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IMAGE SOFTWARE INC
Form 10-K405
March 14, 2001

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 12/31/2000
- OR
- () TRANSITION REPORT PURSUANT TO SECTION 13 OF 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934. For the transition period -----
-----to ----- .

IMAGE 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 Numbers)

6025 S. QUEBEC ST. SUITE 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

Aggregate market value of the voting stock held by non-affiliates of the Registrant as of February 28, 2001: \$1,472,772.

As of February 28, 2001, there were 3,146,554 shares of the Registrant's Common Stock outstanding.

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PART I

ITEM 1. BUSINESS

Introduction

Image 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 IMAGE(R) 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 IMAGE 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,

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spreadsheets, databases, Web pages, 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, IMAGE 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 IMAGE system is designed to integrate easily with existing IT infrastructure, using a vast 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 2000, the Company concentrated its efforts on selling production document imaging software to its niche market, users of MultiValue Relational Data Base Management Systems ("RDBMS"). 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 targets its market through VARs, systems integrators, and other companies which market complementary software, services, or other products. IMAGE software has an established worldwide presence in a multitude of industries, including automotive retail, building materials, 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 IMAGE(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.

IMAGE(R) DOCUMENT MANAGEMENT - IMAGE is a powerful electronic image management system created to operate the same on UNIX, Linux and Windows NT(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.

Add-on modules to IMAGE(R) include the following:

- o 1SCAN for scanning and pre-indexing
- o 1FAX for inbound and outbound fax and cover sheet management
- o 1COLD for Computer Output to Laser Disk (character report data) management
- o 1FORM for business form template administration
- o 1RENDITION for merging spooled data with images for billing
- o 1WORKFLOW for electronically moving a document from one task to another

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- o 1OCR/OMR for automatic indexing and data capture via optical and mark character recognition
- o 1SUITE for bringing images to Windows-based PC clients
- o 1SERVER for accessing documents via the Internet
- o 1VIEW for using standard browsers to access images over the Intranet and Internet

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

- o Open Systems compliant with UNIX and Linux Operating Systems, Windows NT(TM), CCITT Group 4 Compression, TIFF, JPEG, PCX, PCL, or HPGL file formats. The server software (IMAGE) operates on UNIX, Linux and Windows NT servers; supporting clients include Microsoft Windows, Windows NT workstations, X-Windows, and browser clients
- o Device connectivity via Ethernet or token ring networks using TCP/IP communication protocol or over the Internet
- o Compatibility with IBM AIX, HP-UX, Sun Solaris, SCO UNIX, DG-UX, Red Hat Linux and Windows NT
- o Recognition technology and scanning tasks run on Microsoft Windows 95, 98, or NT.
- o UniVerse and UniData ("U2" databases) Relational Database software from Informix Software, Inc.

IMAGE includes several distinguishing features: the ability to use many different types of workstations or terminals, 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 UNIX, Linux and Windows NT operating systems and open systems technology, the Company seeks to offer its customers an imaging solution at a reasonable cost.

During 2000, sales of IMAGE software licenses (excluding annual license fees) accounted for \$880,906 (41% of total revenue); in 1999, revenue from sales of software licenses accounted for \$637,820 (35% of total revenue). IMAGE utilizes the popular UNIX, Linux and Windows NT operating systems and Informix Software's U2 RDBMS software. The Company's open systems technology makes its software transportable to numerous hardware products from varying manufacturers, including IBM's AS/400 systems. Because of the number of hardware manufacturers using the UNIX, Linux and Windows NT 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 2000, revenue from hardware sales accounted for \$113,217 (5%) of the Company's total revenue, as compared to \$150,008 (8%) of total revenue for 1999.

SERVICES AND ANNUAL FEES

The Company licenses its IMAGE 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 2000 and 1999, annual license fees accounted for \$896,376 and \$751,712, 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 installation services and technical support to its customers. Technical support includes training, consulting

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services and other ongoing support. For the years ended December 31, 2000 and 1999, the revenues from these services accounted for \$272,164, or 13%, and \$266,808, or 15%, 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 IMAGE with ten resellers specializing in a variety of industries, including automotive retail, health care, public safety, utilities, employee benefit services, and a domestic and an international ASP (Application Service Provider). Under the business partner programs, the Company provides its IMAGE to independent software integrators (resellers), who in turn market products, including or featuring IMAGE, 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 IMAGE through its direct sales force. Its general strategy is to (1) help its customers define the goals for their system, (2) provide the means of achieving those goals through its 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 personnel training and classroom educational programs. In addition, the Company markets its products and services over the Internet.

CUSTOMERS

The Company sells its IMAGE software to businesses in a wide variety of industries and markets, facilitated through the use of VARs.

During the years 2000 and 1999, the Company generated 35% and 29%, 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 IMAGE (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 an engineering and maintenance agreement with Reynolds for the purpose of developing and providing new products, enhancements, maintenance, consulting, and programming services on an ongoing basis. License fees are paid to the Company for certain products subsequently available in newer releases of IMAGE. These features include the Company's client software. Management believes that the loss of this customer would have a significantly adverse impact on the Company. Management does not believe that there is a substantial risk of any such loss in the foreseeable future.

SOURCES OF SUPPLY

The current dealer agreement with Informix Software, Inc. to remarket their U2 RDBMS software runs through May 15, 2002. 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

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The Company's current focus on offering its proprietary imaging software to a broader range of customers, through its emerging MultiValue RDBMS reseller network and its direct sales force, is expected to lessen the historical quarterly fluctuations in the Company's operating results. Nevertheless, large sales or groups of sales of IMAGE licenses may cause significant variances in quarterly results which 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 or software license, typically ranges from two to nine months. 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 competition in its business from competitors

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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 readily available from a number of competitors of the Company, some of which are larger and have greater financial, technical, marketing and other resources than the Company. The Company believes that the principal factors affecting a prospective customer's choice of a system are the database it uses, performance, service and price. The Company believes that usage of the popular Linux and UNIX operating systems and the MultiValue RDBMS has strengthened the Company's competitive position by making the Company's software compatible with more types of hardware and with the MultiValue application software offered by MultiValue 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 NT-based open systems architecture and the MultiValue RDBMS 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. While such 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, the Company believes that a strong national economy is important to the success of its sales efforts.

PRODUCT DEVELOPMENT

The computer industry is characterized by rapid technological changes in both software and hardware. In order to maintain the usefulness of its products and their compatibility with future hardware and software, the Company must continually modify and enhance its products. The Company capitalizes software development costs once technological feasibility is established. During 2000 and 1999, the Company spent \$290,745 and \$302,747, respectively, for computer software development.

EMPLOYEES

As of February 28, 2001, the Company employed twenty-two persons, nineteen of whom serve on a full-time basis and three on a part-time basis. Responsibilities are divided as follows: nine 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

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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, 2000.

PART II

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

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
1999 ----	High	Low

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	----	---
First Quarter	\$.97	\$.53
Second Quarter	2.03	.97
Third Quarter	1.56	.94
Fourth Quarter	1.22	.66

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

On February 28, 2001, the closing bid price per share for the Common Stock was \$.65 as reported on OTC:BB. On that same date, there were approximately 1,326 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:	2000	1999	1998	1997	1996
	----	----	----	----	----
Net Sales	\$2,163	\$1,806	\$2,151	\$1,809	\$2,005
Cost of Sales	934	987	935	918	905
Gross Profit	1,229	819	1,216	891	1,100
Gross Profit (as a % of Net Sales)	57%	45%	57%	49%	55%
Selling, General & Administrative expenses	1,211	1,163	1,097	1,363	1,280
Income(Loss) before Income Taxes	11	(365)	5	(479)	(91)
Net Income(Loss)	8	(367)	2	(484)	(96)
Net Income(loss) Per Share	.00	(.16)	.00	(0.23)	(0.05)
Weighted Average Number of Outstanding Shares	3,056	2,330	2,173	2,146	2,055

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BALANCE SHEETS

YEARS ENDED DECEMBER 31,

In thousands:

	2000	1999	1998	1997	1996
	----	----	----	----	----
Working Capital/(Deficit)	\$ (93)	\$ (186)	\$ 196	\$ 43	\$ 165
Total Assets	1,428	1,364	1,710	1,602	1,980
Long Term Obligations	3	1	154	159	8
Total Stockholders Equity	714	654	922	860	1,200

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

RESULTS OF OPERATIONS

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

The Company's revenue for the year ended December 31, 2000 of \$2,162,663 was 20% greater than \$1,806,348 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 comprise just 5% of the total revenue, as compared to 8% a year ago. The professional service group increased consulting 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 just 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 \$8,154 for 2000 reflects 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.

YEAR ENDED DECEMBER 31, 1999 COMPARED TO YEAR ENDED DECEMBER 31, 1998.

The Company's net sales of \$1,806,348 for the year ended December 31, 1999 were \$345,000 (16%) lower than \$2,151,451 reported for the same period a year earlier. The decrease in revenue is attributable to extremely slow software sales in the fourth quarter, as customers held back purchases of new technology in anticipation of Y2K problems. Revenue for the first nine months of 1999 was slightly ahead of the comparable period in 1998. While total revenue does not reflect the number of systems sold, the Company licensed 213 IMAGE software systems to a single reseller during 1999, as compared to 90 in 1998, an increase of 136%. Due to a licensing arrangement signed back in 1994, minimal royalty payments are due for these systems. Software sales to resellers increased \$64,000 (22%) over the year earlier, as the Company recognized first-time revenue from new resellers. Total revenue from resellers comprised 36% of total revenue for 1999, compared to 34% of total revenue in 1998.

Gross profit decreased \$398,000 (33%) as a result of lower revenue from software sales in 1999. Revenue from services and annual fees of \$1,018,520 was \$144,000 less than total selling, general & administrative ("SG&A") expenses of \$1,163,000 in 1999. It remains an important goal for

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the Company to have all SG&A expense covered by services and recurring annual fees so the net effective margin on revenue from software sales can be very high. SG&A expenses increased \$66,000 (6%) for the twelve months ended December 31, 1999, as a result of slight increases in sales and marketing efforts. Loss from operations in 1999 was (\$343,978), as compared to income from operations of \$120,045 (before merger expenses) in 1998. Net loss of (\$367,193) or (\$.16) per share were reported for the year ended December 31, 1999, versus net income of \$2,380 or (\$.00) per share for the same period in 1998.

LIQUIDITY AND CAPITAL RESOURCES

The Company's cash and cash equivalents decreased \$103,473 during the twelve months ended December 31, 2000 due to timing of collections on accounts receivable. Accounts receivable on December 31, 2000 were \$407,251, an increase of \$203,144 from December 31, 1999. Cash of \$290,745 was used for software development costs incurred primarily to develop new client, server and workflow products that facilitate viewing images via the Internet. The Company had working capital of (\$92,704) on December 31, 2000. Deferred income of \$213,000 is recorded as a current liability and represents pro-rated revenue for software licenses billed in 2000.

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 has a \$200,000 revolving line of credit. The loan is collateralized by all accounts and general intangibles of the Company. Borrowings outstanding under the line of credit at February 28, 2001 were \$150,000.

The Company has no material commitments for capital expenditures for 2001.

Management believes that inflation has not had a material impact on its results of operations to date.

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

IMAGE SOFTWARE, INC.

INDEX TO FINANCIAL STATEMENTS

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INDEPENDENT ACCOUNTANTS' REPORT

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

We have audited the accompanying balance sheets of Image Software, Inc. as of December 31, 2000 and 1999, and the related statements of operations, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2000. 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 generally accepted auditing standards. 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 Image Software, Inc. as of December 31, 2000 and 1999, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2000, in conformity with generally accepted accounting principles.

/s/ BAIRD, KURTZ & DOBSON

Denver, Colorado
February 2, 2001

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IMAGE SOFTWARE, INC.
BALANCE SHEETS
DECEMBER 31, 2000 AND 1999

	2000	1999
ASSETS	----	----
CURRENT ASSETS:		
Cash and cash equivalents	\$ 150,457	\$ 253,930
Receivables:		
Trade (less allowance: 2000, \$10,000; 1999, \$10,000)	407,251	204,107
Related parties	-	1,635
Inventory	38,654	49,207
Prepaid expenses and other current assets	21,233	13,428
	-----	-----
Total current assets	617,595	522,307
PROPERTY AND EQUIPMENT, at cost, net	55,177	69,263
OTHER ASSETS:		
Software development costs, net	754,734	771,919
Other	100	100
	-----	-----
TOTAL ASSETS	\$1,427,606	\$1,363,589
	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Line of credit	\$ 200,000	\$ 168,235
Current portion of capital lease obligations	1,785	3,857
Deferred revenue	213,494	210,000
Accounts payable	185,468	209,882
Accrued liabilities	109,450	116,647
	-----	-----
Total current liabilities	710,197	708,621
LONG-TERM OBLIGATIONS:		
Capital lease obligations	3,224	521
SHAREHOLDERS' EQUITY:		
Common Stock, \$.004 par value		
- - 10,000,000 shares authorized;		
shares outstanding: 2000 -		
3,146,554; 1999 - 2,642,493	12,586	10,569
Additional paid-in capital	7,238,658	7,189,091
Accumulated deficit	(6,537,059)	(6,545,213)
	-----	-----
Total shareholders' equity	714,185	654,447
	-----	-----
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$1,427,606	\$1,363,589
	=====	=====

See notes to financial statements.

IMAGE SOFTWARE, INC.
STATEMENTS OF OPERATIONS

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FOR THE YEARS ENDED DECEMBER 31, 2000, 1999, AND 1998

	2000 -----	1999 -----	1998 -----
REVENUE:			
System sales and software licenses	\$ 994,123	\$ 787,828	\$1,059,864
Services and annual fees	1,168,540	1,018,520	1,091,587
	-----	-----	-----
Total revenue	2,162,663	1,806,348	2,151,451
	-----	-----	-----
COST OF REVENUE:			
System sales and software licenses	558,016	596,128	608,895
Services and annual fees	375,356	391,277	325,963
	-----	-----	-----
Total cost of revenue	933,372	987,405	934,858
	-----	-----	-----
GROSS PROFIT	1,229,291	818,943	1,216,593
OPERATING EXPENSES:			
Selling, general & administrative	1,211,288	1,162,921	1,096,548
	-----	-----	-----
INCOME/(LOSS) FROM OPERATIONS	18,003	(343,978)	120,045
	-----	-----	-----
OTHER INCOME/(EXPENSE):			
Interest income	8,059	9,665	5,724
Canceled merger costs	-	-	(85,277)
Interest expense	(15,408)	(32,140)	(34,046)
Other	-	1,760	(1,566)
	-----	-----	-----
Total other income (expense)	(7,349)	(20,715)	(115,165)
	-----	-----	-----
INCOME/(LOSS) BEFORE INCOME TAXES	10,654	(364,693)	4,880
PROVISION FOR INCOME TAXES	2,500	2,500	2,500
	-----	-----	-----
NET INCOME/(LOSS)	\$ 8,154	\$ (367,193)	\$ 2,380
	=====	=====	=====
BASIC AND DILUTED INCOME (LOSS) PER COMMON SHARE			
	\$ 0.00	\$ (.16)	\$ 0.00
	=====	=====	=====
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING			
	3,055,600	2,329,818	2,172,932
	=====	=====	=====

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See notes to financial statements.

IMAGE SOFTWARE, INC.
 STATEMENTS OF SHAREHOLDERS' EQUITY
 FOR THE YEARS ENDED DECEMBER 31, 2000, 1999, AND 1998

	Common Stock Shares	Amount	Additional Paid-In Capital
Balances, January 1, 1998	2,142,845	\$ 8,571	\$ 6,845,100
Exercise of incentive stock options	60,174	240	59,147
Net income	-	-	-
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

	Accumulated Deficit	Total
Balances, January 1, 1998	(6,180,400)	\$673,271
Exercise of incentive stock options	-	59,387
Net income	2,380	2,380
Balances, December 31, 1998	(6,178,020)	735,038
Conversion of notes payable	-	-

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into Common Stock	-	202,486
Exercise of incentive stock options	-	66,070
Issuance of non-qualified stock options	-	18,046
Net loss	(367,193)	(367,193)

Balances, December 31, 1999	(6,545,213)	654,447
Exercise of incentive stock options	-	197,837
Surrender shares for exercise of incentive stock options	-	(128,207)
Exercise of Class A Warrants	-	43,750
Surrender shares for exercise of Class A Warrants	-	(43,750)
Cancellation of non-qualified stock options	-	(18,046)
Net income	8,154	8,154

Balances, December 31, 2000	\$ (6,537,059)	\$ 714,185
=====		

See notes to financial statements.

IMAGE SOFTWARE, INC.
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2000, 1999, AND 1998

	2000	1999	1998
	-----	-----	-----
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net earnings/(loss)	\$ 8,154	\$ (367,193)	\$ 2,380
Adjustments to reconcile earnings/(loss) to net cash provided by operating activities:			
Depreciation and amortization	342,338	367,838	398,806
(Cancellation)/Issuance of stock options for services	(18,046)	18,046	-
Changes in assets and liabilities:			
Receivables	(201,509)	328,083	(265,923)
Inventory	10,553	6,597	37,919
Prepaid expenses and other assets	(7,805)	(3,707)	(2,048)
Accounts payable	(24,414)	(83,001)	101,345
Accrued liabilities and deferred income	(3,703)	6,519	(43,667)
	-----	-----	-----
Net cash provided by operating activities	105,568	273,182	228,812
	-----	-----	-----
CASH FLOWS FROM INVESTING ACTIVITIES:			
Purchase of property and equipment	(14,125)	(25,870)	(7,908)
Additions to capitalized software	(290,745)	(302,747)	(295,266)
Redemption of certificate of deposit	-	25,000	-
Increase in other assets	-	-	(100)
	-----	-----	-----
Net cash used for investing activities	(304,870)	(303,617)	(303,274)

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CASH FLOWS FROM FINANCING ACTIVITIES:			
Additions to line of credit	300,000	68,235	60,000
Repayment of line of credit	(268,235)	(50,000)	(60,000)
Repayment of long-term obligations	(5,566)	(4,611)	(12,047)
Proceeds from exercise of Common Stock options	69,630	66,070	59,387
Net cash provided by financing activities	95,829	79,694	47,340
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(103,473)	49,259	(27,122)
CASH AND CASH EQUIVALENTS, beginning of year	253,930	204,671	231,793
CASH AND CASH EQUIVALENTS, end of year	\$ 150,457	\$253,930	\$204,671

See notes to financial statements

IMAGE SOFTWARE, INC.
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2000, 1999, AND 1998

	2000	1999	1998
	----	----	----
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:			
Cash paid for interest	\$15,408	\$15,820	\$16,204
	=====	=====	=====
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	\$ -	\$ -
	=====	=====	=====

IMAGE SOFTWARE, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2000, 1999 AND 1998

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND ORGANIZATION

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

The Company develops and markets a UNIX, Linux and Windows NT-based

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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.

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, 2000, 1999, and 1998 were \$290,745, \$302,747, and \$295,266, respectively. Amortization of these costs totaled \$307,930, \$317,400, and \$322,319, 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. Credit losses to customers have generally been within management's expectations.

One customer accounted for 35% of 2000 revenues. One customer accounted for 28% of accounts receivable at December 31, 2000.

One customer accounted for 29% of 1999 revenues. Two different customers accounted for 11% and 10% of accounts receivable at December 31, 1999.

One customer accounted for 28% of 1998 revenues. Two different

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customers accounted for 42% and 15% of accounts receivable at December 31, 1998.

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 primary 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 full valuation allowance against all deferred tax assets due to the uncertainty of ultimate realizability.

ESTIMATES -The preparation of financial statements in conformity with generally accepted accounting principles 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:

	2000	1999
	----	----
Equipment	\$ 626,656	\$ 606,333
Furniture	43,313	43,313
Leasehold improvements	8,262	8,262
	-----	-----
	678,231	657,908
Less: accumulated depreciation	(623,054)	(588,645)
	-----	-----
	\$ 55,177	\$ 69,263
	=====	=====

3. ACCRUED LIABILITIES

Accrued liabilities at December 31 consists of the following:

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	2000 -----	1999 -----
Sales tax payable	\$ 22,949	\$ 38,465
Accounting and audit fees	15,486	21,000
Accrued compensation	32,124	9,773
Other	38,891	47,409
	-----	-----
	\$109,450	\$116,647
	=====	=====

4. LINE OF CREDIT

The Company has a \$200,000 revolving bank line of credit which is due February 24, 2001 and bears interest at prime plus 1.5% (total rate of 11.0% at December 31, 2000) and is collateralized by all accounts and general intangibles of the Company. Total borrowings outstanding under the line of credit were \$200,000 and \$168,235 at December 31, 2000 and 1999, respectively.

5. CONVERTIBLE NOTES PAYABLE TO RELATED PARTIES

The Company had convertible notes payable to related parties (shareholders) at December 31, 1998 of \$150,000 plus accrued interest of \$52,486. The principal and interest amounts were converted into 326,474 shares of Common Stock during 1999.

Interest expense for the years ended December 31, 2000, 1999, and 1998 to related parties was \$0, \$16,321, and \$17,842, respectively.

6. SHAREHOLDERS' EQUITY

STOCK COMPENSATION PLANS

At December 31, 2000, 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:

	2000 -----	1999 -----	1998 -----
Net income (loss):			
As reported	\$ 8,154	\$ (367,193)	\$ 2,380
Pro forma	\$ (147,361)	\$ (518,211)	\$ (127,196)
Loss per common share:			
As reported	\$ 0.00	\$ (0.16)	\$ 0.00
Pro forma	\$ (0.05)	\$ (0.22)	\$ (0.06)

The fair value of each option grant is estimated on the date of grant

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using the Black-Scholes option-pricing model with the following weighted-average assumptions for grants in 2000, 1999 and 1998:

	2000 ----	1999 ----	1998 ----
Dividend Yield	0%	0%	0%
Expected Volatility	135%	144%	151%
Risk-Free Interest Rate	5.00%	6.00%	6.00%
Expected Lives	3.2 years	8.7 years	8.9 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 -----	Value Per Share -----	Total -----	Weighted Avg. Exercise Price -----
Balances, January 1, 1998	275,000	\$.44 - \$1.47	\$131,219	\$.48
Canceled	(235,000)	\$.63 - \$1.25	(175,003)	(.74)
Granted	413,000	\$.34 - \$.78	239,702	.58
	-----		-----	
Balances, December 31, 1998	453,000		195,918	.43
Granted	375,000	\$.33-\$1.29	233,100	.62
	-----		-----	
Balances, December 31, 1999	828,000		429,018	.52
Granted	192,500	\$.63-\$1.44	126,813	.66
Canceled	(189,000)	\$.33-\$.66	(105,976)	(.56)

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Exercised	(198,000)	\$.34-\$1.47	(79,137)	(.40)
Balances, December	=====		=====	
31, 2000	633,500		\$370,71	\$.59
	=====		=====	

The following table summarizes information about stock options under the plan at December 31, 2000.

Range of Exercise Prices	Outstanding		Exercisable		
	Number Out-standing	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
0.34 to 0.44	235,000	6.5 years	0.44	235,000	0.44
0.63 to 0.84	382,500	8.6 years	0.64	292,000	0.65
1.28 to 2.06	16,000	9.0 years	1.36	16,000	1.36

At December 31, 2000, options for 543,000 shares were exercisable under the 1996 Plan. There were 168,500 shares available for future grant.

The weighted-average fair value of options granted during the year totaled \$.52, \$.65, and \$.36, per share for the years ended December 31, 2000, 1999, and 1998 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	Value Per Share	Total	Weighted Avg. Exercise Price
Balances,				
January 1, 1998	281,175	\$.63 - \$1.44	\$ 189,264	\$.67
Granted	200,500	\$.34	68,972	.34

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Canceled	(50,000)	\$.63 - \$.88	(33,100)	(.66)
Exercised	(10,174)	\$.63 - \$1.44	(9,388)	(.92)

Balances,				
December 31, 1998	421,501		215,748	.51
Granted	104,000	\$.66	68,245	.66
Canceled	(13,501)	\$.34 - \$1.44	(7,956)	(.59)
Exercised	(113,000)	\$.34 - \$.78	(66,070)	(.58)

Balances,				
December 31, 1999	399,000		209,967	.53
Granted	9,500	\$.63	5,939	.63
Canceled	(5,250)	\$.34 - \$1.28	(4,614)	(.88)
Exercised	(86,000)	\$.34 - \$1.28	(45,974)	(.53)
=====				
Balances,				
December 31, 2000	317,250		\$ 165,318	\$.52

Stock Grants		Grant Price	Total	Weighted Average Exercise Price
-----		-----	-----	-----
Balances, January 1, 1998	83,166	\$.84 - \$1.13	\$138,247	\$1.66
Granted/Canceled	-	-	-	-
Balances, December 31, 1998	83,166		138,247	1.66
Granted/Canceled	-	-	-	-

Balances, December 31, 1999	83,166		138,247	1.66
Granted/Canceled	-	-	-	-

Balances, December 31, 2000	83,166		\$138,247	\$1.66

The following table summarizes information about stock options under the plan at December 31, 2000.

Range of Exercise Prices	Number Outstanding	Outstanding		Number Exercisable	Exercisable	
		Weighted Average Remaining Contractual Life	Weighted Average Exercise Price		Weighted Average Exercise Price	Weighted Average Exercise Price
-----	-----	-----	-----	-----	-----	-----
0.34 to 0.44	126,750	5.5 years	0.34	78,500	0.34	
0.63 to 0.84	190,500	4.5 years	0.64	125,000	0.63	

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The weighted-average fair value of options granted during the year totaled \$.48, \$.64, and \$.33, per share for the years ended December 31, 2000, 1999, and 1998, respectively.

At December 31, 2000, options to purchase 203,500 shares of Common Stock were exercisable and 3,599 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 non-qualified 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	Value Per Share	Total	Weighted Avg. Exercise Price
	-----	-----	-----	-----
Balances, January 1, 1998	245,275	\$.77 - \$1.37	\$ 261,950	\$ 1.07
Canceled	(236,275)	\$.63 - \$1.81	(254,231)	(1.08)
Granted	230,675	\$.34 - \$.44	100,593	.44
	-----		-----	
Balances, December 31, 1998	239,675		108,312	.45
Canceled/Granted	-		-	-
	-----		-----	
Balances, December 31, 1999	239,675		108,312	.45
Granted	-		-	-
Exercised	(163,375)	\$.44 - \$.75	(72,727)	(.45)
	-----		-----	
Balances, December 31, 2000	76,300		\$35,585	\$.47
	=====		=====	

The following table summarizes information about stock options under the plan at December 31, 2000.

Outstanding	Exercisable
-----	-----
Weighted	

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Range of Exercise Prices	Number Outstanding	Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
0.34 to 0.44	71,300	5.6 years	0.43	69,550	0.44
0.63 to 0.84	4,000	6.0 years	0.75	4,000	0.75
1.28 to 2.06	1,000	5.5 years	1.72	1,000	1.72

The weighted-average fair value of options granted during the year totaled \$.44 for the year ended December 31, 1998.

At December 31, 2000, options for 74,550 shares were exercisable under the 1993 Plan. There were options for 3,500 shares available for 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, 2000.

COMMON STOCK RESERVED

Common Stock reserved at December 31, 2000 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 for income taxes for the years ended December 31, consists of:

Current:	2000	1999	1998
	----	----	-----
Federal	\$ -	\$ -	\$ -
State	2,500	2,500	2,500
	-----	-----	-----
Total current	2,500	2,500	2,500
	-----	-----	-----
Deferred:			
Federal	-	-	-
State	-	-	-
	-----	-----	-----

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Total deferred \$2,500 =====	\$2,500 =====	\$2,500 =====
---------------------------------	------------------	------------------

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

	2000 ----	1999 ----	1998 ----
Federal income taxes at statutory rate \$	3,600	\$ (124,845)	\$ 1,659
Increase(decrease) in taxes resulting from state income taxes	(800)	(16,380)	107
Increase(decrease) in deferred tax asset valuation allowance	(133,000)	76,000	(20,000)
Expiration of business tax credits	121,000	61,000	30,000
Other, net	11,700	6,725	(9,266)
	-----	-----	-----
Provision for income taxes	\$ 2,500 =====	\$ 2,500 =====	\$ 2,500 =====

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

	2000 ----	1999 ----
Deferred tax liability	\$2,000	\$1,000
Deferred tax asset	(2,286,000)	(2,418,000)
Valuation allowance	2,284,000	2,417,000
	-----	-----
	\$ -	\$ -
	=====	=====

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:

	2000 ----	1999 ----
Future income (deductions):		
Net operating loss	\$ (2,242,000)	\$ (2,234,000)
Allowance for doubtful accounts	(4,000)	(4,000)
General business tax credits	(14,000)	135,000
Depreciation	(18,000)	(30,000)
Stock options	(5,000)	(12,000)
Other	(1,000)	(2,000)
	-----	-----
	\$ (2,284,000) =====	\$ (2,417,000) =====

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The Company has net operating loss carry forwards for federal income tax purposes of approximately \$5,561,000. General business tax credits carry forwards of approximately \$14,000 are available to reduce future federal income taxes. These carry forwards expire on varying dates from 2001 through 2013.

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, 2000, 1999, and 1998, the Company contributed \$3,988, \$2,476, and \$1,289 to the 401(k) Plan.

9. COMMITMENTS AND CONTINGENCIES

At December 31, 2000 and 1999, equipment with a net book value of \$10,735 and \$7,635, net of accumulated amortization of \$9,626 and \$6,002, 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 -----	
2001	\$ 3,574	\$ 89,304	
2002	3,060	89,304	
2003	510	52,094	
	-----	-----	
Total minimum lease payments	7,144	\$ 230,702	
		=====	
Amount representing interest	(2,135)		

Present value of min. lease payments	5,009		
Current portion	(1,785)		

Long-term portion	\$ 3,224		
	=====		

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 \$15,968, \$1,312, and \$9,536 under these agreements for the years ended December 31, 2000, 1999, and 1998, 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

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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, 2000 are as follows:

	Carrying Amount	Fair Value
	-----	-----
Assets		

Cash and cash equivalents	\$ 150,457	\$ 150,457
Receivables	\$ 407,251	\$ 407,251
Liabilities		

Accounts payable	\$ 185,468	\$ 185,468
Line of credit	\$ 200,000	\$ 200,000

The estimated fair values of the Company's financial instruments at December 31, 1999 are as follows:

	Carrying Amount	Fair Value
	-----	-----
Assets		

Cash and cash equivalents	\$ 253,930	\$ 253,930
Receivables (including \$1,635 from related parties)	\$ 205,742	\$ 205,742
Liabilities		

Accounts payable	\$ 209,882	\$ 209,882
Line of credit	\$ 168,235	\$ 168,235

12. SEGMENT INFORMATION

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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 \$57,911, \$102,831, and \$35,003 for the years ending December 31, 2000, 1999, and 1998, respectively.

INDEPENDENT ACCOUNTANTS' REPORT
ON FINANCIAL STATEMENT SCHEDULES

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

In connection with our audit of the financial statements of Image Software, Inc. for each of the three years in the period ended December 31, 2000, 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.

/s/ Baird, Kurtz & Dobson

Denver, Colorado
February 2, 2001

Image Software, Inc.

SCHEDULE VIII
VALUATION AND QUALIFYING ACCOUNTS

	Additions		
Balance at beginning of period	charged to: Costs and expenses	Additions charged to: deductions	Balance at end of period

For the Year Ended
December 31, 2000

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Allowance for Doubtful Accounts For the Year Ended December 31, 1999	\$10,000	\$31,403	\$31,403	\$10,000
Allowance for Doubtful Accounts For the Year Ended December 31, 1998	\$15,000	\$39,485	\$44,485	\$10,000
Allowance for Doubtful Accounts	\$20,000	\$41,984	\$46,984	\$15,000

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	55	1981	President, Chief Executive Officer and Director
Robert Wiegand II	54	1992	Secretary and Director
Mary Anne DeYoung	47	1994	Treasurer, Chief Financial Officer, Asst. Secretary and Director
Richard A. Knapp	55	1997	Director
James J. Capeless	61	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.

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

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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. District Court (Colorado and ED-Louisiana) and before the U.S. Court of Appeals (5th Circuit).

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.

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 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.

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NAME AND PRINCIPAL POSITION	YEAR	ANNUAL COMPENSATION*		LONG TERM COMPENSATION**	ALL OTHER COMPENSATION
		SALARY (\$)	BONUS (\$)	AWARDS SECURITIES UNDERLYING OPTIONS (#)	*** (\$)
David R. DeYoung	2000	144,435	8,872	50,000	3,767
President, CEO	1999	132,053	730	60,000	4,812
	1998	129,820	4,817	432,375**	5,772
Mary Anne DeYoung	2000	102,898	7,096	50,000	2,187
CFO, Treasurer,	1999	95,214	582	60,000	2,155
Asst. Secretary	1998	93,246	3,854	199,800***	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.

** For 1998, includes 337,375 stock options which were repriced to fair market value on January 15, 1998.

*** For 1998, includes 124,800 stock options which were repriced to fair market value on January 15, 1998.

**** 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(#)	% of Total Options Granted to Employees in Fiscal Year	Exercise or Base Price (\$/Share)	Expiration Date
D.R. DeYoung	50,000	25%	.625	12/04/10
Mary Anne DeYoung	50,000	25%	.625	12/04/10

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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 unexercised in-the-money options at fiscal year-end (\$)*
D.R. DeYoung	254,375	\$907,462	288,000/0	\$190,080/0
Mary Anne DeYoung	75,000	\$271,950	234,800/0	\$154,968/0

*Based upon the fair market value of the Common Stock on December 31, 2000 of \$.66, 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.

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COMPENSATION OF DIRECTORS

The Company currently pays non-employee Directors \$1,000 per quarter plus specific hourly fees for special meetings or additional participation. In lieu of cash compensation for directors' services, Mr. Capeless was granted a stock option for 15,000 shares of the Company's common stock. 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 \$1.4375, the fair market value on that date. In addition to the automatic grants, the Board of Directors granted each non-employee director 5,000 stock options to purchase shares of Common Stock at \$0.625 per share, the fair market value on December 4, 2000.

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 to 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 February 23, 2001.

Name and Address of Beneficial Owner	Beneficial Ownership(1)	Percent of Class
David R. DeYoung 6025 So. Quebec Street #300, Englewood, Colorado 80111	777,591 (2), (3)	22.6%
Robert Wiegand II 5261 So. Quebec Street, Greenwood Village, Colorado 80111	73,500 (4)	2.3%
Mary Anne DeYoung 6025 So. Quebec Street #300, Englewood, Colorado 80111	305,301 (5)	9.0%
Richard A. Knapp 900 W. Castleton Rd, #120, Castle Rock, Colorado 80104	18,500 (6)	0.6%
James J. Capeless 2 Nadine Road Acton, MA 01720	24,000 (7)	.8%
Spencer D. Lehman 1250 4th Street, Santa Monica, California 90401	280,606	8.9%
John G. Mazza	302,937	9.6%

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6613 Zumirez Drive,
Malibu, California 90265

All Executive Officers and Directors

as a Group - 5 persons 1,198,892 (8) 31.8%

- (1) Beneficial owners are believed to have sole voting and investment power with respect to the shares shown unless otherwise indicated.
- (2) Includes: 288,000 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 53,500 options to purchase Common Stock
- (5) Includes 234,800 options to purchase Common Stock
- (6) Consists of 18,500 options to purchase Common Stock
- (7) Consists of 24,000 options to purchase Common Stock
- (8) Includes 618,800 options to purchase Common Stock

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

There were no related transactions for the year ended December 31, 2000.

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
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- | | |
|-----------|--|
| 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. |
| 4.1***** | - Form 1994 Class A Warrant issued to David R. DeYoung dated February 1, 1995. |
| 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. |

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10.24***** - Equity Incentive Plan
23 - Consent of Baird, Kurtz and Dobson

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-8 Registration Statement
No. 333-3078, on July 3, 1997.
***** Filed as an Exhibit to Form S-3 Registration Statement
No. 333-35265, on September 10, 1997.

There were no reports filed on Form 8-K for the quarter ended December 31,
2000

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.

IMAGE SOFTWARE, INC.

By: /s/ David R. DeYoung Date: March 14, 2001

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 14, 2001
David R. DeYoung, President
and Principal Chief Executive Officer

By: /s/ Robert Wiegand, II Date: March 14, 2001
Robert Wiegand, II
Director and Secretary

By: /s/ Mary Anne DeYoung Date: March 14, 2001
Mary Anne DeYoung
Vice President, Finance
Principal and Accounting Officer

By: /s/ Richard A. Knapp Date: March 14, 2001
Richard A. Knapp
Director

By: /s/ James J. Capeless Date: March 14, 2001
James J. Capeless
Director

EXHIBIT INDEX

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No.	Description
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23	Consent of Baird, Kurtz and Dobson