying or use. If we are unsuccessful in protecting our intellectual property, we may lose any technological advantages we have over competitors and our financial condition and results of operations could be materially and adversely affected.

**We may become involved in an intellectual property dispute that could subject us to significant liability, divert the time and attention of our management and prevent us from selling our products, any of which could materially and adversely affect our financial condition and results of operations.**

In recent years, there has been significant litigation in the United States and internationally involving claims of alleged infringement of patents and other intellectual property rights. Litigation may be necessary to enforce our intellectual property rights, defend ourselves against alleged infringement and determine the scope and validity of our intellectual property rights.

Any such litigation, whether or not successful, could result in substantial costs, divert the time and attention of our management and prevent us from selling our products. If a claim of patent infringement was decided against us, we could be required to:

- pay substantial damages to the party making such claim;
- stop selling, making, having made or using products or services that incorporate the challenged intellectual property;
- obtain from the holder of the infringed intellectual property right a license to sell, make or use the relevant technology, which license may not be available on commercially reasonable terms, or at all; or
- redesign those products or services that incorporate such intellectual property.

The failure to obtain the necessary licenses or other rights could preclude the sale, manufacture or distribution of our products and could materially and adversely affect our financial condition and results of operations.

**The U.S. government's right to use technology developed by us with government funds could limit our intellectual property rights.**

We have developed, and may in the future develop, improvements to our technology that are funded in part by the U.S. government. As a result, we do not have the right to prohibit the U.S. government from using certain technologies developed by us with such government funds or to prohibit third parties from using those technologies to provide products and services at the request of the U.S. government. Although such government rights do not affect our ownership of the technology developed using such funds, the U.S. government has the right to royalty-free use of technologies that we have developed under such contracts. We are free to commercially exploit those government funded technologies and may assert our intellectual property rights to seek to block other non-government users thereof, but we cannot assure you that we can successfully do so.

**We rely on subcontractors to manufacture and deliver our products. Any quality or performance failures by our subcontractors or changes in their financial condition could disrupt our ability to supply quality products to our customers in a timely manner, resulting in business interruptions, increased costs, claims for damages, reputation damage and reduced revenue.**

In order to meet the requirements under our contracts, we rely on subcontractors to manufacture and deliver our products to our customers. For example, during the year ended December 31, 2007, we relied on Flextronics International Ltd. for the purchase of approximately 47% of our components and finished goods. Any quality or performance failures by our subcontractors or changes in their financial or business condition could disrupt our ability to supply quality products to our customers in a timely manner. If we are unable to fulfill orders from our customers in a timely manner, we could experience business interruption, increased costs, damage to our reputation and loss of our customers. In addition, we may be subject to claims from our customers for failing to meet our contractual obligations. Although we have several sources for production, the inability to provide our products to our customers in a timely manner could result in the loss of customers and our revenues could be materially reduced. In addition, there is great competition for the most qualified and competent subcontractors. If we are unable to hire qualified subcontractors, the quality of our services and products could decline. Furthermore, third-party manufacturers in the electronic component industry are consolidating. The consolidation of third-party manufacturers may give remaining manufacturers greater leverage to increase the prices that they charge, thereby increasing our manufacturing costs. If we are unable to pass the increased costs onto our customers, our profitability could be materially and adversely affected.

**We rely on a limited number of suppliers for several significant components and raw materials in our products. If we are unable to obtain these components or raw materials on a timely basis, we will be unable to meet our customers' orders, which could reduce our revenues, subject us to claims for damages and adversely affect our relationships with our customers.**

We rely on a limited number of suppliers for the components and raw materials used in our products, including Flextronics. Although there are many suppliers for most of our component parts and raw materials, we are dependent on a limited number of suppliers for many of our significant components and raw materials. This reliance involves a number of significant risks, including:

- unavailability of materials and interruptions in delivery of components and raw materials from our suppliers, which could result in manufacturing delays; and
- fluctuations in the quality and price of components and raw materials.

We currently do not have any long-term or exclusive purchase commitments with any of our suppliers. In addition, our suppliers may enter into exclusive arrangements with our competitors, be acquired by our competitors, stop selling their products or components to us at commercially reasonable terms or at all. We may not be able to develop alternative sources for the components and raw materials. Even if alternate suppliers are available to us, identifying them is often difficult and time consuming. If we are unable to obtain ample supply of product or raw materials from our existing suppliers or alternative sources of supply, we may be unable to satisfy our customers' orders, which could reduce our revenues, subject us to claims for damages and adversely affect our relationships with our customers.

**If we lose our executive officers, or are unable to recruit additional personnel, our ability to manage our business could be materially and adversely affected.**

We are dependent on the continued employment and performance of our executive officers, particularly Jeffrey M. Jagid, Chief Executive Officer, Kenneth S. Ehrman, Chief Operating Officer, Ned Mavrommatis, Chief Financial Officer, Michael Ehrman, Executive Vice President Engineering, and Peter Fausel, Executive Vice President Sales, Marketing and Customer Service. We currently do not have employment agreements with any of our executive

officers. Like other companies in our industry, we face intense competition for qualified personnel. Many of our competitors have greater resources than we have to hire qualified personnel. Accordingly, if we are not successful in attracting or retaining qualified personnel in the future, our ability to manage our business could be materially and adversely affected.

**The industry in which we operate is highly competitive, and competitive pressures from existing and new companies could have a material adverse effect on our financial condition and results of operations.**

The industry in which we operate is highly competitive and influenced by the following:

- advances in technology;
- new product introductions;
- evolving industry standards;
- product improvements;
- rapidly changing customer needs;
- intellectual property invention and protection;
- marketing and distribution capabilities;
- ability to attract highly skilled professionals;
- competition from highly capitalized companies;
- entrance of new competitors;
- ability of customers to invest in information technology; and
- price competition.

The products marketed by us and our competitors are becoming more complex. As the technological and functional capabilities of future products increase, these products may begin to compete with products being offered by traditional computer, network and communications industry participants that have substantially greater financial, technical, marketing and manufacturing resources than we do.

Although we are not aware of any current competitors that provide the precise capabilities of our systems, we are aware of competitors that offer subsets of our system capabilities or alternate approaches to the needs our products address. Those companies include both emerging companies with limited operating histories, such as ShockWatch, a division of Media Recovery, Inc., and Access Control Group L.L.C., and companies with longer operating histories, greater name recognition and/or significantly greater financial, technical and marketing resources than ours, such as Savi Technology, Inc., which was acquired by Lockheed Martin Company in June 2006, Symbol Technologies, Inc., which was acquired by Motorola, Inc. in January 2007, Intermec, Inc. and WhereNet Corp, which was acquired by Zebra Technologies Corporation in January 2007.

If we do not keep pace with product and technology advances, including the development of superior products by our competitors, or if we are unable to otherwise compete successfully against our competitors, there could be a material adverse effect on our competitive position, revenues and prospects for growth. As a result, our financial condition and results of operations could be materially and adversely affected.

**The federal government or independent standards organizations may implement significant regulations or standards that could adversely affect our ability to produce or market our products.**

Our products transmit radio frequency waves, the transmission of which is governed by the rules and regulations of the Federal Communications Commission, or FCC, as well as other federal and state agencies. Our ability to design, develop and sell our products will continue to be subject to these rules and regulations for the foreseeable future. In addition, our products and services may become subject to independent industry standards. The implementation of unfavorable regulations or industry standards, or unfavorable interpretations of existing regulations by courts or regulatory bodies, could require us to incur significant compliance costs, cause the development of the affected products to become impractical or otherwise adversely affect our ability to produce or market our products. The adoption of new industry standards applicable to our products may require us to engage in rapid product development efforts that would cause us to incur higher expenses than we anticipated. In some circumstances, we may not be able to comply with such standards, which could materially and adversely affect our ability to generate revenues through the sale of our products.

**Because our products are complex, they may have undetected errors or failures when they are introduced that could seriously harm our business.**

Technical products like ours often contain undetected errors or failures when first introduced. Despite our efforts to eliminate these flaws, there still may be flaws in our products, even after the commencement of commercial shipments. Because our products are used in business-critical applications, we could be subject to product liability claims if our systems fail to perform as intended. Even unsuccessful claims against us could result in costly litigation and the diversion of management's time and resources and could damage our reputation and impair the marketability of our systems. Although we maintain insurance, we cannot assure you that:

- our insurance will provide adequate coverage against potential liabilities if our products cause harm or fail to perform as promised; or
- adequate product liability insurance will continue to be available to us in the future on commercially reasonable terms or at all.

If our insurance is insufficient to pay any product liability claim, our financial condition and results from operations could be materially and adversely affected. In addition, any such claims could permanently injure our reputation.

**We may need to obtain additional capital to fund our operations that could have negative consequences on our business.**

We may require additional capital in the future to develop and commercialize additional products and technologies or take advantage of other opportunities that may arise, including potential acquisitions. We may seek to raise the necessary funds through public or private equity offerings, debt financings or strategic alliances and licensing arrangements. To the extent we raise additional capital by issuing equity securities, our existing stockholders may experience substantial dilution. If additional capital is raised through debt, such debt may subject us to significant restrictive covenants that could affect our ability to operate our business. In addition, we may be required to relinquish rights to our technologies or systems, or grant licenses on terms that are not favorable to us in order to raise additional funds through alliance, joint venture and licensing arrangements. If adequate funds are not available, we may be required to delay, reduce the scope of or eliminate one or more of our development programs, and our business, financial condition, results of operations and stock price could be materially and adversely affected.



**If we do not adequately anticipate and respond to the risks inherent in growing our business internationally, our operating results and the market price of our common stock could be materially and adversely affected.**

We have not generated significant revenues outside of North America. As part of our growth strategy, we are seeking ways to expand our operations outside of North America by establishing offices overseas and developing relationships with global distributors to market and sell our systems internationally. For example, as of December 31, 2007, we have hired two salespersons in Germany to market and sell our systems in Europe. There are a number of risks inherent in doing business in such markets, including:

- unexpected legal or regulatory changes;
- unfavorable political or economic factors;
- less developed infrastructure;
- difficulties in recruiting and retaining personnel, and managing international operations;
- fluctuations in foreign currency exchange rates;
- lack of sufficient protection for intellectual property rights; and
- potentially adverse tax consequences.

Until recently, we had no operations outside of North America, and we have limited experience establishing or operating businesses outside of North America. If we do not adequately anticipate and respond to the risks inherent in international operations, our operating results and the market price of our common stock could be materially and adversely affected. In addition, although we intend to expand our business outside of North America, there are risks associated with conducting an international operation, including the risks listed above, and such expansion may not be successful or have a positive effect on our financial condition and results of operations.

**We have never made any acquisitions of any businesses and cannot assure you that we will be able to successfully integrate any businesses, products, technologies or personnel that we might acquire in the future.**

We may, from time to time, consider investments in complementary companies, products or technologies. In the event of any future acquisitions, we could:

- issue stock that would dilute our current stockholders' percentage ownership;
- incur debt;
- assume liabilities;
- incur expenses related to the impairment of goodwill; or
- incur large and immediate write-offs.

Our operation of any acquired business will also involve numerous risks, including:

- problems combining the acquired operations, technologies or products;
- unanticipated costs;
- diversion of management's time and attention from our core business;
- adverse effects on existing business relationships with suppliers and customers;
- risks associated with entering markets in which we have no or limited prior experience; and
- potential loss of key employees, particularly those of acquired companies.

We have never made any acquisitions of any businesses and cannot assure you that we will be able to successfully integrate any businesses, products, technologies or personnel that we might acquire in the future. Any failure to do so could have a material adverse effect on our financial condition and results of operations.

**The concentration of common stock ownership among our executive officers and directors could limit your ability to influence the outcome of corporate transactions or other matters submitted for stockholder approval.**

As of March 3, 2008, our executive officers and directors beneficially owned, in the aggregate, 9.3% of our outstanding common stock, not including 1,619,508 shares of common stock that our executive officers and directors may acquire upon the exercise of outstanding options or if they otherwise acquire additional shares of common stock in the future. As a result, our officers and directors may have the ability to influence the outcome of all corporate actions requiring stockholder approval, irrespective of how our other stockholders may vote, including the following actions:

- the election of directors;
- adoption of stock option plans;
- the amendment of our organizational documents; and
- the approval of certain mergers and other significant corporate transactions, including a sale of substantially all of our assets.

**The unpredictability of our quarterly operating results could adversely affect the market price of our common stock.**

Our revenues and operating results may vary significantly from quarter to quarter due to a number of factors, many of which are outside of our control and any of which could adversely affect the market price of our common stock. The main factors that may affect us include the following:

- variations in the sales of our products to our significant customers;
- variations in the mix of products and services provided by us;
- the timing and completion of initial programs and larger or enterprise-wide purchases of our products by our customers;

- the length and variability of the sales cycle for our products;
- the timing and size of sales;
- changes in market and economic conditions, including fluctuations in demand for our products; and
- announcements of new products by our competitors.

As a result of these and other factors, revenues for any quarter are subject to significant variation that could adversely affect the market price for our common stock.

**Future sales of our common stock, including sales of our common stock acquired upon the exercise of outstanding options, may cause the market price of our common stock to decline.**

The market price of our common stock could decline as a result of sales by our existing stockholders of shares of common stock in the market, or sales of our common stock acquired upon the exercise of outstanding options, or the perception that these sales could occur. These sales also may make it more difficult for us to sell equity securities at a time and price that we deem appropriate.

We have 10,855,000 shares of common stock outstanding as of March 3, 2008, of which 9,849,000 shares are freely transferable without restriction and 1,006,000 shares are held by our officers and directors which are subject to the applicable volume, manner of sale, holding period and other limitations of Rule 144. In addition, as of March 3, 2008, options to purchase 2,794,000 shares of our common stock were issued and outstanding, of which 1,939,000 were vested. The remaining options will vest ratably over a five-year period measured from the date of grant. The weighted-average exercise price of the vested stock options is \$7.47. We also may issue additional shares of stock in connection with our business, including in connection with acquisitions, and may grant additional stock options to our employees, officers, directors and consultants under our stock option plans or warrants to third parties. If a significant portion of these shares were sold in the public market, the market value of our common stock could be adversely affected.

**A decline in the value of the auction rate securities included in our investments could materially adversely affect our liquidity and income.**

Our investments include auction rate securities, with estimated fair value of \$25 million at December 31, 2007. Auction rate securities are securities with short-term interest rate reset dates of generally less than ninety days but with contractual maturities that can be well in excess of ten years. At the end of each reset period, investors typically can sell at auction or continue to hold the securities. These securities are subject to fluctuations in fair value depending on the supply and demand at each auction. Our auction rate securities consist of interests in pools of student loan receivables issued by agencies established by counties, cities, states and other municipal entities. Liquidity for our auction rate securities typically is provided by an auction process that resets the applicable interest rate every 28 days.

In February 2008, our auction rate securities failed to sell at auction due to sell orders exceeding buy orders. Prior to the auction rate failures, we sold approximately \$5 million of auction rate securities in 2008. In 2008, the funds associated with our auction rate securities that have failed auction, may not be accessible until a successful auction occurs, a buyer is found outside of the auction process, the security is called or the underlying securities have matured. As a result of the recent instability in the market for auction rate securities, there may be a future decline in the value of our auction rate securities. A decline in the value of these securities that is not temporary could materially adversely affect our liquidity and income.

**Interest rate fluctuations may adversely affect our income and results of operations.**

As of December 31, 2007, we had cash, cash equivalents and marketable securities of \$65.0 million. In a declining interest rate environment, reinvestment typically occurs at less favorable market rates, negatively impacting future investment income. Accordingly, interest rate fluctuations may adversely affect our income and results of operations..

**Declines in general economic conditions could result in decreased demand for our products and services, which could adversely affect our business, financial condition and results of operations.**

Our results of operations are affected by the levels of business activities of our customers, which can be affected by economic conditions in the U.S. and globally. During periods of economic downturns, our customers may decrease their demand for wireless technology solutions, as well as the maintenance, support and consulting services we provide. As we enter 2008, it appears that the United States economy is beginning to experience a slowdown in growth. It is possible that this slowdown will have an effect on the wireless solutions industry in general and on demand for our products and services, but the magnitude of that impact is uncertain. Our future growth is dependent, in part, upon the demand for our products and services. Prolonged weakness in the economy may cause business enterprises to delay or cancel wireless solutions projects, reduce their overall wireless solutions budgets and/or reduce or cancel orders for our services. This, in turn, may lead to longer sales cycles, delays in purchase decisions, payment and collection issues, and may also result in price pressures, causing us to realize lower revenues and operating margins. Additionally, if our customers cancel or delay their wireless solutions initiatives, our business, financial condition and results of operations could be materially and adversely affected.

**Provisions of Delaware law or our charter documents could delay or prevent an acquisition of our company, even if the acquisition would be beneficial to our stockholders, and could make it more difficult for you to change management.**

Provisions of our certificate of incorporation and bylaws may discourage, delay or prevent a merger, acquisition or other change in control that stockholders may consider favorable, including transactions in which stockholders might otherwise receive a premium for their shares. This is because these provisions may prevent or frustrate attempts by stockholders to replace or remove our current management or members of our board of directors. These provisions, among other things:

- . permit our board of directors to issue, without further action by our stockholders, up to 5,000,000 shares of preferred stock, with any rights, preferences and privileges as they may designate, including the right to approve an acquisition or other change in control;
- . provide that special meetings of stockholders may be called only by (i) our board of directors pursuant to a resolution adopted by a majority of the entire board of directors, either upon motion of a director or upon written request by the holders of at least 50% of the voting power of all the shares of our capital stock entitled to vote in the election of directors, voting as a single class, or (ii) our Chairman of the Board or President; and

· require the affirmative vote of at least 75% of the voting power of all the shares of our capital stock entitled to vote in the election of directors, voting as a single class, to amend or repeal the provisions dealing with meetings of stockholders.

In addition, Section 203 of the Delaware General Corporation Law prohibits us from engaging in a business combination with any of our interested stockholders for three years after such stockholder became an interested stockholder unless certain specified conditions are met. As a result, these provisions and Delaware law could limit the price that investors are willing to pay in the future for shares of our common stock.

### **Cautionary Note Regarding Forward-Looking Statements.**

This Annual Report on Form 10-K may contain forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act.

Forward-looking statements include statements with respect to our beliefs, plans, objectives, goals, expectations, anticipations, assumptions, estimates, intentions, and future performance, and involve known and unknown risks, uncertainties and other factors, which may be beyond our control, and which may cause our actual results, performance or achievements to be materially different from future results, performance or achievements expressed or implied by such forward-looking statements.

All statements other than statements of historical fact are statements that could be forward-looking statements. You can identify these forward-looking statements through our use of words such as “may,” “will,” “can,” “anticipate,” “assume,” “should,” “indicate,” “would,” “believe,” “contemplate,” “expect,” “seek,” “estimate,” “continue,” “plan,” “point to,” “project,” “intend,” “target,” “potential,” and other similar words and expressions of the future. These forward-looking statements may not be realized due to a variety of factors, including, without limitation:

- future economic and business conditions;
- the loss of any of our key customers or reduction in the purchase of our products by any such customers;
- the failure of the market for our products to continue to develop;
- our inability to protect our intellectual property;
- our inability to manage our growth;
- the effects of competition from a wide variety of local, regional, national and other providers of wireless solutions;
- changes in laws and regulations, including tax and securities laws and regulations and interstate and regulations promulgated by the FCC;
- changes in accounting policies, rules and practices;
- changes in technology or products, which may be more difficult or costly, or less effective than anticipated; and
- the other factors listed under this Item 1A - “Risk Factors.”

All forward-looking statements are expressly qualified in their entirety by this cautionary notice. You are cautioned not to place undue reliance on any forward-looking statements, which speak only as of the date of this Annual Report on Form 10-K. We have no obligation, and expressly disclaim any obligation, to update, revise or correct any of the forward-looking statements, whether as a result of new information, future events or otherwise. We have expressed our expectations, beliefs and projections in good faith and we believe they have a reasonable basis. However, we cannot assure you that our expectations, beliefs or projections will result or be achieved or accomplished.

**Item 1B. Unresolved Staff Comments**

None.

**Item 2. Properties**

Our executive and administrative offices are located in Hackensack, New Jersey. In November 1999, we entered into a lease for this facility, covering approximately 22,500 square feet, that expires on March 31, 2010. The rent is currently \$34,825 per month. During 2003, we entered into an agreement to sublease to a third party 6,270 square feet through the end of the lease. The sublease provided for monthly payments of \$11,619, subject to adjustments for increases in real estate taxes and certain operating expenses. In July 2007, the Company released the sublessee from the sublease and reassumed the space.

In March 2007, we entered into a lease for office space located in Suwanee, Georgia for sales, marketing and customer service. The lease expired in September 2007 and was subsequently renewed until March 2008. The rent is currently \$1,120 per month.

In September 2007, we entered into a lease for warehouse space located in Clifton, New Jersey. The lease expires in September 2008 and the rent is currently \$800 per month.

We believe that our existing facilities are adequate for our existing needs.

**Item 3. Legal Proceedings**

As of March 3, 2008, we were not involved in any material litigation.

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

None.

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

(a) Market Information . Our common stock is quoted on the Nasdaq National Market under the symbol "IDSY." The following table sets forth, for the periods indicated, the high and low sales price for our common stock as reported on such quotation system.

| <b>Quarter Ending</b> |    | <b>High</b> |    | <b>Low</b> |
|-----------------------|----|-------------|----|------------|
| <b>2006</b>           |    |             |    |            |
| March 31, 2006        | \$ | 25.03       | \$ | 19.40      |
| June 30, 2006         |    | 25.84       |    | 16.21      |
| September 30, 2006    |    | 23.84       |    | 15.14      |
| December 31, 2006     |    | 23.59       |    | 18.00      |
| <b>2007</b>           |    |             |    |            |
| March 31, 2007        | \$ | 18.90       | \$ | 11.82      |
| June 30, 2007         |    | 14.85       |    | 11.13      |
| September 30, 2007    |    | 13.09       |    | 8.96       |
| December 31, 2007     |    | 14.75       |    | 11.89      |

Set forth below is a line-graph presentation comparing the cumulative shareholder return on our common stock on an indexed basis against the cumulative total returns of the Nasdaq Market Value Index and the Hemscott Industry Communication Equipment Group Index (consisting of 86 publicly traded communication equipment companies) ("Hemscott Group Index") for the period from January 1, 2002 through December 31, 2007.

| COMPANY/INDEX/MARKET    | 12/31/2002 | 12/31/2003 | 12/31/2004 | 12/30/2005 | 12/29/2006 | 12/31/2007 |
|-------------------------|------------|------------|------------|------------|------------|------------|
| I.D. Systems Inc        | 100.00     | 159.59     | 426.03     | 544.52     | 429.68     | 284.47     |
| Communication Equipment | 100.00     | 151.96     | 184.62     | 208.16     | 222.61     | 240.43     |
| NASDAQ Market Index     | 100.00     | 150.36     | 163.00     | 166.58     | 183.68     | 201.91     |

(b)  Holders  . As of March 3, 2008, there were 25 registered holders of our common stock.

(c)  Dividends . We have never paid a cash dividend on our common stock and do not expect to pay a cash dividend in the near future. We currently intend to retain future earnings, if any, to finance our operations and expand our business. Any future determination to pay cash dividends will be at the discretion of our board of directors and will depend upon our financial condition, operating results, capital requirements and any other factors our board of directors deems relevant. In addition, our agreements with our lenders may, from time to time, restrict our ability to pay dividends.

(d)  Sales of Unregistered Securities  .

None.

(e)  Purchases of Equity Securities by the Issuer .

The following table provides a month-to-month summary of our share repurchase activity during the three months ended December 31, 2007:

**Issuer Purchases of Equity Securities <sup>(1)</sup>**

| Period                   | Total number of<br>shares (or<br>unit)<br>purchased | Average price<br>paid per share (or<br>unit) | Total number of<br>shares (or units)<br>purchased as part of<br>publicly announced<br>plans or programs | Maximum number (or<br>approximate dollar<br>value) of shares (or<br>units) that may yet be<br>purchased under the<br>plans or programs |
|--------------------------|---|--|---|--|
| 10/1/07 through 10/31/07 | 31,616  | 12.62  | 31,616  | \$ 4,632,960   |
| 11/1/07 through 11/30/07 | 7,047   | 12.60  | 7,047   | \$ 4,544,194   |
| 12/1/07 through 12/31/07 | 10,000  | 12.75  | 10,000  | \$ 4,416,675   |
| <b>Total</b>             | 48,663  | 12.64  | 48,663  | \$ 4,416,675   |

(1) On May 3, 2007, we announced that our Board of Directors had authorized the repurchase of issued and outstanding shares of our common stock having an aggregate value of up to \$10,000,000 pursuant to a share repurchase program established under Rule 10b-18 of the Securities Exchange Act of 1934, as amended. The amount and timing of such repurchases are dependent upon the price and availability of shares, general market conditions and the availability of cash, as determined in the discretion of our management. The repurchases are funded from our working capital. Our share repurchase program does not have an expiration date, and we may discontinue or suspend the share repurchase program at any time. All of the repurchases set forth in this table were made under the share repurchase program in open market transactions. All shares of common stock repurchased under our share repurchase program are held as treasury stock.



**Item 6. Selected Financial Data**

The following table sets forth selected financial data for each of the five years ended December 31, 2007 derived from our audited financial statements. You should read the information in the table below together with the section of this Annual Report on Form 10-K entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations," which discusses the 2005, 2006 and 2007 fiscal year, and our financial statements and related notes and the other financial data included elsewhere in this Annual Report on Form 10-K.

|  | Year Ended December 31, |               |               |                |                |
|--|-------------------------|---------------|---------------|----------------|----------------|
|  | 2003                    | 2004          | 2005          | 2006           | 2007           |
| <b>Statement of Operations Data:</b>                 |                         |               |               |                |                |
| Revenues   | \$ 7,959,000            | \$ 13,741,000 | \$ 19,004,000 | \$ 24,740,000  | \$ 17,083,000  |
| Cost of revenues                                     | 4,075,000               | 6,509,000     | 9,708,000     | 13,701,000     | 8,929,000      |
| Gross profit   | 3,884,000               | 7,232,000     | 9,296,000     | 11,039,000     | 8,154,000      |
| Operating expenses:                                  |                         |               |               |                |                |
| Selling, general and administrative expenses         | 4,456,000               | 5,879,000     | 7,140,000     | 12,943,000     | 15,963,000     |
| Research and development expenses                    | 891,000                 | 1,234,000     | 1,625,000     | 2,639,000      | 2,849,000      |
| Income (loss) from operations                        | (1,463,000)             | (119,000)     | 531,000       | (4,543,000)    | (10,658,000)   |
| Interest income                                      | 269,000                 | 195,000       | 222,000       | 2,801,000      | 3,238,000      |
| Interest expense                                     | (59,000)                | (63,000)      | (53,000)      | (29,000)       | (10,000)       |
| Other income   | 54,000                  | 147,000       | 151,000       | 155,000        | 89,000         |
| Net income (loss)                                    | \$ (1,199,000)          | \$ 398,000    | \$ 851,000    | \$ (1,616,000) | \$ (7,341,000) |
| Net income (loss) per share - basic                  | \$ (0.17)               | \$ 0.05       | \$ 0.11       | \$ (0.15)      | \$ (0.66)      |
| Net income (loss) per share - diluted                | \$ (0.17)               | \$ 0.05       | \$ 0.09       | \$ (0.15)      | \$ (0.66)      |
| Weighted average common shares outstanding - basic   | 6,905,000               | 7,455,000     | 7,771,000     | 10,501,000     | 11,205,000     |
| Weighted average common shares outstanding - diluted | 6,905,000               | 8,783,000     | 9,332,000     | 10,501,000     | 11,205,000     |
| <b>Balance Sheet Data (at end of period):</b>        |                         |               |               |                |                |
| Cash and cash equivalents                            |                         | 3,179,000     | 8,440,000     | 2,138,000      | 9,644,000      |
| Marketable securities                                |                         | 3,339,000     | 3,195,000     | 5,463,000      | 60,716,000     |
| Total assets   |                         | 13,470,000    | 17,159,000    | 19,840,000     | 84,905,000     |
| Long-term debt                                       |                         | 836,000       | 648,000       | 449,000        | 240,000        |
|  |                         |               |               | 240,000        | 19,000         |

|                            |            |            |            |            |            |
|----------------------------|------------|------------|------------|------------|------------|
| Total stockholders' equity | 10,979,000 | 13,572,000 | 15,166,000 | 81,284,000 | 71,670,000 |
|----------------------------|------------|------------|------------|------------|------------|

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## Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operation

*The following discussion is intended to assist you in understanding our financial condition and results of operations and should be read in conjunction with the financial statements and related notes included elsewhere in this Annual Report on Form 10-K. Many of the amounts and percentages in this section have been rounded for convenience of presentation, but actual recorded amounts have been used in computations. Accordingly, some information may appear not to compute accurately.*

### Overview

We develop, market and sell wireless solutions for managing and securing high-value enterprise assets. These assets include industrial vehicles, such as forklifts and airport ground support equipment, and rental vehicles. Our patented Wireless Asset Net system, which utilizes RFID technology, addresses the needs of organizations to control, track, monitor and analyze their assets. Our solutions enable our customers to achieve tangible economic benefits by making timely, informed decisions that increase the security, productivity and efficiency of their operations.

We sell our system to both executive and division-level management. Typically, our initial system deployment serves as a basis for potential expansion across the customer's organization. Ford, Walgreens, the U.S. Postal Service, Target and Wal-Mart Stores, Inc. are all examples of this progression.

- Ford initially implemented our system at one plant in 1999, which led to a blanket purchase order to deploy our system across its North American operations. As of December 31, 2007, we had deployed our system at 38 Ford facilities.
- Walgreens initially deployed our system at a single distribution center in 2003. As of December 31, 2007, we had deployed our system at 8 distribution centers.
- The U.S. Postal Service used the implementation of our system at one of its facilities to form the basis of a solicitation for competitive bids for a powered vehicle management system. Based on our proposal for that program, the U.S. Postal Service awarded us a national contract in 2004 to deploy our system at up to 460 U.S. Postal Service facilities nationwide. As of December 31, 2007, we had deployed our system at 80 facilities.
- Beginning in 2003, Target utilized our system on a limited number of vehicles at one of its facilities. As of December 31, 2007, we had deployed our system at 31 facilities.
- Wal-Mart initially deployed our system at a single distribution center in 2005. After testing our system, Wal-Mart deployed our system in 20 additional facilities.

We work closely with customers like these to help maximize the utilization and benefits of our system and demonstrate the value of enterprise-wide deployments.

Although we generated net income of \$851,000 for the year ended December 31, 2005, we incurred net losses of approximately \$1.6 million and \$7.3 million for the years ended December 31, 2006 and 2007, respectively, and have incurred additional net losses since inception. At December 31, 2007, we had an accumulated deficit of approximately \$19.5 million. During 2007, our revenue decreased, and our expenses increased, primarily as a result of an increase in payroll and related expenses due to the hiring of additional staff within our sales and customer service departments.

During the year ended December 31, 2007, we generated revenues of \$17.1 million, the U.S. Postal Service, Wal-Mart Stores, Inc. and Ford Motor Company accounted for 37%, 32% and 10% of our revenues, respectively. During the

year ended December 31, 2006, we generated revenues of \$24.7 million, and the U.S. Postal Service and Wal-Mart Stores, Inc. accounted for 61% and 14% of our revenues, respectively.

Our ability to increase our revenues and generate net income will depend on a number of factors, including our ability to:

- increase sales of products and services to our existing customers;
- convert our initial programs into larger or enterprise-wide purchases by our customers;
- increase market acceptance and penetration of our products; and
- develop and commercialize new products and technologies.

### **Critical Accounting Policies And Estimates**

We have adopted various accounting policies that govern the application of accounting principles generally accepted in the United States in the preparation of our financial statements. Our significant accounting policies are described in Note B to our financial statements. Certain accounting policies involve significant judgments and assumptions by our management that can have a material impact on the carrying value of certain assets and liabilities. We consider such accounting policies to be our critical accounting policies. The judgments and assumptions used by our management in these critical accounting policies are based on historical experience and other factors that our management believes to be reasonable under the circumstances. Because of the nature of these judgments and assumptions, actual results could differ significantly from these judgments and estimates, which could have a material impact on the carrying values of our assets and liabilities and our results of operations. Our critical accounting policies are described below.

### ***Revenue Recognition***

We derive our revenues from: (i) sales of our Wireless Asset Net system, which includes training and technical support; (ii) post-contract maintenance and support agreements; and periodically (iii) leasing arrangements. Our system consists of on-asset hardware, communication infrastructure and software. Revenue is allocated to each element based upon vendor specific objective evidence (VSOE) of the fair value of the element. VSOE of the fair value is based upon the price charged when the element is sold separately. Revenue from the sale of our system is recognized as the element is earned based on the selling price of each element and when there are no undelivered elements that are essential to the functionality of the delivered elements. Our system is typically implemented by the customer or a third party and, as a result, revenues are recognized when title and risk of loss passes to the customer, which usually is upon delivery of the system, pervasive evidence of an arrangement exists, sales price is fixed and determinable, collectability is reasonably assured and contractual obligations have been satisfied. In some instances, we are also responsible for providing installation services. The additional installation services, which could be performed by third parties, are considered another element in a multi-element deliverable and revenue for installation services is recognized at the time the installation is provided. Revenues from training and technical support are recognized as such services are provided.

We also enter into post-contract maintenance and support agreements. Revenues are recognized over the service period and the cost of providing these services is expensed as incurred.

### ***Stock-Based Compensation***

Prior to our fiscal year ended December 31, 2006, we accounted for stock-based employee compensation under Accounting Principles Board, or APB, Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations, and had adopted the disclosure-only provisions of SFAS No. 123, "Accounting for Stock-Based Compensation" and SFAS No. 148, "Accounting for Stock-Based Compensation — Transition and Disclosure." In December 2004, the Financial Accounting Standards Board issued SFAS No. 123 (revised 2004), "Share-Based Payment," which replaced SFAS 123 and superseded APB Opinion No. 25. Under the provisions of SFAS 123R, companies are generally required to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. That cost is recognized over the period during which an employee is required to provide service in exchange for the award, usually the vesting period. SFAS 123R requires that compensation expense be recognized for the unvested portions of existing options granted prior to its effective date and the cost of options granted to employees after the effective date based on the fair value of the stock options at grant date. Commencing January 1, 2006, we adopted SFAS 123R, and have applied the modified prospective method such that periods prior to adoption have not been restated. Pursuant to SFAS No. 123(R), stock based compensation expense amounted to \$2,975,000 and \$3,288,000 for the fiscal years ended December 31, 2006 and 2007, respectively.

**Results of Operations**

The following table sets forth certain items related to our statement of operations as a percentage of revenues for the periods indicated and should be read in conjunction with our financial statements and the related notes included elsewhere in this Annual Report on Form 10-K. A detailed discussion of the material changes in our operating results is set forth below.

|   | <b>Year Ended December 31,</b> |               |                |
|---|--------------------------------|---------------|----------------|
|   | 2005                           | 2006          | 2007           |
| <b>Revenue:</b>                                     |                                |               |                |
| Product   | 78.4%                          | 65.5%         | <b>64.6%</b>   |
| Services  | 21.6                           | 34.5          | <b>35.4</b>    |
|   | 100.0                          | 100.0         | <b>100.0</b>   |
| <b>Cost of Revenues:</b>                            |                                |               |                |
| Product cost of revenue                             | 41.1                           | 33.3          | <b>34.3</b>    |
| Service cost of revenue                             | 10.0                           | 22.1          | <b>18.0</b>    |
| <b>Total Gross Profit</b>                           | <b>48.9</b>                    | <b>44.6</b>   | <b>47.7</b>    |
| <b>Selling, general and administrative expenses</b> | <b>37.6</b>                    | <b>52.3</b>   | <b>93.4</b>    |
| <b>Research and development expenses</b>            | <b>8.6</b>                     | <b>10.7</b>   | <b>16.7</b>    |
| <b>Income (loss) from operations</b>                | <b>2.8</b>                     | <b>(18.4)</b> | <b>(62.4)</b>  |
| <b>Interest income</b>                              | <b>1.2</b>                     | <b>11.3</b>   | <b>19.0</b>    |
| <b>Interest expense</b>                             | <b>(0.3)</b>                   | <b>(0.1)</b>  | <b>(0.1)</b>   |
| <b>Other income</b>                                 | <b>0.8</b>                     | <b>0.6</b>    | <b>0.5</b>     |
| <b>Net income (loss)</b>                            | <b>4.5%</b>                    | <b>(6.5)%</b> | <b>(43.0)%</b> |

***Year Ended December 31, 2007 Compared to the Year Ended December 31, 2006***

***REVENUES.*** Revenues decreased by \$7.7 million, or 30.9%, to \$17.1 in 2007 from \$24.7 million in 2006.

Revenues from product decreased by \$5.2 million, or 31.9%, to \$11.0 million in 2007 from \$16.2 million in the same period in 2006. The decrease in product revenue was primarily attributable to a decrease in product revenue from the United States Postal Service of approximately \$6.2 million, offset by an increase of product revenue from Wal-Mart Stores, Inc of approximately \$2.0 million, and a decrease in product revenue from other customers.

Revenues from service decreased \$2.5 million, or 29.2%, to \$6.0 million in 2007 from \$8.5 million in the same period in 2006. The decrease in revenues was primarily attributable to a decrease in service revenue from the United States Postal Service of approximately \$2.7 million, partially offset by an increase in service revenue from other customers.

***COST OF REVENUES.*** Cost of revenues decreased by \$4.8 million, or 34.8%, to \$8.9 million in 2007 from \$13.7 million in 2006. Gross profit was \$8.2 million in 2007 compared to \$11.0 million in 2006. As a percentage of revenues, gross profit increased to 47.7% in 2007 from 44.6% in 2006.

Cost of product decreased by \$2.4 million, or 28.8%, to \$5.9 million in 2007 from \$8.2 million in the same period in 2006. Gross profit from product revenue was \$5.2 million in 2007 compared to \$8.0 million in 2006. As a percentage of product revenues, gross profit decreased to 46.9% in 2007 from 49.2% in 2006. The decrease in gross profit is primarily attributable to an increase to the inventory reserve of \$417,000 in 2007. Excluding the impact of the increase in inventory reserve, gross profit was 51.6% in 2007.

Cost of service decreased by \$2.4 million, or 43.9%, to \$3.1 million in 2007 from \$5.5 million in the same period in 2006. Gross profit from service revenue was \$3.0 million in 2007 compared to \$3.1 million in 2006. As a percentage of service revenues, gross profit increased to 49.2% in 2007 from 35.9% in 2006. The increase was primarily attributable to the fact that a larger percentage of the service revenue in 2007 was from engineering services and maintenance, which typically have higher gross margins than revenue from implementation services.

***Selling, General and Administrative Expenses.*** Selling, general and administrative expenses increased \$3.0 million, or 23.3%, to \$16.0 million in 2007 compared to \$12.9 million in 2006. This increase was attributable primarily to (i) the increase in payroll of approximately \$2.2 million primarily resulting from the hiring of additional staff within our sales and customer service departments and (ii) an increase to the stock based employee compensation expense of \$439,000 in 2007. As a percentage of revenues, selling, general and administrative expenses increased to 93.4% in 2007 from 52.3% in 2006 due to the aforementioned increase to payroll and payroll related expenses as well as to a decrease in revenue.

***Research and Development Expenses.*** Research and development expenses increased \$210,000, or 8.0%, to \$2.8 million in 2007 from \$2.6 million in 2006. This increase was attributable primarily to the work performed relating to the development of European compliant products. As a percentage of revenues, research and development expenses increased to 16.7% in 2007 from 10.7% in 2006 due to the aforementioned increase to expenses as well as to a decrease in revenue.



**Interest Income.** Interest income increased \$437,000, or 15.6%, to \$3.2 million in 2007 from \$2.8 million in 2006. This increase was attributable primarily to the increase in cash and cash equivalents and investments resulting from the proceeds received in connection with the public offering completed by us in March 2006.

**Interest Expense.** Interest expense decreased \$19,000, or 65.5%, to \$10,000 in 2007 from \$29,000 in 2006. The decrease was attributable to a reduction in the principal amount of our outstanding debt in 2007.

**Other Income.** Other income decreased \$66,000, or 42.6%, to \$89,000 in 2007 from \$155,000 in the same period in 2006 and reflects rental income earned from a sublease arrangement. In July 2007, we released the sublessee from the sublease and reassumed the space.

**Net Income (Loss).** Net loss was \$7.3 million or \$(0.66) per basic and diluted share in the year ended December 31, 2007 as compared to net loss of \$1.6 million or \$(0.15) per basic and diluted share for the year ended December 31, 2006. The increase in net loss was due primarily to the reasons described above.

#### ***Year Ended December 31, 2006 Compared to the Year Ended December 31, 2005***

**REVENUES.** Revenues increased by \$5.7 million, or 30.2%, to \$24.7 in 2006 from \$19.0 million in 2005.

Revenues from product increased by \$1.3 million, or 8.7%, to \$16.2 million in 2006 from \$14.9 million in the same period in 2005. The increase in product revenues was attributable primarily to increased sales of our wireless system for tracking and managing industrial vehicles to U.S. Postal Service and Wal-Mart Stores, Inc.

Revenues from service increased \$4.4 million, or 108.2%, to \$8.5 million in 2006 from \$4.1 million in the same period in 2005. The increase in service revenues was attributable primarily to the increase in implementation services to the U.S. Postal Service.

**COST OF REVENUES.** Cost of revenues increased by \$4.0 million, or 41.1%, to \$13.7 million in 2006 from \$9.7 million in 2005. Gross profit was \$11.0 million in 2006 compared to \$9.3 million in 2005. As a percentage of revenues, gross profit decreased to 44.6% in 2006 from 48.9% in 2005.

Cost of product increased by \$413,000, or 5.3%, to \$8.2 million in 2006 from \$7.8 million in the same period in 2005. Gross profit from product revenue was \$8.0 million in 2006 compared to \$7.1 million in 2005. As a percentage of product revenues, gross profit increased to 49.2% in 2006 from 47.6% in 2005. Included in costs of revenues for 2005 was \$480,000 of amortized capitalized costs associated with the application of the cost recovery method of revenue recognition. In accordance with the cost recovery method, these capitalized contract costs were reduced dollar for dollar by the amount of revenue recognized. Excluding the amortization of these capitalized contract costs, gross profit as a percentage of revenues would have been 50.2%

Cost of service increased by \$3.6 million, or 189.2%, to \$5.5 million in 2006 from \$1.9 million in the same period in 2005. Gross profit from service revenue was \$3.1 million in 2006 compared to \$2.2 million in 2005. As a percentage of service revenues, gross profit decreased to 35.9% in 2006 from 53.8% in 2005. The decrease was primarily due to the hiring of third party subcontractors to perform implementation services at the U.S. Postal Service.

**Selling, General and Administrative Expenses.** Selling, general and administrative expenses increased \$5.8 million, or 81.3%, to \$12.9 million in 2006 compared to \$7.1 million in 2005. This increase was attributable primarily to (i) the adoption of SFAS No. 123(R) in which we expensed \$2.2 million of the value of stock based employee compensation and (ii) the increase in payroll and related expenses due to the hiring of additional personnel to support our continued growth. As a percentage of revenues, selling, general and administrative, expenses increased to 52.3% in 2006 from 37.6% in 2005.

**Research and Development Expenses.** Research and development expenses increased \$1.0 million, or 62.4%, to \$2.6 million in 2006 from \$1.6 million in 2005. This increase was attributable primarily to (i) the adoption of SFAS No. 123(R) in which we expensed \$723,000 of the value of stock based employee compensation and (ii) the increase in payroll and payroll related expenses. As a percentage of revenues, research and development expenses increased to 10.7% in 2006 from 8.6% in 2005.

**Interest Income.** Interest income increased \$2.6 million, or 1,161.7%, to \$2.8 million in 2006 from \$222,000 in 2005. This increase was attributable primarily to the increase in cash and cash equivalents and investments resulting from the proceeds received in connection with the public offering completed by us in March 2006.

**Interest Expense.** Interest expense decreased \$24,000, or 45.3%, to \$29,000 in 2006 from \$53,000 in 2005. The decrease was attributable to a reduction in the principal amount of our outstanding debt in 2006.

**Other Income.** Other income, which increased slightly to \$155,000 in 2006 from \$151,000 in 2005, reflects rental income earned from a sublease arrangement.

**Net Income (Loss).** Net loss was \$1.6 million or \$(0.15) per basic and diluted share in the year ended December 31, 2006 as compared to net income of \$851,000 or \$0.11 per basic and \$0.09 per diluted share for the year ended December 31, 2005. The increase in net loss was due primarily to the reasons described above.

### **Liquidity and Capital Resources**

Historically, our capital requirements have been funded from cash flow generated from our business and net proceeds from the issuance of our securities, including the issuance of our common stock upon the exercise of options and warrants. As of December 31, 2007, we had cash, cash equivalents and marketable securities of \$65.0 million and working capital of \$70.4 million compared to \$31.9 million and \$80 million, respectively, as of December 31, 2006.

Our marketable securities include auction rate securities with estimated fair value of \$25 million at December 31, 2007. Auction rate securities are securities with short-term interest rate reset dates of generally less than ninety days but with contractual maturities that can be well in excess of ten years. At the end of each reset period, investors typically can sell at auction or continue to hold the securities. These securities are subject to fluctuations in fair value depending on the supply and demand at each auction. Our auction rate securities consist of interests in pools of student loan receivables issued by agencies established by counties, cities, states and other municipal entities. Liquidity for our auction rate securities typically is provided by an auction process that resets the applicable interest rate every 28 days.

In February 2008, our auction rate securities failed to sell at auction due to sell orders exceeding buy orders. Prior to the auction rate failures, we sold approximately \$5 million of these auction rate securities in 2008. The funds associated with our auction rate securities that have failed auction, may not be accessible until a successful auction occurs, a buyer is found outside of the auction process, the security is called or the underlying securities have matured. As of February 29, 2008, the collateral related to the auction rate securities have not been impacted, credit ratings have not changed and the fair market values have not fallen below par value. As a result of the recent instability in the market for auction rate securities, there may be a future decline in the value of our auction rate securities. A decline in the value of these securities that is not temporary could materially adversely affect our liquidity and income.

### **Operating Activities**

Net cash provided by operating activities was \$604,000 for the year ended December 31, 2007 compared to net cash used in operating activities of \$1.1 million in the year ended December 31, 2006. The change was due primarily to (i) a decrease in accounts receivable resulting from improved collections and (ii) a decrease in finished goods inventory, partially offset by an increase in net loss.

Net cash used in operating activities was \$1.1 million for the year ended December 31, 2006 compared to net cash used in operating activities of \$4.1 million in the year ended December 31, 2005. The decrease was due primarily to a significant decrease in accounts receivable resulting from improved collections, offset by (i) an increase in net loss, (ii) an increase in finished goods inventory manufactured to meet anticipated customer orders and (iii) an increase to

accounts payable and accrued expenses attributable to an increase to operating expenses.

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### ***Investing Activities***

Net cash provided by investing activities was \$284,000 for the year ended December 31, 2007 compared to net cash used in investing activities of \$56.0 million for the year ended December 31, 2006. The change was due primarily to an increase in the maturities of investments and fewer purchases of investments in 2007.

Net cash used in investing activities was \$56.0 million for the year ended December 31, 2006 compared to net cash used in investing activities of \$2.8 million for the year ended December 31, 2005. The increase was due primarily to a significant increase in the purchase of investments with the net proceeds received in connection with the public offering that was completed by us in March 2006.

### ***Financing Activities***

Net cash used in financing activities was \$5.4 million for the year ended December 31, 2007 compared to net cash provided by \$64.5 million for the year ended December 31, 2006. The decrease was due primarily to the proceeds received in connection with the public offering that was completed in March 2006 that were not received in 2007, as well as the purchase of shares of our issued and outstanding common stock during 2007 pursuant to our share purchase program authorized by our Board of Directors in May 2007.

Net cash provided by financing activities was \$64.5 million for the year ended December 31, 2006 compared to \$544,000 for the year ended December 31, 2005. The increase was due primarily to the proceeds received in connection with the public offering that was completed by us in March 2006.

### ***Capital Requirements***

We believe that with the proceeds received from our public offering that was completed by us in March 2006, the cash we have on hand and operating cash flows we expect to generate, we will have sufficient funds available to cover our capital requirements for at least the next 12 months.

Our capital requirements depend on a variety of factors, including, but not limited to, the length of the sales cycle, the rate of increase or decrease in our existing business base, the success, timing, and amount of investment required to bring new products to market, revenue growth or decline and potential acquisitions. Failure to generate positive cash flow from operations will have a material adverse effect on our business, financial condition and results of operations. We may determine in the future that we require additional funds to meet our long-term strategic objectives, including to complete potential acquisitions. Any additional equity financing may be dilutive to stockholders, and debt financing, if available, may involve significant restrictive covenants, and we cannot assure you that such financing will be extended on terms acceptable to us or at all.

## Term Loan

In January 2003, we closed on a five-year term loan for \$1,000,000 with a financial institution. Interest at the 30-day LIBOR plus 1.75% and principal are payable monthly. To hedge the loan's floating interest expense, we entered into an interest rate swap contemporaneously with the closing of the loan and fixed the rate of interest at 5.28% for the five-year term. The loan is secured by all of our assets and we are in compliance with the covenants under the term loan. The fair value of the interest rate swap is not material to our financial condition or results of operations. At December 31, 2006 and 2007, the outstanding balance on the loan was \$240,000 and \$19,000, respectively.

## Contractual Obligations and Commitments

The following table summarizes our significant contractual obligations and commitments as of December 31, 2007:

|                                    | Total      | Payment due by Period |              |              |               |
|------------------------------------|------------|-----------------------|--------------|--------------|---------------|
|                                    |            | Less than one year    | 1 to 3 years | 3 to 5 years | After 5 years |
| Long-Term Debt Obligations         | \$ 19,000  | \$ 19,000             | \$ —         | \$ —         | \$ —          |
| Operating Leases                   | 951,000    | 429,000               | 522,000      | —            | —             |
| Total Contractual Cash Obligations | \$ 970,000 | \$ 448,000            | \$ 522,000   | \$ —         | \$ —          |

Purchase orders or contracts for the purchase of raw materials and other goods and services are not included in the table above. We are not able to determine the aggregate amount of such purchase orders that represent contractual obligations, as purchase orders may represent authorizations to purchase rather than binding agreements. Although we have entered into contracts for services, the obligations under these contracts were not significant and the contracts generally contain clauses allowing for cancellation without significant penalty.

The expected timing or payment of obligations discussed above is estimated based on current information. Timing of payments and actual amounts paid may be different depending on changes to agreed upon amounts for some obligations.

## **Inflation**

We believe our operations have not been and, in the foreseeable future, will not be materially and adversely affected by inflation or changing prices.

## **Off-Balance Sheet Arrangements**

We do not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to investors.

## **Recently Issued Accounting Pronouncements**

In September 2006, the FASB issued SFAS No. 157, "*Fair Value Measurements*", to define fair value, establish a framework for measuring fair value in accordance with generally accepted accounting principles, and expand disclosures about fair value measurements. SFAS No. 157 will be effective for fiscal years beginning after November 15, 2007, the beginning of our 2008 fiscal year. We are currently assessing the impact of the adoption of SFAS No. 157 will have on our financial position and results of operations.

In February 2007, the FASB issued SFAS No. 159 "The Fair Value Option for Financial Assets and Financial Liabilities" including an amendment of SFAS No. 115. SFAS No. 159 provides companies with an option to report selected financial assets and financial liabilities at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007, the beginning of our 2008 fiscal year. We are currently assessing the impact of the adoption of SFAS No. 159 will have on our financial position and results of operations.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 141R, "Business Combinations" ("SFAS No. 141R"), which replaces FASB Statement No. 141. Under SFAS No. 141R, an acquiring entity will be required to recognize all the assets acquired and liabilities assumed in a transaction at the acquisition date fair value with limited exceptions. SFAS No. 141R establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, any non-controlling interest in the acquire and the goodwill acquired. This statement also establishes disclosure requirements which will enable users to evaluate the nature and financial effects of the business combination. SFAS No. 141R is effective for financial statements issued for fiscal years beginning after December 15, 2008. Earlier adoption is prohibited. We have not yet determined the impact, if any, that the implementation of SFAS No. 141R will have on our results of operations or financial condition.

In December 2007, the FASB issued FASB Statement No. 160, Noncontrolling Interests in Consolidated Financial Statements – An Amendment of ARB No. 51 ("SFAS No. 160"). SFAS No. 160 establishes new accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. Specifically, this statement requires the recognition of a noncontrolling interest (minority interest) as equity in the consolidated financial statements an separate from the parent's equity. The amount of net income attributable to the noncontrolling interest will be included in consolidated net income on the face of the income statement. SFAS No. 160 clarifies that changes in a parent's ownership interest in a subsidiary that do not result in deconsolidation are equity transactions if the parent retains its controlling financial interest. In addition, this statement require that a parent recognize a gain or loss in net income when a subsidiary is deconsolidated. Such gain or loss will be measured using the fair value of the noncontrolling equity investment on the deconsolidated date. SFAS No. 160 also includes expanded disclosure requirements regarding the interests of the parent and its noncontrolling interest. SFAS No. 160 is effective for fiscal years beginning on or after December 15, 2008. Earlier adoption is prohibited. We have not yet determined the impact, if any, that the implementation of SFAS No. 160 will have on our results of operations or

financial condition.

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**Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

We are subject to market risks in the form of changes in corporate tax rates, which risks are currently immaterial to us.

We also are subject to market risk from changes in interest rates which could affect our future results of operations and financial condition. We manage our exposure to these risks through our regular operating and financing activities. As of December 31, 2007, we had cash, cash equivalents and marketable securities of \$65.0 million.

As of December 31, 2007 the carrying value of our cash and cash equivalents approximated fair value. Due to the conservative nature and relatively short duration of our investments, interest rate risk is mitigated. However, in a declining interest rate environment, as short-term investments mature, reinvestment occurs at less favorable market rates, negatively impacting future investment income.

Our investments include auction rate securities, these securities have an estimated fair value of \$25 million at December 31, 2007. Auction rate securities are securities that are structured with short-term interest rate reset dates of generally less than ninety days but with contractual maturities that can be well in excess of ten years. At the end of each reset period, investors typically can sell at auction or continue to hold the securities at par. These securities are subject to fluctuations in fair value depending on the supply and demand at each auction. Our auction rate securities consist of interests in collateralized pools of student loan receivables issued by agencies established by counties, cities, states and other municipal entities. Liquidity for our auction rate securities typically is provided by an auction process that resets the applicable interest rate every 28 days. In February 2008, our auction rate securities failed to sell at auction due to sell orders exceeding buy orders. Prior to the auction rate failures, we sold approximately \$5 million of auction rate securities in 2008. In 2008, the funds associated with our auction rate securities that have failed auction, may not be accessible until a successful auction occurs, a buyer is found outside of the auction process, the security is called or the underlying securities have matured. As a result of the recent instability in the market for auction rate securities, there may be a future decline in the value of our auction rate securities. A decline in the value of these securities that is not temporary could materially adversely affect our liquidity and income.

**Item 8. Financial Statements and Supplementary Data**

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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

Board of Directors and Stockholders of  
I.D. Systems, Inc.

We have audited the accompanying balance sheets of I.D. Systems, Inc. as of December 31, 2006 and 2007 and the related statements of operations, changes in stockholders' equity and cash flows for each of the years in the three year period ended December 31, 2007. Our audits also included the financial statement schedule II - Valuation and Qualifying Accounts. These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of I.D. Systems, Inc. as of December 31, 2006 and 2007, and the results of their operations and their cash flows for each of the years in the three year period ended December 31, 2007, in conformity with accounting principles generally accepted in the United States. Also, in our opinion, the financial statement schedule referred to above, when considered in relation to the financial statements, taken as a whole, presents fairly, in all material respects, the information stated therein.

As discussed in Note B to the financial statements, effective January 1, 2006, the Company adopted the provisions of Statement of Financial Accounting Standards No. 123 (R), "Share-Based Payment" applying the modified - prospective method.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), I.D. Systems, Inc.'s internal control over financial reporting as of December 31, 2007, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission, and our report dated March 11, 2008 expressed an unqualified opinion thereon.

/s/ Eisner LLP

New York, New York  
March 11, 2008

**I.D. SYSTEMS, INC.****Balance Sheets**

|   | <b>As of December 31,</b> |                      |
|---|---------------------------|----------------------|
|   | <b>2006</b>               | <b>2007</b>          |
| <b>ASSETS</b>   |                           |                      |
| Current assets:   |                           |                      |
| Cash and cash equivalents   | \$ 9,644,000              | \$ 5,103,000         |
| Marketable securities – short term  | 60,716,000                | 21,385,000           |
| Accounts receivable, net of allowance for doubtful accounts of \$239,000 in 2006 and 2007   | 5,101,000                 | 2,875,000            |
| Unbilled receivables  | 1,042,000                 | 580,000              |
| Inventory   | 6,430,000                 | 4,420,000            |
| Interest receivable   | 179,000                   | 142,000              |
| Officer loan  | 8,000                     | —                    |
| Prepaid expenses and other current assets   | 271,000                   | 291,000              |
| <b>Total current assets</b>   | <b>83,391,000</b>         | <b>34,796,000</b>    |
| Marketable securities –long term  | —                         | 38,515,000           |
| Fixed assets, net   | 1,394,000                 | 1,398,000            |
| Deferred contract costs   | 33,000                    | —                    |
| Other assets  | 87,000                    | 87,000               |
|   | <b>\$ 84,905,000</b>      | <b>\$ 74,796,000</b> |
| <b>LIABILITIES</b>  |                           |                      |
| Current liabilities:  |                           |                      |
| Accounts payable and accrued expenses   | \$ 2,950,000              | \$ 2,594,000         |
| Current portion of long term debt   | 221,000                   | 19,000               |
| Deferred revenue  | 221,000                   | 291,000              |
| <b>Total current liabilities</b>  | <b>3,392,000</b>          | <b>2,904,000</b>     |
| Long term debt  | 19,000                    | —                    |
| Deferred revenue  | 133,000                   | 167,000              |
| Deferred rent   | 77,000                    | 55,000               |
|   | <b>3,621,000</b>          | <b>3,126,000</b>     |
| Commitments and Contingencies (Note J)  |                           |                      |
| <b>STOCKHOLDERS' EQUITY</b>   |                           |                      |
| Preferred stock; authorized 5,000,000 shares, \$0.01 par value; none issued   | —                         | —                    |
| Common stock; authorized 50,000,000 shares, \$.01 par value; 11,337,000 and 11,561,000 shares issued at December 31, 2006 and 2007, respectively, shares outstanding, 11,297,000 and 11,015,000 at December 31, 2006 and 2007, respectively | 113,000                   | 115,000              |
| Additional paid-in capital  | 93,423,000                | 97,076,000           |
| Accumulated deficit   | (12,151,000)              | (19,492,000)         |

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|  |               |               |
|--|---------------|---------------|
| Comprehensive income   | 12,000        | 11,000        |
|  | 81,397,000    | 77,710,000    |
| Treasury stock; 40,000 shares and 546,000 shares at cost at December 31, 2006 and 2007, respectively | (113,000)     | (6,040,000)   |
| Total stockholders' equity   | 81,284,000    | 71,670,000    |
| Total liabilities and stockholders' equity   | \$ 84,905,000 | \$ 74,796,000 |

SEE ACCOMPANYING NOTES TO FINANCIAL STATEMENTS

**I.D. SYSTEMS, INC.**  
**Statements of Operations**

|  | Year Ended December 31, |                |                |
|--|-------------------------|----------------|----------------|
|  | 2005                    | 2006           | 2007           |
| <b>Revenue:</b>                                      |                         |                |                |
| Product  | \$ 14,905,000           | \$ 16,205,000  | \$ 11,037,000  |
| Service  | 4,099,000               | 8,535,000      | 6,046,000      |
|  | 19,004,000              | 24,740,000     | 17,083,000     |
| <b>Cost of Revenue:</b>                              |                         |                |                |
| Cost of product                                      | 7,816,000               | 8,229,000      | 5,859,000      |
| Cost of service                                      | 1,892,000               | 5,472,000      | 3,070,000      |
|  | 9,708,000               | 13,701,000     | 8,929,000      |
| Gross Profit   | 9,296,000               | 11,039,000     | 8,154,000      |
| <b>Operating expenses:</b>                           |                         |                |                |
| Selling, general and administrative expenses         | 7,140,000               | 12,943,000     | 15,963,000     |
| Research and development expenses                    | 1,625,000               | 2,639,000      | 2,849,000      |
|  | 8,765,000               | 15,582,000     | 18,812,000     |
| Income (loss) from operations                        | 531,000                 | (4,543,000)    | (10,658,000)   |
| Interest income                                      | 222,000                 | 2,801,000      | 3,238,000      |
| Interest expense                                     | (53,000)                | (29,000)       | (10,000)       |
| Other income   | 151,000                 | 155,000        | 89,000         |
| Net income (loss)                                    | \$ 851,000              | \$ (1,616,000) | \$ (7,341,000) |
| Net income (loss) per share - basic                  | \$ 0.11                 | \$ (0.15)      | \$ (0.66)      |
| Net income (loss) per share - diluted                | \$ 0.09                 | \$ (0.15)      | \$ (0.66)      |
| Weighted average common shares outstanding - basic   | 7,771,000               | 10,501,000     | 11,205,000     |
| Weighted average common shares outstanding - diluted | 9,332,000               | 10,501,000     | 11,205,000     |

SEE ACCOMPANYING NOTES TO FINANCIAL STATEMENTS

**I.D. SYSTEMS, INC.****Statements of Changes in Stockholders' Equity**

|  | Common Stock |           | Additional    | Accumulated     | Accumulated   | Treasury  | Stockholders' |
|--|--------------|-----------|---------------|-----------------|---------------|-----------|---------------|
|  | Number of    | Amount    | Paid-in       | Deficit         | Other         | Stock     | Equity        |
|  | Shares       |           | Capital       |                 | Comprehensive |           |               |
|  |              |           |               |                 | Income        |           |               |
| <b>Balance at January 1, 2005</b>  | 7,690,000    | \$ 77,000 | \$ 24,994,000 | \$ (11,386,000) | —             | (113,000) | \$ 13,572,000 |
| Net income   |              |           |               | 851,000         |               |           | 851,000       |
| Comprehensive income (loss) - unrealized gain(loss) on investments                     |              |           |               |                 | -             |           |               |
| Total comprehensive income   |              |           |               | 851,000         | -             |           | 851,000       |
| Shares issued pursuant to exercise of stock options                                    | 161,000      | 2,000     | 741,000       |                 |               |           | 743,000       |
| <b>Balance at December 31, 2005</b>  | 7,851,000    | \$ 79,000 | \$ 25,735,000 | \$ (10,535,000) | —             | (113,000) | \$ 15,166,000 |
| Net loss   |              |           |               | (1,616,000)     |               |           | (1,616,000)   |
| Comprehensive income - unrealized gain on investments                                  |              |           |               |                 | 12,000        |           | 12,000        |
| Total comprehensive loss   |              |           |               | (1,616,000)     | 12,000        |           | (1,604,000)   |
| Shares issued pursuant to exercise of stock options                                    | 200,000      | 2,000     | 784,000       |                 |               |           | 786,000       |
| Shares issued pursuant to a public offering  | 2,750,000    | 28,000    | 55,500,000    |                 |               |           | 55,528,000    |
| Shares issued pursuant to exercise of overallotment options related to public offering | 413,000      | 4,000     | 8,429,000     |                 |               |           | 8,433,000     |
| Issuance of restricted stock   | 91,000       |           | 478,000       |                 |               |           | 478,000       |
| Issuance of performance shares   | 32,000       |           | 602,000       |                 |               |           | 602,000       |
| Stock based compensation - options   |              |           | 1,895,000     |                 |               |           | 1,895,000     |

|  |            |            |               |                 |           |                |               |
|--|------------|------------|---------------|-----------------|-----------|----------------|---------------|
| <b>Balance at<br/>December 31, 2006</b>                      | 11,337,000 | \$ 113,000 | \$ 93,423,000 | \$ (12,151,000) | \$ 12,000 | \$ (113,000)   | \$ 81,284,000 |
| Net loss   |            |            |               | (7,341,000)     |           |                | (7,341,000)   |
| Comprehensive loss -<br>unrealized loss on<br>investments    |            |            |               |                 | (1,000)   |                | (1,000)       |
| Total comprehensive<br>loss                                  |            |            |               | (7,341,000)     | (1,000)   |                | (7,342,000)   |
| Shares issued<br>pursuant to<br>exercise of stock<br>options | 205,000    | 2,000      | 365,000       |                 |           |                | 367,000       |
| Shares repurchased   |            |            |               |                 |           | (5,583,000)    | (5,583,000)   |
| Shares withheld<br>pursuant to stock<br>issuances            |            |            |               |                 |           | (344,000)      | (344,000)     |
| Issuance of restricted<br>stock                              | 19,000     |            |               |                 |           |                |               |
| Stock based<br>compensation –<br>restricted stock            |            |            | 941,000       |                 |           |                | 941,000       |
| Stock based<br>compensation -<br>options                     |            |            | 2,347,000     |                 |           |                | 2,347,000     |
| <b>Balance at<br/>December 31, 2007</b>                      | 11,561,000 | \$ 115,000 | \$ 97,076,000 | \$ (19,492,000) | \$ 11,000 | \$ (6,040,000) | \$ 71,670,000 |

SEE ACCOMPANYING NOTES TO FINANCIAL STATEMENTS



**I.D. SYSTEMS, INC.**  
**Statements of Cash Flows**

|  | Year Ended December 31, |                     |                     |
|--|-------------------------|---------------------|---------------------|
|  | 2005                    | 2006                | 2007                |
| <b>Cash flows from operating activities:</b>   |                         |                     |                     |
| Net income (loss)  | \$ 851,000              | \$ (1,616,000)      | \$ (7,341,000)      |
| Adjustments to reconcile net income (loss) to cash (used in) provided by operating activities: |                         |                     |                     |
| Inventory reserve  | 105,000                 | 100,000             | 517,000             |
| Accrued interest income  | 42,000                  | (153,000)           | 20,000              |
| Stock based compensation   | —                       | 2,975,000           | 3,288,000           |
| Depreciation and amortization  | 362,000                 | 468,000             | 544,000             |
| Deferred rent expense  | (13,000)                | (22,000)            | (22,000)            |
| Deferred revenue   | (41,000)                | 109,000             | 104,000             |
| Provision for uncollectible accounts   | 20,000                  | 211,000             | —                   |
| Deferred contract costs  |                         |                     |                     |
| Changes in:  | 423,000                 | 20,000              | 33,000              |
| Accounts receivable  | (4,656,000)             | 756,000             | 2,226,000           |
| Unbilled receivables   | (891,000)               | 251,000             | 462,000             |
| Inventory  | (1,318,000)             | (3,578,000)         | 1,493,000           |
| Prepaid expenses and other assets  | 85,000                  | (130,000)           | (20,000)            |
| Investment in sales type leases  | (394,000)               | 467,000             | —                   |
| Accounts payable and accrued expenses  | 1,340,000               | (931,000)           | (700,000)           |
| Net cash (used in) provided by operating activities  | (4,085,000)             | (1,073,000)         | 604,000             |
| <b>Cash flows from investing activities:</b>   |                         |                     |                     |
| Purchase of fixed assets   | (512,000)               | (703,000)           | (548,000)           |
| Purchase of investments  | (5,963,000)             | (68,481,000)        | (15,691,000)        |
| Maturities of investments  | 3,703,000               | 13,214,000          | 16,523,000          |
| Net cash (used in) provided by investing activities  | (2,772,000)             | (55,970,000)        | 284,000             |
| <b>Cash flows from financing activities:</b>   |                         |                     |                     |
| Repayment of term loan   | (199,000)               | (209,000)           | (221,000)           |
| Proceeds from exercise of stock options  | 743,000                 | 786,000             | 367,000             |
| Net proceeds from public offering  | —                       | 63,961,000          | —                   |
| Collection of officer loan   | 11,000                  | 11,000              | 8,000               |
| Purchase of treasury shares  | —                       | —                   | (5,583,000)         |
| Net cash provided by (used in) financing activities  | 555,000                 | 64,549,000          | (5,429,000)         |
| <b>Net (decrease) increase in cash and cash equivalents</b>                                    |                         |                     |                     |
|  | (6,302,000)             | 7,506,000           | (4,541,000)         |
| Cash and cash equivalents - beginning of period  | 8,440,000               | 2,138,000           | 9,644,000           |
| <b>Cash and cash equivalents - end of period</b>   | <b>\$ 2,138,000</b>     | <b>\$ 9,644,000</b> | <b>\$ 5,103,000</b> |
| <b>Supplemental disclosure of cash flow information:</b>                                       |                         |                     |                     |
| Cash paid for:   |                         |                     |                     |
| Interest   | \$ 53,000               | \$ 29,000           | \$ 10,000           |

SEE ACCOMPANYING NOTES TO FINANCIAL STATEMENTS



**I.D. SYSTEMS, INC.**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2006 and 2007**

**NOTE A - THE COMPANY**

I.D. Systems, Inc. (the “Company”) develops, markets and sells wireless solutions for managing and securing high-value enterprise assets. These assets include industrial vehicles, such as forklifts and airport ground support equipment, and rental vehicles. The Company’s patented Wireless Asset Net system, which utilizes radio frequency identification, or RFID, technology, addresses the needs of organizations to control, track, monitor and analyze their assets. The Company’s solutions enable customers to achieve tangible economic benefits by making timely, informed decisions that increase the security, productivity and efficiency of their operations. The Company outsources its hardware manufacturing operations to contract manufacturers. The Company was incorporated in Delaware in 1993 and commenced operations in January 1994.

**NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**[1] Use of estimates:**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the 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. The Company continually evaluates estimates used in the preparation of the financial statements for reasonableness. The significant areas of estimation include market value of auction rates and any other non readily tradable securities, collectability of accounts receivable, sales returns, recoverability of inventory, realization of deferred tax assets, useful lives, and the impairment of tangible and intangible assets.

**[2] Cash and cash equivalents:**

The Company considers all highly liquid debt instruments with an original maturity of three months or less when purchased to be cash equivalents.

**[3] Marketable securities:**

The Company has marketable debt securities, including, government and state agency bonds, corporate bonds and auction rate certificates, which are classified as either available for sale or held to maturity, depending on management’s investment intentions relating to these securities. Available for sale securities, except for auction rate securities which are discussed below, are marked to market based on quoted market values of the securities, with the unrealized gain and (losses), reported as comprehensive income or (loss). Investments categorized as held to maturity are carried at amortized cost because the Company has both the intent and the ability to hold these investments until they mature. The Company has classified short term securities for those securities that mature within one year, and all other securities are classified as long term.

The Company’s auction rate securities estimated fair value of \$25 million at December 31, 2007 represent interest in collateralized pools of student loan receivables issued by agencies established by counties, cities, states and other municipal entities. During 2006, the Company had the ability to readily convert these instruments in to cash to fund operation, or satisfy other cash requirements as needed. Accordingly, in 2006 we had classified these securities as short term. In February 2008, these auction rate securities failed to sell at auction due to sell orders exceeding buy orders. Liquidity for these auction rate securities is typically provided by an auction process that resets the applicable

interest rate every 28 days. The funds associated with failed auctions will not be accessible until a successful auction occurs or a buyer is found outside of the auction process. As a result, as of December 31, 2007, the Company has classified these securities as long term.

**[4] Inventory:**

Inventory, which consists of components for the Company's products and finished goods to be shipped to customers under existing orders, is stated at the lower of cost or market using the first-in first-out method. At December 31, 2006 and 2007, the Company's inventory consisted of components of approximately \$465,000 and \$155,000 and finished goods of approximately \$5,965,000 and \$4,265,000, respectively.

**[5] Unbilled receivables and deferred revenue:**

Under certain customer contracts the Company invoices progress billings once certain milestones are met. The milestone terms vary by customer and can include upon receipt of purchase order, delivery, installation and launch. As the systems are delivered, and services are performed, and all of the criteria for revenue recognition are satisfied, the Company recognizes revenue. The difference between revenue recognized for financial reporting purposes, and amounts invoiced is recorded as unbilled receivables or deferred revenue. As of December 31, 2006 and 2007, unbilled receivables were \$1,042,000 and \$580,000, respectively and deferred revenue was \$354,000 and \$458,000, respectively.

**[6] Fixed assets and depreciation:**

Fixed assets are recorded at cost and depreciated using the straight-line method over the estimated useful lives of the assets which range from three to ten years. Leasehold improvements are amortized using the straight-line method over the terms of the respective leases, or their estimated useful lives, whichever is shorter.

**[7] Long-lived assets:**

The Company evaluates impairment losses on its long-lived assets in accordance with Statement of Financial Accounting Standards ("SFAS") No. 144, "*Accounting for the Impairment or Disposal of Long-Lived Assets*," . In the evaluation, the Company compares the carrying values of such assets to the estimated undiscounted future cash flows expected from the use of the assets and their eventual disposition. When the estimated undiscounted future cash flows are less than the carrying amount an impairment loss is recognized equal to the difference between the assets fair value and their carrying value. For the years ended December 31, 2005, 2006 and 2007, the Company has not incurred an impairment charge.

**[8] Research and development:**

Research and development costs are charged to expense as incurred.

**[9] Patent costs:**

Costs incurred in connection with acquiring patent rights are charged to expense as incurred.

**[10] Revenue recognition:**

The Company's revenues are derived from contracts with multiple element arrangements, which include the Company's system, training and technical support. Revenue is allocated to each element based upon vendor specific objective evidence (VSOE) of the fair value of the element. VSOE of the fair value is based upon the price charged when the element is sold separately. Revenue is recognized as each element is earned based on the selling price of each element and when there are no undelivered elements that are essential to the functionality of the delivered elements. The Company's system is typically implemented by the customer or a third party and, as a result, revenue is recognized when title and risk of loss passes to the customer, which usually is upon delivery of the system, persuasive evidence of an arrangement exists, sales price is fixed and determinable, collectibility is reasonably assured and contractual obligations have been satisfied. Training and technical support revenue are generally recognized at time of performance.

The Company also enters into post-contract maintenance and support agreements. Revenue is recognized over the service period and the cost of providing these services is expensed as incurred.

**[11] Benefit plan:**

The Company maintains a retirement plan under Section 401(k) of the Internal Revenue Code, which covers all eligible employees. The Company did not make any contributions to the plan during the years ended December 31, 2005, 2006 and 2007.

[12]

**Rent expense:**

Expense related to the Company's facility lease is recorded on a straight-line basis over the lease term. The difference between rent expense incurred and the amounts required to be paid in accordance with the lease term is recorded as deferred rent and is amortized over the lease term.

[13]

**Stock-based compensation:**

Commencing January 1, 2006, the Company adopted Statement of Financial Accounting Standard No. 123R, "*Share Based Payment*" ("*SFAS 123R*"), which requires all share-based payments, including grants of stock options, to be recognized in the statement of operations as an operating expense, based on their fair values on grant date.

Prior to adopting SFAS 123R, the Company accounted for stock-based employee compensation under Accounting Principles Board Opinion No. 25, "*Accounting for Stock Issued to Employees*" and related interpretations. No stock-based compensation cost was recognized in the statement of operations for the year ended December 31, 2005, as all options granted under the Plans had an exercise price equal to the market value of the underlying common stock on date of grant. The Company has applied the modified prospective transition method in adopting SFAS 123R. Accordingly, periods prior to adoption have not been restated. As a result of adoption, the Company recorded stock based compensation expense of \$2,975,000 and \$3,288,000 for the years ended December 31, 2006 and 2007, respectively, resulting in a corresponding increase in loss from operations and net loss and a reduction of \$0.28 per basic and \$ 0.26 per diluted share for the year ended December 31, 2006 and \$0.29 per basic and diluted share for the year ended December 31, 2007.

SFAS 123R requires companies to estimate the fair value of share based payment awards on the grant date using an option pricing model. The value of the portion of the award that is ultimately expected to vest is recognized as expense over the requisite service period in the Company's statement of operations. SFAS 123 requires forfeitures to be estimated at the time of grant in order to estimate the amount of share based awards that will ultimately vest. The estimate is based on the Company's historical rates of forfeitures. Share based compensation expense recognized by the Company in 2006 and 2007 includes (i) compensation expense for share based awards granted prior to, but not yet vested as of December 31, 2005, based on the grant date fair value estimated in accordance with the pro forma provisions of SFAS 123 and (ii) compensation expense for the share based payment awards granted subsequent to December 31, 2005, based on the grant date fair value estimated in accordance with the provisions of SFAS 123R. This is based on awards ultimately expected to vest and hence it has been reduced for estimated forfeitures. In the Company's pro forma information required under SFAS 123 for the periods prior to 2006, the Company accounted for forfeitures as they occurred. SFAS 123R also requires estimated forfeitures to be revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates.

The following table illustrates the effect on reported net income and earnings per share if the fair value based method had been applied to the year ended December 31, 2005.

|  |              |
|--|--------------|
| Reported net income  | \$ 851,000   |
| Stock-based employee compensation expense included in reported net income, net of related tax effects      | 0            |
| Stock-based employee compensation determined under the fair value based method, net of related tax effects | (1,612,000)  |
| Pro forma net loss   | \$ (761,000) |
| Net income (loss) per share basic  |              |
| As reported  | \$ 0.11      |

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|                                     |    |        |
|-------------------------------------|----|--------|
| Pro forma                           | \$ | (0.10) |
| Net income (loss) per share diluted |    |        |
| As reported                         | \$ | 0.09   |
| Pro forma                           | \$ | (0.10) |

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The fair value of each option grant on the date of grant is estimated using the Black-Scholes option-pricing model reflecting the following weighted average assumptions:

|                          | 2005    | December 31,<br>2006 | 2007    |
|--------------------------|---------|----------------------|---------|
| Expected volatility      | 51%     | 60%                  | 53%     |
| Expected life of options | 5 years | 5 years              | 5 years |
| Risk free interest rate  | 4%      | 5%                   | 5%      |
| Dividend yield           | 0%      | 0%                   | 0%      |

Expected volatility is based on historical volatility of the Company's stock and the expected life of options is based on historical data with respect to employee exercise periods.

**[14] Income taxes:**

The Company uses the asset and liability method of accounting for deferred income taxes. Deferred income taxes are measured by applying enacted statutory rates to net operating loss carryforwards and to the differences between the financial reporting and tax bases of assets and liabilities. Deferred tax assets are reduced, if necessary, by a valuation allowance if it is more likely than not that some portion or all of the deferred tax assets will not be realized.

The Company adopted the provisions of Financial Accounting Standards Board ("FASB") Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" ("FIN 48") on January 1, 2007. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109, "Accounting for Income Taxes." FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of an income tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. As of December 31, 2007, the Company did not have any unrecognized tax benefits. The Company recognizes any interest accrued related to unrecognized tax benefits in interest expense and penalties in operating expenses. For the year ended December 31, 2007, there was no such interest or penalty.

**[15] Net income (loss) per share:**

|  | 2005       | December 31,<br>2006 | 2007           |
|--|------------|----------------------|----------------|
| <b>Basic income (loss) per share</b>   |            |                      |                |
| Net income (loss)                      | \$ 851,000 | \$ (1,616,000)       | \$ (7,341,000) |
| Weighted average shares outstanding    | 7,771,000  | 10,501,000           | 11,205,000     |
| Basic income (loss) per share          | \$ 0.11    | \$ (0.15)            | \$ (0.66)      |
| <b>Diluted income (loss) per share</b> |            |                      |                |
| Net income (loss)                      | \$ 851,000 | \$ (1,616,000)       | \$ (7,341,000) |
| Weighted average shares outstanding    | 7,771,000  | 10,501,000           | 11,205,000     |
| Dilutive effect of stock options       | 1,561,000  | —                    | —              |



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|  |           |            |            |
|--|-----------|------------|------------|
| Weighted average shares outstanding, diluted | 9,332,000 | 10,501,000 | 11,205,000 |
| Diluted income (loss) per share              | \$ 0.09   | \$ (0.15)  | \$ (0.66)  |

Basic income (loss) per share is calculated by dividing net income (loss) by the weighted average number of common shares outstanding during the period. Diluted income (loss) per share reflects the potential dilution assuming common shares were issued upon the exercise of outstanding options and the proceeds thereof were used to purchase outstanding common shares. For the years ended December 31, 2006 and 2007, the basic and diluted weighted average shares outstanding are the same since the effect from the potential exercise of outstanding stock options of 2,784,000 and 2,761,000, respectively, would have been anti-dilutive.

**[16] Financial instruments:**

The carrying amounts of cash equivalents, accounts receivable, marketable securities (excluding auction rate securities), and other liabilities approximate their fair values due to the short period to maturity of these instruments. For auction rate securities, for which there are no available observable market prices, the Company establishes fair value by reference to public available indexes of securities with the same rating and comparable or similar underlying collaterals or industries' exposure, using "mark to market" bids and "mark to model" valuations received from the structuring financial institutions.

**[17] Advertising and Marketing Expense:**

Advertising and marketing costs are expensed as incurred. Advertising and marketing expense for the years ended December 31, 2005, 2006 and 2007 amounted to \$143,000, \$217,000 and \$314,000, respectively.

**[18] Reclassifications:**

Certain prior year amounts have reclassified to conform with the current year presentation.

**[19] Recently Issued Accounting Pronouncements:**

In September 2006, the FASB issued SFAS No. 157, "*Fair Value Measurements*", to define fair value, establish a framework for measuring fair value in accordance with generally accepted accounting principles, and expand disclosures about fair value measurements. SFAS No. 157 will be effective for the beginning of our 2008 fiscal year. We are currently assessing the impact of the adoption of SFAS No. 157 will have on our financial position and results of operations.

In February 2007, the FASB issued SFAS No. 159 "The Fair Value Option for Financial Assets and Financial Liabilities" including an amendment of SFAS No. 115. SFAS No. 159 provides companies with an option to report selected financial assets and financial liabilities at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. SFAS No. 159 is effective for the beginning of our 2008 fiscal year. We are currently assessing the impact of the adoption of SFAS No. 159 will have on our financial position and results of operations.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 141R, "Business Combinations" ("SFAS No. 141R"), which replaces FASB Statement No. 141. Under SFAS No. 141R, an acquiring entity will be required to recognize all the assets acquired and liabilities assumed in a transaction at the acquisition date fair value with limited exceptions. SFAS No. 141R establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, any non-controlling interest in the acquire and the goodwill acquired. This statement also establishes disclosure requirements which will enable users to evaluate the nature and financial effects of the business combination. SFAS No. 141R is effective for financial statements issued for fiscal years beginning after December 15, 2008. Earlier adoption is prohibited. We have not yet determined the impact, if any, that the implementation of SFAS No. 141R will have on our results of operations or financial condition.

In December 2007, the FASB issued FASB Statement No. 160, Noncontrolling Interests in Consolidated Financial Statements – An Amendment of ARB No. 51 ("SFAS No. 160"). SFAS No. 160 establishes new accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. Specifically, this statement requires the recognition of a noncontrolling interest (minority interest) as equity in the consolidated financial statements an separate from the parent's equity. The amount of net income attributable to the noncontrolling interest will be included in consolidated net income on the face of the income statement. SFAS No.

160 clarifies that changes in a parent's ownership interest in a subsidiary that do not result in deconsolidation are equity transactions if the parent retains its controlling financial interest. In addition, this statement require that a parent recognize a gain or loss in net income when a subsidiary is deconsolidated. Such gain or loss will be measured using the fair value of the noncontrolling equity investment on the deconsolidated date. SFAS No. 160 also includes expanded disclosure requirements regarding the interests of the parent and its noncontrolling interest. SFAS No. 160 is effective for fiscal years beginning on or after December 15, 2008. Earlier adoption is prohibited. We have not yet determined the impact, if any, that the implementation of SFAS No. 160 will have on our results of operations or financial condition.

#### **NOTE C - MARKETABLE SECURITIES**

The Company has marketable debt securities, including, government and state agency bonds, corporate bonds and auction rate certificates, which are classified as either available for sale or held to maturity, depending on management's investment intentions relating to these securities. Available for sale securities are marked to market based on quoted market values of the securities, with the unrealized gain and (losses), reported as comprehensive income or (loss). Investments categorized as held to maturity are carried at amortized cost because the Company has both the intent and the ability to hold these investments until they mature. The Company has classified short term securities for those securities that mature within one year, and all other securities are classified as long term.

The Company's auction rate securities with estimate fair value of \$25 million at December 31, 2007, represent interest in pools of student loan receivables issued by agencies established by counties, cities, states and other municipal entities. During 2006, the Company had the ability to readily convert these instruments in to cash to fund operation, or satisfy other cash requirements as needed. Accordingly, in 2006 we had classified these securities as short term. In February 2008, these auction rate securities failed to sell at auction due to sell orders exceeding buy orders. Liquidity for these auction rate securities is typically provided by an auction process that resets the applicable interest rate every 28 days. Prior to the auction rate failure, we sold approximately \$5 million of these auctionable securities in 2008. As of February 29, 2008, the collateral related to the auction rate securities have not been impacted, credit ratings have not changed and the fair market values have not fallen below par value. The funds associated with failed auctions will not be accessible until a successful auction occurs or a buyer is found outside of the auction process. As a result, as of December 31, 2007, the Company has classified these securities as long term.

The cost, gross unrealized gains (losses) and fair value of available for sale and held to maturity securities by major security type at December 31, 2006 and 2007 were as follows:

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| December 31, 2006                               | Cost                 | Unrealized<br>Gain | Unrealized<br>Loss | Fair<br>Value        |
|---|----------------------|--------------------|--------------------|----------------------|
| <b>Available for sale securities:</b>           |                      |                    |                    |                      |
| Government agency bonds                         | \$ 6,662,000         | \$ 11,000          | -                  | \$ 6,673,000         |
| State bonds                                     | 36,550,000           | -                  | -                  | 36,550,000           |
| Corporate bonds                                 | 261,000              | 1,000              | -                  | 262,000              |
| Mutual funds                                    | 3,257,000            | -                  | -                  | 3,257,000            |
| <b>Total available for sale securities</b>      | <b>46,730,000</b>    | <b>12,000</b>      | <b>-</b>           | <b>46,742,000</b>    |
| <b>Held to maturity securities:</b>             |                      |                    |                    |                      |
| Certificates of deposit                         | 190,000              | -                  | -                  | 190,000              |
| Government agency bonds                         | 9,255,000            | -                  | -                  | 9,255,000            |
| Corporate bonds                                 | 4,529,000            | -                  | -                  | 4,529,000            |
| <b>Total held to maturity securities</b>        | <b>13,974,000</b>    | <b>-</b>           | <b>-</b>           | <b>13,974,000</b>    |
| <b>Total marketable securities</b>              | <b>\$ 60,704,000</b> | <b>\$ 12,000</b>   | <b>\$ -</b>        | <b>\$ 60,716,000</b> |
| <br>  |                      |                    |                    |                      |
| December 31, 2007                               | Cost                 | Unrealized<br>Gain | Unrealized<br>Loss | Fair<br>Value        |
| <b>Marketable securities - short term</b>       |                      |                    |                    |                      |
| <b>Available for sale</b>                       |                      |                    |                    |                      |
| Government agency bonds                         | \$ 12,086,000        | \$ 2,000           | \$ (7,000)         | \$ 12,081,000        |
| Mutual funds                                    | 2,457,000            | -                  | -                  | 2,457,000            |
| <b>Total available for sale</b>                 | <b>14,543,000</b>    | <b>2,000</b>       | <b>(7,000)</b>     | <b>14,538,000</b>    |
| <b>Held to maturity securities</b>              |                      |                    |                    |                      |
| Government agency bonds                         | 6,847,000            | -                  | -                  | 6,847,000            |
| <b>Total marketable securities - short term</b> | <b>21,390,000</b>    | <b>2,000</b>       | <b>(7,000)</b>     | <b>21,385,000</b>    |
| <b>Marketable securities - long term</b>        |                      |                    |                    |                      |
| <b>Available for sale</b>                       |                      |                    |                    |                      |
| Auction rate securities                         | 25,125,000           | -                  | -                  | 25,125,000           |
| Government agency bonds                         | 8,895,000            | 16,000             | -                  | 8,911,000            |
| <b>Total available for sale</b>                 | <b>34,020,000</b>    | <b>16,000</b>      | <b>-</b>           | <b>34,036,000</b>    |
| <b>Held to maturity securities</b>              |                      |                    |                    |                      |
| Government agency bonds                         | 885,000              | -                  | -                  | 885,000              |
| Corporate bonds                                 | 3,594,000            | -                  | -                  | 3,594,000            |
| <b>Total held to maturity securities</b>        | <b>4,479,000</b>     | <b>-</b>           | <b>-</b>           | <b>4,479,000</b>     |
| <b>Total marketable securities - long term</b>  | <b>38,499,000</b>    | <b>16,000</b>      | <b>-</b>           | <b>38,515,000</b>    |
| <b>Total marketable securities</b>              | <b>\$ 59,889,000</b> | <b>\$ 18,000</b>   | <b>\$ (7,000)</b>  | <b>\$ 59,900,000</b> |



**NOTE D - FIXED ASSETS**

Fixed assets are stated at cost, less accumulated depreciation and amortization, and at December 31, 2006 and 2007, are summarized as follows:

|   | As of December 31, |              |
|---|--------------------|--------------|
|   | 2006               | 2007         |
| Equipment                                 | \$ 1,059,000       | \$ 1,144,000 |
| Computer software                         | 475,000            | 695,000      |
| Computer hardware                         | 531,000            | 654,000      |
| Furniture and fixtures                    | 206,000            | 238,000      |
| Automobile                                | —                  | 35,000       |
| Leasehold improvements                    | 447,000            | 500,000      |
|   | 2,718,000          | 3,266,000    |
| Accumulated depreciation and amortization | (1,324,000)        | (1,868,000)  |
|   | \$ 1,394,000       | \$ 1,398,000 |

Depreciation expense was \$310,000, \$416,000 and \$544,000 for the years ended December 31, 2005, 2006 and 2007, respectively.

**NOTE E - OFFICER LOAN**

In June 2002, the Company loaned \$56,000 to an officer. The loan was payable together with interest of 4% in semi-monthly installments of \$500 through August 2007. The loan was repaid and there was no amount due at December 31, 2007. At December 31, 2006, \$8,000 was due to the Company. This loan was made prior to the enactment of the Sarbanes-Oxley Act of 2002. The Company is prohibited from making any loans to officers in the future.

**NOTE F – LONG TERM DEBT**

In January 2003, we closed on a five-year term loan for \$1,000,000 with a financial institution. Interest at the 30-day LIBOR plus 1.75% and principal are payable monthly. To hedge the loan's floating interest expense, we entered into an interest rate swap contemporaneously with the closing of the loan and fixed the rate of interest at 5.28% for the five-year term. The loan is secured by all of our assets and we are in compliance with the covenants under the term loan. The fair value of the interest rate swap is not material to our financial condition or results of operations. At December 31, 2006 and 2007, the outstanding balance on the loan was \$240,000 and \$19,000, respectively.

**NOTE G - STOCKHOLDERS' EQUITY****[1] Common stock:**

On March 15, 2006, the Company completed the sale of 2,750,000 shares of its common stock in a public offering. In connection therewith, the Company received net proceeds of approximately \$55,528,000.

On March 28, 2006, the Company completed the sale of 412,500 shares of its common stock pursuant to the full exercise by the underwriters of their over-allotment option granted in connection with the Company's public offering of its common stock. In connection therewith, the Company received net proceeds of approximately \$8,433,000.

At the Company's Annual Meeting of Stockholders, held on June 9, 2006, the stockholders of the Company approved an amendment to the Company's Amended and Restated Certificate of Incorporation to increase the aggregate number of authorized shares of the Company's common stock from 15,000,000 shares to 50,000,000 shares.

**[2] Preferred stock:**

The Company is authorized to issue 5,000,000 shares of \$0.01 par value preferred stock. The Company's Board of Directors has the authority to issue shares of preferred stock and to determine the price and terms of those shares.

**[3] Stock options:**

The Company adopted the 1995 Stock Option Plan, pursuant to which the Company had the right to grant options to purchase up to an aggregate of 1,250,000 shares of common stock. The Company also adopted the 1999 Stock Option Plan and the 2007 Equity Compensation Plan, pursuant to which the Company may grant stock awards and options to purchase up to 2,813,000 and 2,000,000 shares, respectively, of common stock. The Company also adopted the 1999 Director Option Plan, pursuant to which the Company may grant options to purchase up to an aggregate of 600,000 shares of common stock. The Plans are administered by the Compensation Committee of the Company's Board of Directors, which has the authority to determine the term during which an option may be exercised (not more than 10 years), the exercise price of an option and the vesting provisions.

A summary of the status of the Company's stock option plans as of December 31, 2005, 2006 and 2007 and changes during the years then ended, is presented below:

|                                  | 2005      |  | 2006      |  | 2007      |  |
|----------------------------------|-----------|--|-----------|--|-----------|--|
|                                  | Shares    | Weighted<br>Average<br>Exercise<br>Price | Shares    | Weighted<br>Average<br>Exercise<br>Price | Shares    | Weighted<br>Average<br>Exercise<br>Price |
| Outstanding at beginning of year | 2,291,000 | \$ 5.04                                  | 2,730,000 | \$ 6.94                                  | 2,784,000 | \$ 8.97                                  |
| Granted                          | 677,000   | 13.10                                    | 388,000   | 21.30                                    | 308,000   | 13.37                                    |
| Exercised                        | (161,000) | 4.61                                     | (200,000) | 3.92                                     | (205,000) | 1.79                                     |
| Forfeited                        | (77,000)  | 9.30                                     | (134,000) | 10.94                                    | (126,000) | 18.26                                    |
| Outstanding at end of year       | 2,730,000 | \$ 6.94                                  | 2,784,000 | \$ 8.97                                  | 2,761,000 | \$ 9.57                                  |
|                                  | 1,320,000 | \$ 4.27                                  | 1,535,000 | \$ 5.49                                  | 1,677,000 | \$ 7.13                                  |

Exercisable at end of  
year

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**I.D. SYSTEMS, INC.**  
**NOTES TO FINANCIAL STATEMENTS**

The following table summarizes information about stock options at December 31, 2007:

| Exercise Prices | Number Outstanding | Options Outstanding                         |                                 |                           | Options Exercisable |                                 |                           |
|-----------------|--------------------|---|---------------------------------|---------------------------|---------------------|---------------------------------|---------------------------|
|                 |                    | Weighted Average Remaining Contractual Life | Weighted Average Exercise Price | Aggregate Intrinsic Value | Number Outstanding  | Weighted Average Exercise Price | Aggregate Intrinsic Value |
| 1.20 - 3.81     | 319,000            | 1 years                                     | \$ 1.64                         |                           | 319,000             | \$ 1.64                         |                           |
| 4.07 - 10.00    | 1,238,000          | 5 years                                     | 6.12                            |                           | 1,004,000           | 6.11                            |                           |
| 10.25 - 19.94   | 943,000            | 8 years                                     | 13.24                           |                           | 291,000             | 13.31                           |                           |
| 20.06 - 25.38   | 261,000            | 8 years                                     | 22.36                           |                           | 63,000              | 22.63                           |                           |
|                 | 2,761,000          | 6 years                                     | \$ 9.57                         | \$ 11,883,000             | 1,677,000           | \$ 7.13                         | \$ 10,041,000             |

|  | Number Outstanding | Weighted Average Exercise Price | Aggregate Intrinsic Value | Weighted Average Remaining Contractual Life |
|--|--------------------|---------------------------------|---------------------------|---|
| Options exercisable at December 31, 2007         | 1,677,000          | \$ 7.13                         | \$ 10,041,000             | 4.37  |
| Vested and expected to vest at December 31, 2007 | 2,687,000          | \$ 9.43                         | \$ 11,826,000             | 5.62  |

The weighted average fair value of options granted during the years ended December 31, 2005, 2006 and 2007 were \$7.02, \$11.88 and \$7.05, respectively. The total intrinsic value of options exercised during the years ended December 31, 2005, 2006 and 2007 was \$1,327,000, \$3,601,000 and \$1,899,000, respectively.

A summary of the status of the Company's non-vested stock options as of December 31, 2007 and changes during the year then ended, is presented below:

|                               | Non-vested Shares | Weighted Average Grant Date Fair Value |
|-------------------------------|-------------------|--|
| Non-vested at January 1, 2007 | 1,249,000         | \$ 7.11                                |
| Granted                       | 308,000           | 7.05                                   |
| Vested                        | (369,000)         | 6.09                                   |
| Forfeited                     | (104,000)         | 10.35                                  |

|                                 |           |    |      |
|---------------------------------|-----------|----|------|
| Non-vested at December 31, 2007 | 1,084,000 | \$ | 7.16 |
|---------------------------------|-----------|----|------|

As of December 31, 2007, there was \$5,810,000 of total unrecognized compensation costs related to non-vested options granted under the plans. That cost is expected to be recognized over a weighted average period of 2.59 years

**[4] Restricted stock awards and performance shares:**

As of December 31, 2007, there were 65,000 shares of unvested restricted stock that were outstanding and granted to employees, including executive officers, pursuant to the 1999 Stock Option Plan, as amended and restated effective April 20, 2005. The Plan is administered by the Compensation Committee, which has the authority to determine the terms of those shares. For the year ended December 31, 2007, the Company recorded a \$941,000 stock based compensation expense in connection with the restricted stock grant. As of December 31, 2007, there was \$539,000 of total unrecognized compensation cost related to non-vested shares. That cost is expected to be recognized over the next two years.

In June 2006, the Compensation Committee granted 85,000 performance shares to key employees pursuant to the 1999 Stock Option Plan. The issuance of the shares of the Company's common stock underlying the performance shares is subject to the achievement of revenue and gross margin levels during a two-year performance period. If the performance criterion is not met during that two year period, then the performance shares will not vest and will automatically be returned to the Plan. If the performance trigger is met, then the shares will be issued to the employees. For the year ended December 31, 2006, performance criteria was met for 31,875 shares which were subsequently issued in 2007 and 10,625 performance shares were returned to the plan. For the year ended December 31, 2006, the Company recorded \$602,000 of stock based compensation expense in connection with the performance shares. For the year ended December 31, 2007, the performance criteria was not met, and 42,500 shares were returned to the plan.

In January 2007, the Compensation Committee granted 62,500 performance shares to key employees pursuant to the 1999 Stock Option Plan. The issuance of the shares of the Company's common stock underlying the performance shares is subject to the achievement of revenue and gross margin levels during a two-year performance period. If the performance criterion is not met during that two year period, then the performance shares will not vest and will automatically be returned to the Plan. If the performance trigger is met, then the shares will be issued to the employees. For the year ended December 31, 2007, the performance criteria was not met, and 31,250 shares were returned to the plan.

**[5] Stock repurchase program:**

On May 3, 2007, the Company announced that it's Board of Directors had authorized the repurchase of issued and outstanding shares of our common stock having an aggregate value of up to \$10,000,000 pursuant to a share repurchase program established under Rule 10b-18 of the Securities Exchange Act of 1934, as amended. The amount and timing of such repurchases are dependent upon the price and availability of shares, general market conditions and the availability of cash, as determined in the discretion of our management. The repurchases are funded from the Company's working capital. The Company's share repurchase program does not have an expiration date, and it may discontinue or suspend the share repurchase program at any time. All shares of common stock repurchased under our share repurchase program are held as treasury stock. During, 2007, the Company purchased approximately 483,000 shares in open market transactions under the program at an average cost of \$11.55 per share.

**NOTE H- INCOME TAXES**

At December 31, 2007, the Company has an aggregate net operating loss carryforward of approximately \$25,187,000 for United States federal income tax purposes of which \$5,930,000 relates to stock options for which there were no compensation charges for financial reporting. At December 31, 2007, the Company had an aggregate net operating loss carryforward of approximately \$20,555,000 for state income tax purposes. Accordingly, any future tax benefit upon utilization of that net operating loss would be credited to additional paid-in capital. The Company has not included this amount in deferred tax assets. Substantially all of the net operating loss carryforwards expire from 2020 through 2027 for federal purposes and from 2008 through 2014 for state purposes. The net operating loss carryforwards maybe limited to use in any particular year based on Internal Revenue Code sections related to change of ownership restrictions. In addition, future stock issuances may subject the Company to annual limitations on the utilization of its net operating loss carryforwards under the same Internal Revenue Code provision.

The Company has a deferred tax asset of approximately \$6,292,000 and \$8,332,000 at December 31, 2006 and 2007, respectively. The increase in the deferred tax asset is primarily attributed to \$3,288,000 of stock based compensation expensed during 2007 in accordance with SFAS 123R, and operating loss for the year. At December 31, 2006, certain of the Company's stock options were treated as non-qualified options during the preparation of the Company's 2006 income tax provision. During 2007, management determined that these awards were incentive stock options and the Company adjusted the deferred tax assets relating thereto. As the Company's net deferred tax assets at December 31, 2006 and 2007 have a full valuation allowance, this change did not impact the Company's balance sheets or statements of operations. There were no other significant temporary differences between financial and tax reporting.

The Company has elected to use the incremental approach for financial statement purposes. Under which the Company will utilize net operating loss carry forwards before utilizing excess benefit from exercise of options during the current year. The Company has provided a valuation allowance against the full amount of its deferred tax asset, since the likelihood of realization cannot be determined. The valuation allowance increased during 2005, decreased in 2006 and increased in 2007 by \$129,000 and \$(150,000) and \$2,040,000, respectively.

The difference between income taxes at the statutory federal income tax rate and income taxes reported in the statements of operations is attributable to the following:

|  | <b>Year Ended December 31,</b> |              |                |
|--|--------------------------------|--------------|----------------|
|  | <b>2005</b>                    | <b>2006</b>  | <b>2007</b>    |
| Income tax expense (benefit) at the federal statutory rate   | \$ 289,000                     | \$ (549,000) | \$ (2,496,000) |
| State and local income taxes, net of effect on federal taxes | (20,000)                       | (81,000)     | (436,000)      |
| Increase (decrease) in valuation allowance                   | 129,000                        | (150,000)    | 2,040,000      |
| Fixed assets accumulated book/tax difference - prior year    | -                              | 117,000      | —              |
| ISO grants and restricted shares                             | —                              | 599,000      | 837,000        |
| Stock options  | (451,000)                      | -            | -              |
| Other  | 53,000                         | 64,000       | 55,000         |
|  | <b>\$ 0</b>                    | <b>\$ 0</b>  | <b>\$ 0</b>    |

**NOTE I - COMMITMENTS, CONTINGENCIES AND OTHER MATTERS****[1] Operating leases:**

The Company is obligated under an operating lease for its facility. The Company's operating lease provides for minimum annual rental payments as follows:

**Year  
Ending  
December  
31,**

|      |                   |
|------|-------------------|
| 2008 | 429,000           |
| 2009 | 418,000           |
| 2010 | 104,000           |
|      | <b>\$ 951,000</b> |

The office lease, which expires in 2010, also provides for escalations relating to increases in real estate taxes and certain operating expenses. Expenses relating to operating leases aggregated approximately \$398,000, \$396,000 and \$389,000 for the years ended December 31, 2005, 2006 and 2007, respectively.

During 2003, the Company entered into an agreement to sublease a portion of its space through the end of the lease. The sublease provides for monthly payments of approximately \$12,000 and also provides for escalations relating to increases in real estate taxes and certain operating expenses. Other income of \$151,000, \$155,000 and \$89,000 for the years ended December 31, 2005, 2006 and 2007, respectively reflects rent received by the Company under the sublease. In July 2007, the Company released the sublessee from the sublease and reassumed the space.

In March 2007, we began leasing office space in Suwanee, Georgia. The lease expired in September 2007 and has subsequently been renewed until March 2008. The rent is currently \$1,120 per month.

In September 2007, we began leasing warehouse space in Clifton, NJ. The lease expires in September 2008 and the rent is currently \$800 per month.

**[2] Concentration of customers:**

Three customers accounted for 37%, 32% and 10%, respectively, of the Company's revenue during the year ended December 31, 2007. Two of these customers accounted for 50% and 10%, respectively, of the Company's accounts receivables and unbilled receivables at December 31, 2007.

Two customers accounted for 61% and 14%, respectively, of the Company's revenue during the year ended December 31, 2006. One of these customers accounted for 47% of the Company's accounts receivable and unbilled receivables at December 31, 2006.

Two customers accounted for 45% and 18%, respectively, of the Company's revenue during the year ended December 31, 2005. One of these customers accounted for 72% of the Company's accounts receivable and unbilled receivables at December 31, 2005.

**[3] Officers bonus:**

The Board has awarded bonuses of approximately \$135,000 and \$128,000 to certain officers for the years ended December 31, 2006 and 2007, respectively. The bonuses are based on certain operating criteria, and is in addition to their base salaries.

**NOTE J - QUARTERLY SELECTED FINANCIAL DATA (UNAUDITED)**

The following tables contain selected quarterly financial data for each quarter for the years ended December 31, 2006 and 2007. We believe the following information reflects all normal recurring adjustments necessary for a fair presentation of the information for the periods presented. The operating results for any period are not necessarily indicative of results for any future periods.

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|  | <b>Year Ended December 31, 2006</b> |                    |                    |                       |
|--|-------------------------------------|--------------------|--------------------|-----------------------|
|  | <b>1st Quarter</b>                  | <b>2nd Quarter</b> | <b>3rd Quarter</b> | <b>4th Quarter</b>    |
| <b>Revenue:</b>                                    |                                     |                    |                    |                       |
| Product  | \$ 4,132,000                        | \$ 4,582,000       | \$ 5,751,000       | \$ 1,740,000          |
| Service  | 2,258,000                           | 1,781,000          | 2,323,000          | 2,173,000             |
|  | 6,390,000                           | 6,363,000          | 8,074,000          | 3,913,000             |
| <b>Cost of revenue:</b>                            |                                     |                    |                    |                       |
| Cost of product                                    | 2,010,000                           | 2,241,000          | 2,995,000          | 984,000               |
| Cost of service                                    | 1,193,000                           | 1,232,000          | 1,504,000          | 1,542,000             |
|  | 3,203,000                           | 3,473,000          | 4,499,000          | 2,526,000             |
| <b>Gross Profit</b>                                | <b>3,187,000</b>                    | <b>2,890,000</b>   | <b>3,575,000</b>   | <b>1,387,000</b>      |
| <b>Selling, general and administrative expense</b> |                                     |                    |                    |                       |
|  | 2,748,000                           | 2,910,000          | 3,162,000          | 4,123,000             |
| Research and development expense                   | 493,000                             | 560,000            | 673,000            | 913,000               |
| Other income and (expense)                         | 179,000                             | 761,000            | 892,000            | 1,095,000             |
| <b>Net income (loss)</b>                           | <b>\$ 125,000</b>                   | <b>\$ 181,000</b>  | <b>\$ 632,000</b>  | <b>\$ (2,554,000)</b> |
| <b>Income (loss) per share - basic</b>             | <b>\$ 0.01</b>                      | <b>\$ 0.02</b>     | <b>\$ 0.06</b>     | <b>\$ (0.23)</b>      |
| <b>Income (loss) per share - diluted</b>           | <b>\$ 0.01</b>                      | <b>\$ 0.01</b>     | <b>\$ 0.05</b>     | <b>\$ (0.23)</b>      |

|  | <b>Year Ended December 31, 2007</b> |                       |                     |                       |
|--|-------------------------------------|-----------------------|---------------------|-----------------------|
|  | <b>1st Quarter</b>                  | <b>2nd Quarter</b>    | <b>3rd Quarter</b>  | <b>4th Quarter</b>    |
| <b>Revenue:</b>                                    |                                     |                       |                     |                       |
| Product  | \$ 2,310,000                        | \$ 705,000            | \$ 5,466,000        | \$ 2,556,000          |
| Service  | 2,311,000                           | 1,518,000             | 1,052,000           | 1,165,000             |
|  | 4,621,000                           | 2,223,000             | 6,518,000           | 3,721,000             |
| <b>Cost of revenue:</b>                            |                                     |                       |                     |                       |
| Cost of product                                    | 1,146,000                           | 411,000               | 2,725,000           | 1,577,000             |
| Cost of service                                    | 1,233,000                           | 785,000               | 546,000             | 506,000               |
|  | 2,379,000                           | 1,196,000             | 3,271,000           | 2,083,000             |
| <b>Gross Profit</b>                                | <b>2,242,000</b>                    | <b>1,027,000</b>      | <b>3,247,000</b>    | <b>1,638,000</b>      |
| <b>Selling, general and administrative expense</b> |                                     |                       |                     |                       |
|  | 3,824,000                           | 3,880,000             | 4,004,000           | 4,255,000             |
| Research and development expense                   | 706,000                             | 594,000               | 828,000             | 721,000               |
| Other income and (expense)                         | 826,000                             | 803,000               | 795,000             | 893,000               |
| <b>Net loss</b>                                    | <b>\$ (1,462,000)</b>               | <b>\$ (2,644,000)</b> | <b>\$ (790,000)</b> | <b>\$ (2,445,000)</b> |
| <b>Income (loss) per share – basic and diluted</b> | <b>\$ (0.13)</b>                    | <b>\$ (0.23)</b>      | <b>\$ (0.07)</b>    | <b>\$ (0.22)</b>      |





## **Item 9. Changes In and Disagreements with Accountants on Accounting and Financial Disclosure**

None.

### **Item 9A. Controls and Procedures**

#### Evaluation of Disclosure Controls and Procedures

During the fourth quarter of our fiscal year ended December 31, 2007, our management, including the principal executive officer and principal financial officer, evaluated our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) related to the recording, processing, summarization, and reporting of information in our reports that we file with the SEC. These disclosure controls and procedures have been designed to ensure that material information relating to us is made known to our management, including these officers, by other of our employees, and that this information is recorded, processed, summarized, evaluated and reported, as applicable, within the time periods specified in the SEC's rules and forms. Due to the inherent limitations of control systems, not all misstatements may be detected. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. Our controls and procedures can only provide reasonable, not absolute, assurance that the above objectives have been met.

Based on their evaluation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of December 31, 2007, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) are effective as of December 31, 2007 to reasonably ensure that the information required to be disclosed by us in the reports that we file or submit under the Exchange Act, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and that information required to be disclosed by us in the reports we file or submit under the Exchange Act is accumulated and communicated to our management, including our principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

#### Management's Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f) and 15d-15(f) for us. Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our evaluation under this framework, our management concluded that our internal control over financial reporting was effective as of December 31, 2007.

Eisner LLP, the independent registered accounting firm that audited our consolidated financial statements included in this Annual Report on Form 10-K, has audited management's assessment of the effectiveness of our internal control over financial reporting as of December 31, 2007. The report, which expresses unqualified opinions on management's assessment and on the effectiveness of our internal control over financial reporting as of December 31, 2007, is included below.

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

Board of Directors and Stockholders of  
I.D. Systems, Inc.

We have audited I.D. Systems, Inc.'s internal control over financial reporting as of December 31, 2007, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). I.D. Systems, Inc.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

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

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

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

In our opinion, ID Systems, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2007, based on criteria established in Internal Control - Integrated Framework issued by the COSO.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the balance sheets of I.D. Systems, Inc. as of December 31, 2006 and 2007, and the related statements of operations, changes in stockholders' equity, and cash flows for each of the years in the three year period ended December 31, 2007, and our report dated March 11, 2008 expressed an unqualified opinion thereon.

/s/ Eisner LLP

New York, New York  
March 11, 2008



Changes in Internal Control Over Financial Reporting

There have been no changes in our internal control over financial reporting that occurred during our last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**Item 9B. Other Information**

None.

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### PART III.

#### Item 10. Directors, Executive Officers and Corporate Governance

The registrant incorporates by reference herein information to be set forth in its definitive proxy statement for its 2007 annual meeting of stockholders that is responsive to the information required with respect to this Item 10; provided , however , that such information shall not be incorporated herein:

- if the information that is responsive to the information required with respect to this Item 10 is provided by means of an amendment to this Annual Report on Form 10-K filed with the Securities and Exchange Commission prior to the filing of such definitive proxy statement; or
- If such proxy statement is not mailed to stockholders and filed with the Securities and Exchange Commission within 120 days after the end of the registrant's most recently completed fiscal year, in which case the registrant will provide such information by means of an amendment to this Annual Report on Form 10-K.

#### Item 11. Executive Compensation

The registrant incorporates by reference herein information to be set forth in its definitive proxy statement for its 2007 annual meeting of stockholders that is responsive to the information required with respect to this Item 11; provided , however , that such information shall not be incorporated herein:

- if the information that is responsive to the information required with respect to this Item 11 is provided by means of an amendment to this Annual Report on Form 10-K filed with the Securities and Exchange Commission prior to the filing of such definitive proxy statement; or
- If such proxy statement is not mailed to stockholders and filed with the Securities and Exchange Commission within 120 days after the end of the registrant's most recently completed fiscal year, in which case the registrant will provide such information by means of an amendment to this Annual Report on Form 10-K.

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

The registrant incorporates by reference herein information to be set forth in its definitive proxy statement for its 2007 annual meeting of stockholders that is responsive to the information required with respect to this Item 12; provided , however , that such information shall not be incorporated herein:

- if the information that is responsive to the information required with respect to this Item 12 is provided by means of an amendment to this Annual Report on Form 10-K filed with the Securities and Exchange Commission prior to the filing of such definitive proxy statement; or
- If such proxy statement is not mailed to stockholders and filed with the Securities and Exchange Commission within 120 days after the end of the registrant's most recently completed fiscal year, in which case the registrant will provide such information by means of an amendment to this Annual Report on Form 10-K.

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

The registrant incorporates by reference herein information to be set forth in its definitive proxy statement for its 2007 annual meeting of stockholders that is responsive to the information required with respect to this Item 13; provided , however , that such information shall not be incorporated herein:

- if the information that is responsive to the information required with respect to this Item 13 is provided by means of an amendment to this Annual Report on Form 10-K filed with the Securities and Exchange Commission prior to the filing of such definitive proxy statement; or
- If such proxy statement is not mailed to stockholders and filed with the Securities and Exchange Commission within 120 days after the end of the registrant's most recently completed fiscal year, in which case the registrant will provide such information by means of an amendment to this Annual Report on Form 10-K.

**Item 14. Principal Accountant Fees and Services**

The registrant incorporates by reference herein information to be set forth in its definitive proxy statement for its 2007 annual meeting of stockholders that is responsive to the information required with respect to this Item 14; provided , however , that such information shall not be incorporated herein:

- if the information that is responsive to the information required with respect to this Item 14 is provided by means of an amendment to this Annual Report on Form 10-K filed with the Securities and Exchange Commission prior to the filing of such definitive proxy statement; or
- If such proxy statement is not mailed to stockholders and filed with the Securities and Exchange Commission within 120 days after the end of the registrant's most recently completed fiscal year, in which case the registrant will provide such information by means of an amendment to this Annual Report on Form 10-K.

**PART IV.**

**Item 15. Exhibits, Financial Statement Schedules**

(a) List of Financial Statements, Financial Statement Schedules, and Exhibits .

1. Financial Statements. The following financial statements of I.D. Systems, Inc. are included in Item 8 of Part II of this Annual Report on Form 10-K:

Report of Independent Registered Public Accounting Firm

Balance Sheets as of December 31, 2006 and 2007

Statements of Operations for the Years Ended December 31, 2005, 2006 and 2007

Statements of Changes in Stockholders' Equity for the Years Ended December 31, 2005, 2006 and 2007

Statements of Cash Flows for the Years Ended December 31, 2005, 2006 and 2007

Notes to the Financial Statements

2. Financial Statement Schedules.

Schedule II - Valuation and Qualifying Accounts

All other financial statement schedules are omitted from this Annual Report on Form 10-K, as they are not required or applicable or the required information is included in the financial statements or notes thereto.

3. Exhibits. The following exhibits are filed with this Annual Report on Form 10-K or are incorporated herein by reference, as indicated.

- 3.1 Amended and Restated Certificate of Incorporation of I.D. Systems, Inc. (incorporated herein by reference to the I.D. Systems, Inc.'s Form SB-2 filed with the SEC on June 30, 1999).
- 3.2 Amended and Restated By-Laws of I.D. Systems, Inc. (incorporated herein by reference to I.D. Systems, Inc.'s Form SB-2 filed with the SEC on June 30, 1999).
- 4.1 Specimen Certificate of I.D. Systems, Inc.'s Common Stock (incorporated herein by reference to I.D. Systems, Inc.'s Form SB-2 filed with the SEC on June 30, 1999).
- 10.1 Agreement between I.D. Systems, Inc. and the United States Postal Service: Offer and Award Standard dated August 22, 1997, as modified on May 12, 1998, September 8, 1998, and March 5, 1999 (incorporated herein by reference to I.D. Systems, Inc.'s Form SB-2 filed with the SEC on June 30, 1999).

- 10.2 Federal Supply Service Information Technology Schedule Award, effective April 16, 1999 through April 15, 2004 (incorporated herein by reference to I.D. Systems, Inc.'s Form SB-2 filed with the SEC on June 30, 1999).
- 10.3 1995 Non-Qualified Stock Option Plan (incorporated herein by reference to I.D. Systems, Inc.'s Form SB-2 filed with the SEC on June 30, 1999).
- 10.4 1999 Stock Option Plan (incorporated herein by reference to I.D. Systems, Inc.'s Form SB-2 filed with the SEC on June 30, 1999).
- 10.5 1999 Director Option Plan (incorporated herein by reference to I.D. Systems, Inc.'s Form SB-2 filed with the SEC on June 30, 1999).
- 10.6 Office Lease dated November 4, 1999 between I.D. Systems, Inc. and Venture Hackensack Holding, Inc. (incorporated herein by reference to I.D. Systems, Inc.'s Annual Report on Form 10-KSB for the fiscal year ended December 31, 1999 filed with the SEC on March 29, 2000).
- 10.7 2007 Equity Compensation Plan (incorporated by reference to I.D. Systems, Inc.'s Form S-8 filed with the SEC on July 19, 2007).
- 23.1 Consent of Eisner LLP.
- 31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(b) Exhibits . The exhibits required by Item 601 of Regulation S-K are filed herewith or incorporated by reference.

(c) Financial Statement Schedules and Other Financial Statements .

#### Schedule II - Valuation and Qualifying Accounts

All other financial statement schedules are omitted from this Annual Report on Form 10-K, as they are not required or applicable or the required information is included in the financial statements or notes thereto.



**SIGNATURES**

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

Date: March 14, 2008

I.D. SYSTEMS, INC.

By: /s/ Jeffrey M. Jagid  
 Jeffrey M. Jagid  
 Chief Executive Officer  
 (Principal Executive Officer)

By: /s/ Ned Mavrommatis  
 Ned Mavrommatis  
 Chief Financial Officer  
 (Principal Financial and Accounting Officer)

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

| <b>Signature</b>                           | <b>Title</b>  | <b>Date</b>    |
|--|---|----------------|
| /s/ Jeffrey M. Jagid<br>Jeffrey M. Jagid   | Chief Executive Officer and Director<br>(Principal Executive Officer)   | March 14, 2008 |
| /s/ Kenneth S. Ehrman<br>Kenneth S. Ehrman | President, Chief Operating Office and Director                          | March 14, 2008 |
| /s/ Ned Mavrommatis<br>Ned Mavrommatis     | Chief Financial Officer (Principal Financial<br>and Accounting Officer) | March 14, 2008 |
| /s/ Lawrence Burstein<br>Lawrence Burstein | Director  | March 14, 2008 |
| /s/ Michael Monaco<br>Michael Monaco       | Director  | March 14, 2008 |
| /s/ Beatrice Yormark<br>Beatrice Yormark   | Director  | March 14, 2008 |

**I.D. SYSTEMS, INC.**  
**SCHEDULE II - VALUATION AND QUALIFYING ACCOUNTS**

| Description                                    | Balance at<br>Beginning<br>Period | Charged to<br>(Write-off)<br>to Costs and<br>Expenses | Balance at<br>End of<br>Period |
|--|-----------------------------------|---|--------------------------------|
| Year ended December 31, 2007 Inventory reserve | \$ 125                            | \$ 517  | \$ 642                         |
| Year ended December 31, 2006 Inventory reserve | \$ 305                            | \$ (180)  | \$ 125                         |
| Year ended December 31, 2005 Inventory reserve | \$ 200                            | \$ 105  | \$ 305                         |

| Description  | Balance at<br>Beginning<br>Period | Charged to<br>(Write-off )<br>to Costs and<br>Expenses | Balance at<br>End of<br>Period |
|--|-----------------------------------|--|--------------------------------|
| Year ended December 31, 2007 allowance for doubtful accounts | \$ 239                            | \$ —   | \$ 239                         |
| Year ended December 31, 2006 allowance for doubtful accounts | \$ 28                             | \$ 211   | \$ 239                         |
| Year ended December 31, 2005 allowance for doubtful accounts | \$ 8                              | \$ 20  | \$ 28                          |