IMAGE SOFTWARE INC
Form 10-K
April 01, 2002

FORM 10-K
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

(X) ANNUAL REPORT PURSUANT TO SECTION 13 OF 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934. For the fiscal year ended 12/31/2001

OR

( ) TRANSITION REPORT PURSUANT TO SECTION 13 OF 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934. For the transition period from ______ to ______.

1MAGE SOFTWARE, INC.
(Exact name of Registrant as specified in its charter)

0-12535
(Commission File Number)

COLORADO	84-0866294
(State of Incorporation)	(IRS Employer Identification Number)
6025 S. QUEBEC ST. #300 - ENGLEWOOD CO 80111	(303) 694-9180
(Address of principal executive offices)	(Registrant's telephone number, including area code)

Securities Registered Pursuant to Section 12(b) of the Act:

NONE	NONE
(Title of Class)	(Name of Exchange)

Securities Registered Pursuant to Section 12(g) of the Act:

COMMON STOCK - $.004 PAR VALUE
(Title of Class)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports) and, (2) has been subject to such filing requirements for the past 90 days. Yes X No ______

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

Aggregates market value of the voting stock held by non-affiliates of the Registrant as of March 15, 2002: $1,096,950.

As of March 15, 2002, there were 3,146,554 shares of the Registrant's Common Stock outstanding.

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PART I

ITEM 1. BUSINESS

INTRODUCTION

1mage Software, Inc., (the "Company") develops and markets computer-based document imaging systems that capture, store and display electronic files and paper documents as graphical images. Document management systems like 1MAGE(R) (pronounced "one image") offer organizations of every size the ability to deliver the information embedded in millions of documents to their workers across their existing computing infrastructure, as well as the tools to efficiently manage the proliferation of digital documents for eBusiness deployment. The modular 1MAGE system captures entire documents from a variety of sources. Memos, letters, source documents, contracts, purchase orders, word processing files, e-mail, fax, industry and market studies, spreadsheets, databases, multimedia, maps and regulatory forms are examples of documents that are automatically converted into secure, permanent digital images that are indexed for instantaneous retrieval. Using an open, client/server architecture design, 1MAGE provides a comprehensive solution for scanning, indexing, storing and retrieving document images so that they may be viewed, printed, faxed, e-mailed or made available for eBusiness or eCommerce applications. The 1MAGE system is designed to integrate easily with existing IT infrastructure, using an extensive library of multi-platform APIs (Application Programming Interfaces), rather than forcing expensive investments in re-engineered or new computing hardware and software.

Today's workplace is dramatically changing with the advent of eBusiness, eCommerce, and affordable electronic document imaging. During 2001, the Company concentrated its efforts on selling document imaging software to its niche markets. This market includes users that prefer (1) operating platforms other than Microsoft Windows, such as RedHat Linux and Unix, or (2) Open Systems databases such as IBM's and Raining Data's MultiValue databases. The Company also continued to make progress toward its goal of establishing a broad-based Value Added Reseller ("VAR") network for its imaging software. In addition to VARs, the Company seeks to partner with software developers and other businesses, which provide software to their targeted vertical markets.

IMAGING SOFTWARE MARKET

The Company markets its products through its direct sales force and its indirect channel partners. The Company targets VARs, systems integrators, and other companies that market complementary software, services, or other products. 1MAGE software has an established presence in a multitude of industries, including automotive retail, building materials, construction, distribution, education, employee benefit plans, government, healthcare, laboratories, manufacturing, oil and gas, public libraries, public safety, retailing, transportation and utilities.

The Company offers a comprehensive reseller program, which provides, in the context of a cooperative marketing effort, a broad range of sales, marketing, and technical support. The program includes technical training and assistance, marketing communications, sales training and assistance, excellent support and training, lead referral services, customized product literature, and a discounted demonstration/development system.

PRODUCTS

As noted above, the Company's flagship product is 1MAGE(R), its proprietary document imaging software package. The Company is continually enhancing this product in order to improve its performance and expand its possible uses.

1MAGE(R) DOCUMENT MANAGEMENT - 1MAGE is a powerful electronic image management system created to operate the same on Linux, Unix, and Windows(TM)-based computer systems. It provides a comprehensive solution for the scanning, indexing, storage and retrieval of images and is designed to file, route, track, archive, and manage an organization's incoming and outgoing documents and electronic files.

Additional products include the following:

- 1SCAN for scanning and pre-indexing
- 1FAX for inbound and outbound fax and cover sheet management
- 1COLD/ERM for storing computer-generated formatted data on external mass storage devices
- 1FORM for business form template administration
- 1RENDITION for merging spooled data with images for billing
- 1WORKFLOW for electronically moving a document from one task to another
- 1OCR/OMR for automatic indexing and data capture via optical and mark character recognition
- 1SUITE for bringing images to Windows-based PC clients
- 1SERVER for accessing documents via the Internet
- 1VIEW for using standard browsers to access images over the Intranet and Internet
- 1APPROVE for electronically approving invoices and other document related business functions
- 1ACCESS for bringing images to computers that support JAVA programming languages

A key element of the Company's product line is its open systems technology, namely:

- Open Systems compliant with Linux, Unix, and Windows Operating Systems. Supports file formats in TIFF, JPEG, PCX, PCL, PDF, HTML or HPGL. The server software (1MAGE) operates on Linux, Unix, and Windows servers. Supporting clients include Microsoft Windows, X-Windows, ASCII, JAVA and browser clients
- Device connectivity via Ethernet or token ring networks using TCP/IP communication protocol or over the Internet
- Compatibility with IBM AIX, HP-UX, Sun Solaris, SCO Unix, Red Hat Linux and Windows
- Recognition technology and scanning tasks run on Microsoft Windows
- UniVerse and UniData ("U2") Relational Database software from IBM

1MAGE includes several distinguishing features: the ability to use many different types of workstations, the ability to quickly and easily integrate with the existing business application software using application programming interfaces (APIs), and the ability to handle the needs of companies of all sizes economically. Through the use of the Linux, Unix, and Windows operating systems and open systems technology, the Company seeks to offer its customers an imaging solution at a reasonable cost. Because 1MAGE is a server-based product, the Linux operating system ("O/S") has become very popular with end users of our software. In 2001, the majority of systems sold through the direct sales force installed their document imaging systems on servers running the Linux O/S.

During 2001, sales of 1MAGE software licenses (excluding annual license fees) accounted for $1.1 million (42% of total revenue); in 2000, revenue from sales of software licenses accounted for $881,000 (41% of total revenue). 1MAGE utilizes the Linux, Unix, and Windows operating systems and IBM's U2 database software. The Company's open systems technology makes its software transportable to numerous hardware products from varying manufacturers. Because of the number of hardware manufacturers using the Linux, Unix, and Windows operating systems, the Company's software customers are rarely restricted in their choice of hardware manufacturers.

The Company also sells peripheral products, at the customer's request, such as scanners and jukeboxes, although this aspect of the Company's business has been de-emphasized in recent years. Because computer hardware and peripheral products are purchased upon request to fill customer orders, no inventory is maintained. Hardware is generally shipped directly from the manufacturer to the customer. In 2001, revenue from hardware sales accounted for $67,000 (2%) of the Company's total revenue, as compared to $113,000 (5%) of total revenue for 2000.

SERVICES AND ANNUAL FEES

The Company licenses its 1MAGE software to its customers and charges an annual license fee which must be paid to continue receiving support for the use of the software. During 2001 and 2000, annual license fees accounted for $1.1 million (or 41%) and $896,000 (or 42%), respectively, of the Company's net sales. The Company believes recurring annual license fees from new and existing customers will contribute to the long-term stability of the Company. The Company also provides professional services to its customers. These services include preparation of image management plans for customers, installation, training, image enabling existing software, and consulting services. For the years ended December 31, 2001 and 2000, the revenues from these services accounted for $407,000, or 15%, and $272,000, or 13%, of the Company's net sales. The Company does not provide service for hardware; rather, service for computer hardware sold by the Company is provided directly by the manufacturer or the manufacturer's authorized dealer.

MARKETING AND DISTRIBUTION

To date, the Company has signed VAR agreements for 1MAGE with ten resellers specializing in a variety of industries, including automotive retail, health care, construction, collection services, public safety, utilities, and employee benefit services. In addition, the Company licenses its software and certain other products and services through agreements with two Application Service Providers (ASPs) in the healthcare industry. The Company provides its software to independent software integrators (resellers), who in turn market products, including or featuring 1MAGE, to each of their individual markets. The Company's overall marketing objective is to support the current business partners and to continue to enroll new software integrators in the program. The Company provides training aids, an Internet demonstration site, user instruction manuals and other documentation, and a newsletter to keep its resellers, as well as prospective resellers and customers, informed of new product applications and developments.

The Company also markets 1MAGE through its direct sales force. The general strategy is to (1) help customers define the goals for their system, (2) provide the means of achieving those goals through our document management software and appropriately configured computer systems, and (3) help assure the ongoing success of this collaborative process by providing continuing support, including on-site training and educational programs. The Company also markets its products and services over the Internet.

CUSTOMERS

The Company sells its 1MAGE software to businesses in a wide variety of industries and markets, facilitated through the use of VARs and its direct sales force.

During the years 2001 and 2000, the Company generated 36% and 35%, respectively, of its revenue from one customer, Reynolds & Reynolds ("Reynolds"). Reynolds is a Fortune 500 company headquartered in Dayton, Ohio. In May 1994, the Company signed a software license agreement with Reynolds for the exclusive right to sublicense certain modules of 1MAGE (without payment of further license fees to the Company) to businesses primarily engaged in retail sales of new or used automobiles, trucks, or tractors. In 1996, the Company signed a Subscription and Maintenance agreement with Reynolds. License fees are paid to the Company for certain products subsequently available in newer releases of 1MAGE. These features include the Company's client software.

On January 18, 2002, Reynolds notified the Company of its intent to terminate the 1996 Subscription and Maintenance agreement effective April 22, 2002. As of this date, the Company has not yet determined what new agreements, if any, it will enter into with Reynolds to govern its future licensing arrangements. Notwithstanding the termination of the 1996 agreement, management believes that Reynolds will continue to provide a significant flow of revenue from existing installations of 1MAGE, but the level of future sales cannot be predicted. The loss of this customer would have a significantly adverse impact on the Company. Reynolds has installed the 1MAGE document management software in approximately 1,000 of its customer sites in the United States and Canada. The Company currently derives approximately $35,000 per month in revenues from licensing and other fees from these installations. The Company cannot predict at this time how much of this revenue will be lost as a result of the termination of the 1996 contract by Reynolds but it is possible that much, if not substantially all, of such revenue will be lost.

SOURCES OF SUPPLY

The Company has an OEM Software Agreement with IBM Corp. to sublicense their Universe and UniData database programs. The agreement authorizes the Company to include certain IBM programs as part of their imaging solution. This agreement currently runs until September 28, 2002 and it may be renewed for additional one (1) year terms. The Company has designed its product such that third party software can be easily integrated into the core products with minimal difficulty and effort.

POSSIBLE FLUCTUATIONS IN OPERATING RESULTS

The Company's current focus on offering its proprietary imaging software to a broader range of customers, through its emerging reseller network and its direct sales force, is expected to lessen the historical quarterly fluctuations in the Company's operating results. Nevertheless, large volume sales or groups of sales of 1MAGE licenses may cause significant variances in quarterly results that may be difficult to predict.

The Company's sales cycle, which generally commences at the time a prospective customer issues a request for proposal or otherwise demonstrates a serious interest in purchasing a system or software license and ends upon execution of a sales contract, is lengthy and not predictable with any degree of certainty. Prior sales and implementation cycles are not necessarily an indication of future cycles. Operating results could vary from period to period as a result of the length of the sales cycle, the timing of individual system sales, resellers' performance and conditions in the target markets and the economy in general.

TRADE SECRET AND COPYRIGHT LAWS

The Company regards its software as proprietary and relies for protection upon trade secret and copyright laws and non-disclosure agreements with its employees as well as restrictions on disclosure and transferability contained in its software license agreements with its customers. Despite these restrictions, it may be possible for competitors or customers to copy, or reverse compile, aspects of the Company's products or obtain information that the Company regards as proprietary. Furthermore, there can be no assurance that others will not independently develop software products similar to those developed or planned by the Company. Although the Company believes its software does not infringe on the proprietary rights of others and has not received any notice of claimed infringement, it is possible that portions of the software marketed by the Company could be claimed to infringe on existing proprietary rights. In the unlikely event that any such infringements are found to exist, there can be no assurance that any necessary licenses or rights could be obtained, or could be obtained on terms satisfactory to the Company. Further, in such event, the Company could be required to modify the infringing software. There can be no assurance that the Company would be able to do so in a timely manner, upon acceptable terms and conditions, or at all; even though the failure to do so could have a material adverse effect on the Company.

BACKLOG

As a practical matter, the Company's business has evolved to the point where the Company has minimal backlog at any given point in time. With respect to software license sales, because there is no time delay between receipt of an order and delivery of the software, electronically or otherwise, there is effectively no backlog. For hardware, because of direct delivery of the hardware by the manufacturer, hardware sales have such short lead times that unfilled firm orders seldom, if ever, build up to significant levels.

The Company normally receives a deposit of between 25% and 50% of the hardware and software price when an order is placed. This deposit may or may not be returned upon cancellation, depending on the circumstances of the cancellation.

COMPETITION

The Company experiences intense competition in its business from competitors who target one or more of the same markets or market segments as the Company. Software and systems that perform many of the same functions as the Company's systems and software are also available from a number of competitors of the Company. Some of these competitors are larger and have longer operating histories, significantly greater financial, technical, marketing and other resources, significantly greater name recognition and a larger installed base than we do. As a result, these competitors may be able to respond more quickly to emerging technologies and changes in customer requirements, or to devote greater resources to the development, promotion and sale of their products than we can.

The Company believes that usage of the popular Linux and Unix operating systems and the IBM U2 databases has strengthened the Company's competitive position by making the Company's software compatible with more types of hardware and with the IBM U2 application software offered by software developers and system integrators. The Company further believes that its principal advantage over its competitors is the Company's utilization of the Linux, Unix, and Windows-based open systems architecture and the IBM U2 databases that can be offered at lower prices.

LIMITED MARKETS

The reseller program targets complementary markets and allows the Company to draw from a variety of industries with respect to its imaging software products. As noted above, the Company's strategy has been to expand the domestic and international markets for its imaging software by engaging resellers for various industries and markets.

The Company's experience has been that economic downturns or increased competitive pressures in its niche markets sometimes result in reduction or deferral of capital expenditures by potential customers. Certain adverse conditions can sometimes lead to opportunities as potential customers downsize to smaller, more cost-efficient computer systems or replace custom designed systems that require higher levels of support and maintenance.

PRODUCT DEVELOPMENT

The software and services market in which we compete is characterized by (1) rapid technological change, (2) frequent introduction of new products and enhancements, and (3) changing customer needs. Our future success depends on our ability to support existing products and develop new products. The Company capitalizes software development costs once technological feasibility is established. During 2001, the Company developed a new release of 1MAGE which employs new technologies, including Application Service Provider (ASP) requirements and three JAVA systems (i.e. 1APPROVE, 1ACCESS and 1ADMIN) which will operate on any platform that supports JAVA programming language. In addition, improvements were made to the hardware/software compatibility offerings available for Linux users. During 2001 and 2000, the Company spent $271,000 and $291,000, respectively, for computer software development.

EMPLOYEES

As of March 15, 2002, the Company employed twenty-one persons, twenty of whom serve on a full-time basis and one on a part-time basis. Responsibilities are divided as follows: eight persons in sales and marketing, ten in technical support and programming functions, and three in administrative positions.

Because the competition for skilled employees in the computer industry is intense, the Company provides incentive compensation packages to many of its employees, including its executive officers. The Company's chief executive officer, David R. DeYoung, receives a quarterly bonus equal to 5% of the Company's pretax profits. (See "Executive Compensation") The Company's chief financial officer receives a quarterly bonus equal to 4% of the Company's pretax profits. Sales personnel receive a commission based upon sales. The Company has a policy of encouraging the effort and loyalty of all of its employees by making all employees eligible for the grant of stock options under its Equity Incentive Plan, subject to vesting schedules. The Company believes that these incentive programs are important in attracting and retaining skilled personnel. The future success of the Company will depend in large part upon the quality of its employees and the efforts they expend on behalf of the Company.

None of the Company's employees are represented by a labor union, and the Company has experienced no work stoppage. The Company believes that its employee relations are good.

ITEM 2. PROPERTIES

The Company's executive offices consist of approximately 4,181 square feet at Plaza Quebec, 6025 South Quebec Street, Suite 300, Englewood, Colorado, 80111 and are occupied pursuant to a sublease agreement between the Company and Communications World International, Inc. with monthly rental payments of $7,442. The term of the sublease commenced February 1, 1999 and will terminate on July 31, 2003. The landlord is responsible for property taxes, utilities, janitorial services, repairs, and maintenance. The Company believes that its facilities and equipment are in good condition and are satisfactory for their present uses.

ITEM 3. LEGAL PROCEEDINGS

There are no material pending legal proceedings to which the Company is a party.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The Company did not submit any matters to a vote of security holders through the solicitation of proxies or otherwise during the fourth quarter of the Company's calendar year ended December 31, 2001.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED SHAREHOLDER MATTERS

MARKET INFORMATION

The Company's Common Stock is quoted in the OTC Bulletin Board under the symbol ISOL. The following table sets forth, for the fiscal quarters indicated, the high and low bid prices per share for the Common Stock as reported on the OTC Bulletin Board.

2001

	High	Low
First Quarter	$ 1.00	$ 0.63
Second Quarter	0.95	0.63
Third Quarter	1.00	0.55
Fourth Quarter	0.75	0.55

2000

	High	Low
First Quarter	$ 4.19	$ 1.19
Second Quarter	3.00	1.13
Third Quarter	1.50	.88
Fourth Quarter	1.06	.63

These quotations reflect interdealer prices, without retail mark-up, mark down or commission and may not necessarily represent actual transactions.

On March 15, 2002, the closing bid price per share for the Common Stock was $.60 as reported on OTC:BB. On that same date, there were approximately 1,038 holders of record of the Common Stock.

DIVIDENDS

The Company has never declared or paid cash dividends on its Common Stock and has no present intention to do so. For the foreseeable future, any earnings will be retained to finance the development and expansion of the Company's business. The declaration and payment of future dividends will be determined by the Company's Board of Directors in light of conditions then existing, including the Company's earnings, financial condition and capital requirements.

ITEM 6. SELECTED FINANCIAL DATA

The following table sets forth, for the periods indicated, selected financial data of the Company. This table should be read in conjunction with the financial statements and notes included in Item 8 of this Form 10-K and the section entitled "Management's Discussion and Analysis of Results of Operations and Financial Condition" following this section.

Statements of Operations	Years Ended December 31,				
In thousands, except for per share data:	2001	2000	1999	1998	1997
Net Sales	$2,776	$2,163	$1,806	$2,151	$1,809
Cost of Sales	1,109	934	987	935	918
Gross Profit	1,667	1,229	819	1,216	891
Gross Profit (as a % of Net Sales)	60%	57%	45%	57%	49%
Selling, General & Administrative expenses	1,500	1,211	1,163	1,097	1,363
Income(Loss) before Income Taxes	161	11	(365)	5	(479)
Net Income(Loss)	211	8	(367)	2	(484)
Net Income(Loss) Per Share	.07	.00	(.16)	.00	(0.23)
Weighted Average Number of Outstanding Shares	3,146	3,056	2,330	2,173	2,146

Balance Sheets	Years Ended December 31,				
In thousands:	2001	2000	1999	1998	1997
Working Capital/(Deficit)	$ 140	$ (93)	$(186)	$ 196	$ 43
Total Assets	1,496	1,428	1,364	1,710	1,602
Long Term Obligations	1	3	1	154	159
Total Stockholders Equity	925	714	654	922	860

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

YEAR ENDED DECEMBER 31, 2001 COMPARED TO YEAR ENDED DECEMBER 31, 2000.

The Company's total revenue was $2.8 million for the year ended December31, 2001 compared to $2.2 million for the year ended December 31, 2000, representing an increase of $613,000 or 28%. The increase in revenue is primarily due to the combination of a 31% increase, or $276,000, in software license revenue and a 28% increase, or $248,000, in annual license fees. The number of systems sold through our direct sales force in 2001 was more than double the number sold in 2000, as customers seemed to be scrutinizing their budgets for technology upgrades more closely in light of the global economic weakness. The increase in annual license fees was due to the growing size of the Company's installed base of customers. The professional service group increased service revenue by 50% for the year due to support and technical services provided to existing customers and expanded pre-installation offerings to new customers. Hardware sales comprised 2% of the total revenue, as compared to 5% a year ago. Gross profit on revenue for the year 2001 increased to 60%, as compared to 57% for 2000, as a result of the increase in software license revenue. Selling, general and administrative expenses increased 23% or $ 284,000, in 2001. This increase was attributed to higher salaries and benefits, sales commissions, and various marketing expenses. In addition, the Company wrote off inventory that was deemed to be obsolete. Net income of $211,000 for 2001 reflects a significant gain over the $8,000 net income posted for the previous year. Earnings per share for the year 2001 were $.07, as compared to $.00 per share for 2000.

Sales through reseller channels increased 28%, or $246,000, to $1.1 million from $923,000 reported for 2000. Revenue from indirect channels for any period is subject to significant variations. As a result, the Company believes that period to period comparisons of indirect revenue are not necessarily meaningful and should not be relied upon as an indication of future performance. See the discussion of Reynolds & Reynolds below.

The events of September 11th resulted in a number of delays by customers of potential orders and may continue to adversely affect demand for the Company's products in certain industries.

YEAR ENDED DECEMBER 31, 2000 COMPARED TO YEAR ENDED DECEMBER 31, 1999.

The Company's revenue for the year ended December 31, 2000 of $2.2 million was 20% greater than $1.8 million reported for the year earlier. The increase in revenue is attributable to the combination of a $243,000 (38%) increase in software sales and a $145,000 (19%) increase in recurring annual license fees. Management believes these two components of revenue are crucial for the long-term success of the Company. Hardware sales comprised just 5% of the total revenue, as compared to 8% a year ago. The professional service group increased Service revenue by 2% for the year, posting revenue of $272,000. Sales through reseller channels increased $220,000, or 33%, from the year earlier. Gross profit on revenue for the year 2000 increased to 57%, as compared to 45% for 1999, as a direct result of the significant increase in software sales. Selling, general and administrative expenses increased 4% (or $48,000) for the year over year periods. Sales and marketing expenses increased $61,000 as the Company made concerted efforts to expand its presence in targeted markets. Net income of $8,000 for 2000 reflected a $375,000 gain over the previous year, when the Company experienced a significant slowdown in sales due to the Y2K situation. Earnings per share for the year 2000 were $.00, as compared to a loss per share of ($.16) for 1999.

LIQUIDITY AND CAPITAL RESOURCES

The Company's cash and cash equivalents increased approximately $62,000 during the twelve months ended December 31, 2001 as compared to December 31, 2000. In addition, during 2001, the Company used cash of $200,000 to repay the total outstanding principal amount of its line of credit. The Company had working capital of approximately $140,000 on December 31, 2001. The Company's cash flow from operations increased to approximately $565,000 for 2001.

On January 18, 2002, Reynolds and Reynolds gave notice of the termination of its 1996 Subscription and Maintenance agreement with the Company effective April 22, 2002. As of this date, it is not possible to predict what impact this will have on future cash flows. The Company may continue to receive substantial cash payments under one or more new agreements with Reynolds, but the amount and the duration of such revenue is uncertain. If the Company is not able to replace this revenue stream with revenue from new customers or its installed base of customers, the termination of this agreement would have a significantly adverse effect on the short-term cash flow of the Company. The Company believes that any shortfall in near term cash flow can be compensated for by increased borrowings.

The Company's internal sources of liquidity are revenues from operations and cash on hand. The Company receives most of its revenues for software licenses and system sales upon installation and does not maintain inventory balances. The Company believes that its existing cash, cash and the cash flows generated from operations, will be sufficient to meet its anticipated cash needs for working capital for at least the next twelve months. The Company has a $200,000 revolving line of credit. The loan is collateralized by all accounts receivable and general intangibles of the Company. There were no borrowings outstanding under the line of credit at March 29, 2002.

The Company has no material commitments for capital expenditures for 2002.

Management believes that fourth quarter sales were impacted as a result of the significant global economic slowdown in the technology sector as well as the events on September 11, 2001. Our customers make a discretionary decision to implement our products based upon their individual resources and budget constraints. As a result, the loss or delay of individual orders could have a significant impact on quarterly operating results and revenue. Due to poor visibility as a result of the current economic and political environment, we are not currently able to assess the likely trend of software revenue in future periods.

RISKS TO FUTURE FINANCIAL PERFORMANCES

VARIABLE OPERATING RESULTS. Our future operating results may vary significantly and are difficult to predict due to a number of factors, of which many are beyond our control. These factors include:

- demand for our products;
- the level of product and price competition;
- the length of our sales cycle;
- the size and timing of individual license transactions;
- the delay or deferral of customer implementations;
- our success in expanding our customer support organization, direct sales force and indirect distribution channels;
- the timing of new product introductions and product enhancements;
- changes in our pricing policy;
- the mix of products and services sold;
- our ability to develop and market new products and control costs;
- current economic and political conditions; and
- our future relationship with Reynolds and Reynolds and other large customers.

CURRENT ECONOMIC AND POLITICAL CONDITIONS MAY AFFECT RESULTS. During the last three months of 2001, we experienced a decrease in software revenue. We believe that this decrease was due to a broader economic slowdown that may or may not persist for some time. The slowdown has decreased our visibility and increased the risk to our revenue stream. Additionally, due to the September 11, 2001 terrorist attacks in New York City and Washington, D.C. and related events, the political landscape has significantly changed and could have a material impact on results going forward. We believe there has been an industry-wide slowdown in IT spending. Due to the discretionary nature of our customers' budget and purchase cycles and the absence of long-term customer purchase commitments, it is difficult to avoid fluctuations in quarterly operating results.

FORWARD LOOKING STATEMENTS

Some of the statements made herein are not historical facts and may be considered "forward looking statements." All forward-looking statements are, of course, subject to varying levels of uncertainty. In particular, statements which suggest or predict future events or state the Company's expectations or assumptions as to future events may prove to be partially or entirely inaccurate, depending on any of a variety of factors, such as adverse economic conditions, new technological developments, competitive developments, competitive pressures, changes in the management, personnel, financial condition or business objectives of one or more of the Company's customers, increased governmental regulation or other actions affecting the Company or its customers as well as other factors.

ITEM 8: FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

1MAGE SOFTWARE, INC.

INDEX TO FINANCIAL STATEMENTS

INDEPENDENT ACCOUNTANTS' REPORT

To the Board of Directors and Shareholders of
1mage Software, Inc.
Englewood, Colorado

We have audited the accompanying balance sheets of 1mage Software, Inc. as of December 31, 2001 and 2000, and the related statements of operations, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2001. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of 1mage Software, Inc. as of December 31, 2001 and 2000, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2001, in conformity with accounting principles generally accepted in the United States of America.

BKD, LLP

Denver, Colorado
January 18, 2002

1MAGE SOFTWARE, INC.
BALANCE SHEETS
DECEMBER 31, 2001 AND 2000

	2001	2000
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 212,421	$ 150,457
Receivables:		
Trade (less allowance: 2001, $10,000; 2000, $10,000)	421,977	407,251
Inventory	9,070	38,654
Deferred tax asset	50,000	--
Prepaid expenses and other current assets	15,597	21,233
Total current assets	709,065	617,595
PROPERTY AND EQUIPMENT, at cost, net	57,878	55,177
OTHER ASSETS:		
Software development costs, net	725,606	754,734
Inventory	2,928	--
Other	100	100
TOTAL ASSETS	$ 1,495,607	$ 1,427,606

LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Line of credit	$ --	$ 200,000
Current portion of capital lease obligations	1,784	1,785
Deferred revenue	233,000	213,494
Accounts payable	187,878	185,468
Accrued liabilities	146,510	109,450
Total current liabilities	569,172	710,197
LONG-TERM OBLIGATIONS:		
Capital lease obligations	1,093	3,224
SHAREHOLDERS' EQUITY:		
Common Stock, $.004 par value - 10,000,000 shares authorized; shares outstanding: 2001 and 2000-3,146,554	12,586	12,586
Additional paid-in capital	7,238,658	7,238,658
Accumulated deficit	(6,325,902)	(6,537,059)
Total shareholders' equity	925,342	714,185
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 1,495,607	$ 1,427,606

See notes to financial statements.

1MAGE SOFTWARE, INC.
STATEMENTS OF OPERATIONS
FOR THE YEARS ENDED DECEMBER 31, 2001, 2000, AND 1999

	2001	2000	1999
REVENUE:			
System sales and software licenses	$ 1,224,057	$ 994,123	$ 787,828
Services and annual fees	1,551,874	1,168,540	1,018,520
Total revenue	2,775,931	2,162,663	1,806,348
COST OF REVENUE:			
System sales and software licenses	520,299	558,016	596,128
Services and annual fees	589,122	375,356	391,277
Total cost of revenue	1,109,421	933,372	987,405

GROSS PROFIT	1,666,510	1,229,291	818,943
OPERATING EXPENSES:			
Selling, general & administrative	1,500,038	1,216,288	1,162,921
INCOME/(LOSS) FROM OPERATIONS	166,472	13,003	(343,978)
OTHER INCOME/(EXPENSE):			
Interest income	4,891	8,059	9,665
Interest expense	(10,206)	(15,408)	(32,140)
Other	--	--	1,760
Total other income(expense)	(5,315)	(7,349)	(20,715)
INCOME/(LOSS) BEFORE INCOME TAXES	161,157	10,654	(364,693)
PROVISION/(CREDIT) FOR INCOME TAXES	(50,000)	2,500	2,500
NET INCOME/(LOSS)	$ 211,157	$ 8,154	$ (367,193)
BASIC AND DILUTED INCOME (LOSS) PER COMMON SHARE	$ .07	$ 0.00	$ (.16)
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING	3,146,554	3,055,600	2,329,818

See notes to financial statements.

1MAGE SOFTWARE, INC.
STATEMENTS OF SHAREHOLDERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2001, 2000, AND 1999

	Common Stock		Additional
	Shares	Amount	Paid-In Capital
Balances, December 31, 1998	2,203,019	8,811	6,904,247
Conversion of notes payable into Common Stock	326,474	1,306	201,180
Exercise of incentive stock options	113,000	452	65,618
Issuance of non-qualified stock options	--	--	18,046
Net loss			
Balances, December 31, 1999	2,642,493	10,569	7,189,091
Exercise of incentive stock options	447,375	1,790	196,047
Surrender shares for exercise of incentive			

stock options	(32,294)	(129)	(128,078)
Exercise of Class A Warrants	100,000	400	43,350
Surrender shares for exercise of Class A Warrants	(11,020)	(44)	(43,706)
Cancellation of non-qualified stock options	--	--	(18,046)
Net income	--	--	--
Balances, December 31, 2000	3,146,554	$ 12,586	$ 7,238,658
Net income	--	--	--
Balances, December 31, 2001	3,146,554	$ 12,586	$ 7,238,658

See notes to financial statements.

1MAGE SOFTWARE, INC.
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2001, 2000, AND 1999

	2001	2000	199
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net earnings/(loss)	$ 211,157	$ 8,154	$(367,
Adjustments to reconcile earnings/(loss) to net cash provided by operating activities:			
Depreciation and amortization	327,663	342,338	367,
Deferred tax asset	(50,000)	--	
Deferred revenue	19,506		
(Cancellation)/Issuance of stock options for services	--	(18,046)	18,
Changes in assets and liabilities:			
Receivables	(14,726)	(201,509)	328,
Inventory	26,626	10,553	6,
Prepaid expenses and other assets	5,636	(7,805)	(3,
Accounts payable	2,410	(24,414)	(83,
Accrued liabilities and deferred income	37,060	(3,703)	6,
Net cash provided by operating activities	565,332	105,568	273,
CASH FLOWS FROM INVESTING ACTIVITIES:			
Purchase of property and equipment	(30,263)	(14,125)	(25,
Additions to capitalized software	(270,973)	(290,745)	(302,
Redemption of certificate of deposit	--	--	25,
Net cash used for investing activities	(301,236)	(304,870)	(303,
CASH FLOWS FROM FINANCING ACTIVITIES:			

Additions to line of credit	185,000	300,000	68,
Repayment of line of credit	(385,000)	(268,235)	(50,
Repayment of long-term obligations	(2,132)	(5,566)	(4,
Proceeds from exercise of Common Stock options	--	69,630	66,
Net cash provided by financing activities	(202,132)	95,829	79,
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	61,964	(103,473)	49,
CASH AND CASH EQUIVALENTS, beginning of year	150,457	253,930	204,
CASH AND CASH EQUIVALENTS, end of year	$ 212,421	$ 150,457	$ 253,

See notes to financial statements

1MAGE SOFTWARE, INC.
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2001, 2000, AND 1999

	2001	2000	1999
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:			
Cash paid for interest	$ 10,206	$15,408	$15,820
Income taxes paid	$ 2,500	$ 2,500	$ 2,500
SUPPLEMENTAL SCHEDULE OF NON-CASH ACTIVITIES:			
Acquisition of property and equipment by assuming capital lease obligations	$ --	6,197	$ --

1MAGE SOFTWARE, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2001, 2000, AND 1999

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND ORGANIZATION

ORGANIZATION AND NATURE OF BUSINESS - 1mage Software, Inc. (the "Company") was incorporated in Colorado in December 1981.

The Company develops and markets a Linux, Unix, and Windows-based electronic document image management and retrieval system. The Company earns the majority of its revenues in the United States.

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

INVENTORIES consist of finished goods and are stated at the lower of cost (specific identification method) or market (net realizable value).

PROPERTY AND EQUIPMENT are stated at cost. Depreciation and amortization are computed using the straight-line method over the estimated useful lives (generally five years) of the assets or the lease term, if shorter. The Company capitalizes all expenditures for property and equipment in excess of $500.

ADVERTISING COSTS are expensed as incurred. Advertising expenses totaled $121,718, $103,621, and $65,348 in 2001, 2000 and 1999, respectively.

SOFTWARE DEVELOPMENT COSTS are capitalized when technological feasibility is established. Such costs are stated at the lower of unamortized cost or net realizable value. Amortization is computed using either the straight-line method based on estimated economic lives of the products (five years) or the ratio that current product revenues bear to the total of current and anticipated future product revenues, whichever is greater. It is reasonably possible that those estimates of anticipated future gross revenues, the remaining estimated economic life of the products, or both will be reduced significantly in the near term due to competitive pressure. As a result, the carrying amount of the capitalized software costs may be reduced materially in the near term. The amounts capitalized for the years ended December 31, 2001, 2000, and 1999 were $270,973, $290,745, and $302,747, respectively. Amortization of these costs totaled $300,101, $307,930, and $317,400, respectively. The net realizable value of such capitalized costs is reviewed by management on a periodic basis, and costs in excess of net realizable value, if any, are charged to operations.

REVENUE RECOGNITION - Revenue from the sale of software licenses, computer equipment, and existing application software packages is recognized when the software and computer equipment are shipped to the customer, remaining vendor obligations are insignificant, there are no significant uncertainties about customer acceptance and collectibility is probable. Revenue from related services, including installation and software modifications, is recognized upon performance of services. Maintenance revenue is recognized ratably over the maintenance period.

The Company performs credit evaluations of its customers' financial condition and generally does not require collateral. The Company retains a security interest in the equipment and software sold until they are paid in full. Receivables are generally due within 30 days, with those customers not meeting those requirements being subject to stricter credit policies.

A single customer accounted for 36%, 35% and 28% of revenues in 2001, 2000 and 1999, respectively.

Two different customers accounted for 18% and 10% of accounts receivable at December 31, 2001.

One customer accounted for 28% of accounts receivable at December 31, 2000. Two different customers accounted for 11% and 10% of accounts receivable at December 31, 1999.

EARNINGS (LOSS) PER SHARE is computed by dividing net income (loss) by the weighted average number of common and equivalent shares outstanding during the year. The potential dilution from Common Stock equivalents is not material. Fully diluted earnings per share are either anti-dilutive or not materially different from basic earnings per share.

INCOME TAXES The Company follows the liability method of accounting for income taxes in accordance with Statement of Financial Accounting Standards (SFAS) No. 109. Under this method, deferred income taxes are recorded based upon differences between the financial reporting and tax bases of assets and liabilities and are measured using enacted tax rates and laws that will be in effect when the underlying assets or liabilities are received or settled.

The Company has recorded a valuation allowance against the deferred tax assets due to the uncertainty of ultimate realizability.

ESTIMATES - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reporting periods. Actual results could differ from those estimates.

RECLASSIFICATION - The Company has reclassified certain amounts from prior years to conform with the current year presentation. These reclassifications had no effect on net income.

2. PROPERTY AND EQUIPMENT

Property and equipment at December 31 consists of the following:

	2001	2000
Equipment	$ 651,055	$ 626,656
Furniture	49,177	43,313
Leasehold improvements	8,262	8,262
	708,494	678,231
Less: accumulated depreciation	(650,616)	(623,054)
	$ 57,878	$ 55,177

3. ACCRUED LIABILITIES

Accrued liabilities at December 31 consists of the following:

	2001	2000
Sales tax payable	$ 36,694	$ 22,949
Accounting and audit fees	14,481	15,486
Accrued compensation	39,036	32,124
Other	56,299	38,891
	$146,510	$109,450

4. LINE OF CREDIT

The Company has a $200,000 annual revolving bank line of credit which is extended until February 24, 2003 and bears interest at prime plus 1.5% (total rate of 8.25% at December 31, 2001) and is collateralized by all accounts receivable and general intangibles of the Company. Total borrowings outstanding under the line of credit were $0 and $200,000 at December 31, 2001 and 2000, respectively.

5. SHAREHOLDERS' EQUITY

STOCK COMPENSATION PLANS

At December 31, 2001, the Company has three stock-based compensation plans, which are described below. The Company applies Accounting Principles Board (APB) Opinion 25 and related interpretations in accounting for its plans. Accordingly, no compensation cost has been recognized. Had compensation cost for the Company's three stock-based compensation plans been determined based on the fair value at the dates of awards under those plans consistent with the method of FASB Statement 123, the Company's net income (loss) and earnings (loss) per share would have been as indicated below:

		2001	2000	1999
Net income (loss):				
	As reported	$ 211,157	$ 8,154	$ (367,193
	Pro forma	$ 112,349	$ (147,361)	$ (518,211
Income/(Loss) per common share:				
	As reported	$ 0.07	$ 0.00	$ (0.16)
	Pro forma	$ 0.04	$ (0.05)	$ (0.22)

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions for grants in 2001, 2000, and 1999:

	2001	2000	1999
Dividend Yield	0%	0%	0%
Expected Volatility	124%	135%	144%
Risk-Free Interest Rate	4.75%	5.0%	6.00%
Expected Lives	8.4years	3.2 years	8.7 years

The Black-Scholes option-pricing model was developed for use in estimating the fair value of traded options, which have no vesting restrictions and are freely transferable. In addition, option valuation models require the input of highly subjective assumptions, including the expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

1996 EQUITY INCENTIVE PLAN

In September 1996, the Board of Directors authorized 1,000,000 shares of Common Stock for issuance under its 1996 Equity Incentive Plan ("1996 Plan") as incentive stock options ("ISOs") or non-qualified stock options ("NQSOs"). The Company grants ISOs only to employees. The Company grants NQSOs and restricted stock to persons who are employees of the Company and to non-employee directors.

The options are granted to purchase Common Stock at the fair market value on the grant date or at other prices as determined by the Board of Directors. The option-vesting period is determined at the time of each grant, and all options expire two to ten years from the grant date.

A summary of the 1996 Plan stock option activity follows:

	Outstanding Shares	Exercise Price	Weighted Avg. Exercise Price
Balances, January 1, 1999	453,000		$.43
Granted	375,000	$.33-$1.29	.62
Balances, December 31, 1999	828,000		.52
Granted	192,500	$.63-$1.44	.66
Canceled	(189,000)	$.33-$.66	(.56)
Exercised	(198,000)	$.34-$1.47	(.40)
Balances, December 31, 2000	633,500		.59
Granted	145,000	$.56 - $.75	.60
Canceled	(8,500)	$.63 - $.66	.65
Balances, December 31, 2001	770,000		$.59

The following table summarizes information about stock options under the plan at December 31, 2001:

	Outstanding			Exercisable	
Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price

0.34 to 0.44	235,000	5.5 years	0.44	235,000	0.44
0.56 to 0.84	519,000	7.8 years	0.64	382,934	0.65
1.28 to 2.06	16,000	8.0 years	1.36	16,000	1.36

At December 31, 2001, options for 633,934 shares were exercisable under the 1996 Plan. There were 32,000 shares available for future grant.

The weighted-average grant-date fair value of options granted during 2001, 2000, and 1999 were $.60, $.52, and $.65, respectively.

1994 STOCK OPTION AND GRANT PLAN
In April 1994, the Company authorized 700,000 shares of Common Stock for issuance under its 1994 Stock Option and Grant Plan ("1994 Plan") to employees and directors.

The options are granted to purchase Common Stock at the fair market value on the date of grant or at other prices as determined by the Board of Directors ("the Board"). Options issued under the 1994 Plan become exercisable in one or more installments during its term and the right to exercise may be cumulative, as determined by the Board. Options expire as determined by the Board, but not more than 10 years after the date of grant.

Details of activity under the 1994 Plan are as follows:

Stock Options	Outstanding	Exercise Price	Weighted Average Exercise Price
Balances, January 1, 1999			$.51
Granted	104,000	$.66	.66
Canceled	(13,501)	$.34 - $1.44	(.59)
Exercised	(113,000)	$.34 - $.78	(.58)
Balances, December 31, 1999	399,000		.53
Granted	9,500	$.63	.63
Canceled	(5,250)	$.34 - $1.28	(.88)
Exercised	(86,000)	$.34 - $1.28	(.53)
Balances, December 31, 2000	317,250		.52
Granted	4,500	$.56	.56
Canceled	(1,000)	$.625	(.63)
Balances, December 31, 2001	320,750		$.52

Stock Grants		Grant Price	Weighted Average Exercise Price
Balances, January 1, 1999	83,166	$.84 - $1.13	$1.66
Granted/Canceled	--	--	--
Balances, December 31, 1999	83,166		1.66
Granted/Canceled	--	--	--
Balances, December 31, 2000	83,166		1.66
Granted/Canceled	--	--	--
Balances, December 31, 2001	83,166		$1.66

The following table summarizes information about stock options under the plan at December 31, 2001:

	Outstanding			Exercisable	
Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
0.34 to 0.44	126,750	3.7 years	0.34	101,125	0.34
0.56 to 0.84	194,000	3.6 years	0.64	151,435	0.64

The weighted-average grant-date fair value of options granted during 2001, 2000, and 1999 were $.56, $.48, and $.64, respectively.

At December 31, 2001, options to purchase 252,560 shares of Common Stock were exercisable and 99 shares were available for future grant.

1993 STOCK OPTION PLAN

In May 1994, the Company authorized 235,000 shares of Common Stock for issuance under its 1993 Stock Option Plan ("1993 Plan") as incentive or non-qualified stock options. The Company grants nonqualified stock options to officers, directors and employees. Incentive stock options may be granted to employees.

The options are granted to purchase Common Stock at the fair market value on the grant date or at other prices as determined by the Board of Directors. The option-vesting period is determined at the time of each grant, and all options expire two to ten years from the grant date.

A summary of the 1993 Plan stock option activity follows:

	Outstanding Shares	Exercise Price	Weighted Avg. Exercise Price
Balances, January 1, 1999	239,675		$.45
Canceled/Granted	--		--
Balances, December 31, 1999	239,675		.45
Granted	--		--
Exercised	(163,375)	$.44 - $.75	(.45)
Balances, December 31, 2000	76,300		.47
Granted	3,500	$.56	.56
Balances, December 31, 2001	79,800		$.47

The following table summarizes information about stock options under the plan at December 31, 2001.

	Outstanding			Exercisable	
Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
0.34 to 0.44	71,300	4.2 years	0.43	70,425	0.43
0.56 to 0.84	7,500	7.3 years	0.66	7,500	0.66
1.28 to 2.06	1,000	4.0 years	1.72	1,000	1.72

The weighted-average grant-date fair value of options granted during 2001 was $.56.

At December 31, 2001, options for 78,925 shares were exercisable under the 1993 Plan. There were no shares available for future grant.

COMMON STOCK WARRANTS

On January 28, 1994, the Board of Directors granted 100,000 warrants to an officer to purchase shares of Common Stock at an exercise price of $1.5625 per share, expiring on January 31, 1999. In January 1998, these warrants were repriced to $.44 per share and the term was extended until January 28, 2004. In March 2000, the officer exercised these warrants. There are no common stock warrants outstanding as of December 31, 2001.

COMMON STOCK RESERVED

Common Stock reserved at December 31, 2001 was as follows:

1996 Equity Incentive Plan	802,000
1994 Stock Option and Grant Plan	320,849
1993 Stock Option Plan	79,800
	1,202,649

7. INCOME TAXES

The provisions (credit) for income taxes for the years ended December 31, consists of:

	2001	2000	1999
Current:			
Federal	$ --	$ --	$ --
State	--	2,500	2,500
Total current	2,500	2,500	
Deferred:			
Federal	--	--	--
State	--	--	--
Total deferred	(50,000)	--	--
	$(50,000)	$ 2,500	$ 2,500

The following is a reconciliation of statutory federal income taxes to the actual provision (credit) for income taxes:

	2001	2000
Federal income taxes at statutory rate	$ 65,000	$ 3,600
Increase (decrease) in taxes resulting from state income taxes	6,300	(800)
Increase (decrease) in deferred tax asset valuation allowance	(141,000)	(133,000)
Expiration of business tax credits	14,000	121,000
Other, net	5,700	11,700
Provision/(credit) for income taxes	$ (50,000)	$ 2,500

The components of the net deferred tax (liability) asset recognized in the accompanying balance sheets are as follows:

2001

Deferred tax liability	$	(2,000)
Deferred tax asset		2,109,000
Valuation allowance		(2,057,000)
	$	50,000

The types of temporary differences between the tax bases of assets and liabilities and their financial reporting amounts that give rise to a significant portion of the deferred tax asset and their approximate tax effects are as follows:

		2001
Future income (deductions):		
Net operating loss	$	2,090,000
Allowance for doubtful accounts		4,000
General business tax credits		--
Depreciation		12,000
Other, net		1,000
	$	2,107,000

The Company has net operating loss carry forwards for federal income tax purposes of approximately $5,394,000. These carry forwards expire on varying dates from 2005 through 2019.

8. EMPLOYEE BENEFIT PLAN

The Company has a Cash or Deferred Profit Sharing Plan ("the 401(k) Plan"). The 401(k) Plan is designed to qualify under Section 401(k) of the Internal Revenue Code and allows the Company to make discretionary contributions as determined by the Company's Board of Directors. For the years ended December 31, 2001, 2000, and 1999, the Company contributed $4,650, $3,988, and $2,476 to the 401(k) Plan.

9. COMMITMENTS AND CONTINGENCIES

At December 31, 2001 and 2000, equipment with a net book value of $6,663 and $10,735, net of accumulated amortization of $13,698 and $9,626, respectively, has been leased under capital leases.

The Company leases its executive offices under a noncancelable operating lease which expires in July 2003. Future minimum payments for lease obligations are as follows:

		Capital	Operating
	2002	$ 3,060	$ 89,304
	2003	510	52,094
Total minimum lease payments		3,570	$141,398
Amount representing interest		(693)	
Present value of min. lease payments		2,877	
Current portion		(1,784)	
Long-term portion		$ 1,093	

The Company has bonus agreements with two officers that provide for quarterly bonuses of 5% and 4%, respectively, of the Company's pre-tax profits. The Company expensed bonuses of $33,352, $15,968, and $1,312 under these agreements for the years ended December 31, 2001, 2000, and 1999, respectively.

11. FINANCIAL INSTRUMENTS

All financial instruments are held for purposes other than trading. The following methods and assumptions were used to estimate the fair value of each financial instrument for which it is practicable to estimate that value:

CASH AND CASH EQUIVALENTS

The carrying amount approximates fair value because of the short maturity of those instruments.

DEBT

The fair value of the Company's debt is estimated based on borrowing rates currently available to the Company for bank loans with similar terms and maturities.

The estimated fair values of the Company's financial instruments at December 31, 2001 are as follows:

	Carrying Amount	Fair Value
Assets:		
Cash and cash equivalents	$ 212,421	$ 212,421
Receivables	$ 421,977	$ 421,977
Liabilities:		
Accounts Payable	$ 187,878	$ 187,878
Line of Credit	$ --	$ --

The estimated fair values of the Company's financial instruments at December 31, 2000 are as follows:

	Carrying Amount	Fair Value
Assets:		
Cash and cash equivalents	$ 150,457	$ 150,457
Receivables	$ 407,257	$ 407,257
Liabilities:		
Accounts Payable	$ 185,468	$ 185,468
Line of Credit	$ 200,000	$ 200,000

12. SEGMENT INFORMATION

The Company operates in one industry segment consisting of the development and marketing of electronic document image management and retrieval systems. The Company's technologies are managed as one segment because it offers similar products in similar markets and the factors determining strategic decisions are comparable for all products and markets.

Sales to foreign markets totaled $67,846, $57,911, and $102,831 for the years ending December 31, 2001, 2000, and 1999, respectively.

INDEPENDENT ACCOUNTANTS' REPORT
ON FINANCIAL STATEMENT SCHEDULES

To the Board of Directors and Shareholders of
1mage Software, Inc.
Englewood, Colorado

In connection with our audit of the financial statements of 1mage Software, Inc. for each of the three years in the period ended December 31, 2001, we have also audited the following financial statement schedule. This financial statement schedule is the responsibility of the Company's management. Our responsibility is to express an opinion on this financial statement schedule based on our audits of the basic financial statements. The schedule is presented for purposes of complying with the Securities and Exchange Commission's rules and regulations and is not a required part of the financial statements.

In our opinion, the financial statement schedule referred to above, when considered in relation to the basic financial statements taken as a whole, presents fairly, in all material respects, the information required to be included herein.

BKD, LLP

Denver, Colorado
January 18, 2002

1MAGE SOFTWARE, INC.

SCHEDULE VIII
VALUATION AND QUALIFYING ACCOUNTS

	Balance at beginning of period	Additions charged to: Costs and expenses	Additions charged to: Deductions	Balance at end of period
For the Year Ended December 31, 2001:				
Allowance for Doubtful Accounts	$ 10,000	$ 62,888	$ 62,888	$ 10,000
For the Year Ended December 31, 2000:				
Allowance for Doubtful Accounts	$ 10,000	$ 31,403	$ 31,403	$ 10,000
For the Year Ended December 31, 1999:				
Allowance for Doubtful Accounts	$ 15,000	$ 39,485	$ 44,485	$ 10,000

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

There were no disagreements with accountants on accounting and financial disclosure.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

The following sets forth certain information concerning the Company's Executive Officers and Directors:

Name	Age	First Year As Executive Officer or Director	Position With Company
David R. DeYoung	57	1981	President, Chief Executive Officer and Director

Mary Anne DeYoung	48	1994	Treasurer, Chief Financial Officer, Asst. Secretary
Robert Wiegand II	55	1992	Secretary and Director
Richard A. Knapp	56	1997	Director
James J. Capeless	62	2000	Director

DAVID R. DEYOUNG - CHAIRMAN, PRESIDENT, CHIEF EXECUTIVE OFFICER AND DIRECTOR

Mr. DeYoung has been President, Chief Executive Officer and a Director of the Company since its formation in 1981. He served in similar capacities with the Company's predecessor corporation from 1979 to 1981. He holds a Bachelor of Science Degree in Business Administration and Computer Science from California State Polytechnic University. Mr. DeYoung is the spouse of Mary Anne DeYoung.

MARY ANNE DEYOUNG - TREASURER, CHIEF FINANCIAL OFFICER, ASSISTANT SECRETARY AND DIRECTOR

Ms. DeYoung was elected to the Board of Directors in April 1996. Ms. DeYoung was appointed Treasurer, Chief Financial Officer and Assistant Secretary of the Company on December 15, 1994. Ms. DeYoung has served as Vice President, Finance and Administration since July 1986. Ms. DeYoung joined the Company as Controller in April 1981. From 1975 to 1981, Ms. DeYoung was a systems analyst with Arthur Andersen LLP, a financial analyst, and an independent financial consultant. Ms. DeYoung holds a Bachelor of Science Degree in Accounting from the University of Santa Clara. Ms. DeYoung is the spouse of David R. DeYoung.

ROBERT WIEGAND II - SECRETARY AND DIRECTOR

Mr. Wiegand was elected to the Board of Directors in July 1992. Mr. Wiegand was appointed to the office of Secretary of the Company on March 1, 1994. Mr. Wiegand is presently a lawyer in private practice. From January 15, 1992 to December 26, 1992, he was Vice-President of Administration for Rose Manufacturing Co., a privately held manufacturer of safety equipment based in Englewood, Colorado. Mr. Wiegand has practiced law for 23 years, and prior to joining Rose Manufacturing, was special counsel with Pendleton & Sabian, P.C., a law firm in Denver. Mr. Wiegand graduated Phi Beta Kappa from the Tulane University of Louisiana in 1970 and went on to receive a law degree and was admitted to practice in Louisiana in 1972 and Colorado in 1977. Since 1976, Mr. Wiegand's practice has been limited to securities offerings, estate planning, business organizations and tax law. In addition to membership in six bar Associations, Mr. Wiegand has been admitted to practice before the U.S. Supreme Court, the U.S. District Court (Colorado and ED-Louisiana) and before the U.S. Court of Appeals (5th Circuit).

RICHARD A. KNAPP - DIRECTOR

Mr. Knapp was elected to the Board of Directors in May 1997. Mr. Knapp is currently the President and CEO of Lease Capital Corporation, a leasing company located in Castle Rock, CO., and has served in that capacity since 1990. From 1984 until 1990, Mr. Knapp was a regional manager for both Paccom Leasing Corporation and Security Pacific Business Finance. In total, Mr. Knapp has been associated with the banking/finance industry for nearly thirty years. He holds a Bachelor of Science degree in Finance from the University of Arizona.

JAMES J. CAPELESS - DIRECTOR

Mr. Capeless was elected to the Board of Directors in May 2000. Mr. Capeless currently serves as a consultant to small and medium size businesses in the high technology sector. Mr. Capeless served as CEO of VMARK Software, Inc. (VMARK) in Westborough, MA from 1988 until 1996. Under his leadership, VMARK achieved seven-plus years of revenue and profit growth from business operations, including a string of 25 consecutive quarters. From 1985 until 1988, he served as Vice President, Marketing for VMARK. From 1983 until 1985, Mr. Capeless served as Vice President, Marketing Development for Infinet, Inc. in Andover, MA. He served as Director of International Marketing for Prime Computer (Natick, MA) from 1980-1983. Prior to that, Mr. Capeless served in various capacities at Honeywell Information Systems in Waltham, MA from 1962 until 1980. Mr. Capeless holds both BA and MA degrees from the University of Massachusetts.

ITEM 11. EXECUTIVE COMPENSATION

SUMMARY COMPENSATION TABLE

The following table sets forth the executive compensation of two of the Company's Executive Officers for each of the Company's last three fiscal years. There were no other Executive Officers serving at the end of the last fiscal year whose compensation was greater than $100,000.

		Annual Compensation *		Long Term Compensation	All Other Compensation
		Salary	Bonus	Awards	**
Name and Principal				Securities Underlying	
Position	Year	($)	($)	Options(#)	($)
David R. DeYoung	2001	145,260	18,529	25,000	3,156
President, CEO	2000	144,435	8,872	50,000	3,767
	1999	132,053	730	60,000	4,812
Mary Anne DeYoung	2001	103,586	14,823	25,000	2,187
CFO, Treasurer, Asst. Secretary	2000	102,898	7,096	50,000	2,187
	1999	95,214	582	60,000	2,155

* Neither Mr. DeYoung nor Ms. DeYoung received additional compensation other than noted above, the aggregate amount of which was the lesser of either $50,000 or 10% of their annual salary and bonus.

** Includes insurance premiums paid by the Company for term life and disability insurance, as well as premiums paid for a key-man life insurance policy which has the death benefit assigned to the Company and the cash value of the policy intended to accrue for the benefit of Mr. DeYoung.

OPTION GRANTS IN LAST FISCAL YEAR

The following table sets forth the information concerning individual grants of stock options during the last fiscal year to the named Executive Officers:

Individual Grants				
Name	Number of Securities Underlying Options Granted (#)	Percent of Total Options Granted to Employees in Fiscal Year	Exercise or Base Price ($/Share)	Expiration Date
D.R.DeYoung	25,000	21%	$.616	12/28/11
Mary Anne DeYoung	25,000	21%	$.56	12/28/11

AGGREGATED OPTION EXERCISES IN LAST FISCAL YEAR AND FISCAL YEAR-END OPTION VALUES

The following table sets forth information concerning each exercise of stock options during the last fiscal year by the named Executive Officers and the fiscal year-end value of unexercised options:

Name	Shares acquired on exercise (#)	Value Realized ($)	Number of securities underlying unexercised options at fiscal year-end (#)	Value of unexe the-money opti fiscal year-en
			Exercisable/unexercisable	Exercisable/un
D.R. DeYoung	0	$ 0	313,000 / 0	$77,875 /
Mary Anne DeYoung	0	$ 0	259,800 / 0	$68,600 /

*Based upon the fair market value of the Common Stock on December 31, 2001 of $.60, being the closing price as quoted on the OTC: BB.

EMPLOYMENT CONTRACTS

Mr. DeYoung, the Company's President and Chief Executive Officer, is employed pursuant to a three-year employment contract between the Company and Mr. DeYoung, which expires on October 31, 2002. Since November 1, 1999, the compensation of Mr. DeYoung has been established under the terms of this employment contract. The contract calls for an annual base salary, in an amount determined annually by the Board of Directors, payable semi-monthly, plus expenses and normal fringe benefits. Mr. DeYoung earns a bonus of 5% of the Company's pretax earnings, calculated on a quarterly basis. An annual bonus may be paid to Mr. DeYoung based on the performance of the Company and at the discretion of the Board of Directors. Mr. DeYoung's employment contract provides that should his employment be terminated for any reason other than for cause, he is entitled to a cash severance package equal to one year's cash compensation. In addition, Mr. DeYoung is entitled to receive a grant of a sufficient number of ten-year options as are necessary to permit him to retain the same percentage of beneficial ownership interest in the Company as he held on December 16, 1996. These grants would be made from the Company's Equity Incentive Plan at the fair market value of the Common Stock on the date of grant.

Ms. DeYoung, the Company's Vice President of Finance and Chief Financial Officer, is employed pursuant to a three-year employment contract between the Company and Ms. DeYoung which was effective September 1, 1999. Her compensation is established under the terms of this employment contract. The contract calls for an annual base salary, expenses, normal fringe benefits, as well as a bonus equal to 4% of the Company's pretax

earnings, calculated on a quarterly basis. In addition, Ms. DeYoung's employment contract provides that should her employment be terminated for any reason other than for cause, she is entitled to a cash severance package equal to one year's cash compensation.

COMPENSATION OF DIRECTORS

The Company currently pays non-employee Directors $1,500 per quarter plus specific hourly fees for special meetings or additional participation. In lieu of cash compensation for directors' services, on December 31, 2001, Mr. Capeless was granted a stock option for 10,000 shares of the Company's Common Stock at $.60, the fair market value of the stock on the date of grant. Pursuant to the 1996 Stock Option Plan (the "1996 Plan"), members of the compensation committee of the Board of Directors are automatically granted an option on the last trading day in June to purchase 4,000 shares of Common Stock at 100% of the fair market value on such date. On June 30, 2000 each member of the compensation committee received an automatic grant to purchase 4,000 shares of Common Stock at $.75, the fair market value on that date. In addition to the automatic grants, the Board of Directors granted each non-employee director 2,000 stock options to purchase shares of Common Stock at $0.56 per share, the fair market value on December 28, 2001.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following sets forth the number of shares of Common Stock owned by each Executive Officer and Director of the Company, by all persons known by the Company to be the beneficial owner of more than 5% of any class of the Company's voting securities, and by all Executive Officers and Directors as a group.

Unless otherwise noted, the share ownership specified in the following table represents both record and beneficial ownership as of March 15, 2002.

Name and Address of Beneficial Owner	Beneficial Ownership(1)	Percent of Class
David R. DeYoung 6025 So. Quebec Street #300, Englewood, Colorado 80111	798,591 (2),(3)	23.1%
Mary Anne DeYoung 6025 So. Quebec Street #300, Englewood, Colorado 80111	330,301 (4)	9.7%
Robert Wiegand II 5261 So. Quebec Street, Greenwood Village, Colorado 80111	84,500 (5)	2.6%
Richard A. Knapp 900 W. Castleton Rd, #120, Castle Rock, Colorado 80104	20,500 (6)	0.6%
James J. Capeless 2 Nadine Road, Acton, MA 01720	40,000 (7)	1.3%
Spencer D. Lehman 1250 4th Street, Santa Monica, California 90401	300,638	9.6%
John G. Mazza 6613 Zumirez Drive, Malibu, California 90265	302,937	9.6%
All Executive Officers and Directors as a Group - 5 persons	1,273,892 (8)	33.1%

(1) Beneficial owners are believed to have sole voting and investment power with respect to the shares shown unless otherwise indicated.
(2) Includes: 313,000 options to purchase Common Stock. See EXECUTIVE COMPENSATION - Employment Contract.
(3) Excludes: any shares attributable to Mr. DeYoung's right under his employment contract to maintain his proportional ownership of the Company under certain circumstances. See EXECUTIVE COMPENSATION - Employment Contract.
(4) Includes 259,800 options to purchase Common Stock
(5) Includes 64,500 options to purchase Common Stock
(6) Consists of 20,500 options to purchase Common Stock
(7) Consists of 40,000 options to purchase Common Stock
(8) Includes 697,800 options to purchase Common Stock

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

There were no related transactions for the year ended December 31, 2001.

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

(a)1. Financial Statements
See Financial Statement Index on Page 13

2. Financial Statement Schedules
See Financial Statement Index on Page 13

3. List of Exhibits

Exhibit Number	Description and Incorporation by Reference
3.1*	- Restated Articles of Incorporation of the Company, as amended.
3.2*	- Bylaws of the Company, as amended.
3.3*	- Articles of Amendment to the Articles of Incorporation of the Company dated April 18, 1991
3.4**	- Articles of Amendment to the Articles of Incorporation dated May 21, 1993.
3.4**	- Articles of Amendment to the Articles of Incorporation dated June 28, 1994.
10.5*	- UniVerse(TM)Distributor Agreement between INFORMIX SOFTWARE, INC. and the Company dated May 15, 1991
10.14*******	- President Employment Agreement between David R. DeYoung and the Company dated November 1, 1999.
10.15*******	- Chief Financial Officer Employment Agreement between Mary Anne DeYoung and the Company dated September 1, 1999.
10.21****	- Software License Agreement between Reynolds+Reynolds and the Company. This exhibit is subject to a grant of confidential treatment filed separately with the Securities and Exchange Commission.
10.22***	- 1994 Stock Option and Grant Plan.
10.23**	- 1993 Stock Option Plan.
10.24	- Equity Incentive Plan
23	- Consent of BKD, LLP

See Index to Financial Statements on Page 13

* Filed as an Exhibit to Form S-1 Registration Statement No. 33-44717, on December 23, 1991.

** Filed as an Exhibit to Form S-8 Registration Statement No. 33-86760, on November 29, 1994

*** Filed as an Exhibit to Form S-8 Registration Statement No. 33-78096, on April 22, 1994.

**** Filed as an Exhibit to Form 10-K for the period ended December 31, 1994.

****** Filed as an Exhibit to Form S-3 Registration Statement No. 333-35265, on September 10, 1997.

******* Filed as an Exhibit to Form 10-K for the period ended December 31, 1999

There were no reports filed on Form 8-K for the quarter ended December 31, 2001.

SIGNATURES

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

1MAGE SOFTWARE, INC.

By: /s/ David R. DeYoung Date: March 29, 2002

David R. DeYoung
President

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the date indicated.

By: /s/ David R. DeYoung Date: March 29, 2002

David R. DeYoung, President
and Principal Chief Executive Officer

By: /s/ Mary Anne Deyoung Date: March 29, 2002

Mary Anne DeYoung
Vice President, Finance
Principal and Accounting Officer

By: /s/ Robert Wiegand, II Date: March 29, 2002

Robert Wiegand, II
Director and Secretary

By: /s/ Richard A. Knapp Date: March 29, 2002

Richard A. Knapp
Director

By: /s/ James J. Capeless Date: March 29, 2002

James J. Capeless
Director