HALOSOURCE
Making Water Better

FOR IMMEDIATE RELEASE

9 September 2014

HaloSource, Inc.

("HaloSource" or the "Company")

Interim results for the six months ended 30 June 2014

HaloSource, Inc. (HALO.LN), the global clean water technology company trading on London's AIM, today announces its unaudited interim results for the six months ended 30 June 2014.

Financial Highlights

- Overall revenue for H1 2014 increased to $7.3 million, up 24% from H1 2013:
    - Drinking Water revenues increased to $2.0 million, up 124% from H1 2013
    - Environmental Water revenues increased to $1.2 million, up 29% from H1 2013
    - Recreational Water revenues increased to $4.0 million, up 1% from H1 2013
    - Antimicrobial Coatings revenue were $0.1 million, versus $0.1 million in H1 2013
- Gross margins increased two percentage points (from 37% to 39%) representing approximately $0.7 million of margin improvement versus the same period a year ago.
- Operating expenses fell by more than 7% to $8.4 million, versus the same period a year ago, representing a $0.7 million reduction, as a result of a continued focus on cost management across the Company.
- The Company ended the period with $8.3 million in cash, comprising $2.3 million of cash and cash equivalents, $4.5 million of short-term investments and $1.5 million of restricted cash, compared with $13.0 million in total cash as at 31 December 2013. Cash flows used in operations of $4.7 million decreased by 34%, or $2.3 million, compared to H1 2013.

Operational Highlights

- Drinking Water momentum continues to build rapidly as orders with strategic partners accelerate in line with expectations for our class leading differentiated disinfection technology with a succession of successful launches in China, India and most recently, Latin America.
- Revenues in our Environmental Water business for H1 2014 increased as we continue to expand relationships with key strategic players such as Rain for Rent, one of the largest US industrial water solutions providers to the construction industry. Growth in the segment was also driven by Stormtec in Canada (primarily in construction) and Nalco (in coal mining applications) in the US, as well as a new application in oil production where our unique chemistry is enabling oil well operators to realize increased oil recovery from existing wells.
- Our SeaKlear Recreational Water business grew modestly in H1 2014 despite a decline in the entire US recreational water specialty chemicals segment in the face of adverse weather conditions particularly in the northeast of the US. We saw improved industry performance toward the end of H1 2014 and expect continued market expansion in H2 2014.
- Post balance sheet events include the strategic partnership alliance with Rain for Rent to provide customers with enhanced water filtration solutions announced on 16 July 2014; and HaloSource entering a strategic supply agreement with Fluidra, S.A., to accelerate the delivery of HaloSource's enhanced recreational water solutions into the European and Australian pool and spa markets, announced 8 September 2014.

Martin Coles, President and Chief Executive Officer of HaloSource, said:

"As envisaged, we continued to see accelerated revenue growth in H1 2014 driven by increasing orders from existing and new partners across our portfolio of water solutions. The inherent scalability of our operating and financial model enables us to expand revenue and gross margin with minimal increases in administrative expense. As a result, we expect continued decreases in cash burn in line with current market expectations.

"Our strategy, put in place almost three years ago, is yielding significant and increasingly positive results as we continue to take our differentiated technology to market in partnership with leading multi-national companies in the rapidly growing multi-billion dollar global market for water purification and remediation solutions.

"With three clearly defined and relevant platform technologies in place for water disinfection, turbidity removal and dissolved solids absorption (Lead, Arsenic, Selenium etc.) we have achieved progress across all sectors. We are ideally positioned for growth into the second half of 2014 led by the critical Drinking Water segment.

"We remain confident that our focus on what we do best, innovation in the chemistry of water purification, coupled with strategic partnerships with key players in each segment, will deliver continued rapid sector and geographic growth in revenue, margins and profitability."

For further information:

HaloSource, Inc.
Martin Coles, Chief Executive Officer — via Newgate
James Thompson, Chief Financial Officer

Newgate Communications (Financial PR)
James Benjamin — +44 20 7680 6550
Madeleine Palmstierna — halosource@newgatecomms.com
Georgia Lewis

Liberum Capital (NOMAD)
Simon Atkinson — +44 203 100 2222
Richard Bootle

About HaloSource

HaloSource, Inc. designs solutions that serve people, preserve the planet, and protect our most valuable resource – water. The company works with scientists and industry experts in search of new ways to improve water quality around the globe. The team of HaloSource chemists, biochemists and microbiologists hold more than 100 patents, giving the company the power to provide environmentally conscious solutions. The company's mission is to make water better and help return previously contaminated water into the environment in the most clean, natural pure state.

Founded in Seattle, Washington, HaloSource has grown to become an influential leader in–three key sectors: drinking water, recreational water, and environmental water treatment and remediation. HaloPure®, HaloKlear® and SeaKlear® are the distinct brands that optimize the unique chemistry platforms across these primary sectors. Learn more about these cutting edge technologies by visiting HaloSource.com

Financial and Operational Review

The Company increased revenues in each key segment during H1 2014, with consolidated revenue increasing by 24% to $7.3 million. Within this, the Drinking Water and Environmental Water segments grew significantly during the first half of 2014.

Drinking Water revenue for the period increased 124% to $2.0 million (H1 2013: $0.89 million), driven by growth with key strategic partners in China and in India. Perfect, China's largest direct-seller of household products and a trusted consumer brand, has taken delivery of 370,000 cartridges powered by HaloSource's class leading

HaloPure® disinfection technology over the past 12 months. The cartridges are deployed in Perfect's newly launched pressure-fed water purification device, which is building momentum in the burgeoning Chinese water purification market. We expect to see continued acceleration in sales of Perfect's device, as well as revenues from subsequent replacement cartridges for the device.

Environmental Water revenue grew 29% to $1.22 million (H1 2013: $0.95 million) as the Company focused its efforts on partnering with established solution providers in North America in two key segments: mining and construction sediment removal.

Recreational Water revenue grew 1% to $4.01 million (H1 2013: $3.96 million) in a challenging period for the North American Specialty Chemicals market that shrank in the first half of the year, driven by a difficult start to the 2014 season as a result of adverse weather impacting much of the seasonal pool and spa industry.

Gross margin was 39%, up from 37% for the same period last year, representing $0.7 million in incremental margin. This increase occurred primarily as a result of decreased raw material costs in our Recreational Water business and increased economies of scale related to higher sales volumes in our Drinking Water and Environmental Water segments.

Operating expenses for H1 2014 totaled $8.4 million, decreasing by 7%, or $0.7 million, compared to the first half of the prior year. The decline was driven largely by reduced legal expenses and travel costs, offset in part by severance payments incurred during the period. The Company reduced its executive team wages costs by approximately 13% compared to the same period in 2013. The litigation settlement with Molycorp Minerals in 2013 has led to reduced legal expenses going forward.

The consolidated net loss was $5.7 million for the period, down from a net loss of $7.0 million for the same period a year ago, driven by a combination of both improved gross margins and decreased operating expenses as detailed above.

The Company ended the period with $8.3 million of cash and cash equivalents, short-term investments and restricted cash, of which $1.5 million is restricted in its use, as compared to $13.0 million in total as at 31 December, 2013. Cash used in operations for the first half was $4.7 million; down from $7.1 million during the same period in 2013 resulting from a decrease in operating expenses incurred during the period as well as improved gross margins and a $1.3 million reduction in non-cash working capital employed during the period. The Company expects to continue to reduce cash flows used in operations in the second half of 2014.

People

HaloSource is a technology business, and the quality of its team is critical to stay on the leading edge of innovation. In this regard the Company continues to attract very high quality talent with critical skills. Management believes the ability to attract high performing candidates is a direct result of offering workplace challenge and excitement, while providing the opportunity to make a direct impact on improving the environment as well as the lives of others around the world.

The Company's headcount at 30 June 2014 was 119, versus 124 at 30 June 2013. As we continue to narrow our cash-burn, headcount is a critical metric, representing approximately 60% of total operating expenses. While not reflected directly in the total employee headcount, we have shifted our talent base in the last 12 months to focus to a larger degree on scientific innovation, local execution and strategic account management. This shift will continue to be a focus of management as we progress toward the cash flow break-even point.

Outlook

We are pleased to see the strategy that was implemented three years ago continue to drive operational and financial improvement in our company. By focusing on "innovation in the chemistry of water purification" we provide a value-proposition that is unmatched in the markets we serve. Our customers consider us to be their water technology partner, bringing key innovation insights to address specific water contamination challenges and, most importantly, to enable them to differentiate their products in the rapidly growing, multi-billion dollar market for water purification and remediation solutions.

We believe the Drinking Water business is poised for continued growth as major partners are actively expanding sales activity for new, HaloPure® powered, water purification devices in emerging markets. During 2013 we added several significant partners that now are driving order volumes in the current year, giving us confidence in our forecasts for continued growth. As we advance our technology platform we expect growth in orders from existing partners as well as select new partners in new geographies who are looking to address increased water contamination, regulation and health challenges.

We also expect growth to continue in our Environmental Water segment, as the benefits of our unique green solutions are increasingly recognised in this highly regulated sector. We provide cleaner, greener and more effective water treatment solutions for water recycle and discharge unmatched in cost and performance. Partners like Rain-4-Rent, Stormtec and Nalco are pioneering the use of these polymers in mining, construction and oil and gas applications.

In our Recreation Water segment we continue to launch innovative new products, as evidenced by our development and introduction of SeaKlear® Mighty Pods™ products, where we have received industry acclaim for making water chemistry easier for pool and spa owners. While weather will always play a role in this segment's outcomes, we expect to drive growth in this business through harnessing technical insights gained in other areas of our water portfolio to bring additional product innovation to market. As with our other segments, we will effectively continue to expand our presence in the market with partners that bring marketing and distribution expertise to the industry.

We remain confident that our relentless focus on innovation across all segments will yield robust, sustainable growth in revenue, margins and profitability.

HaloSource, Inc. Financial Statements

Unaudited Interim Condensed Consolidated Statements of Comprehensive Loss

(US$000's, except per share data)	*Six months ended* June 30, 2014	*Six months ended* June 30, 2013
Revenue - net	$ 7,302	$ 5,882
Cost of goods sold	4,435	3,696
Gross profit	2,867	2,186
Operating expenses		
Research and development	1,295	1,578
Selling, general, and administrative	7,094	7,462
Total operating expenses	8,389	9,040
Operating loss	(5,522)	(6,854)
Other expense, net	(143)	(153)
Loss before income taxes	(5,665)	(7,007)
Income taxes	-	(6)
Net loss	$ (5,665)	$ (7,013)
Other comprehensive income (loss)		
Unrealized gain (loss) on available-for-sale investments	4	(33)
Reclassification adjustment of net realized loss on available-for-sale investments included in net loss	-	(13)
Foreign currency translation adjustments	(46)	88
Other comprehensive income (loss)	(42)	42
Comprehensive loss	$ (5,707)	$ (6,971)
Basic and diluted net loss per share	$ (0.04)	$ (0.04)
Shares used to compute basic and diluted loss per share (000's)	156,518	156,301

See accompanying notes to unaudited interim condensed consolidated financial statements.

HALOSOURCE
Making Water Better

HaloSource, Inc. and Subsidiaries

Unaudited Interim Condensed Consolidated Balance Sheets

(US$000's)	*June 30,* 2014	*December 31,* 2013
ASSETS		
Current assets		
Cash and cash equivalents	**$ 2,262**	$ 1,762
Restricted cash	**1,552**	1,941
Short term investments	**4,483**	9,314
Accounts receivable, less allowance for doubtful accounts of $20 and $20, respectively	**4,643**	6,085
Inventories, net	**4,114**	3,626
Prepaid expenses and other current assets	**981**	1,539
Total current assets	**18,035**	24,267
Property and equipment, net	**3,576**	4,018
Goodwill	**2,180**	2,180
Other intangible assets, net	**785**	846
Deposits	**280**	276
Total Assets	**$ 24,856**	$ 31,587
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	**$ 1,924**	$ 2,549
Accrued expenses	**880**	1,257
Salaries and benefits payable	**470**	603
Current portion of debt and capital lease obligations	**1,113**	1,082
Total current liabilities	**4,387**	5,491
Long-term portion of debt and capital lease obligations	**35**	45
Deferred rent	**1,114**	1,167
Deferred tax liability	**49**	104
Total liabilities	**5,585**	6,807
Stockholders' equity		
Common stock, no par value	**130,863**	130,665
Accumulated other comprehensive income	**31**	73
Accumulated deficit	**(111,623)**	(105,958)
Total stockholders' equity	**19,271**	24,780
Total liabilities and stockholders' equity	**$ 24,856**	$ 31,587

See accompanying notes to unaudited interim condensed consolidated financial statements.

HaloSource, Inc. and Subsidiaries

Unaudited Interim Condensed Consolidated Statements of Stockholders' Equity

(US$000's, except shares in 000's)	Common Stock Shares	Common Stock Amount	Accumulated Other Comprehensive Income (Loss)	Accumulated Deficit	Total Stockholders' Equity
Balance, December 31, 2012	156,193	$ 130,097	$ 4	$ (93,495)	$ 36,606
Exercise of common stock options	8	1	-	-	1
Issuance of shares upon vesting of restricted stock	182	-	-	-	-
Share-based compensation	-	288	-	-	288
Other comprehensive income	-	-	42	-	42
Net loss	-	-	-	(7,013)	(7,013)
Balance, June 30, 2013	**156,383**	**$ 130,386**	**$ 46**	**$ (100,508)**	**$ 29,924**
Balance, December 31, 2013	156,383	$ 130,386	$ 6	$ (100,508)	$ 29,924
Exercise of common stock options	10	1	-	-	1
Issuance of shares upon vesting of restricted stock	100	-	-	-	-
Share-based compensation	-	197	-	-	197
Other comprehensive loss	-	-	(42)	-	(42)
Net loss	-	-	-	(5,665)	(5,665)
Balance, June 30, 2014	**156,493**	**$ 130,584**	**$ 4**	**$ (106,173)**	**$ 24,415**

See accompanying notes to unaudited interim condensed consolidated financial statements.

HALOSOURCE
Making Water Better

HaloSource, Inc. and Subsidiaries

Unaudited Interim Condensed Consolidated Statements of Cash Flows

(US$000's)	**Six months ended June 30, 2014**	Six months ended June 30, 2013
Operating activities		
Net loss	**$ (5,665)**	$ (7,013)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	**505**	533
Allowance for inventory, sales returns, and bad debts	**(90)**	88
Share-based compensation	**197**	288
Realized loss on sale of short-term investments	**-**	13
Loss on disposal of property, equipment and other assets	**14**	-
Deferred income taxes	**-**	(4)
Changes in operating assets and liabilities:		
Accounts receivable	**1,446**	12
Inventories	**(365)**	(674)
Prepaid expenses and other assets	**565**	(217)
Accounts payable	**(712)**	129
Accrued expenses and other current liabilities	**(394)**	31
Salaries and benefits payable	**(167)**	(168)
Deferred rent	**(57)**	(87)
Net cash used in operating activities	**(4,723)**	(7,069)
Cash flows from investing activities		
Proceeds on disposal of property and equipment	**110**	-
Purchase of property and equipment	**(86)**	(223)
Purchase of short-term investments	**(415)**	(8,078)
Sale of short-term investments	**5,250**	1,740
Decrease (increase) in restricted cash	**390**	(16)
Net cash provided by (used in) investing activities	**5,249**	(6,577)
Cash flows from financing activities		
Borrowings under short-term debt	**-**	64
Repayments of debt and capital lease obligations	**(28)**	(25)
Proceeds from exercise of stock options and warrants	**1**	1
Net cash (used in) provided by financing activities	**(27)**	40
Effect of exchange rate changes on cash	**1**	(11)
Net increase (decrease) in cash and cash equivalents	**500**	(13,617)
Cash and cash equivalents, beginning of period	**1,762**	15,635
Cash and cash equivalents, end of period	**$ 2,262**	$ 2,018
Supplemental disclosures of noncash investing and financing activities:		
Increase in accrued property and equipment purchases	**$ 29**	$ 295

See accompanying notes to unaudited interim condensed consolidated financial statements.

Notes to Condensed Consolidated Financial Statements

1. **General information**

HaloSource, Inc. and its subsidiaries (together, the "Company" or "HaloSource") are a global clean water technology company, headquartered near Seattle in Bothell, WA, U.S.A., with subsidiaries in India and China and operations in other markets around the world through its relationships with distributors and other third parties. HaloSource is committed to relentless innovation, industry-leading products and ongoing support for water-related philanthropy. The Company's proprietary technologies for drinking and recreational water, textile coatings, and environmentally friendly wastewater recycling, enable our partners to rid the world's water of impurities and return it responsibly to the earth. HaloSource markets its products under its brand names of HaloPure®, HaloShield, SeaKlear®, AquaPill, PoolMark, HaloKlear™, StormKlear and Mighty Pods™.

2. Basis of preparation

The condensed consolidated financial statements include the accounts of HaloSource and its wholly owned subsidiaries. Intercompany transactions and balances have been eliminated.

The principal accounting policies have been applied consistently throughout the period in the preparation of these consolidated financial statements. In the opinion of management, all adjustments necessary for the fair statement of the financial position, results of operations and cash flows for the periods have been included and are of a normal, recurring nature.

The condensed consolidated financial information for the six month periods ended June 30, 2013 and 2014 has been prepared in accordance with generally accepted accounting principles in the United States of America ("U.S. GAAP") which is appropriate given the Company is incorporated in the State of Washington in the United States. References to U.S. GAAP issued by the Financial Accounting Standards Board ("FASB") in the Company's notes to its condensed consolidated financial statements are to the FASB Accounting Standards Codification, sometimes referred to as the "Codification" or "ASC". The condensed consolidated financial information should be read in conjunction with the audited annual financial statements for the year ended December 31, 2013, which have also been prepared in accordance with U.S. GAAP and were made available on March 26, 2014. The financial information for the six-month periods ended June 30, 2014 and June 30, 2013 is unaudited.

Liquidity and capital resources

The Company has generally incurred net losses and negative operating cash flows since inception, and as of June 30, 2014, the Company had an accumulated deficit of approximately $111.6 million. For the six months ended June 30, 2014, the Company's net loss was $5.7 million and cash used in operating activities was $4.7 million. As of June 30, 2014, the Company has $2.3 million of unrestricted cash and cash equivalents, $4.5 million of unrestricted short term investments, and $1.5 million of restricted cash.

The Company has implemented certain cost savings measures and implemented other plans that have reduced the net loss and cash used by operations in 2014 as compared to 2013 and are expected to continue to do so. In order to generate sufficient revenue to achieve profitability, the Company must successfully maintain its existing relationships and build significant new relationships with its customers to develop the reach and application of the Company's technologies. There can be no assurance that these efforts will be successful. The Company continues to face significant risks associated with successful execution of its strategy. These risks include, but are not limited to, technology and product development, introduction and market acceptance of new products and services, changes in the marketplace, liquidity, competition from existing and new competitors which may enter the marketplace, and retention of key personnel. Management plans to continue to finance the Company's operations with a combination of currently available cash and short-term investments and may attempt to raise additional funds in the near future. Management believes current funding will be sufficient to finance the Company's operations through the remainder of 2014; however, if necessary, the Company may seek other financing options. If adequate funds are not available, the Company may be required to reduce the scope, delay or eliminate some or all of its planned commercial activities. The accompanying financial statements have been prepared assuming that the Company will continue as a going concern, which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of business. The financial statements for the period ended June 30, 2014 do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities that may result from uncertainty related to the Company's ability to continue as a going concern.

Use of estimates

The preparation of condensed consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could materially differ from those estimates. Estimates include the allowance for doubtful accounts, sales returns allowances, inventory obsolescence, share-based compensation, and impairment evaluations for goodwill and long-lived assets.

3. Accounting policies

The accounting policies applied are consistent with those of the annual financial statements for the year ended December 31, 2013, except as described below.

Recent accounting pronouncements

In July 2013, the FASB issued Accounting Standards Update ("ASU") 2013-11, *Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists*, to clarify the balance sheet presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. ASU 2013-11 is effective for fiscal years beginning after December 15, 2013. The Company adopted the ASU effective January 1, 2014, with no material effect on the Company's consolidated financial statements.

In June 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers.* The update gives entities a single comprehensive model to use in reporting information about the amount and timing of revenue resulting from contracts to provide goods or services to customers. The ASU, which applies to any entity that enters into contracts to provide goods or services, will supersede current revenue recognition requirements and most industry-specific guidance throughout the Industry Topics of the Codification. The update is effective for the Company for its financial year ending December 31, 2017, including interim periods within that reporting period and early adoption is not permitted. The Company is currently reviewing the provisions of this ASU to determine if there will be any material effect on its consolidated financial statements.

4. Commitments and contingencies

Litigation and other contingencies

The Company may be subject to a variety of legal proceedings that could arise in the ordinary course of business or from its shareholders. The Company evaluates its exposure to threatened or pending litigation on a regular basis. To the extent it were required, the Company would evaluate the potential amount of loss related to litigation as well as the potential range of outcomes related to such loss. Determining the amount of potential loss and the range of potential outcomes requires significant judgment. The Company will record a loss contingency if an amount becomes both probable and measurable. In addition, any such proceedings, whether meritorious or not, could be time consuming, costly, and result in the diversion of significant operational resources or management time.

Operating and capital leases

The Company has entered into operating lease agreements for its various office and manufacturing facilities worldwide and capital lease agreements for certain equipment. These leases are in effect through 2023.

Total rent expense under operating lease agreements for the six months ended June 30, 2014 and 2013 was $435,000 and $423,000, respectively.

5. Restricted cash

Restricted cash primarily represents cash collateral used to secure working capital borrowing needs related to operations of the Company's foreign subsidiaries. In April 2011, the Company established a working capital line of credit arrangement through Axis Bank in India. In consideration for establishing this working capital line of credit with Axis Bank, the Company entered a Sanction of Credit Facilities Agreement with Axis Bank to secure all borrowings under this line of credit. (See Note 12, below).

6. Segment reporting

The Company measures the results of its reportable segments based on revenue and gross profit. The Company does not allocate operating expenses, income taxes or interest income (expense) to the reportable business units for purposes of reporting to the chief operating decision maker.

The Company's operating segments are: Drinking Water, Recreational Water, Environmental Water Remediation, and Anti-microbial Coatings. Information on reportable segments and reconciliation to condensed consolidated net loss for the six-month periods ended June 30, 2014 and 2013 are presented below. Also presented below are total assets by operating segment as of June 30, 2014 and December 31, 2013. The Company does not report to the chief operating decision maker its capital expenditures or assets for the Recreational Water or Environmental Water segments and does not assign intangible assets to the segments.

Six months ended June 30, 2014

(US $000's)	Recreational Water	Environmental Water	Drinking Water	Antimicrobial Coatings	Unallocated	Consolidated
Revenue	$ 4,010	$ 1,219	$ 1,996	$ 77	$ -	$ 7,302
Gross profit	2,176	312	315	64	-	2,867
Operating expenses	-	-	-	-	(8,389)	(8,389)
Other expenses, net	-	-	-	-	(143)	(143)
Net loss	-	-	-	-	-	$ (5,665)
Assets	-	-	$ 6,318	$ 17	$ 18,521	$ 24,856

Six months ended June 30, 2013, except assets as of December 31, 2013

(US $000's)	Recreational Water	Environmental Water	Drinking Water	Antimicrobial Coatings	Unallocated	Consolidated
Revenue	$ 3,961	$ 949	$ 890	$ 82	$ -	$ 5,882
Gross profit (loss)	1,895	244	(19)	66	-	2,186
Operating expenses	-	-	-	-	(9,040)	(9,040)
Other expenses, net	-	-	-	-	(159)	(159)
Net loss	-	-	-	-	-	$ (7,013)
Assets	-	-	$ 5,822	$ -	$ 25,765	$ 31,587

7. Net loss per share

Basic net loss per share is computed using the weighted average number of common shares outstanding during the period. Diluted net loss per share is computed using the weighted average number of common and potentially dilutive shares outstanding during the period. Potentially dilutive shares consist of the incremental common shares issuable upon conversion of the exercise of common stock options, restricted stock grants and warrants. The Company had a net loss for all periods presented herein; therefore, none of the options, restricted stock grants or warrants outstanding during each of the periods presented have been included in the computation of diluted loss per share as they were antidilutive. Total potentially dilutive shares of common stock of 7,186,000 and 6,426,000 were excluded from the calculations of diluted loss per share for the six months ended June 30, 2014 and 2013, respectively.

8. Inventories

Inventories at June 30, 2014 and December 31, 2013 consist of the following:

(US $000's)	**June 30, 2014**	December 31, 2013
Raw materials	**$ 2,491**	$ 2,163
Finished goods	**1,623**	1,463
Inventories, net	**$ 4,114**	$ 3,626

During the six month periods ended June 30, 2014 and 2013, the Company recorded cost of goods sold of $98,000 and $89,000, respectively, to reduce certain inventory items from their recorded cost to their estimated net realizable value. The inventory reported in the condensed consolidated balance sheets as of June 30, 2014 and December 31, 2013 is net of write-downs of inventory carrying values due to obsolescence of $537,000 and $443,000, respectively.

9. Property and equipment

Property and equipment as of June 30, 2014 and December 31, 2013 consist of the following:

(US $000's)	**June 30, 2014**	December 31, 2013
Manufacturing equipment	**$ 3,068**	$ 3,329
Furniture and fixtures	**228**	228
Office equipment	**966**	939
Leasehold improvements	**2,707**	2,710
Construction in process	**18**	10
	6,987	7,216
Less accumulated depreciation and amortization	**(3,411)**	(3,198)
Property and equipment, net	**$ 3,576**	$ 4,018

10. Related party transactions

During the six months ended June 30, 2014 and 2013, the Company paid royalties for certain patent rights of $225,000 and $225,000, respectively, to a university which held stock in the Company. Royalty payments are allocated between cost of goods sold, where there are identifiable product and sublicense revenues, and research and development expenses in the accompanying condensed consolidated statements of comprehensive loss. The Company had no outstanding accounts payable to the university at June 30, 2014 or December 31, 2013.

11. Business and credit concentration

For the six-month periods ended June 30, 2014 and 2013, one of the Company's Recreational Water customers individually accounted for 10% and 17% of the Company's revenue, respectively. Accounts receivable from this customer represented 7% and 17% of the total accounts receivable at June 30, 2014 and December 31, 2013, respectively.

Essentially all of the Company's revenue from its Drinking Water segment is generated in emerging market countries, including India and China. During 2014 and 2013, the majority of Drinking Water revenue was derived from one customer in India and one customer in China. In addition, essentially all raw materials and manufacturing facilities used in the

Drinking Water segment are sourced from, or located in, the same emerging market countries. These markets represent varying political and regulatory environments that can potentially affect Drinking Water operations.

12. Foreign line of credit

In May 2011, Halosource Technologies Pvt. Ltd. ("Halosource Technologies"), a wholly-owned subsidiary of Halosource, Inc. which is located in Bangalore, India, entered into a Sanction of Credit Facilities Agreement with Axis Bank for a credit facility for up to an amount of Rs. 70,000,000, or approximately $1,166,000 at June 30, 2014. This line of credit is available for borrowings to support working capital needs of Halosource Technologies. Any borrowings under the line of credit will bear interest at Axis Bank's base-rate as determined under guidelines issued by the Reserve Bank of India, plus 1.85%, or approximately 12% annually as of June 30, 2014. As of June 30, 2014, borrowings under this line of credit totaled Rs. 65,670,000, or approximately $1,094,000. As of June 30, 2014, the Company is in compliance with all terms and conditions of this line of credit and the line of credit is payable upon demand.

As a condition to borrowing under this line of credit, the Company is required to maintain a standby letter of credit through Wells Fargo Bank NA in an amount equivalent to 110% of the line of credit, or Rs. 77,000,000, approximately $1,282,000 at June 30, 2014; further, Wells Fargo Bank NA requires a restricted cash balance of 105.3% of the standby letter of credit. The Company has in turn restricted cash of $1,552,000 under the standby letter of credit to serve as collateral for the outstanding borrowings under the foreign line of credit. (See Note 5, above).

13. Forward exchange contracts

The Company is exposed to foreign currency exchange-rate fluctuations in the normal course of its business, which the Company manages from time to time through the use of forward foreign exchange contracts. Forward foreign exchange contracts are used to hedge the impact of fluctuations of foreign exchange on certain assets or liabilities denominated in a currency other than the functional currency of the Company or its subsidiaries. The Company has chosen not to apply hedge accounting to these foreign exchange contracts. The Company uses forward foreign exchange contracts to mitigate risk and does not intend to engage in speculative transactions. The forward foreign exchange contracts are entered into by the Company and its subsidiaries primarily to hedge intercompany payables denominated primarily in Indian Rupee. These contracts do not contain any credit-risk-related contingent features. Further, the Company seeks to manage the counterparty risk associated with these forward foreign exchange contracts by limiting transactions to counterparties with which the Company has an established banking relationship. In addition, the contracts are limited to a time period of less than one year, generally three months or less.

For the six-month periods ended June 30, 2014 and 2013 these forward foreign exchange contracts resulted in net realized gains (losses) of $(162,000) and $67,000, respectively. The realized gains and losses were partially offset by realized and unrealized gains and losses on foreign denominated accounts receivable and foreign intercompany payables during the same periods. Realized gains and losses related to forward foreign exchange contracts are recorded in foreign exchange gain (loss) on the condensed consolidated statements of comprehensive loss and the assets and liabilities for these contracts are recorded in prepaid and other assets and accrued liabilities on the condensed consolidated balance sheets. As of June 30, 2014 and December 31, 2013, the Company had no outstanding forward foreign exchange contracts.

14. Stock options and share-based compensation

The Company recognizes compensation expense for awards of equity instruments to employees and directors based on the grant date fair value of those awards. For stock options, the Company utilizes the Black-Scholes option pricing model to estimate the fair value of employee stock-based compensation at the date of the grant, which requires the input of subjective assumptions including expected volatility, expected term, and a risk free interest rate. Because the Company has limited historical patterns, the expected life of stock options is based on the experience of similar publicly traded companies and management's judgment. The expected volatility is based on volatility from comparable options with similar publicly traded companies. The risk free interest rate is estimated using comparable published federal funds rates. Compensation expense is recognized over the requisite service period for those options expected to vest, net of a forfeiture rate.

In conjunction with the Company's 2013 Annual General Meeting which was held in April 2013, the Company included a proposal to its shareholders to increase the number of shares of Common Stock reserved for issuance under its 2010 Equity Incentive Plan (the "2010 Plan") by 5,000,000, from 3,000,000 to 8,000,000. The Company was successful in obtaining the required number of shareholder votes to approve this proposal. During the six month periods ended June 30, 2014 and 2013, the Company issued stock options and restricted stock awards under its 2010 Plan totaling 1,555,000, and 1,988,000, respectively. As of June 30, 2014, the Company had 2,106,000 shares available for issuance under the 2010 Plan.

The Company typically recognizes share-based compensation costs for an award on a straight-line basis over the requisite service period for each separately vesting portion of the award as if the award was, in substance, multiple awards. For the six-month periods ended June 30, 2014 and 2013, the Company recorded stock based compensation expense of $197,000 and $288,000, respectively. No income tax benefit was recognized in the condensed consolidated statements of comprehensive loss for share-based compensation arrangements.

15. Common stock

Total authorized common shares are 200,000,000. As of June 30, 2014, the Company has 156,594,000 issued and outstanding shares of common stock.

16. Subsequent events

The Company has evaluated subsequent events through the date on which the financial statements were available to be issued. No transactions or events have occurred that would require further disclosure.