BIO KEY INTERNATIONAL INC
Form 424B3
December 29, 2004

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Filed pursuant to Rule 424(b)(3)
Registration No. 333-120104

PROSPECTUS

11,723,152 Shares

BIO-key International, Inc.

Common Stock

We are registering up to 11,723,152 shares of our common stock for offer or sale by the selling security holders named in this prospectus. Of the shares being registered, 8,946,933 shares are issuable upon conversion of convertible term notes issued to certain of the selling security holders and 2,776,219 shares are issuable upon exercise of warrants issued to certain of the selling security holders. The selling security holders may offer or sell all or a portion of their shares publicly or through private transactions at prevailing market prices or at negotiated prices. We will not receive any proceeds from the shares being registered for offer and sale by the selling security holders. We will, however, receive proceeds from the exercise price of certain warrants held by the selling security holders to the extent that such warrants are exercised.

Investing in our common stock involves a high degree of risk.
See "Risk Factors" beginning on page 4.

Our common stock is traded on the OTC Bulletin Board under the symbol "BKYI." The last reported sale price of our common stock on December 7, 2004 was $1.01 per share.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or passed upon the accuracy or adequacy of this prospectus. Any representation to the contrary is a criminal offense.

December 28, 2004

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You should rely only on the information contained in this prospectus. We have not authorized anyone to provide you with information that is different. This prospectus may only be used where it is legal to sell these securities. The information in this prospectus may only be accurate on the date of this prospectus, regardless of the time of delivery of this prospectus or of any sale of our common stock. Applicable rules of the Securities and Exchange Commission may require us to update this prospectus in the future.

PROSPECTUS SUMMARY

About BIO-key International, Inc.

BIO-key International, Inc. (the "Company," "BIO-key," "we" or "us") is in the business of delivering advanced identification solutions and information services to law enforcement departments, public safety agencies and other government and private sector customers. Our mobile wireless technology provides first responders with critical, reliable, real-time data and images from local, state, and national databases. More than 2,500 police, fire and emergency services departments in North America currently utilize the our solutions, making us a leading supplier of mobile and wireless solutions for public safety.

Our scalable biometric finger identification technology identifies and authenticates users of wireless and enterprise data to improve security, convenience and privacy as well as reducing identity theft. Biometrics is the science of analyzing specific human characteristics which are unique to an individual in order to identify a specific individual from a broader population. Our technology scans a person's fingerprint and identifies that person within seconds without using a password, key card, personal identification number or any other identifying data. Fingerprint analysis is an accurate and reliable method to distinguish one individual from another and is generally viewed as less intrusive than many other biometric identification methods. We believe our technology and products will have a broad range of applications relating to protecting access to information and assets in both electronic and physical environments, including:

- Delivering mission critical centralized enterprise information to field personnel graphically and wirelessly through standard off-the-shelf hardware devices;
- Securing access to logical networks and applications;
- Securing access to buildings and restricted areas; and
- Prevention of identity and data theft.

Our technology provides a reliable and secure user identification/authentication system for public and private computer networks. WEB-key is designed to secure access to proprietary information residing on remote servers which is transmitted via the Internet. It is compatible with Oracle server software and new security features in Microsoft's Internet Explorer Versions 5.5 SP2 and 6.0. Network authentication is typically accomplished by using passwords. Since passwords can be lost, transferred, stolen or forgotten, we believe our WEB-key biometric solution is a more secure method for verifying the identity of remote users and eliminates the substantial administrative costs associated with tracking and reissuing new passwords.

On March 30, 2004, we acquired Public Safety Group, Inc. ("PSG"), a privately held leader in wireless solutions for law enforcement and public safety markets. PSG's primary technology is a software solution that provides police officers and other security personnel instantaneous access to criminal, civil and private database information in a wireless environment. PocketCop© is a handheld application that allows law enforcement officers to access state and federal databases over the wireless network for PalmOS, Windows CE and PocketPC. With the use of a portable wireless handheld device and PocketCop© application software, an authorized user can access suspect information such as wanted status, warrant status, vehicle registration and driver license status. With our acquisition of PSG, we believe there is a substantial market opportunity to integrate our VST and WEB-key biometric technologies with the PSG mobile solution.

On September 30, 2004, we acquired the Mobile Government Division ("Aether Mobil Government") of Aether Systems, Inc. ("Aether"). Pursuant to the Asset Purchase Agreement dated as of August 16, 2004 by and among the Company, Aether, Cerulean Technology, Inc. and SunPro, Inc., we paid Aether a purchase price of $10,000,000 in cash, subject to post-closing adjustments to reflect changes in Aether Mobile Government's working capital and cash flows since June 30, 2004. In connection with this acquisition, we also issued a subordinated secured promissory note to Aether in the face amount of $6,884,588 (the "Aether Note"). The Aether Note evidences a contingent reimbursement obligation of the Company to Aether and a surety fee payable by the Company to Aether, in each case with respect to a letter of credit maintained by Aether for the Company's benefit in connection with the acquisition. Our obligations under the Aether Note are secured by a security interest granted to Aether in all or substantially all of our assets, subordinate to the security interests described in the "Convertible Debt Financing Transactions" section of this prospectus below.

Aether Mobile Government provides wireless data solutions for use by public safety organizations, primarily state and local police, fire and rescue and emergency medical services organizations, that enable such organizations to access law enforcement databases to validate identities and obtain suspect information. Its public safety solutions are integrated into fifty (50) different state databases, as well as local and federal databases, and its products deliver real-time information in seconds, without the need for human dispatchers or other resources.

Although biometric based solutions currently compete with more traditional security methods such as keys, cards, personal identification numbers and security personnel, biometric technology is becoming an acceptable approach to physical and logical security. Our current business plan is to:

- License our core technology "VST" to original equipment manufacturers, systems integrators and application developers to develop and market products and applications which can then be sold to end users;

- License WEB-key , our web-based biometric authentication solution; and

- Provide for "device independent" finger identification matching for virtually any application utilizing the latest advances in scanning technology.

- License our wireless software solutions for law enforcement and public safety markets.

We have evolved from a development stage company to a revenue generating company, but we have sustained substantial losses to date. We completed a private placement equity offering in March 2004 that resulted in approximately $12,000,000 in gross proceeds to the Company and a private placement convertible debt offering in September 2004 that resulted in approximately $10,000,000 in gross proceeds to the Company (a portion of which was used to finance the acquisition of Aether Mobile Government), and management believes that we now have sufficient funds to meet our working capital requirements for at least the next twenty-four (24) months. To the extent that we will require additional capital to support our operations, expand our marketing and sales efforts and to execute our business plan, we may need to obtain additional financing.

Our principal executive offices are located at 1285 Corporate Center Drive, Suite 175, Eagan, Minnesota 55121 and our telephone number is (651) 687-0414.

About the Offering

This prospectus covers the public resale of up to 11,723,152 shares of our common stock to be sold by the selling security holders identified herein. 4,338,105 shares of our common stock covered by this prospectus are issuable upon conversion of secured convertible term notes in the aggregate principal amount of $5,050,000, together with accrued interest and fees due thereon, issued to Laurus Master Fund, Ltd. and other institutional and accredited investors pursuant to a Securities Purchase Agreement dated as of September 29, 2004 (the "Senior Purchase Agreement") by and among the Company and such investors. 1,122,222 shares of our common stock covered by this prospectus are issuable upon exercise of warrants issued to the investors party to the Senior Purchase Agreement. 4,608,828 shares of our common stock covered by this prospectus are issuable upon conversion of subordinated convertible term notes in the aggregate principal amount of $4,950,000, together with accrued interest and fees due thereon, issued to The Shaar Fund Ltd. and other institutional and accredited investors pursuant to a Securities Purchase Agreement dated as of September 29, 2004 (the "Subordinated Purchase Agreement") by and among the Company and such investors. 1,099,997 shares of our common stock covered by this prospectus are issuable upon exercise of warrants issued to the investors party to the Subordinated Purchase Agreement. 10,000 shares of our common stock covered by this prospectus are issuable upon the exercise of a warrant issued by the Company to Kreiger & Prager, LLP on November 26, 2001 in consideration for legal advisory services performed by Kreiger & Prager LLP in connection with the recapitalization of the Company's then outstanding convertible debt and equity securities that occurred on November 26, 2001. 100,000 shares of our common stock covered by this prospectus are issuable upon the exercise of a warrant issued by the Company to The November Group, Ltd. on July 15, 2004 in connection with certain consulting services performed by The November Group, Ltd. with respect to the Company's business development and strategic initiatives. The remaining 444,000 shares of our common stock covered by this prospectus are issuable upon the exercise of warrants issued by the Company to Jesup & Lamont Securities Corp. and certain of its employees on March 31, 2004, which warrants represent a portion of fees earned by Jesup & Lamont Securities Corp. for acting as financial advisor and placement agent in connection with the private placement financing transaction that occurred on March 31, 2004, resulting in approximately $12,000,000 in aggregate gross proceeds to the Company.

RISK FACTORS

An investment in our common stock involves a high degree of risk. You should carefully consider the following information about certain of the risks of investing in our common stock, together with other information contained in this prospectus, before you decide to purchase our common stock.

Business and Financial Risks

Since our formation, we have historically generated minimal revenue and have sustained substantial operating losses.

From inception through December 31, 2003, we accumulated a deficit of approximately $27,676,000 and negative cash flow from operations of approximately $19,038,000. As of December 31, 2003, we had positive working capital of approximately $1,085,000, but a stockholders' deficit of approximately $9,136,000. Since our inception, we have focused almost exclusively on developing our core technology and have not generated any significant historical revenue. In order to generate revenue, we have developed a direct sales force and anticipate the need to retain additional sales, marketing and technical support personnel and incur substantial expenses. We cannot assure you that we will be able to secure these necessary resources, that a significant market for our technology will develop or that we will be able to achieve our targeted revenue.

Our technology has yet to gain widespread market acceptance and we do not know how large of a market will develop for our technology.

Biometric technology has received only limited market acceptance, particularly in the private sector. Our technology represents a novel security solution and we have not generated any significant sales. Although recent security concerns relating to identification of individuals has increased interest in biometrics generally, it remains an undeveloped, evolving market. Biometric based solutions compete with more traditional security methods including keys, cards, personal identification numbers and security personnel. Acceptance of biometrics as an alternative to such traditional methods depends upon a number of factors including:

- the reliability of biometric solutions,
- public perception regarding privacy concerns,
- costs involved in adopting and integrating biometric solutions.

For these reasons, we are uncertain whether our technology will gain widespread acceptance in any commercial markets or that demand will be sufficient to create a market large enough to produce significant revenue or earnings. Our future success depends upon business customers adopting biometrics generally, and our solution specifically.

Biometric technology is a new approach to internet security which must be accepted in order for our WEB-key solution to generate significant revenue.

Our WEB-key authentication initiative represents a new approach to Internet security which has been adopted on a limited basis by companies which distribute goods, content or software applications over the Internet. The implementation of our WEB-key solution requires the distribution and use of a finger scanning device and integration of database and server side software. Although we believe our solution provides a higher level of security for information transmitted over the Internet than existing traditional methods, unless business and consumer markets embrace the use of a scanning device and believe the benefits of increased accuracy outweigh implementation costs, our solution will not gain market acceptance.

Our software may contain defects which will make it more difficult for us to establish and maintain customers.

Although we have completed the development of our core technology, it has only been used by a limited number of business customers. Despite extensive testing during development, our software may contain undetected design faults and software errors, or "bugs," that are discovered only after it has been installed and used by customers. Any such default or error in new or existing software or applications could cause delays in delivering our technology or require design modifications. These could adversely affect our competitive position and cause us to lose potential customers or opportunities. Since our technology is intended to be utilized to secure physical and electronic access, the effect of any such bugs or delays will likely have a detrimental impact on us. In addition, given that biometric technology generally, and our technology specifically, has yet to gain widespread acceptance in the market, any delays would likely have a more detrimental impact on our business than if we were a more established company.

While we have commenced a significant sales and marketing effort, we have only developed a limited distribution channel and may not have the resources or ability to sustain these efforts or generate any meaningful sales.

In order to generate revenue, we are dependent upon independent original equipment manufacturers, system integrators and application developers which we do not control. As a result, it may be more difficult to generate sales.

We market our technology through licensing arrangements with:

- Original equipment manufacturers, system integrators and application developers which develop and market products and applications which can then be sold to end users; and

- Companies which distribute goods, services or software applications over the Internet.

As a technology licensing company, our success will depend upon the ability of these manufacturers and developers to effectively integrate our technology into products and services which they market and sell. We have no control over these licensees and cannot assure you that they have the financial, marketing or technical resources to successfully develop and distribute products or applications acceptable to end users or generate any meaningful revenue for us. These third parties may also offer the products of our competitors to end users.

We face intense competition and may not have the financial and human resources necessary to keep up with rapid technological changes which may result in our technology becoming obsolete.

The Internet, facility access control and information security markets are subject to rapid technological change and intense competition. We compete with both established biometric companies and a significant number of startup enterprises as well as providers of more traditional methods of access control. Most of our competitors have substantially greater financial and marketing resources than we do and may independently develop superior technologies which may result in our technology becoming less competitive or obsolete. We may not be able to keep pace with this change. If we are unable to develop new applications or enhance our existing technology in a timely manner in response to technological changes, we will be unable to compete in our chosen markets. In addition, if one or more other biometric technologies such as voice, face, iris, hand geometry or blood vessel recognition is widely adopted, it would significantly reduce the potential market for our fingerprint identification technology.

We depend on our chairman of the board and chief executive officer and need additional marketing and technical personnel to successfully market our technology. We cannot assure you that we will be able to retain or attract such persons.

A loss of our current Chairman of the Board of Directors or Chief Executive Officer could severely and negatively impact our operations. We have an employment contract with Michael W. DePasquale, our Chief Executive Officer. Although the contract does not prevent him from resigning, it does contain confidentiality and non-compete clauses which are intended to prevent him from working for a competitor within one year after leaving our Company. We continue to retain additional employees with expertise in developing, marketing and selling software solutions. In order to successfully market our technology, we will need to retain additional engineering, technical support and marketing personnel. The market for such persons remains highly competitive and our limited financial resources will make it more difficult for us to recruit and retain qualified persons.

We cannot assure you that the limited intellectual property protection for our core technology provides a meaningful competitive advantage or barrier to entry against our competitors.

Our success and ability to compete is dependent in part upon proprietary rights to our technology. We rely primarily on a combination of patent, copyright and trademark laws, trade secrets and technical measures to protect our propriety rights. We have filed a patent application relating to both the optic technology and biometrics solution components of our technology wherein several claims have been allowed. More recently, we filed a patent application with respect to our VST (Vector Segment Technology), the core algorithm of our biometric identification solution. We cannot assure you that any patents will be issued, or that, if issued, that we will have the resources to protect any patent from infringement. Although we believe our technology does not currently infringe upon patents held by others, we cannot assure you that such infringements do not exist or will not exist in the future, particularly as the number of products and competitors in the biometric industry segment grows.

We may need to obtain additional financing to execute our business plan which may not be available. If we are unable to raise additional capital or generate significant revenue, we may not be able to continue operations.

Since our inception, we have not generated any significant revenue and have experienced substantial losses, including approximately $3,826,000 during 2003. We also have a stockholders' deficit as of December 31, 2003. In March 2004, we completed a private placement equity offering that resulted in approximately $12,000,000 in gross proceeds to the Company and a private placement convertible debt offering in September 2004 that resulted in approximately $10,000,000 in gross proceeds to the Company (a portion of which was used to finance the acquisition of Aether Mobile Government), and management now believes that we have sufficient funds to meet our working capital requirements for at least the next twenty-four (24) months. To the extent that we will require additional capital to support our operations, expand our marketing and sales efforts and to execute our business plan to substantially increase revenue, we may need to obtain additional financing through the issuance of debt or equity securities. We have not and cannot assure you that we will ever be able to secure any such financing on terms acceptable to us. If we cannot obtain such financing or generate such revenues, we may not be able to execute our business plan or continue operations.

We may not be able to successfully integrate recent acquisitions into our operations.

On September 30, 2004, we completed our transaction with Aether to purchase Aether Mobil Government based in Marlborough, Massachusetts, a provider of wireless data solutions for use by public safety organizations, as described further in the "Acquisition of Aether Mobile Government" section of this prospectus. The integration of Aether Mobile Government into our operations involves a number of risks, including:

- difficulty integrating operations and personnel;
- diversion of management attention;
- potential disruption of ongoing business;
- inability to retain key personnel;
- inability to successfully incorporate the acquired products and services into our product and service offerings and to develop new products and services; and
- impairment of relationships with employees, customers or vendors.

Failure to overcome these risks or any other problems encountered in connection with the acquisition of Aether Mobile Government could slow our growth or lower the quality of our services, which could reduce customer demand. The result could be an adverse effect on our financial results.

We may not achieve profitability with respect to our law enforcement and public safety division if we are unable to maintain, improve and develop the wireless data services we offer.

We believe that our future business prospects depend in part on our ability to maintain and improve our current services and to develop new ones on a timely basis. Our services will have to achieve market acceptance, maintain technological competitiveness and meet an expanding range of customer requirements. As a result of the complexities inherent in our service offerings, major new wireless data services and service enhancements require long development and testing periods. We may experience difficulties that could delay or prevent the successful development, introduction or marketing of new services and service enhancements. Additionally, our new services and service enhancements may not achieve market acceptance. If we cannot effectively develop and improve services we may not be able to recover our fixed costs or otherwise become profitable.

Our law enforcement and public safety division depends upon wireless networks owned and controlled by others.

If we do not have continued access to sufficient capacity on reliable networks, we may be unable to deliver services and our sales could decrease. Our ability to grow and achieve profitability partly depends on our ability to buy sufficient capacity on the networks of wireless carriers such as Verizon Wireless, Bell South Corporation, Metrocall, Motient and AT&T Wireless and on the reliability and security of their systems. All of our services are delivered using airtime purchased from third parties. We depend on these companies to provide uninterrupted and bug free service and would not be able to satisfy our customers' needs if they failed to provide the required capacity or needed level of service. In addition, our expenses would increase and our profitability could be materially adversely affected if wireless carriers were to increase the prices of their services. Our existing agreements with the wireless carriers generally have one-year terms. Some of these wireless carriers are, or could become, our competitors and if they compete with us they may refuse to provide us with their services.

New laws and regulations that impact our law enforcement and public safety division could increase our costs or reduce our opportunities to earn revenue.

We are not currently subject to direct regulation by the Federal Communications Commission or any other governmental agency, other than regulations applicable to businesses in general. However, in the future, we may become subject to regulation by the FCC or another regulatory agency. In addition, the wireless carriers who supply us airtime and certain of our hardware suppliers are subject to regulation by the FCC and regulations that affect them could increase our costs or reduce our ability to continue selling and supporting our services.

We granted a blanket security interest in all of our assets to the holders of our secured debt. If we are unable to make our required monthly payments on such debt, or any other event of default occurs, it could have a material adverse effect on our business and operations, and the debt holders may foreclose on our assets.

As part of our recent secured convertible debt financing transactions, we granted to Laurus Master Fund, Ltd. and another holder of such secured debt a blanket security interest in all of our assets, including assets of our subsidiary. See the "Convertible Debt Financing Transactions" section of this prospectus. In the event we default in payment on such debt, or any other event of default occurs under the relevant financing documents, 120% of the outstanding principal amount of the secured notes, plus accrued interest and fees will accelerate and be due and payable in full. See the "Convertible Debt Financing Transactions" section of this prospectus for a list of such potential events of default.

The cash required to pay such accelerated amounts on the secured notes following an event of default would most likely come out of our working capital. As we rely on our working capital for our day to day operations, such a default could have a material adverse effect on our business, operating results, or financial condition to such extent that we are forced to restructure, file for bankruptcy, sell assets or cease operations. In addition, upon an event of default, the holder of the secured debt could foreclose on our assets or exercise any other remedies available to them. If our assets were foreclosed upon, we were forced to file for bankruptcy or cease operations, stockholders may not receive any proceeds from disposition of our assets and may lose their entire investment in our stock.

Our obligations under our recently issued debt securities may adversely affect our ability to enter into potential significant transactions with other parties.

As a result of our recent debt financing transactions with Laurus Master Fund, Ltd., The Shaar Fund, Ltd. and other institutional and accredited investors, we incurred significant repayment obligations and we agreed to certain restrictive covenants. In particular, for so long as 25% of the aggregate principal amount of the convertible term notes remains outstanding, we will need the consent of the holders of such notes before we can take certain actions, including the following:

- pay any dividends;
- merge, effect a material reorganization, liquidate or dissolve;
- materially change the scope of our business; or
- create, incur or assume any debt (other than certain trade debt, equipment financings and debt for the purchase of assets in the ordinary course of business).

Accordingly, unless we obtain the noteholders' consent, we may not be able to enter into certain transactions. In addition, in connection with any potential significant transaction (such as a merger, sale of substantially all our assets, joint venture, or similar transaction), it is likely that we would have to pay off such debt obligations and have the applicable security interests released. Although we have the right at any time to prepay our debt obligations, we can only do so upon payment of 110% of the then principal balance, plus all other amounts owing under the notes. See the "Convertible Debt Financing Transactions" section of this prospectus. Based on an aggregate principal balance of $10 million, a complete prepayment would require a cash payment of $11 million. These provisions could have the practical effect of increasing the costs of any potential significant transaction, and restrict our ability to enter into any such transaction.

Our obligations to the holders of our outstanding preferred stock may further affect our ability to enter into potential significant transactions with other parties.

We will need to obtain the consent of the holders of a majority of the then outstanding shares of our Series C preferred stock before we can take certain actions, including the following:

- a sale or other disposition of any material assets;
- an acquisition of a material amount of assets;
- engaging in a merger, reorganization or consolidation; or
- incur or guaranty any indebtedness in excess of $50,000.

Accordingly, unless we obtain such consent, we may not be able to enter into certain transactions.

Risks Related To Our Common Stock

We have issued a substantial number of securities convertible into shares of our common stock which will result in substantial dilution to the ownership interests of our existing shareholders.

As of October 28, 2004, approximately 34,113,323 shares of our common stock were reserved for issuance upon exercise or conversion of the following securities:

- 8,946,933 shares upon conversion of outstanding convertible term notes;
- 14,737,915 shares upon exercise of outstanding stock options and warrants;
- 804,208 shares upon exercise of options available for future grant under our existing option plans; and
- 9,624,267 shares or more upon conversion of our outstanding shares of Series C convertible preferred stock.

The exercise or conversion of these securities will result in a significant increase in the number of outstanding shares and substantially dilute the ownership interests of our existing shareholders.

A substantial number of our convertible securities are convertible into shares of common stock at a conversion price of $.75 per share. Most of these shares are eligible for public resale. The trading price of our common stock and our ability to raise additional financing may be adversely effected by the influx into the market of such a substantial number of shares.

Our outstanding convertible preferred stock is convertible into 9,624,267 shares of common stock at a per share conversion price of $.75 which is substantially less than the current trading price of our shares. Although many of the shares issuable upon conversion of our convertible preferred stock are eligible for public resale under Securities and Exchange Commission Rule 144, we have agreed to file a registration statement to cover the public resale of all of these shares. This significant increase in the number of shares available for public sale may have a negative impact on the trading price of our shares and substantially dilute the ownership interests of our existing shareholders. In the event that our stock trades below $.75 per share, in order to raise additional financing we would likely be required to issue additional shares of common stock or securities convertible into common stock at a purchase or conversion price, as applicable, of less than $.75 per share. Any issuance of shares at a purchase price of less than $.75 per share would reduce the conversion price of our Series C preferred shares to such lower price. This would require us to issue additional shares upon conversion of our Series C preferred shares and further dilute the ownership interests of our existing shareholders. To the extent these factors are viewed negatively by the market, it may provide an incentive for persons to execute short sales of our common stock that could adversely affect the trading price of our common stock.

Applicable Securities and Exchange Commission rules governing the trading of "penny stocks" limits the trading and liquidity of our common stock which may affect the trading price of our common stock.

Our common stock currently trades on the OTC Bulletin Board. Because our common stock continues to trade below $5.00 per share, our common stock is considered a "penny stock" and is subject to Securities and Exchange Commission rules and regulations which impose limitations upon the manner in which our shares can be publicly traded. These regulations require the delivery, prior to any transaction involving a penny stock, of a disclosure schedule explaining the penny stock market and the associated risks. Under these regulations, certain brokers who recommend such securities to persons other than established customers or certain accredited investors must make a special written suitability determination regarding such a purchaser and receive such purchaser's written agreement to a transaction prior to sale. These regulations have the effect of limiting the trading activity of our common stock and reducing the liquidity of an investment in our common stock.

We do not intend to pay dividends in the foreseeable future.

We have never declared or paid a dividend on our common stock. In addition, the terms of our outstanding Series C preferred shares preclude us from declaring or paying a dividend on our common stock unless a dividend is also declared or paid, as applicable, on our Series C preferred shares. We intend to retain earnings, if any, for use in the operation and expansion of our business and, therefore, do not anticipate paying any dividends on our common stock in the foreseeable future.

The trading price of our common stock may be volatile.

The trading price of our shares has from time to time fluctuated widely and in the future may be subject to similar fluctuations. The trading price may be affected by a number of factors including the risk factors set forth in this prospectus as well as our operating results, financial condition, announcements of innovations or new products by us or our competitors, general conditions in the biometrics and access control industries, and other events or factors. Although we believe that approximately fifteen (15) registered broker dealers currently make a market in our common stock, we cannot assure you that any of these firms will continue to serve as market makers or have the financial capability to stabilize or support our common stock. A reduction in the number of market makers or the financial capability of any of these market makers could also result in a decrease in the trading volume of, and price of, our shares. In recent years, broad stock market indices, in general, and the securities of technology companies, in particular, have experienced substantial price fluctuations. Such broad market fluctuations may adversely affect the future trading price of our common stock.

Minnesota anti-takeover law and certain provisions of our articles of incorporation may discourage attempts to effect a change in control of our company, which may adversely affect the value of our common stock.

We are governed by the provisions of Section 302A.673 of the Minnesota Business Corporation Act ("MBCA"). In general, the law prohibits a public Minnesota corporation from engaging in a "business combination" (with an "interested shareholder") for a period of four years after the date of the transaction in which the person became an interested shareholder, unless the business combination is approved in a prescribed manner. A "business combination" includes mergers, share exchanges, asset sales, plan or proposal of liquidation or dissolution, recapitalization, issuance and transfers of shares in excess of five percent (5%) or more of the Company's shares. An "interested shareholder" means any person who owns directly or indirectly ten percent (10%) or more of a public corporation's outstanding voting stock or an affiliate or associate of a public corporation which owns, or within four years did own, ten percent (10%) or more of the public corporation's outstanding voting stock. These provisions regarding certain business combinations under the MBCA could have the effect of delaying, deferring, or preventing a change in control of the company or the removal of existing management. We have no control over, and therefore cannot predict, what effect these impediments to the ability of third parties to acquire control of us might have on the market price of our common stock. In addition, we are authorized to issue 5,000,000 shares of preferred stock which may be issued by our Board of Directors on such terms and with such rights, preferences and designations as the Board may determine. Depending upon the rights, preferences and designations assigned to it, issuance of shares of preferred stock could delay, deter or prevent a change in control of our company to the detriment of our shareholders.

The selling security holders intend to sell their shares of common stock in the market, which sales may cause our stock price to decline.

The selling stockholders named in this prospectus intend to sell in the public market 11,723,152 shares of our common stock being registered in this offering. That means that up to 11,723,152 shares may be sold pursuant to this registration statement. Such sales may cause our stock price to decline. Our officers and directors and those shareholders who are significant shareholders as defined by the Securities and Exchange Commission will continue to be subject to the provisions of various insider trading and Rule 144 regulations.

FORWARD-LOOKING STATEMENTS

This prospectus contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, or the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act. All statements other than statements of historical facts contained in this prospectus, including statements regarding our future financial position, business strategy and plans and objectives of management for future operations, are forward-looking statements. The words "anticipate," "believe," "estimate," "will," "may," "future," "plan," "intend" and "expect" and similar expressions generally identify forward-looking statements. Although we believe that our plans, intentions and expectations reflected in the forward-looking statements are reasonable, we cannot be sure that they will be achieved. Actual results may differ materially due to a number of factors. Many of these factors are set forth in the "RISK FACTORS" section of this prospectus. Actual results may differ materially from the forward-looking statements contained in this prospectus. These factors are not intended to represent a complete list of the general or specific factors that may affect us. It should be recognized that other factors, including general economic factors and business strategies, may be significant, presently or in the future. Except as required by law, we undertake no obligation to update any forward-looking statement, whether as a result of new information, future events or otherwise.

USE OF PROCEEDS

The shares are being registered hereunder for resale by the selling security holders. We will not receive any proceeds from the sale of the shares by the selling security holders. We will receive the proceeds from the exercise price of certain warrants held by the selling security holders to the extent that such warrants are exercised. We expect to use the proceeds of any such sales for general working capital purposes.

MARKET FOR OUR COMMON STOCK AND RELATED STOCKHOLDER MATTERS

Our common stock currently trades on the OTC Bulletin Board under the symbol "BKYI." The following table sets forth the range of high and low bid prices per share of our common stock for each of the calendar quarters identified below as reported by the OTC Bulletin Board. These quotations represent inter-dealer prices, without retail mark-up, markdown or commission, and may not represent actual transactions.

	High	Low
2004:		
Quarter ended September 30, 2004	$ 1.43	$ 0.60
Quarter ended June 30, 2004	$ 3.00	$ 1.26
Quarter ended March 31, 2004	$ 1.85	$ 1.03
2003:		
Quarter ended December 31, 2003	$ 1.40	$ 0.53
Quarter ended September 30, 2003	$ 0.59	$ 0.38
Quarter ended June 30, 2003	$ 0.64	$ 0.30
Quarter ended March 31, 2003	$ 0.73	$ 0.35
2002:		
Quarter ended December 31, 2002	$ 0.74	$ 0.33
Quarter ended September 30, 2002	$ 0.50	$ 0.26
Quarter ended June 30, 2002	$ 0.75	$ 0.38
Quarter ended March 31, 2002	$ 1.20	$ 0.61

The last price of our common stock as reported on the OTC Bulletin Board on December 7, 2004 was $1.01 per share.

Holders

As of October 25, 2004 the number of stockholders of record of our common stock was 220. Based on broker inquiry conducted in connection with the distribution of proxy solicitation materials in connection with the Company's special meeting of shareholders on August 16, 2004, we believe that there are approximately 3,500 beneficial owners of its common stock.

Dividends

We have not paid any cash dividends to date, and have no intention of paying any cash dividends on our common stock in the foreseeable future. The terms of our outstanding Series C preferred shares preclude us from declaring or paying a dividend on our common stock unless a dividend is also declared or paid, as applicable, on our Series C preferred shares. The declaration and payment of dividends is also subject to the discretion of our Board of Directors and certain limitations imposed under the Minnesota Business Corporation Act. The timing, amount and form of dividends, if any, will depend on, among other things, our results of operations, financial condition, cash requirements and other factors deemed relevant by our Board of Directors.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Management's Discussion and Analysis of Financial Condition and Results of Operations and other parts of this prospectus contain forward-looking statements that involve risks and uncertainties. All forward-looking statements included in this prospectus are based on information available to us on the date hereof, and we assume no obligation to update any such forward-looking statements. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of a number of factors, including those set forth in the section captioned "RISK FACTORS" and elsewhere in this prospectus. The following should be read in conjunction with our audited financial statements included elsewhere herein.

Overview

The following should be read in conjunction with the consolidated financial statements of the Company included elsewhere herein.

We develop and market proprietary fingerprint identification biometric technology and software solutions. We pioneered the development of automated, finger identification technology that can be used without the aid of non-automated methods of identification such as a personal identification, password, token, smart card, ID card, credit card, passport, driver license or other form of possession or knowledge based identification. This advanced BIO-key identification technology improves both the accuracy and speed of finger-based biometrics and is the only finger identification algorithm that has been certified by the International Computer Security Association (ICSA).

Since our inception in 1993, we have spent substantial time and effort in completing the development of what we believe is the most discriminating and effective finger biometric technology available. During the past two years, our focus has shifted to marketing and licensing this technology. We have built a direct sales force of professionals with substantial experience in selling technology solutions to government and corporate customers. We expect to continue to add additional qualified personnel in 2004.

During 2003 and the first two quarters of 2004, we entered into a number of licensing and development agreements. Certain of these arrangements have resulted in our technology being used in commercial applications on a run time basis and we are beginning to generate recurring revenue. We will continue to focus a substantial amount of resources on our sales and marketing efforts and expect revenues to increase substantially during 2004. Our primary objective in 2004 is to generate revenue and increase the recognition, use and acceptance of our technology in the market. To accomplish this, all sales efforts are focused on moving evaluation and development relationships to run time license arrangements as quickly as possible. We continue to see increases in qualified leads resulting in evaluation licenses and run time licenses. Our biggest challenge is obtaining financial and human resources to pursue and follow up on all opportunities available to us.

Although recent security concerns relating to the identification of individuals has increased interest in biometrics generally, it has yet to gain widespread commercial acceptance. We continue to see increasing acceptance of biometric technology, however, and believe the market for our technology is large enough for us to become a successful revenue generating company. Continued concerns regarding security and increased corporate spending on technology are key external conditions which may affect our ability to execute our business plan.

On March 30, 2004, we acquired all of the outstanding capital stock of PSG, a privately-held provider of wireless solutions for law enforcement and public safety markets based in Winter Park, Florida, in exchange for an aggregate of 2,422,108 shares of our common stock, $500,000 in cash, and our assumption of $600,000 in aggregate net liabilities of PSG. The acquisition was completed pursuant to the terms of an agreement and plan of merger by and among the Company, BIO-Key Acquisition Corp., a wholly-owned subsidiary of the Company, PSG and all of the shareholders of PSG. As a result of this transaction, PSG became a wholly-owned subsidiary of the Company and now constitutes a division of our business specializing in the law enforcement and public safety markets.

On March 31, 2004, we completed a private placement equity offering that resulted in approximately $12,000,000 in gross proceeds to the Company. Based on available cash resources, existing funding obligations and projected revenue, we believe our existing financial resources will now be sufficient to sustain operations for at least the next twenty-four (24) months. Our long-term viability and growth will depend upon the successful commercialization of our technologies and our ability to obtain adequate financing, among other matters, as to which there can be no assurances.

As more fully described in our Proxy Statement filed on July 21, 2004 with the Securities and Exchange Commission, we are actively pursuing strategic acquisitions that are expected to be accretive to operating results. To enable us to respond rapidly to acquisition opportunities, and to meet other future needs that could arise, we have obtained shareholder approval to raise the number of shares of common stock that we are authorized to issue from 60 million to 85 million. In that regard, on September 30, 2004, we completed our previously announced acquisition of Aether Mobile Government from Aether. Pursuant to the Asset Purchase Agreement dated as of August 16, 2004 by and among the Company, Aether, Cerulean Technology, Inc. and SunPro, Inc., the Company paid Aether a purchase price of $10,000,000 in cash, subject to post-closing adjustments to reflect changes in Aether Mobile Government's working capital and cash flows since June 30, 2004. In connection with this acquisition, the Company issued a subordinated secured promissory note to Aether in the face amount of $6,884,588 (the "Aether Note"). The Aether Note evidences a contingent reimbursement obligation of the Company to Aether and a surety fee payable by the Company to Aether, in each case with respect to a letter of credit maintained by Aether for the Company's benefit in connection with the acquisition. The Company's obligations under the Aether Note are secured by a security interest granted to Aether in all or substantially all of the Company's assets, subordinate to the security interest described in the "Convertible Debt Financing Transactions" section of this prospectus below.

Aether Mobile Government provides wireless data solutions for use by public safety organizations, primarily state and local police, fire and rescue and emergency medical services organizations, that enable such organizations to access law enforcement databases to validate identities and obtain suspect information. Its public safety solutions are integrated into fifty (50) different state databases, as well as local and federal databases, and its products deliver real-time information in seconds, without the need for human dispatchers or other resources.

On September 29, 2004, we entered into a securities purchase agreement with certain institutional and accredited investors. Under this agreement, the Company issued secured convertible term notes in the aggregate principal amount of $5,050,000, convertible into common stock of the Company in certain circumstances at $1.35 per share, and issued warrants to purchase an aggregate of 1,122,222 shares of our common stock at an exercise price of $1.55 per share. The Company's obligations under these financing documents are secured by a security interest in all or substantially all of the Company's assets. Also on September 29, 2004, we entered into a separate securities purchase agreement with existing shareholders of the Company and other accredited investors. Under this agreement, the Company issued unsecured convertible term notes in the aggregate principal amount of $4,950,000, convertible into common stock of the Company in certain circumstances at $1.35 per share, and issued warrants to purchase an aggregate of 1,099,997 shares of our common stock at an exercise price of $1.55 per share. The proceeds from each of these transactions were used in part to finance a portion of the Company's acquisition of Aether Mobile Government and will be used in part for working capital purposes.

Results of Operations

The discussion below regarding our results of operations for the three and nine months ended September 30, 2004 reflects the combined operations of our historic biometric technology licensing business *and our new public safety division, comprised of the former PSG whereas the corresponding periods in 2003 include only the operations of our historic biometric business. In order to present the following discussion in a manner to provide a more meaningful comparison between the two periods, where possible, we have quantified the material changes in our results of operations which are attributable to the operations of each of our businesses. Because the acquisition of the Mobile Government division of Aether Systems was not completed until September 30, the results of operations for Mobile Government are not included in the three and nine month periods ending September 30, 2004. The acquired assets and liabilities are included in our balance sheet as of September 30, 2004.*

Three Months and Nine Months Ended September 30, 2004 As Compared To Three Months and Nine Months Ended September 30, 2003

Revenue

We generated revenues of approximately $309,000 during the three month period ended September 30, 2004 as compared to approximately $147,000 during the corresponding period in 2003. Of this amount, approximately $101,000 was generated by our biometric technology business, a decrease of $46,000 from the corresponding period in 2003. This decline was due to timing of customer orders. PSG, our law enforcement and public safety division which we acquired on March 30, 2004, accounted for approximately $207,000 of the remaining revenue during the three month period ended September 30, 2004.

We generated revenues of approximately $1,140,000 during the nine month period ended September 30, 2004 as compared to approximately $188,000 during the corresponding period in 2003. Of this amount, approximately $354,000 was generated by our biometric technology business, representing an approximate $167,000 increase over the corresponding period in 2003. This increase was due to an additional number of licensing arrangements, some of which have moved from evaluation to recurring run time licenses. Our law enforcement and public safety division accounted for approximately approximately $785,000 of the remaining revenue during the nine month period ended September 30, 2004.

Consolidated revenue during the nine month period ended September 30, 2004 consisted of approximately $863,000 from license fees, approximately $135,000 from product sales and approximately $142,000 from technical support services. We expect over the next several quarters, the majority of our biometrics and PSG revenue will come from license fees and with technical support and product sales contributing the balance. As our evaluation customers move to run time licensing arrangements, we expect technical support fees to comprise a larger percentage of these revenues and provide additional recurring monthly revenue. With the acquisition of Mobile Government on September 30, 2004, we expect the majority of our consolidated revenue for the next several quarters to be generated from existing Mobile Government customers. Mobile Government revenue is composed of recurring maintenance revenue, licensed software and related services and third party hardware. We will continue to expand our sales and marketing departments in the expectation of additional biometric, PSG and Mobile Government customers and revenue during 2004.

Costs and Other Expenses

Cost of products and services sold were approximately $25,000, or 8% of revenue during the three month period ended September 30, 2004 as compared to approximately $2,600 or 2% of revenue during the corresponding period in 2003. Of this amount, approximately $22,600 was associated with sales by our biometric technology business, a slight increase from the corresponding period. Approximately $2,900 of the remaining cost of products sold in 2004 was attributed to our law enforcement and public safety division.

As our revenue and customer base continues to grow, we expect these costs to continue to increase. Most initial sales by our law enforcement and public safety division involve the sale of a PDA, and most initial sales by our biometrics business involve the sale of a scanner. Sales by our Mobile Government division typically require engineering, program management and technical resources to install products and service customers. During the next several quarters, we expect cost of products on a consolidated basis to continue to increase as the Company's revenues shift towards larger customer contracts. The company's future gross margin will depend on several variables, including; pricing of license, support and product sales and the amount of product sales. Although we generate a margin on hardware sales, our future earnings, if any, will depend primarily upon licensing and technical support fees.

For the nine month period ending September 30, 2004, cost of products and services sold were approximately $126,000 or 11% of revenue as compared to approximately $8,000 or 4% of revenue during the corresponding period in 2003. Of this amount, approximately $59,000 was attributed to sales by our biometric technology business, representing an increase of $51,000 from the corresponding period in 2003. Costs associated with revenues from pubic safety division totaled approximately $67,000 for the nine months ending September 30, 2004.

Selling, general and administrative expenses increased by approximately $1,222,000 to approximately $1,733,000 during the three months ended September 30, 2004 as compared to approximately $511,000 during the corresponding period in 2003. Of this total amount, approximately $1,255,000 was incurred by our biometric technology business, representing a $744,000 increase over the corresponding period in 2003. The increased biometric spending was due to additional investments in sales and marketing of approximately $213,000, for additional operating expenses and increased staffing levels, and approximately $531,000 increase in general and administrative spending. The increase in general and administrative spending is largely due to additional spending of approximately $350,000 for professional services associated with the purchase of Mobile Government and the related filings with the Security and Exchange commission. Approximately $478,000 of the remaining selling, general and administrative expenses were incurred by our public safety division.

While we continue to closely monitor expenses, we intend to hire additional employees in sales, technology and finance positions. As the company grows, we expect continued increases in these functions during 2005 as part of our focus on generating additional revenue and supporting our growing customer base. Accordingly, we expect selling, general and administrative expenses to continue to increase during 2004.

For the nine month period ending September 30, 2004, selling, general and administrative expenses increased by approximately $2,352,000 to $3,901,000 as compared to approximately $1,549,000 for the corresponding period in 2003. Of this total amount, $2,954,000 was incurred by our biometric technology business, representing a $1,405,000 increase over the corresponding period in 2003. The remaining increase of approximately $947,000 was incurred by our public safety division.

Of the approximately $2,352,000 increase in selling, general and administrative expenses during the nine months period ended September 30, 2004, $683,000 was due to an increase in sales and marketing costs as we continue to focus resources to generating revenue, and approximately $1,669,000 was due to an increase in general administrative costs related to the integration of PSG and Mobile Government, increased professional service expenses incurred in connection with additional Securities and Exchange Commission filings, and related activities.

Research, development and engineering expenses increased by approximately $206,000 to approximately $453,000 during the three months ended September 30, 2004 as compared to approximately $247,000 during the corresponding period in 2003. Of this amount, approximately $318,000 was incurred by our biometric technology business, representing a $71,000 increase over the corresponding period in 2003. The remaining increase of $135,000 was incurred by our public safety division. Of the approximately $71,000 increase in biometrics research, development and engineering expenses, approximately $3,000 was related to an increase in general development expense, approximately $21,000 was related to an increase in personnel costs and approximately $47,000 was related to sub contractors or temporary workers.

Having completed the development of our biometrics core technology, biometrics research and development expenses during the remainder of 2004 will consist of enhancing existing software and responses to customer feedback. PSG research and development expenses are not anticipated to significantly increase at this time.

For the nine month period ending September 30, 2004, research, development and engineering expenses increased to approximately $1,067,000 as compared to approximately approximately $721,000 during the corresponding period in 2003. Of this amount, approximately $856,000 was incurred by our biometric technology business, representing an $135,000 increase over the corresponding period in 2003. Of the remaining increase, approximately $211,000 was incurred by our public safety division. Of the $346,000 total increase in research, development and engineering expenses approximately $24,000 was related to an increase in general development expense, approximately $255,000 was associated with increased personnel costs and approximately $67,000 was due to increased use of contractors and temp workers.

Interest expense was approximately $1,000 and $138,000 during the three and nine month periods ended September 30, 2004, respectively, as compared to approximately $318,000 and $912,000 during the corresponding periods in 2003, respectively. Substantially all of the interest expense was incurred by our biometric technology business. The decrease in interest expense during the three and nine months ended September 30, 2004 was due to the decrease in the long-term obligations during these periods. On September 29, 2004 the company incurred new long-term obligations in the amount of $9,419,000.

Year Ended December 31, 2003 As Compared To Year Ended December 31, 2002:

Revenues

We generated revenues of approximately $524,000 during 2003 as compared to approximately $155,000 during 2002. Our 2003 revenues consisted of approximately $411,000 from license fees and approximately $113,000 from products and services as compared to approximately $131,000 from license fees and approximately $24,000 from sales of products and services during 2002. We expect ninety percent (90%) of our future revenues to be generated from license fees and the balance from product sales. We expect revenues to continue to increase during 2004, as we enter into new licensing arrangements and our existing arrangements lead to recurring run time licenses.

Costs and Other Expenses

Selling, general and administrative expenses. Selling, general and administrative expenses increased approximately $192,000 to approximately $2,118,000 during 2003 as compared to approximately $1,926,000 in 2002. Of the increase, approximately $182,000 was related to increased sales and marketing activity, approximately $137,000 was related to an increase in general administrative costs, approximately $266,000 was related to an increase in costs for administrative personnel, and approximately $76,000 was related to an increase in professional services. These amounts were offset by a decrease in marketing consulting costs of approximately $469,000 in 2003. Although we continue to closely monitor expenses, we expect marketing, sales and technical support expenses to increase in 2004 as we continue to focus on generating revenue and supporting our growing customer base. Accordingly, we expect selling, general and administrative expenses to increase during 2004.

Research and Development. Research, development and engineering expenses decreased approximately $47,000 to approximately $1,037,000 in 2003 as compared to approximately $1,084,000 in 2002. Of the decrease, approximately $58,000 was related to a decrease in general development expense, and approximately $44,000 was related to a decrease for services of outside programming sub-contractors. This was offset by an approximate $55,000 increase in personnel costs. Having completed the development of our core technology, research and development expenses in 2004 will consist of enhancing existing software and reacting to customer feedback. We expect research and development costs to stabilize during 2004.

Interest Expense. Interest expense decreased approximately $53,000 to approximately $1,110,000 in 2003 as compared to approximately $1,163,000 in 2002. The decrease was due to a net decrease during 2003 of the amortization of discounts applicable to convertible debt issued during 2001 arising from the warrants issued with such convertible debt and the beneficial conversion features of such debt. We recently converted $6.5 million of long term debt and accrued interest into convertible preferred stock. Unless we are required to raise any necessary financing through issuance of debt securities, we expect interest expenses to decrease substantially in 2004.

Net Operating Loss Carryforwards

As of December 31, 2003 we had federal and Minnesota net operating loss carryforwards of approximately $24,504,000 and $12,406,000 respectively. Because the company expects to incur additional losses during 2004 and 2005, and because these loss carryfowards are further limited in value by changes in the ownership of the Company, as defined in the Internal Revenue Code, these loss carryforwards have a valulation allowance against them. These carryforwards expire between 2011 and 2023.

Liquidity and Capital Resources

Net cash used in operating activities during the nine months ended September 30, 2004 was approximately $3,645,000 compared to approximately $2,049,000 during the nine months ended September 30, 2003. The primary use of cash for both years was to fund the net losses. Net cash used in investing activities for the nine months ended September 30, 2004 was approximately $14,614,000 compared to net cash used in investing activities of approximately $100,000 for the corresponding period in 2003, and consisted primarily of $10,090,000 invested in the acquisition of Mobile Government division, approximately $499,000 invested in the acquisition of PSG, approximately $2,769,000 used for deposits, a net investment in securities of approximately $967,000, and approximately $163,000 invested in capital equipment additions. Net cash provided by financing activities during the nine months ended September 30, 2004 was approximately $20,047,000 compared to approximately $2,191,000 in the corresponding period in 2003 and consisted primarily of approximately $11,249,000 from sales of our common stock and approximately $9,483,000 from long term borrowings. These increases were offset by approximately $400,000 for a note repayment, approximately $80,000 for financing fees, approximately $125,000 for repurchasing warrants, approximately $49,000 in repayment of advances from a shareholder, and approximately $31,000 for other items.

Working capital decreased approximately $902,000 during the nine months ended September 30, 2004 to approximately $183,000 compared to approximately $1,085,000 as of December 31, 2003. The decrease in working capital was due to an increase in current liabilities of approximately $12,990,000, offset by an increase in current assets of approximately $12,088,000. The increase in current liabilities included approximately $4,745,000 of deferred revenue, approximately $4,291,000 of accrued liabilities, approximately $2,159,000 of the current portion of long term debt, approximately $1,369,000 of accounts payable and approximately $426,000 in other liabilities. During the same period, current assets increased by approximately $6,620,000 in costs and earnings in excess of billings on uncompleted contracts, approximately $3,079,000 in accounts receivables and approximately $1,959,000 in cash. Changes in other current assets totaled approximately $430,000 for the nine months ending September 30, 2004.

Since January 7, 1993 (date of inception), our capital needs have been principally met through proceeds from the sale of equity and debt securities. We do not currently maintain a line of credit or term loan with any commercial bank or other financial institution. As of the date of this report, we had cash resources of approximately $3,700,000 and no debt other than as described above with respect to the Senior Investors and Subordinated Investors and current liabilities. We currently require approximately $500,000 per month to conduct our operations. During the first three quarters of 2004, we generated approximately $1,140,000 of revenue and expect to continue to generate increasing revenue from existing and new relationships during 2004.

On October 31, 2003, we entered into an amendment to the January 27, 2003 note purchase agreement with The Shaar Fund Ltd. ("Investor") to provide up to $2,500,000 of additional financing pursuant to the terms of a secured promissory note (the "Secured Note"). Of this amount, $600,000 was advanced at closing and $1,900,000 was funded between December 3, 2003 and March 29, 2004. The Secured Note was due October 1, 2005, secured by substantially all of our assets including our intellectual property, accrued interest at the rate of 7% per annum payable on maturity, and may be prepaid without penalty. The principal amount and accrued interest was convertible at the option of the Investor into either shares of our common stock at a conversion price of $.75 per share or shares of our Series C preferred stock (the "Series C Shares") at a conversion price of $100 per share. The Secured Note also provided that in the event we completed a private placement of our equity securities resulting in gross proceeds in excess of $5,000,000 on or before June 30, 2004, some or all of the principal and accrued interest shall, at the option of the Investor, be either converted into such equity securities at a conversion price equal to the sale price of such securities or repaid in cash. Upon the closing of our recent private placement equity offering, the Investor elected to convert $347,500 of the principal amount of the Secured Note into shares of our common stock and warrants to purchase shares of our common stock, each issued to the Investor in connection with such private placement.

Pursuant to a recapitalization transaction completed on March 3, 2004, all existing promissory notes payable to the Investor, other than the Secured Note, together with all accrued and unpaid interest due thereon (approximately $6,500,000) were cancelled and converted into 65,000 Series C Shares. Series C Shares are convertible into common stock at a conversion price of $.75 per share. In the event that the average closing bid price of our common stock is less than $1.00 per share for thirty (30) consecutive days at any time after March 3, 2007, we will be required to redeem the Series C Shares at a redemption price of $100 per share plus all accrued and unpaid dividends due thereon. In connection with the recapitalization transaction, the Investor sold $375,000 of the principal amount of the Secured Note to Thomas J. Colatosti, our Chairman of the Board of Directors.

On March 30, 2004, the Investor elected to convert $1,827,463 of principal and accrued interest due under the Secured Note into 18,275 Series C Shares. Also on March 30, 2004, the Investor elected to exchange all of the issued and outstanding shares of our series B preferred stock and accrued and unpaid dividends thereon and all accrued and unpaid interest on such dividends into 5,257 additional Series C Shares. On April 29, 2004, Mr. Colatosti elected to convert $375,000 of the principal amount of the Secured Note into 3,750 Series C Shares. As a result of these conversions, as of the date of this report, we have no outstanding indebtedness other than as described in the "Convertible Debt Financing Transactions" section of this prospectus and current liabilities.

Between April 7, 2004 and June 21, 2004, we issued an aggregate of 2,237,198 shares of common stock upon conversion of 16,600 shares of the Company's Series C 7% Convertible Preferred Stock and $17,898 of dividends due theron to the Shaar Fund.

On March 31, 2004, we entered into a securities purchase agreement with certain institutional and accredited investors pursuant to which we issued and sold an aggregate of 8,888,928 shares of our common stock and warrants (the "Warrants") to purchase an aggregate of 4,444,464 shares of our common stock. The investors paid an aggregate purchase price of $1.35 for each share of common stock and Warrant to purchase 0.5 of a share of common stock, resulting in gross proceeds to of approximately $12,000,000.

On March 30, 2004, we completed the acquisition of PSG in exchange for an aggregate of 2,416,108 shares of our common stock, $500,000 in cash, and our assumption of $600,000 in net liabilities of PSG. Any liability or obligation of PSG in excess of such $600,000 limitation will be solely the responsibility of the former shareholders of PSG. In connection with this acquisition, we also issued 6,000 shares of our common stock to Harward Investments, Inc. ("Harward") pursuant to an arrangement involving the discharge of certain outstanding debt obligations of PSG to Harward as of March 30, 2004.

Additional earnout consideration, determined as a proportion of qualified revenues, as defined, attained by the acquired business during fiscal years 2004 and 2005, may be paid to the former shareholders of PSG. During 2004, earnout consideration, if any, will be paid at the following rates: Five percent (5%) of all 2004 Qualifying Revenue less than $2 million, less the Accounts Receivable Holdback; as defined; Ten percent (10%) of all 2004 Qualifying Revenue equal to or greater than $2 million but less than $4 million; Twenty percent (20%) of all 2004 Qualifying Revenue equal to or greater than $4 million but less than $7 million; and Thirty percent (30%) of all 2004 Qualifying Revenue equal to or greater than $7 million. During 2005, earnout consideration, if any, will be paid at the following rates: Ten percent (10%) of all 2005 Qualifying Revenue equal to or greater than $7 million but less than $10 million; and Twenty percent (20%) of all 2005 Qualifying Revenue equal to or greater than $10 million. We will make payments of such additional consideration on the last day of the month following each month in which the acquired business achieves specified revenue milestones during fiscal years 2004 and 2005. Such payments will be made in cash, unless the aggregate amount of earnout consideration exceeds sixty percent (60%) of the aggregate consideration we paid in the merger transaction. Any such excess amounts will be paid in shares of our common stock priced as of two (2) days prior to the date on which any earnout payment becomes due.

We have announced our intention to actively pursue strategic acquisitions that are expected to be accretive to operating results. We believe that an active acquisition strategy is timely because (i) companies with synergistic technology and/or market channels can combine to respond to the need in the homeland security market for complete technology solutions and to create operating efficiencies and (ii) there are many companies in the technology sector that have over-invested in the development stage and now lack sufficient financial resources to invest in the sales and marketing capabilities necessary for growth. To enable us to respond rapidly to acquisition opportunities, and to meet other future needs that could arise, we obtained shareholder approval to increase the number of shares we are authorized to issue from 60 million to 85 million. While some of these newly authorized shares could be used as currency for acquisitions, we may raise the additional capital required for acquisitions through the issuance of convertible instruments that would not be immediately convertible into common stock.

On September 30, 2004, we completed our acquisition of Aether Mobil Government. Pursuant to the Asset Purchase Agreement dated as of August 16, 2004 by and among the Company, Aether, Cerulean Technology, Inc. and SunPro, Inc., the Company paid Aether a purchase price of $10,000,000 in cash, subject to post-closing adjustments to reflect changes in Aether Mobile Government's working capital since June 30, 2004. In connection with this acquisition, the Company issued a Subordinated Secured Promissory Note to Aether in the face amount of $6,884,588 (the "Aether Note"). The Aether Note evidences a contingent reimbursement obligation of the Company to Aether and a surety fee payable by the Company to Aether, in each case with respect to a letter of credit maintained by Aether for the Company's benefit in connection with the acquisition. The Company's obligations under the Aether Note are secured by a security interest granted to Aether in all or substantially all of the Company's assets, subordinate to the security interest described in the "Convertible Debt Financing Transactions" section of this prospectus below.

On September 29, 2004, we entered into a Securities Purchase Agreement (the "Senior Purchase Agreement") with Laurus Master Fund, Ltd. ("Laurus") and certain other institutional and accredited investors (together with Laurus, the "Senior Investors"). Under the Senior Purchase Agreement, the Company issued secured convertible term notes (the "Senior Convertible Notes") in the aggregate principal amount of $5,050,000, convertible into common stock of the Company in certain circumstances at $1.35 per share, and issued warrants (the "Senior Warrants") to purchase an aggregate of 1,122,222 shares of our common stock at an exercise price of $1.55 per share. The proceeds from this transaction were used to finance in part the Company's acquisition of Aether Mobile Government. The Company's obligations under the Senior Purchase Agreement, the Senior Convertible Notes and the Senior Warrants are secured by a security interest in all or substantially all of the Company's assets.

Also on September 29, 2004, we entered into a Securities Purchase Agreement (the "Subordinated Purchase Agreement") with the Investor and other existing shareholders of the Company and accredited investors (collectively, the "Subordinated Investors"). Under the Subordinated Purchase Agreement, the Company issued unsecured convertible term notes (the "Subordinated Convertible Notes") in the aggregate principal amount of $4,950,000, convertible into common stock of the Company in certain circumstances at $1.35 per share, and issued warrants (the "Subordinated Warrants") to purchase an aggregate of 1,099,997 shares of our common stock at an exercise price of $1.55 per share. The proceeds from this transaction were used in part to finance a portion of the Company's acquisition of Aether Mobile Government and will be used in part for working capital purposes. Please see the "Convertible Debt Financing Transactions" section of this prospectus for a more complete description of the transactions consummated in connection with the Senior Purchase Agreement and the Subordinated Purchase Agreement.

Our future liquidity and capital requirements will depend upon numerous factors, including:

- our ability to license our technology to original equipment manufacturers, systems integrators and application developers;
- our ability to successfully integrate PSG's and Aether Mobile Government's technology and customer relationships into our current business plan;
- the costs and timing of product development efforts and the success of these efforts;
- our ability to maintain and grow quality customer base; and
- biometric technology market developments.

As of the date of this prospectus, we had cash resources of approximately $3,200,000 and no debt other than as described in the "Convertible Debt Financing Transactions" section of this prospectus and current liabilities. We currently require approximately $400,000 per month to conduct our operations. During the first two quarters of 2004, we generated approximately $831,000 of revenue and expect to continue to generate increasing revenue from existing and new relationships during 2004.

We now believe our current cash resources and anticipated cash flow from current operations will enable us to maintain operations at current levels for at least the next twenty-four (24) months. We may need to obtain additional funding to (i) conduct the sales, marketing and technical support necessary to execute our plan to substantially grow operations, increase revenue and serve a significant customer base; and (ii) pursue our acquisition strategy. While anticipated revenues are expected to defray operating expenses and reduce the need for additional financing, they are not expected to be sufficient for us to significantly expand operations. To the extent that we would require such additional funding, no assurance can be given that any form of additional financing will be available on terms acceptable to us, that adequate financing will be obtained to meet our needs, or that such financing would not be dilutive to existing stockholders. If available financing is insufficient or unavailable or we fail to continue to generate meaningful revenue, we may be required to further reduce operating expenses, delay the expansion of operations, or be unable to pursue merger or acquisition candidates.

DESCRIPTION OF THE BUSINESS

Overview

The Company was formed in 1993 and is in the business of delivering advanced identification solutions and information services to law enforcement departments, public safety agencies and other government and private sector customers. Our mobile wireless technology provides first responders with critical, reliable, real-time data and images from local, state, and national databases. More than 2,500 police, fire and emergency services departments in North America currently utilize the our solutions, making us a leading supplier of mobile and wireless solutions for public safety. Our scalable biometric finger identification technology identifies and authenticates users of wireless and enterprise data to improve security, convenience and privacy as well as reducing identity theft. Biometric technology, the science of analyzing specific human characteristics which are unique to each individual in order to identify a specific person from a broader population, is an emerging technology. Fingerprint analysis is an accurate and reliable method to distinguish one individual from another and is viewed as less intrusive than many other biometric identification methods. As a result, fingerprint analysis has gained the most widespread use for biometric identification. Biometric technology represents a novel and accurate approach to identity verification and authentication which is now being used in limited applications and is gaining acceptance in the government, commercial and consumer markets.

We have pioneered the development of high performance automated finger identification technology that can be used without the aid of non-automated methods of identification such as a personal identification number (PIN), password, token, smart card, ID card, credit card, passport, driver license or other form of possession based or knowledge based identification.

Our advanced BIO-key identification technology improves both the accuracy and speed of finger-based biometrics and is the only finger identification algorithm that has been certified by the International Computer Security Association. Our proprietary biometric technology scans a person's fingerprint and identifies a person, typically within a few seconds, without the use of any other identifying data. We believe our fingerprint identification technology will have a broad range of possible applications relating to information security and access control, including:

- Securing Internet sites and electronic transactions
- Securing access to logical networks and applications
- Securing access to buildings and restricted areas
- Securing mobile devices such as cell phones and PDA's

In addition to these technologies, on March 30, 2004, we acquired Public Safety Group, Inc. ("PSG"), a privately held leader in wireless solutions for law enforcement and public safety markets. PSG's primary technology, PocketCop©, is a software solution that provides police officers and other security personnel instantaneous access to important criminal, civil and private database information in a wireless environment. PocketCop© is the first and only copyrighted handheld application that allows law enforcement officers to access state and federal databases over the wireless network for PalmOS, Windows CE and PocketPC. With the use of a portable wireless handheld device and PocketCop© application software, an authorized user can access suspect information such as wanted status, warrant status, vehicle registration and driver license status. PSG has deployed its technology in numerous police departments in the United States, including the statewide deployment for the Massachusetts State Police and has developed a number of important strategic marketing partnerships including Hewlett Packard.

On September 30, 2004, we completed a transaction with Aether Systems, Inc. to purchase its Mobil Government division ("Aether Mobil Government"). Aether Mobile Government provides wireless data solutions for use by public safety organizations, primarily state and local police, fire and rescue and emergency medical services organizations. Its public safety solutions are integrated into fifty (50) different state databases, as well as local and federal databases, and its products deliver real-time information in seconds, without the need for human dispatchers or other resources. Together with PSG, Aether Mobile Government now comprises the Law Enforcement and Public Safety Division of our business.

Our current business plan is to:

- License our core technology "VST" to original equipment manufacturers, systems integrators and application developers to develop products and applications which utilize our core technology.
- License WEB-key , our web-based biometric authentication solution.
- Provide for "device independent" finger identification matching for virtually any application utilizing the latest advances in scanning technology.
- License our wireless software solutions for law enforcement and public safety markets.

We actively market and sell our technology principally to biometric system integrators and value added resellers focused on the security and logical access markets. A number of our customers have begun to deploy our technology on a run-time basis which is generating recurring quarterly revenues. After years of technology and product development, we have evolved from a development stage company to a revenue generating company.

Market Overview

Recent concerns relating to Homeland Security and the need for identification of individuals has resulted in an increased interest in biometrics. Biometric based solutions currently compete with more traditional security methods such as keys, cards, personal identification numbers and security personnel, as well as competing biometric technologies including voice, face, iris and hand geometry. The market for business-to-business and business-to-consumer transactions is substantial and continues to grow. Such transactions are subject to fraud resulting in unauthorized individuals gaining access to confidential information. Identity theft is one of the most pressing issues facing corporations today. We believe our biometric technology provides a more reliable method for confirming the identity of persons in local or remote locations than existing traditional methods.

Additionally, law enforcement and public safety are large and growing markets. The ability to quickly and accurately collect data from a variety of database sources and formats and deliver it to first responders opens a new framework to bring real time intelligence to security officers deployed in the field. With our acquisition of PSG, we believe there is a substantial market opportunity to integrate our VST and WEB-key biometric technologies with the PSG mobile solution.

Biometric technology is becoming an acceptable approach to physical and logical security. Acceptance of biometrics as an alternative to traditional security methods depends upon a number of factors including:

- The reliability of biometric solutions
- Public perception regarding privacy concerns