INFORMATION ANALYSIS INC
Form 10-K
March 30, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-K

(Mark One)

þ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2011

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from__________ to __________

Commission File Number 000-22405

Information Analysis Incorporated
(Exact Name of Registrant as Specified in Its Charter)

Virginia (State or Other Jurisdiction of Incorporation or Organization)	54-1167364 (I.R.S. Employer Identification No.)

11240 Waples Mill Road
Suite 201
Fairfax, Virginia 22030

(703) 383-3000
(Address including zip code, and telephone number, including area code, of principal executive offices)

Securities registered pursuant to Section 12(b) of the Act:

None

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, par value $0.01 per share
(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No þ

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No þ

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 (the "Exchange Act") 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 þ No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No o

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 the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. þ

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	o	Accelerated filer	o
Non-accelerated filer (Do not check if a smaller reporting company)	o	Smaller reporting company	þ

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes o No þ

The aggregate market value of the common stock held by nonaffiliates of the registrant based on the closing price of the registrant's common stock on June 30, 2011, was approximately $1,667,795. For purposes of this computation, all officers, directors and 10% beneficial owners of the registrant are deemed to be affiliates. Such determination should not be deemed to be an admission that such officers, directors or 10% beneficial owners are, in fact, affiliates of the registrant.

As of March 27, 2012, there were 11,196,760 outstanding shares of the registrant's common stock.

Documents Incorporated by Reference

Portions of the registrant's definitive proxy statement for the June 12, 2012 Annual Meeting of Stockholders, to be filed within 120 days after the end of the fiscal year covered by this Form 10-K, are incorporated by reference into Part III of this Form 10-K.

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Cautionary Statement Regarding Forward-Looking Statements

This Form 10-K contains forward-looking statements regarding our business, customer prospects, or other factors that may affect future earnings or financial results that are subject to the safe harbor created by the Private Securities Litigation Reform Act of 1995. Such statements involve risks and uncertainties which could cause actual results to vary materially from those expressed in the forward-looking statements. Investors should read and understand the risk factors detailed here in our Form 10-K and in other filings with the Securities and Exchange Commission. These risks include, among others, the following:

- changes in the way the US government contracts with businesses and changes in the budgetary priorities;
- terms specific to US government contracts;
- our failure to keep pace with a changing technological environment;
- intense competition from other companies;
- inaccuracy in our estimates of the cost of services and the timeline for completion of contracts;
- non-performance by our subcontractors and suppliers;
- our failure to adequately integrate businesses we may acquire; and
- fluctuations in our results of operations and its impact on our stock price.

In some cases, you can identify forward-looking statements by terms such as “may,” “will,” “should,” “could,” “would,” “expe “plans,” “anticipates,” “believes,” “estimates,” “projects,” “predicts,” “intends,” “potential” and similar expressions intended to forward-looking statements. These statements reflect our current views with respect to future events and are based on assumptions and subject to risks and uncertainties. Given these uncertainties, you should not place undue reliance on these forward-looking statements. We discuss many of these risks in greater detail under the heading “Risk Factors” in Item 1A. Also, these forward-looking statements represent our estimates and assumptions only as of the date of this report. Except as required by law, we assume no obligation to update any forward-looking statements after the date of this report.

PART I

ITEM 1. BUSINESS.

Overview of Market

Founded in 1979, Information Analysis Incorporated, to which we sometimes refer as IAI, is in the business of modernizing client information systems, developing and maintaining information technology systems, and performing consulting services to government and commercial organizations. Since its inception, we have performed software development and conversion projects for over 100 commercial and government customers including, but not limited to, Computer Sciences Corporation, IBM, Computer Associates, MCI, Sprint, Citibank, U.S. Department of Homeland Security, U.S. Treasury Department, U.S. Department of Agriculture, U.S. Department of Energy, U.S. Army, U.S. Air Force, U.S. Department of Veterans Affairs, and the Federal Deposit Insurance Corporation. At present, we primarily apply our technology, services and experience to legacy software migration and modernization for commercial companies and government agencies, and to developing web-based solutions, including electronic forms conversions, for various agencies of the federal government.

The migration and modernization market is complex and diverse as to the multiple requirements clients possess to upgrade their older systems. Many large legacy systems remain in use because of the enormous cost to re-engineer these systems. Currently, the options available to modernize these systems are many. Performance and capacity of client-server systems, both UNIX and .NET, rival the traditional mainframe systems. There are many brands of software that can interface with legacy systems via PC interfaces. New software development languages also allow users to warehouse and data-mine information from legacy databases. Finally, the evolution of the Internet and intranet technology offer a different approach for collecting and processing large volumes of user transactions, processes which are the forte of older legacy systems. All of these options are very expensive and time consuming because they require starting all over in defining requirements, designing structures, programming, and testing. Costs can range as high as $10 or more per line of new code.

Companies are being driven for various reasons to address the upgrading of their legacy systems. One reason is the difficulty of finding and retaining staff with outdated technical skills, many of which are possessed only by senior programmers nearing retirement. Hardware platforms such as Unisys are reaching the horizon of their usefulness, and consequently, older programming and data base languages are generally poorly supported by their providers. Additionally, maintenance costs are materially increasing as vendors squeeze the most out of clients before the life-cycles of hardware and software expire. In addition, the Internet has added a new level of pressure to compete in the electronic marketplace with sector rivals. We expect that the next ten years should see an upsurge of movement and change as organizations revamp their older legacy systems.

A segment of mainframe users is interested in simply updating their legacy systems without drastic rewritings to these systems in newer languages or adapting expensive off-the-shelf products (such as SAP or Oracle) to their needs. These potential customers are looking for automated tools that can quickly and cost-effectively move applications onto cheaper computer platforms without the risk of failure. Tools such as those provided by Micro Focus can perform this function by preserving the business rules in COBOL but extending the screens to be accessed over the Internet and providing compilers and utilities that allow the application to work on PC and UNIX platforms. It is difficult to determine the exact size of this segment, but even a 5% share of this market would represent hundreds of prospective customers with meaningful opportunities.

The web solutions market continues to be one of the fastest growing segments of the information technology consulting business as individuals, small companies, large companies, and government agencies (state and federal) expand their presence on the Internet. The range of products and services involved in this sector is extensive and therefore, require some specialization for a small company such as IAI to make an impact. Most small web companies are involved in building websites and typically have many short duration projects. More complex web applications generally require knowledge of customers' back-end systems based on mainframe or mid-level computers. Few small companies have the expertise to develop these more sophisticated web applications. We distinguish ourselves among smaller companies by developing such expertise, typically associated with larger companies, both internally and through strategic business relationships with leading-edge software firms.

These types of applications, including innovative solutions in the Business Intelligence and Cybersecurity arenas, should become more prominent in the future as web-based solutions continue to evolve. The need for commercial and public sector managers to access and combine data from disparate sources (internally and externally) for timely decision-making is becoming ever more acute in our fast paced digitally driven environment. The volume of data available to companies and agencies is growing at an exponential rate, as well as the need to protect that data and the systems that house them. This convergence of the need for instantaneous reliable access to real-time data via the web, combined with protecting such information from tampering and theft by unauthorized sources, should result in increased opportunities for IAI's evolving capability skill set.

The commercial and government sectors of the software migration and modernization market can be quite different in their requirements for web-based applications. Many companies are generally interested in cataloging and selling items whereas government agencies wish to disseminate data to the citizenry. There is some overlap in common functionality when web applications are designed for procurement transactions or customer relations. What distinguishes the government requirements is that most government processes are based on forms. Many government agencies rely on thousands of internal and external forms to conduct their business. Any company that wishes to develop governmental web applications must address the forms issue. Adobe electronic forms products resold and supported by IAI are the predominant forms software in the federal government.

Description of Business and Strategy

Since the mid-1990's we have migrated customers from older computer languages generally associated with legacy computer systems to more modern languages used with current-day computer system platforms. Many organizations have become aware of the evolving obsolescence of these systems and are now beginning to fund their modernization. In addition, as part of this modernization, many organizations wish to extend these legacy systems to interface with web-based applications. Our strategy has been to develop and/or acquire tools that will facilitate the modernization process and differentiate our offerings in the marketplace.

In 2004, we aligned with Micro Focus, an established company in the legacy COBOL environment, to participate in an effort intended to promote, quickly and cost-effectively, the conversion of large legacy mainframe systems to PC and Unix server platforms. Micro Focus has developed a suite of products that simplify the conversion process and enable the entry screens to be Internet accessible. The convergence of these tools with the recent advancements in hardware performance of PC servers has finally permitted users to substantially reduce their annual mainframe hardware maintenance costs. As an authorized reseller and installer of the tools, our plan is to derive revenue from software sales and installation services as well as acquire supplementary programming services that typically occur with each engagement.

We have structured our company to address the wide range of requirements that we envision the market will demand. We believe that the Micro Focus tool suite and use of our proprietary ICONS legacy conversion tools suite will give us a competitive edge in performing certain conversions and migrations faster and more economically than many other vendors. The diverse capabilities of our staff in mainframe technology and client-server implementations help to assure that our staff can analyze the original systems properly to conduct accurate and thorough conversions.

Our modernization methodology has developed over the past several years through the completion of successful conversion projects. Senior members of our professional staff can perform both technical and business requirements analyses, prepare general and detail design documentation and develop project plans including milestones, staffing, deliverables, and schedules. The actual work can be performed at customer sites or on our premises, which has mainframe and client-server facilities for the use of our personnel.

Our strategy to exploit the conversion and modernization market is also based on forming alliances with large information technology consulting firms who currently maintain the legacy systems for large government agencies and Fortune 1000 companies. These firms have established relationships with such customers, who rely on their advice in selecting tools and services to modernize legacy systems. We have been successful in forming partnerships with firms such as IBM, EDS, Northrop Grumman, Unisys, SI International, and Oracle. These alliances have resulted in significant contracts in the past and are important in procuring future business.

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In addition to gaining new business, we will focus on retaining and expanding existing contracts.

We are also using the experience we have acquired as an Adobe Lifecycle reseller to help secure engagements for web-based applications requiring forms. The Adobe products have evolved over the years into robust tools that can form the backbone of applications, especially those requiring forms. We have used this expertise to penetrate a number of federal government clients such as the Internal Revenue Service and Veteran Affairs and build sophisticated web applications. Our knowledge of legacy system languages has been instrumental in connecting these web applications to legacy databases residing on mainframe computers. Our company has built a core group of professionals that can build this practice over the coming years.

Concentrating on the niche of electronic forms-related web applications through our relationship with Adobe products, we have developed a cadre of professionals that can quickly and efficiently develop web applications. We will focus on federal government clients during 2012 and beyond and leverage the company's reputation with existing federal customers to penetrate these agencies. We will be able to reference successful projects completed or in development for the Department of Homeland Security, the Department of Veterans Affairs, Federal Mediation and Conciliation Service, U.S. Department of Agriculture, General Services Administration, Army Reserve, and U.S. Air Force Logistics Command.

We recognize the need to enhance our service and product capabilities as a means of expanding our business base and maintaining growth in the future. To that end, beginning in late 2010 and in continuing in 2011, we have aggressively pursued strategic business relationships with certain leading-edge technology firms in our local area that have developed unique and innovative software-based products and services. These new business areas include, but are not limited to, cybersecurity, real-time business intelligence, mobile applications and SharePoint developments. Where appropriate, we have entered into teaming arrangements or product reseller agreements with certain of these firms. These products and services are synergistic to our present business strategy and also allow us to expand into new business areas, both within the federal government and commercial sectors, without the expenditure of significant technical development dollars. Our partners benefit by our potential to leverage their new technology developments into our existing client base, as well as utilize our expertise and credibility in developing applications around their inventive products.

Our management will continue to explore ways to expand our current market spaces and develop new ones that may offer more opportunity. This may take the shape of organic growth or through acquisition of other companies. In any event, IAI will be more aggressive than in the past and will take more risks in terms of investment in business development, exploring the potential of diversified business opportunities, and seeking targets of acquisition. We expect to see the results of these efforts during 2012 and beyond.

Backlog

As of December 31, 2011, we estimated our backlog at approximately $14.3 million over the next three years, of which $3.7 million was funded. This backlog consists of outstanding contracts and general commitments from current clients. We regularly provide services to certain clients on an as-needed basis without regard to a specific contract. General commitments represent those services which we anticipate providing to such clients during a twelve-month period.

Competition

The competition in the conversion and modernization market is very strong. Many software professional services companies have had some involvement in this area and profess proficiency in performing these projects. We also face competition from other companies that purport to substantially automate the process through software tools including Blue Phoenix Solutions, Fujitsu, and IBM. “Off-the-shelf” software for enterprise resource planning, such as SAP and Oracle, provides an additional source of competition, although to date, the cost and lengthy installation time for enterprise resource planning software has slowed its implementation in the market place. No matter what type of solution is offered, many of our competitors have greater name recognition than our company, a larger, more established customer base, and significantly greater financial and market resources.

In the electronic forms arena there are multiple forms vendors such as IBM (Pure Edge), Microsoft, and FormNet. These are formidable competitors who are constantly trying to gain a share of the Adobe market penetration. In the federal marketplace, the cost of switching from Adobe and losing the sizeable investments in forms already developed gives Adobe an advantage in retaining and extending its client base. Also, the prevalence of Adobe’s PDF standard format for presenting images in the electronic world is a difficult obstacle for its competitors to overcome.

There are hundreds of firms performing traditional information technology services, business intelligence and cybersecurity, and general consulting for the federal government. A great number of them are much larger than IAI, and are more established in the marketplace, and have more resources to pursue individual prospects.

Government Regulations

We supply our products and services to the United States federal government pursuant to its General Services Administration Information Technology contract, its General Services Administration Mission Oriented Business Integrated Services contract, and through contracts resulting from competitive bidding processes. We are bound by various rules and regulations promulgated by agencies of the federal government. We have not experienced undue expense beyond those expenses normally incurred in our ordinary course of business in adhering to such rules and regulations.

Intellectual Property

We depend upon a combination of trade secret and copyright laws, nondisclosure and other contractual provisions and technical measures to protect our proprietary rights in our methodologies, databases and software. We have not filed any patent applications covering our methodologies and software. In addition, we attempt to protect the secrecy of our proprietary databases and other trade secrets and proprietary information through agreements with employees and consultants.

We also seek to protect the source code of our proprietary ICONS legacy code conversion tools suite as trade secrets and under copyright law. The copyright protection accorded to databases, however, is fairly limited. While the arrangement and selection of data can be protected, the actual data is not, and others are free to create software performing the same function. We believe, however, that the creation of competing databases would be very time consuming and costly.

Employees

As of December 31, 2011, we employed 23 full-time and 5 part-time individuals. In addition, we maintained subcontractor relationships with companies and individuals that add 13 individuals for professional information technology services. Approximately 95% of our professional employees have at least four years of related experience. For computer related services, we believe that the diverse professional opportunities and interaction among our employees contribute to maintaining a stable professional staff with limited turnover.

We have no collective bargaining agreements or other such labor contracts with our employees and believe that our employee relationships are satisfactory. In the long-term, management will likely hire additional staff to meet its anticipated growth requirements. We do not anticipate encountering material problems in our ability to hire individuals with the requisite employee skill sets, despite a competitive market for our requisite technical skill sets and government clearances, when required. We utilize fee-based recruiting firms when it is necessary to speed up the process of locating and hiring employees with specialized skill sets and clearances.

Available Information

We make available free of charge on or through our website our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to those reports as soon as reasonably practicable after such material is electronically filed with or furnished to the Securities and Exchange Commission, or SEC. Our website address is www.infoa.com.

ITEM 1A. RISK FACTORS.

We operate in a rapidly changing environment that involves a number of risks, some of which are beyond our control. This discussion highlights some of the risks which may affect future operating results. These are the risks and uncertainties we believe are most important for you to consider. Additional risks and uncertainties not presently known to us which we currently deem immaterial or which are similar to those faced by other companies in our industry or business in general, may also impair our business operations. If any of the following risks or uncertainties actually occurs, our business, financial condition and operating results would likely suffer.

Changes in the funding priorities of the US government, and changes in the way the US government contracts with businesses, may materially and adversely affect our revenue and earnings.

Since the US government is our largest customer, both directly and with us as a subcontractor, changes in the funding priorities of the US government may materially and adversely affect us if funding is cut or shifted away from the information technology services that we are equipped to provide. Additionally, changes in the way the government awards contracts may create a disadvantage for us to compete in certain markets.

US government contracts are generally subject to terms more favorable to the customer than commercial contracts.

US government contracts generally contain provisions and are subject to laws and regulations that give the federal government rights and remedies not typically found in commercial contracts, including provisions permitting the federal government to:

- terminate our existing contracts;
- reduce potential future income from our existing contracts;
- modify some of the terms and conditions in our existing contracts;
- suspend or permanently prohibit us from doing business with the federal government or with any specific government agency;
- impose fines and penalties;
- subject the award of some contracts to protest or challenge by competitors, which may require the contracting federal agency or department to suspend our performance pending the outcome of the protest or challenge and which may also require the government to solicit new proposals for the contract or result in the termination, reduction or modification of the awarded contract;
- suspend work under existing multiple year contracts and related task orders if the necessary funds are not appropriated by Congress;
- decline to exercise an option to extend an existing multiple year contract; and
- claim rights in technologies and systems invented, developed or produced by us.

The federal government may terminate a contract either “for convenience” (for instance, due to a change in its perceived needs or its desire to consolidate work under another contract) or if a default occurs by failing to perform under the contract. If the federal government terminates a contract for convenience, we generally would be entitled to recover only our incurred or committed costs, settlement expenses and profit on the work completed prior to termination. If the federal government terminates a contract based upon a default, we generally would be denied any recovery for undelivered work, and instead may be liable for excess costs incurred by the federal government in procuring undelivered items from an alternative source and other damages as authorized by law.

Failure to keep pace with a changing technological environment could negatively impact our business.

The computer industry in general, and the market for our application software offerings and services, is characterized by rapidly changing technology, frequent new technology introductions, and significant competition. In order to keep pace with this rapidly changing market environment, we must continually develop and incorporate into our services new technological advances and features desired by the marketplace at acceptable prices. The successful development and commercialization of new services and technology involves many risks, including the identification of new opportunities, timely completion of the development process, the control and recovery of development and production costs and acceptance by customers of our products and services. If we are unsuccessful in identifying, developing and marketing our services and technology or adapting our business to rapid technological change, it will have a material negative impact on our results of operations.

We are subject to intense competition from other companies engaged in software development and computer related services.

The market for our products and services is competitive, rapidly evolving, and can be affected by new product introductions and other market activities of industry participants. Some of these companies have longer operating histories, greater financial, marketing and other resources, greater name recognition in other markets and a larger base of customers than IAI. In addition, some companies have well-established relationships with our current and prospective customers. As a result, these competitors may be able to devote greater resources to the development, promotion and sale of their products and services than we can. Should we not be able to maintain our competitive advantages in light of these factors, it could have a material negative impact on our results of operations.

If we are unable to accurately estimate the cost of services and the timeline for completion of contracts, the profitability of our contracts may be materially and adversely affected.

Our commercial and federal government contracts are typically awarded on a competitive basis. Our bids are based upon, among other items, the cost to provide the services. To generate an acceptable return on our investment in these contracts we must be able to accurately estimate our costs to provide the services required by the contract and be able to complete the contracts in a timely manner. If we fail to accurately estimate our costs or the time required to complete a contract the profitability of our contracts may be materially and adversely affected.

Contracts on which we utilize subcontractors or suppliers may be adversely affected if our subcontractors or suppliers fail to perform required obligations under the contract.

We frequently utilize subcontract labor on contracts where we bid as partners, we lack a specific type of expertise, or where the subcontractor has brought the opportunity to us. If our subcontractors or suppliers fail to perform as specified, it may adversely affect our contracts and subject us to loss of the contracts, unintended expenses, and/or the inability to secure future contracts due to our nonperformance.

Our federal government contracts typically have terms of one or more base years and one or more option years. Federal governmental agencies generally have the right not to exercise options to extend a contract. A decision to terminate or not to exercise options to extend our existing contracts could have a material adverse effect on our business, prospects, financial condition and results of operations.

We are dependent on key personnel to maintain our profitability and grow our business.

Our future success depends, to a significant extent, on the continued services of our key personnel. A loss of certain key personnel, both managerial and technical, would most likely have an adverse effect on our business. In addition, competition for qualified technical personnel throughout the industry is significant and we may be unable to retain our current personnel or attract, integrate or retain other highly qualified personnel in the future. If we do not succeed in retaining our current personnel or in attracting and motivating new personnel, our business could be adversely affected.

We are dependent upon third-party software and software maintenance suppliers, making us vulnerable to supply shortages and lapses in support.

We obtain software licenses and related software maintenance contracts for resale from third-party suppliers. Any delay in our suppliers' fulfillment of our orders could impair our ability to deliver products and maintenance to customers and, accordingly, could have a material adverse effect on business, results of operations, financial condition, and reputation.

Failure to adequately integrate prospective new businesses or acquisitions could materially impact and disrupt our business.

We are seeking to expand our business and may acquire or make investments in companies or businesses offering complementary products, services and technologies in the future. Acquisitions and investments typically involve numerous risks including, but not limited to difficulties in integrating operations, technologies, services and personnel and diversion of financial and managerial resources from existing operations. To manage this prospective growth effectively, we may need to implement additional management information systems capabilities, further develop our operating, administrative, financial and accounting systems and controls, improve coordination among accounting, finance, marketing and operations and hire and train additional personnel. Should these prospective integrations prove more difficult and time consuming than anticipated, it could negatively impact our results of operations.

Fluctuations in our results of operations from period to period may cause fluctuations in our stock price.

Our financial results vary from quarter to quarter based on certain factors such as the timing of significant orders, contract funding approvals and contract completions, some of which are beyond our control. As a consequence, our quarterly and annual revenue and operating results may fluctuate from period to period, and period comparisons may therefore not be meaningful. Such fluctuations in the future could contribute to corresponding fluctuations in our stock price and in certain cases cause the trading price of our stock to decline.

The exercise of outstanding options to purchase our common stock could substantially dilute shareholders' investments.

Under the terms of existing outstanding options to acquire our common stock issued to employees and others, the holders thereof are given an opportunity to profit from a rise in the market price of our common stock that, upon the exercise of such options, could result in dilution in the interests of our other shareholders.

Our business potential could be impacted by our failure to adequately protect our intellectual property.

Our success depends in part on our ability to obtain and maintain proprietary protection for our technologies, products, and processes, and our ability to operate without infringing the proprietary rights of other parties. We may not be able to obtain copyright, patent or other protection for our proprietary technologies or for certain processes developed by our employees. Legal standards relating to intellectual property rights in computer software are still developing and this area of the law is evolving with new technologies. Any copyrights, patents or other registrations may not sufficiently protect us against competitors with similar technology. In addition, our intellectual property rights may be challenged, narrowed, invalidated or circumvented. Our intellectual property rights do not guarantee any competitive advantage. Because our success in part relies upon our technologies, if proper protection is not available or can be circumvented, our business may be negatively impacted.

There is a limited public market for our common stock.

Our common stock is presently quoted on the OTC Bulletin Board under the symbol "IAIC", and the securities are traded through broker-dealers. Because our stock trades on the OTC Bulletin Board rather than on a national securities exchange, a shareholder may find it difficult to either dispose of or obtain quotations as to the price of our common stock. There has historically been a low trading volume of our shares which may have an adverse impact on a shareholder's ability to execute transactions of our shares.

Our forward-looking statements and projections may prove to be inaccurate.

Our actual financial results likely will be different from those projected due to the inherent nature of projections and may be better or worse than projected. Given these uncertainties, you should not rely on forward-looking statements. The forward-looking statements contained in this Form 10-K speak only as of the date of this Form 10-K. We expressly disclaim a duty to provide updates to forward-looking statements after the date of this Form 10-K to reflect the occurrence of subsequent events, changed circumstances, changes in our expectations, or the estimates and assumptions associated with them. The forward-looking statements in this Form 10-K are intended to be subject to the safe harbor protection provided by the federal securities laws.

ITEM 2. PROPERTIES.

Our offices are located at 11240 Waples Mill Road, Fairfax, VA 22030. We hold a lease for 4,434 square feet. This lease expires on May 31, 2013. We believe that our current facility is suitable and adequate to meet our current needs, and that suitable additional or substitute space will be available as needed to accommodate expansion of our operations.

ITEM 3. LEGAL PROCEEDINGS.

There are presently no pending legal proceedings to which we are a party or to which any of our property is subject and, to the best of our knowledge, no such actions against us are contemplated or threatened.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.

Market Information

Our Common Stock trades on the Over-the-Counter Bulletin Board under the symbol IAIC. The following table sets forth, for the fiscal periods indicated, the high and low bid prices of the Common Stock, as reported by Yahoo Finance:

	Fiscal Year Ended December 31, 2011				Fiscal Year Ended December 31, 2010			
	Quarter Ended:				Quarter Ended:			
	3/31/11	6/30/11	9/30/11	12/31/11	3/31/10	6/30/10	9/30/10	12/31/10
High	$0.19	$0.20	$0.22	$0.24	$0.20	$0.26	$0.25	$0.20
Low	$0.15	$0.15	$0.17	$0.13	$0.15	$0.16	$0.06	$0.13

The quotations on which the above data are based reflect inter-dealer prices without adjustment for retail mark-up, mark-down or commission, and may not necessarily represent actual transactions.

Because our stock trades on the OTC Bulletin Board rather than on a national securities exchange, a shareholder may find it difficult to either dispose of or obtain quotations as to the price of our common stock. There has historically been a low trading volume of our shares which may have an adverse impact on a shareholder's ability to execute transactions of our shares.

Holders

As of December 31, 2011, we had 113 holders of record of our Common Stock.

Dividends

We have never paid any cash dividends on our common stock and do not anticipate paying cash dividends within the foreseeable future. Our management anticipates that all earnings, if any, will be retained for development of our business. Any future dividends will be subject to the discretion of the board of directors and will depend on, among other things, future earnings, our operating and financial condition, our capital requirements and general business conditions.

Securities authorized for issuance under equity compensation plans

The following table contains information regarding securities authorized and available for issuance under our equity compensation plans for certain employees, directors, and consultants.

Equity Compensation Plan Information

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants, and rights (a)	Weighted-average exercise price of outstanding options, warrants, and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by security holders1,2	1,003,000	$ 0.31	358,000
Equity compensation plans not approved by security holders	-	-	-
Total	1,003,000	$ 0.31	358,000

1 The Company has a stock incentive plan, which became effective May 18, 2006, and expires May 17, 2016 (the “2006 Plan”). The 2006 Plan provides for the granting of equity awards to employees and directors. The maximum number of shares for which equity awards may be granted under the 2006 Plan is 950,000. Options under the 2006 Plan expire no later than ten years from the date of grant or 90 days after employment ceases, whichever comes first, and vest over periods determined by the Board of Directors.
2The Company had a stock option plan, which became effective June 25, 1996, and expired May 29, 2006 (the “1996 Plan”). The plan provided for the granting of stock options to employees and directors. The maximum number of shares for which options could be granted under the 1996 Plan was 3,075,000. Options expire no later than ten years from the date of grant or 90 days after employment ceases, whichever comes first, and vest over periods determined by the Board of Directors.

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

The following discussion should be read in conjunction with the attached financial statements and notes thereto. Reference is made to “Cautionary Statement Regarding Forward-Looking Statements” on page 1 hereof, which describes important factors that could cause actual results to differ from expectations and non-historical information contained herein.

Overview

During 2011 our sales and marketing efforts were focused to capitalize on our expertise in these areas – electronic forms software, conversion, modernization, accessibility, web-enablement, services and tools to address the legacy modernization/conversion market, including third party tools, legacy and post-conversion database support, development and support of database-backed web portals, other web-based solutions, and management consulting services.

In 2011 we had net income of $153,401. Our stockholders' equity was $2,040,189 at December 31, 2011. Our gross margins improved by $56,465 on increased revenue of $960,833. The revenue increase is due to increases in sales of third-party software products and related maintenance contracts. Gross margins as a percentage of sales were consistent with 2010 for both professional services and software sales. Our expenses related to selling, general and administrative infrastructure increased 1.5% in 2011, but fell as a percentage of sales. Commission expense increased 3.0% due to the increases in software sales.

Cash and cash equivalents decreased $687,151, primarily due to one large outstanding product-related receivable for which we had already paid $1 million toward the total cost to our supplier. We were able to maintain and to grow our investment in interest bearing accounts, and we were able to operate throughout 2011 without borrowing against our line of credit.

Results of Operations

The following table sets forth, for the periods indicated, selected information from our Statements of Operations, expressed as a percentage of revenue:

	Years Ended December 31, 2011		December 31, 2010	
Revenue	100.0	%	100.0	%
Cost of Goods Sold	68.8	%	65.2	%
Gross Profit	31.2	%	34.8	%
Operating Expenses				
Selling, general and administrative	(20.0	%)	(22.5	%)
Commissions on sales	(9.3	%)	(10.3	%)
Income from operations	1.9	%	2.0	%
Other income	0.1	%	0.1	%
Income before income taxes	2.0	%	2.1	%
Provision for income taxes	(0.0	%)	(0.0	%)
Net income	2.0	%	2.1	%

2011 Compared to 2010

Revenue. Revenue for 2011 increased $961,000, or 14.0%, to $7.82 million from $6.86 million in 2010. Revenue from professional services fees decreased $155,000, or 3.2%, to $4.70 million in 2011 from $4.86 million in 2010. Revenue from software sales increased $1.12 million, or 55.7%, to $3.12 million in 2011 from $2.00 million in 2010. Revenue from software sales comprised 39.9% of total sales in 2011, compared to 29.2% of total sales in 2010. Our software sales increases were due to new product and maintenance contract sales.

Gross Profit. Gross profit increased $56,000, or 2.4% in 2011 versus 2010. Gross profit as a percentage of revenue decreased to 31.20% of revenue in 2011 from 34.8% of revenue in 2010. The decrease in gross profit as a percentage of revenue is due to the change in the ratio of professional fees to software sales. Gross profit from professional fees was 42.3% in 2011 on 60.1% of total sales while gross profit from software sales was 14.6% on 39.9% of total sales. In 2010, gross profit from professional fees was 43.1% on 70.8% of total sales while gross profit from software sales was 14.6% on 29.2% of total sales. Professional services gross margin was $1.99 million, or 42.3% of revenue in 2011, compared to $2.09 million, or 43.1% of revenue in 2010. Software sales gross margin increased from $293,000 in 2010 to $456,000 in 2011. Gross margin as a percentage of revenue for software sales remained constant at 14.6% in both 2011 and 2010.

Selling, General and Administrative. Selling, general and administrative expense for 2011 increased $23,000 to $1.56 million, or 20.0% of revenue, from $1.54 million, or 22.5% of revenue, in 2010. We were able to limit this expense increase to 1.5% versus a revenue increase of 14.0%. The costs related to our current selling, general, and administrative infrastructure do not vary significantly with fluctuations in revenue-producing activity.

Commission Expense. Commission expense in 2011 was $729,000, or 9.3% of revenue, versus $708,000, or 10.3% in 2010. Commission expenses vary with income generated from contracts sold by our commission-based sales associates.

Recent Accounting Pronouncements

ASU 2011-04, “Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs.” In May 2011, the FASB issued ASU 2011-04 to allow for common fair value measurement and disclosure requirements in GAAP and IFRS. Consequently, the wording used to describe many of the requirements in GAAP for measuring fair value and for disclosing information about fair value measurements has changed. FASB does not intend for the changes to result in a change in the application of the requirements in the fair value standard. ASU 2011-04 clarifies the FASB’s intent about the application of existing fair value measurement requirements. ASU 2011-04 is effective for interim and annual periods beginning after December 15, 2011. We do not expect ASU 2011-04 to have a material impact on our financial statements and processes.

Liquidity and Capital Resources

Our beginning cash and cash equivalents balance, when combined with our cash flow from operations, were sufficient to provide financing for our operations. For 2011, net cash used by operating, investing and financing activities was $687,151. Our net cash used of $687,151, when subtracted from a beginning balance of $1,968,077 yielded cash and cash equivalents of $1,280,926 at December 31, 2011. Our accounts receivable balances increased $2,117,844, and our accounts payable balances increased $921,651, primarily due to outstanding product-related invoices at year end. We had no non-current liabilities at December 31, 2011.

We have a revolving line of credit with a bank providing for demand or short-term borrowings of up to $1,000,000. The line became effective December 20, 2005, and expires on December 1, 2012. As of December 31, 2011, no amounts were outstanding under this line of credit. We did not borrow against this line of credit in 2011.

Based on our current cash position and operating plan, we anticipate that we will be able to meet our cash requirements beyond the next twelve months.

We presently lease our corporate offices on a contractual basis with certain timeframe commitments and obligations. We believe that our existing offices will be sufficient to meet our foreseeable facility requirement. Should we need additional space to accommodate increased activities, management believes we can secure such additional space on reasonable terms.

We have no material commitments for capital expenditures.

Contractual Obligations

		Payments due by period			
Contractual Obligations	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Operating Lease Obligations					
Lease of Principal Offices	135,443	95,263	40,180	-	-
Total	$135,443	$95,263	$40,180	$-	$-

Off-Balance Sheet Arrangements

We do not have any off balance sheet arrangements that have or are likely to have a material current or future effect on our financial condition, or changes in financial condition, liquidity or capital resources or expenditures.

Critical Accounting Policies and Estimates

Our significant accounting policies are described in Note 1 to our accompanying financial statements. We consider the accounting policies related to revenue recognition to be critical to the understanding of our results of operations. Our critical accounting policies also include the areas where we have made what we consider to be particularly difficult, subjective or complex judgments in making estimates, and where these estimates can significantly impact our financial results under different assumptions and conditions. We prepare our financial statements in conformity with accounting principles generally accepted in the United States. As such, we are required to make certain estimates, judgments and assumptions that we believe are reasonable based upon the information available. These estimates, judgments and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the periods presented. Actual results could be different from these estimates.

Revenue Recognition

We generally recognize revenue when a contract has been executed, the contract price is fixed and determinable, delivery of services or products has occurred, and collectability of the contract price is considered probable and can be reasonably estimated. We earn revenue under time and materials and fixed price contracts. For sales of third party software products, we recognize revenue upon delivery.

We recognize revenue on time and materials contracts based on direct labor hours expended at contract billing rates and adding other billable direct costs.

For fixed price contracts that are based on unit pricing, we recognize revenue for the number of units delivered in proportion to total expected units to be delivered in any given reporting period.

For fixed price contracts in which we are paid a specific amount to be available to provide a particular service for a stated period of time, we recognize revenue ratably over the service period. We apply this method of revenue recognition to sales of maintenance contracts on third party software products, as on Adobe and Micro Focus software, for which we are responsible for “first line support” to the customer and for serving as a liaison between the customer and the third party maintenance provider for issues we are unable to resolve.

We engage in fixed price contracts with the U.S. Government involving the complex delivery of technology products and services. Accordingly, these contracts are within the scope of the American Institute of Certified Public Accountants Audit and Accounting Guide for Audits of Federal Government Contractors. To the extent contracts are incomplete at the end of an accounting period, we recognize revenue on the percentage-of-completion method, on a proportional performance basis, using costs incurred in relation to total estimated costs.

Sales of third party software products such as Adobe and Micro Focus products are reported on a gross basis with IAI as a principal under authoritative guidance from the Financial Accounting Standards Board (FASB). This determination was based on the following: 1) We have inventory risk as suppliers are not obligated to accept returns, 2) we have reasonable latitude, within economic constraints, in establishing price, 3) we, in our marketing efforts, frequently aid the customer in determining product specifications, 4) we have physical loss inventory risk as title transfers at the shipping point, 5) we bear full credit risk, and 6) the amount we earn in the transaction is neither a fixed dollar amount nor a fixed percentage.

In October 2009, the FASB amended the accounting standards for certain multiple deliverable revenue arrangements to: 1)provide updated guidance on whether multiple deliverables exist, how the deliverables in an arrangement should be separated, and how the consideration should be allocated; 2) require an entity to allocate revenue in an arrangement using best estimated selling price ("BESP") of deliverables if a vendor does not have vendor-specific objective evidence (“VSOE”) of selling price or third-party evidence ("TPE") of selling price; and 3) eliminate the use of the residual method and require an entity to allocate revenue using the relative selling price method. For our multiple-element arrangements, we determine the selling price for each deliverable using VSOE of selling price, if it exists, or TPE of selling price.

In October 2009, the FASB amended the accounting standards for certain multiple deliverable revenue arrangements to: 1)provide updated guidance on whether multiple deliverables exist, how the deliverables in an arrangement should be separated, and how the consideration should be allocated; 2) require an entity to allocate revenue in an arrangement using best estimated selling price ("BESP") of deliverables if a vendor does not have VSOE of selling price or third-party evidence ("TPE") of selling price; and 3) eliminate the use of the residual method and require an entity to allocate revenue using the relative selling price method.

We elected to adopt this accounting guidance at the beginning of our first quarter of fiscal 2011 on a prospective basis for applicable transactions originating or materially modified beginning January 1, 2011. The application of these new accounting standards, if applied in the same manner to the year ended December 31, 2010, would not have had a material impact on total net revenues for that fiscal year.

Our contracts with agencies of the government are subject to periodic funding by the respective contracting agency. Funding for a contract may be provided in full at inception of the contract or ratably throughout the contract as the services are provided. In evaluating the probability of funding for purposes of assessing collectability of the contract price, we consider our previous experiences with our customers, communications with our customers regarding funding status, and our knowledge of available funding for the contract or program. If funding is not assessed as probable, we defer revenue recognition until realization is deemed probable.

Payments received in advance of services performed are recorded and reported as deferred revenue. Services we perform prior to invoicing customers are recorded as unbilled accounts receivable and are presented on our balance sheets in the aggregate with accounts receivable.

Effects of Inflation

In the opinion of management, inflation has not had a material effect on our operations.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders
Information Analysis Incorporated

We have audited the accompanying balance sheets of Information Analysis Incorporated as of December 31, 2011 and 2010, and the related statements of operations, changes in stockholders' equity, and cash flows for the years then ended. 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 the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company has determined that it is not required to have, nor were we engaged to perform, an audit of its internal controls over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and 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 Information Analysis Incorporated as of December 31, 2011 and 2010, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

/s/ Reznick Group, P.C.

Vienna, Virginia
March 30, 2012

INFORMATION ANALYSIS INCORPORATED
BALANCE SHEETS

	December 31, 2011	December 31, 2010
ASSETS		
Current assets		
Cash and cash equivalents	$1,280,926	$1,968,077
Accounts receivable, net	2,889,658	771,814
Prepaid expenses	787,290	570,948
Note receivable, current	6,668	6,438
Total current assets	4,964,542	3,317,277
Fixed assets, net of accumulated depreciation		
and amortization of $264,837 and $582,854	40,440	35,705
Note receivable, long-term	4,287	10,955
Other assets	6,281	6,281
Total assets	$5,015,550	$3,370,218
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	$998,160	$76,509
Deferred revenue	939,783	652,591
Commissions payable	679,498	446,759
Accrued payroll and related liabilities	247,885	245,518
Other accrued liabilities	107,235	68,759
Taxes payable	2,800	-
Total current liabilities	2,975,361	1,490,136
Stockholders' equity		
Common stock, $0.01 par value, 30,000,000 shares authorized, 12,839,376 issued, 11,196,760 outstanding as of December 31, 2011 and 2010	128,393	128,393
Additional paid-in capital	14,574,128	14,567,422
Accumulated deficit	(11,732,121)	(11,885,522)
Treasury stock, 1,642,616 shares at cost at December 31, 2011 and 2010	(930,211)	(930,211)
Total stockholders' equity	2,040,189	1,880,082
Total liabilities and stockholders' equity	$5,015,550	$3,370,218

The accompanying notes are an integral part of the financial statements

INFORMATION ANALYSIS INCORPORATED
STATEMENTS OF OPERATIONS

	For the years ended December 31,	
	2011	2010
Sales		
Professional fees	$4,700,679	$4,855,760
Software sales	3,120,096	2,004,182
Total sales	7,820,775	6,859,942
Cost of sales		
Cost of professional fees	2,714,118	2,763,416
Cost of software sales	2,664,403	1,710,737
Total cost of sales	5,378,521	4,474,153
Gross profit	2,442,254	2,385,789
Selling, general and administrative expenses	1,564,370	1,540,903
Commissions on sales	729,075	707,959
Income from operations	148,809	136,927
Other income	7,392	9,535
Income before provision for income taxes	156,201	146,462
Provision for income taxes	2,800	--
Net income	$153,401	$146,462
Earnings per common share - basic	$0.01	$0.01
Earnings per common share – diluted	$0.01	$0.01
Weighted average common shares outstanding		
Basic	11,196,760	11,196,760
Diluted	11,224,410	11,211,024

The accompanying notes are an integral part of the financial statements

INFORMATION ANALYSIS INCORPORATED
STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

Shares of