FAQs for the Tax Treatment of Aware's 2014 Special Cash Dividend

Preface

Aware, Inc. ("Aware") paid a special cash dividend of $1.75 per common share on July 24, 2014. We determined that 12.54596% or $0.21955 cents of this dividend was a taxable dividend and 87.45404% or $1.53045 was a nontaxable return of capital to the extent of a shareholder's tax basis.

The purpose of this FAQ is to help shareholders understand the tax treatment for the return of capital portion of the dividend.

FAQs

1. How is a return of capital distribution treated for income tax purposes in the U.S.?

For U.S. income tax purposes, the return of capital portion of the dividend is non-taxable and is treated as a reduction in the tax basis of an Aware shareholder's shares to the extent of the shareholder's tax basis. Once the tax basis in a shareholder's shares is exhausted, the remainder is treated as a capital gain. Shareholders are encouraged to consult their tax advisors to determine the tax treatment for their particular shares.

2. Does a return of capital distribution receive similar tax treatment for state income tax purposes?

Generally yes, unless the state tax law specifically diverges. Again, shareholders are encouraged to consult their tax advisors for the tax treatment in their state.

3. How is the special cash dividend tax treatment reported to shareholders?

Aware is required to complete IRS Form 8937 for each distribution that affects shareholder basis and post it on the Investor Relations portion of its website within 45 days of the dividend payment date. This form provides details on the expected changes in the tax basis of the shares. Once we make a final determination as to the portion of the dividend that is a taxable dividend and the portion that is a return of capital, we must file an amended Form 8937 and update our website.

We made a final determination as to the tax treatment of the special cash dividend in February 2015, and we: i) filed an amended Form 8937 with the IRS; ii) posted the amended Form 8937 on our website; and iii) provided that information to our stock transfer agent who will get the information to brokerage firms via its channels.

Upon receipt of the dividend tax information, brokerage firms will report the tax treatment of the special cash dividend to our U.S. shareholders on Form 1099-DIV . We expect that brokers will mail these forms to U.S. shareholders in February 2015.

4. Do I need to file any additional documentation or paperwork as a result of this change?

No, although shareholders or their brokers will need to track the tax basis of their Aware shares in their tax return work-paper files or brokerage accounts.

5. Where can I find further information regarding the U.S. tax treatment of return of capital distributions?

See IRS Publication 550, Investment Income and Expenses.

Return of Capital Distribution Example

Let's assume the following:

- A shareholder purchased one share of Aware stock in 2013 for $5.00.
- The shareholder received the $1.75 special cash dividend on his share of Aware stock in July 2014.
- Aware communicates to its shareholders that for U.S. tax purposes, 87.5% of the special cash dividend is treated as a return of capital and 11.5% should be treated as a dividend.

Therefore for U.S. tax reporting, this shareholder should treat approximately $1.53 of the $1.75 special dividend as a return of capital and $0.22 of the $1.75 special cash dividend as a taxable dividend. The portion of the distribution that is treated as a dividend for U.S. tax purposes is taxable to the shareholder in the year in which the dividend is received. Accordingly, this shareholder should report $0.22 of dividend income on his 2014 U.S. Income Tax Return.

The portion of the distribution that is treated as a return of capital for U.S. tax purposes will reduce the shareholder's basis in his stock and will therefore impact the amount of the taxable gain or loss recognized by the shareholder in the year in which he sells his stock. Assuming that this shareholder sells his Aware share for $6.00 in 2015, his U.S. taxable gain in 2015 would be calculated as follows:

Original adjusted basis	$5.00
Less: return of capital distributions	(1.53)
New adjusted basis	$3.47
Sale proceeds	$6.00
Less: new adjusted basis (above)	(3.47)
Capital gain reportable in 2015	$2.53