



*The Higher Standard in Virtual Training Simulation*

**FINANCIAL INFORMATION  
(UNAUDITED)**

**SECOND QUARTER REPORT**

**JUNE 30, 2008**

## **AN IMPORTANT NOTE ABOUT THIS REPORT**

VirTra Systems, Inc. (the “Company”) is not subject to the reporting requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 (the “Act”). Accordingly, this Report is not filed with the Securities and Exchange Commission, is not available on the SEC’s EDGAR system, and it does purport to meet the requirements for companies that are subject to the Act’s reporting requirements. The Company does intend in this Report to provide accurate financial information that is consistent with generally accepted reporting standards; however, shareholders and other readers are cautioned that this information is not and cannot be deemed the substantial equivalent of the information required of reporting companies under the Act.

**VIRTRA SYSTEMS INC.**  
**Balance Sheets as of June 30, 2008 and December 31, 2007**

	<b>6/30/08</b>	<b>12/31/07</b>
	<b>(Unaudited)</b>	
<b><u>ASSETS</u></b>		
Cash and cash equivalents	\$ 66,033	\$ 16,646
Accounts receivable, net of allowances	94,387	185,036
Costs and estimated earnings in excess of billings on uncompleted contracts	235,102	2,566
Prepaid expenses	7,775	350,200
Total current assets	<u>403,297</u>	<u>554,448</u>
Property and equipment, net of accumulated depreciation of \$429,340 and \$411,210, respectively	42,270	55,461
Other assets	11,030	14,530
Total non-current assets	<u>53,300</u>	<u>69,991</u>
<b>TOTAL ASSETS</b>	<b><u>\$ 456,597</u></b>	<b><u>\$ 624,439</u></b>
<b><u>LIABILITIES AND STOCKHOLDERS' DEFICIT</u></b>		
<b><u>LIABILITIES</u></b>		
Notes payable	\$ 30,000	\$ 30,000
Obligations under product financing arrangements	396,036	388,636
Convertible debentures, net of discount of \$0 and \$114,141, respectively	-	172,286
Derivative liability	-	338,135
Accounts payable	592,281	869,726
Accrued liabilities	2,438,205	2,619,614
Stock payable	50,000	50,000
Advanced held on deposit	282,874	59,137
Billings in excess of costs and estimated earnings on uncompleted contracts	-	-
Payable to related party	57,185	81,111
Total current liabilities	<u>3,846,581</u>	<u>4,608,645</u>
Redeemable common stock	1,859	1,859
Total non-current liabilities	<u>1,859</u>	<u>1,859</u>
<b>TOTAL LIABILITIES</b>	<b><u>3,848,440</u></b>	<b><u>4,610,504</u></b>
<b><u>SHAREHOLDERS' DEFICIT</u></b>		
Common stock, \$.005 par value, 500,000,000 shares authorized, 129,654,154 and 127,154,154 shares issued and outstanding at June 30, 2008 and December 31, 2007, respectively	648,271	635,771
Additional paid in capital	11,264,460	11,228,153
Accumulated deficit	(15,304,574)	(15,849,989)
Total shareholders' deficit	<u>(3,391,843)</u>	<u>(3,986,065)</u>
<b>TOTAL LIABILITIES AND SHAREHOLDERS' DEFICIT</b>	<b><u>\$ 456,597</u></b>	<b><u>\$ 624,439</u></b>

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

**VIRTRA SYSTEMS, INC.**  
**Statements of Operations for the Three and Six Months Ended June 30, 2008 and 2007**  
**(Unaudited)**

	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2008</b>	<b>2007</b>	<b>2008</b>	<b>2007</b>
<b><u>REVENUE</u></b>				
New system sales	\$ 572,241	\$ 592,361	\$ 1,026,406	\$ 699,338
Other revenue	211,020	12,837	279,020	145,246
Total Revenues	783,261	605,198	1,305,426	844,584
Cost of sales and services	370,613	288,771	847,090	485,945
Gross margin	412,648	316,427	458,336	358,639
<b><u>OPERATING EXPENSES</u></b>				
Gain on legal settlement	-	-	-	(273,607)
General and administrative expenses	140,374	516,444	477,406	1,054,226
Gain/(Loss) from operations	272,274	(200,017)	(19,070)	(421,980)
<b><u>OTHER INCOME AND (EXPENSE) ITEMS:</u></b>				
Forgiveness of debt income	94,672	-	94,672	-
Gain/(loss) on litigation settlements	349,687	-	324,687	-
Impairment of assets	-	-	-	-
Interest expense and finance charges	(35,145)	(163,721)	(194,541)	(238,721)
Gain/(loss) on derivative liability	380,616	783	338,135	783
Gain on sales of assets	-	-	-	2,813
Other income and expense	1,530	-	1,530	-
Total other income and expense items	791,360	(162,470)	564,483	(235,125)
Net income/(loss)	1,063,634	(362,487)	545,413	(657,105)
Weighted average shares outstanding - basic and fully diluted	129,654,154	103,205,897	128,775,033	101,913,097
Net gain(loss) per share - basic and fully diluted	\$ 0.008	\$ (0.00)	\$ 0.004	\$ (0.01)

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

**VIRTRA SYSTEMS, INC.**  
**Statements of Cash Flows for the Six Months Ended June 30, 2008 and 2007**  
**(Unaudited)**

	<b>Six Months Ended June 30,</b>	
	<b>2008</b>	<b>2007</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income/(loss)	\$ 545,413	\$ (657,106)
Adjustments to reconcile net loss to net cash provided by/(used in) operations:		
Depreciation and amortization	18,130	(58,764)
Forgiveness of debt income	-	-
Gain on sale of assets	-	-
Change in fair value of derivative	(338,135)	783
Bad debt expense	-	-
Common stock issued for services and settlement	48,809	487,566
Grant of options and warrants to employees, officers and directors	-	-
(Gain)/loss on settlement of litigation	(286,427)	-
Amortization/impairment of debt discount	114,141	(107,202)
Changes in operating assets and liabilities:		
Accounts receivable	90,649	(344,207)
Prepaid expenses and other	345,925	19,230
Costs in excess of billings/(billings in excess of costs) and estimated earnings on uncompleted projects	(232,536)	76,726
Accounts payable and accrued liabilities	(451,454)	440,779
Advanced held on deposit	223,737	(37,368)
Related party payables	(23,926)	-
Other current liabilities	-	(31,802)
Net cash provided by/(used in) operating activities	54,326	(211,365)
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Capital expenditures	(4,939)	(2,249)
Proceeds from the sale of assets	-	2,813
Net cash provided by/(used in) investing activities	(4,939)	564
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Proceeds from issuance of notes payable	-	106,770
Principal payments on notes payable	-	(26,427)
Proceeds from issuances of common stock	-	81,250
Net cash provided by/(used in) financing activities	-	161,593
Net change in cash and cash equivalents	49,387	(49,208)
Cash and cash equivalents, beginning of period	16,646	91,221
Cash and cash equivalents, end of period	\$ 66,033	\$ 42,013

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

**VIRTRA SYSTEMS, INC.**

**Statement of Stockholders' Deficit For the Year Ended December 31, 2007 and for the Six Months Ended June 30, 2008  
(Unaudited)**

	<u>Common Stock</u>		<b>Additional Paid In Capital</b>	<b>Accum. Deficit</b>	<b>Total</b>
	<b>Shares</b>	<b>Amount</b>			
Balance at December 31, 2007	127,154,154	\$ 635,771	\$11,228,153	\$ (15,849,989)	\$ (3,986,065)
Settlement of lawsuit	2,500,000	12,500	35,000		47,500
Imputed interest on notes	-	-	1,307		1,307
Net loss, three months ended 3/31/08				(518,221)	(518,221)
Balance at March 31, 2008	129,654,154	\$ 648,271	\$11,264,460	\$ (16,368,210)	\$ (4,455,479)
Net income, three months ended 6/30/08				1,063,634	
Balance at June 30, 2008	129,654,154	\$ 648,271	\$11,264,460	\$ (15,304,576)	\$ (3,391,845)

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

**VIRTRA SYSTEMS, INC.**  
**Notes to Financial Statements**

**Note 1. Basis of Presentation**

The accompanying un-audited interim financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America and should be read in conjunction with the audited financial statements and notes thereto for the year ended December 31, 2007. They do not include all information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. However, except as disclosed herein, there has been no material change in the information disclosed in the notes to the financial statements for the year ended December 31, 2007. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation of financial position and the results of operations for the interim periods presented have been included. Operating results for the interim periods are not necessarily indicative of the results that may be expected for the respective full year or for any future reporting period. The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. The Company's continuation as a going concern is dependent on its ability to meet its obligations, to maintain profitability, and to obtain additional financing as may be required. These financial statements do not include any adjustments that might result from the outcome of this uncertainty.

**Note 2. Convertible Debentures**

In August 2005 the Company issued \$500,000 in convertible debentures to Dutchess Private Equities Fund I, LLC. The debentures bear interest at 8% per year payable in cash or registered common stock at the Company's option. The debentures mature in August 2008 and are convertible, at the option of the holder, to shares of the company's common stock at a conversion price per share equal to the lower of (i) 80% of the lowest closing bid price for the common stock for the fifteen days prior to the conversion date; or (ii) 125% of the volume weighted average price on the closing date.

In addition, the Company issued to the holders of the convertible debentures warrants to purchase 500,000 shares of the Company's common stock.

On March 15, 2008 our corporate counsel advised us that the total amount of liability to Dutchess is estimated at \$1,421,264. Since this time, Dutchess has received a judgment for \$1.121 million and 1,650,000 share of stock, the change is reflected in the quarterly results. Currently management is negotiating a settlement agreement with Dutchess. We have included the total amount of this liability and we accrue interest on this judgment balance and have included \$3,737 in interest expense for the three months ended June 30, 2008.

**Note 3. Derivative Liability**

Based on the judgment in Note 2, the Company concluded that these convertible debentures have no further rights or obligations arising out of the financing relationship.

At June 30, 2008, the Company has valued this derivative liability at \$0 and has recognized a gain resulting from the change in value of this derivative liability of \$338,135.

**Note 4. Stock Options and Warrants**

The Company periodically issues incentive stock options to key employees, officers, directors, and outside consultants to provide additional incentives to promote the success of the Company's business and to enhance the ability to attract and retain the services of qualified persons. Warrants are periodically issued in connection with financing arrangements.

The Company has the following options and warrants outstanding at June 30, 2008.

Issued	Expire	Weighted Avg Exercise Price	Outstanding 12/31/07	New Grants	Expiring	Exercises	Outstanding 06/30/08
2005	2010	\$ 0.33	500,000	-	-	-	500,000
2005	2010	\$ 0.34	250,000	-	-	-	250,000
2005	2010	\$ 0.19	500,000	-	-	-	500,000
2005	2010	\$ 0.33	500,000	-	-	-	500,000
2004	2009	\$ 0.31	4,000,000	-	-	-	4,000,000
2006	2012	\$ 0.04	3,000,000	-	-	-	3,000,000
2007	2014	\$ 0.04	13,074,499	-	-	-	13,074,499
			21,824,499	-	-	-	21,824,499

No new options or warrants were granted for the three months ended June 30, 2008.

#### **Note 5. Commitments and Contingencies**

No additional commitments or contingencies were added during the quarter ending June 30, 2008.

#### **Note 6. Common Stock Transactions**

No additional stock grants occurred during the quarter ending June 30, 2008.

#### **Note 7. Accrued Liabilities**

The following table summarizes the major items included in Accrued Liabilities at June 30, 2008 and December 31, 2007:

	<b><u>06/30/08</u></b>	<b><u>12/31/07</u></b>
Accrued payroll taxes, including penalties and interest	\$ 1,010,271	\$ 1,002,641
Accrued interest payable debenture judgment	1,131,337	1,187,870
Accrued lawsuit judgments and settlements	237,837	162,297
Deferred revenue	14,296	29,643
Other	44,464	237,163
<b>Total Accrued Liabilities</b>	<b>\$ 2,438,205</b>	<b>\$ 2,619,614</b>

#### **Note 8. Cost and Estimated Earnings in Excess of Billings (and Billings in Excess of Costs and Estimated Earnings) on Uncompleted Contracts**

We had several projects near the completion stage, our percentage of completion is based on total costs incurred to date compared to the estimated total cost of each contract. Of the partially completed work at June 30, 2008, we have incurred total costs of \$241,779 on contracts totaling \$839,980 of total revenue. We estimate that we will incur approximately \$56,000 of additional costs and do not expect to incur any losses on our uncompleted contracts. Our costs and estimated earnings in excess of billings total \$235,102 at June 30, 2008 .

#### **Note 9. Other Assets**

Other assets at June 30, 2008 are comprised of rental deposits.

## **Business Overview**

Our principal business began in 1993 with the organization of Ferris Productions, Inc. Ferris designed, developed, distributed, and operated virtual reality products for the entertainment, simulation, promotion, and education markets. "Virtual reality" is a generic term associated with computer systems that create a real-time experience that immerses participants into a three-dimensional real-time synthetic environment generated or controlled by one (or several) computer(s). In September of 2001, Ferris merged into GameCom, Inc., a publicly held Texas company. We effectively left the entertainment/amusement market in the spring of 2003 in order to more fully focus on the training/simulation markets.

Our "immersive virtual reality™" devices are computer-based, and display a 180-degree up to a 360-degree field of view. Law enforcement and military customers seem to prefer VirTra's line of firearm simulators mainly due to the increase realism and superior life-saving training they afford. We also provide tetherless recoil kits for firearms and have a patent-pending Threat-Fire™ system that safely simulates return fire by use of an electric stun. By using more real-world simulators, trainees are able to safely perfect skills that translate into improved performance during life-and-death encounters that can occur at any time.

During the second quarter 2008, in order to reduce costs, we deregistered with the SEC and closed our office at 2500 City West Blvd., Suite 300, Houston, Texas 77042. Our corporate administration was moved to the existing engineering, production offices, and demonstration facility, at 1406 West 14th Street, Suite 101, Tempe, Arizona 85281, with a phone number of (480) 968-1488.

We face all the risks, expenses, and difficulties frequently encountered in connection with the expansion and development of a business, difficulties in maintaining delivery schedules if and when volume increases, the need to support systems at widely dispersed physical locations, and the need to control operating and general and administrative expenses.

## **Management's Discussion and Analysis of Financial Condition and Results of Operations**

### **Three Months Ended June 30, 2008 Compared with Three Months Ended June 30, 2007**

Our revenues are up 29% from the second quarter last year due to increased sales activity. For the three months ended June 30, 2008, our revenues increased to \$783,261, a 29% increase over the \$605,198 we posted for the same period in 2007. Our gross margin was \$412,648 or 53%.

Our general and administrative costs for the three months ended June 30, 2008 of \$140,374 is down significantly over the \$516,444 we recorded over the same period in 2007. The majority of the decrease is due to cost reductions enjoyed by filing the form 15 (eliminating substantial legal and accounting fees) and the closing of our Houston, Texas office. The reduction of general and administrative costs greatly assisted our ability to generate operating profit of \$272,274.

Our net profit of \$1,063,634 for the three months ended June 30, 2008 is substantially affected by a one-time adjustment of \$730,303 due to the reduction of the Dutchess liability.

Management plans to carefully invest profits into high return on investment activities such as growing our revenue base both in the US and selective international markets. In addition, management plans to use profits to reduce debts when it is clearly to the advantage of VirTra.

## **OTHER INFORMATION**

### **Item 1 – Legal Proceedings**

No new legal proceedings were added during the quarter ending June 30, 2008.

### **Item 2 – Changes in Securities**

No changes in securities were noted during the quarter ending June 30, 2008.

### **Item 3 – Defaults Upon Senior Securities**

We are not in default on any indebtedness that has not been disclosed in this and previous reports.

### **Item 4 – Submission of Matters to a Vote of Security Holders**

None.

### **Item 5 – Other Information**

None.

These financial statements, and the notes thereto, are based on the best information currently available to the Company, and to the best of my knowledge present fairly, in all material respects, the financial position of the Company and the results of its operations and cash flow for the periods presented, in conformity with accounting principles generally accepted in the United States.

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/s/ Bob Ferris

President