PAPERCLIP SOFTWARE INCE
Form 10KSB
March 31, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-KSB

ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2005

Commission File Number 000-26598

PAPERCLIP SOFTWARE, INC.
(Name of small business issuer in its charter)

Delaware
(State or other jurisdiction of incorporation or organization)

22-3137907
(I.R.S. Employer Identification No.)

1 University Plaza
Hackensack , New Jersey 07601
(Address of principal executive offices) (Zip Code)

(201) 525-1221
(Issuer's telephone number)

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

Title of each class: None Name of exchange on which registered: N/A

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

Common Stock, Par Value $.01
(Title of each Class)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act during the past 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

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B contained in this form, and no disclosure will be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB. [X]

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

The issuer's revenue for the fiscal year ended December 31, 2005 was $1,739,394. As of March 16, 2006, the aggregate market value of the voting stock held by non-affiliates of the registrant was $315,766 (based on the closing price of the OTC Bulletin Board on March 16, 2006). As of March 16, 2006, there were 8,196,521 shares of the registrant's common stock outstanding.

Documents Incorporated by Reference: None. Transitional Small Business Disclosure Format (check one): Yes ___ No X

Certain information included in this Annual Report may be deemed to include forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, that involve risk and uncertainty, such as information relating to the acceptance and sale of the Company's products, the Company's ability to successfully market and distribute its products, product development or enhancements, the Company's ability to generate sufficient cash flow from the sale of its products to meet the Company's cash requirements and to pay its liabilities when due, the Company's ability to raise additional capital, the Company's ability to protect its proprietary property and the Company's ability to attract and retain key employees. In addition, certain statements may involve risk and uncertainty if they are preceded by, followed by, or that include the words "intends," "estimates," "believes," "expects," "anticipates," "should," "could," or similar expressions, and other statements contained herein regarding matters that are not historical facts.

Although we believe that our expectations are based on reasonable assumptions, we can give no assurance that our expectations will be achieved. We do not undertake any obligation to release publicly any revisions to such forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

PART I

Item 1. Description of Business.

INTRODUCTION

PaperClip Software, Inc. formerly known as PaperClip Imaging Software, Inc. (the "Company" or "PaperClip"), a Delaware corporation, is engaged in the development and distribution of computer software for document management and transport of electronic document packages across the public Internet or a private intranet with interoperability, security and tracking capabilities. The Company is the successor by merger, in March 1992, to the original company which had been incorporated in New Jersey in October 1991.

About the Company

The Company's systems allow users of personal computers and personal computer networks to scan, file, retrieve, display, print and route documents and other software objects (such as word processing files, spreadsheets and electronic mail), while continuing to use their existing application software. The Company's systems can be integrated with many personal computer applications with little or no programming and can file and retrieve documents without the time consuming step of manually labeling or indexing each document, or manually searching for documents.

The Company developed and markets a line of software consisting of Professional, Workgroup and Enterprise Editions (the "Systems"). The Company also markets PaperClip COLD, which captures batch file information before it goes to paper and allows expeditious access, retrieval, and printing of COLD documents. "COLD" refers to Computer Output to Laser Disk, which relates to documents that are archived in large volumes of formatted data streams directly to optical media. Instead of printing large paper reports or producing microfilm or microfiche, data is stored on optical disks.

The Company developed its WebServer(TM) Product, which is an add-on to the Systems. This product provides full security for documents stored on a PaperClip System, enables users to make the documents available to anyone with a Web Browser and makes a user's document repository accessible via the Internet or a private intranet. In November 1995, PaperClip acquired, from Cheyenne Software, Inc. ("Cheyenne"), the NOSS (Network Optical Storage System) product line. The Company offers NOSS as part of its systems . The Company has developed the next generation of the NOSS product, which has been deployed on the Microsoft Windows NT server platform. The Company markets the Systems and associated products domestically (i) through a mass distributor, Z Source, which sells to a value added reseller ("VAR") channel that currently consists of approximately 20 resellers and (ii) directly through such VARs. The Company markets its products internationally through approximately 3 VARs.

Industry Background

Many businesses must manage, exchange and process large amounts of information in their day to day activities. Traditional data processing systems have automated the creation and processing of data and text, but they do not provide a means for storing and retrieving documents that must be retained in their original form and used in conjunction with the data.

The greatest difficulty in dealing with paper documents is filing, storing and retrieving them conveniently and cost-effectively. In the course of performing these tasks manually, critical documents can be inadvertently misfiled, physically damaged, or lost. Manual handling is inefficient because documents can only be used by one person at a time and are also inaccessible during the time required to transport them within the organization. Moreover, significant time and resources are often spent storing and locating documents in large filing systems. With the public acceptance of document management and, more importantly, the imaged document as an original document, exchanging electronic documents is a marketing opportunity.

The procedural steps involved in processing incoming documents may include sorting documents as they are received, indexing them for future reference, routing them from one employee to the next, entering information from these documents into computer systems, collecting different documents for appropriate action, creating letters and forms of response and queuing documents for subsequent filing. In order to improve the efficiency of the flow of documents, manage information, and improve office productivity and response times, many companies may seek to automate their paper and electronic document management procedures.

Technological developments in recent years have made possible the low cost capture, storage, retrieval and processing of paper documents as digitized images. In particular, the application of optical disk technology, which permits digitized document images to be stored with densities many times greater than magnetic storage media, has enabled the development of cost effective computer systems for document management.

The Systems have been designed to provide users of personal computers and personal computer networks the ability to exchange, file, retrieve and process large volumes of documents quickly, efficiently and at a low cost. The enhancements developed for the Systems have been designed to allow users to quickly implement workflow technology in their existing environments without the need for costly programming. The Company's Internet products give users the added flexibility of exchanging, accessing and managing stored documents via the Internet.

The Company derives all of its revenues from the licensing or sale of the Systems and associated products and services. The Company's principal products are the Professional, Workgroup and Enterprise Editions, as well as the Internet Express and eXpressLink products.

The Company has begun marketing a new document management and work flow product which has been customized for the mortgage broker industry. The Company's sales from this product were approximately $125,000 and $25,000 in 2005 and 2004, respectively. The product is available in either a client server model and installed at the customer site, or in an ASP model and hosted by PaperClip. ASP refers to a model where PaperClip hosts the clients information on PaperClip's computers. The client server product is named Mortgage Assistant (MA) and the hosted product is named Virtual Loan Folder. The Company believes that this product may represent a promising opportunity for its business, although there are competitors in this business and there can be no assurance that the Company can generate meaningful revenues from this product.

The Company has also begun marketing its PaperClip32 product in ASP model hosted by PaperClip. PaperClip32 is the name for PaperClip's document management software. To date interest in this service has been shown by the life insurance industry. The Company believes that this product may represent a promising opportunity for its business although there is at least one competitor in this business and there can be no assurance that the Company can generate meaningful revenues from this product.

PaperClip leveraged its workflow application in 2005 by adding support for forms recognition and processing data in the ACORD 103 EDI format (XML). This technology development resulted in two new service offerings, ImageIn and IGO Service. ImageIn provides the ability to correctly identify incoming document types eliminating the need for manual identification. IGO Service provides an "In Good Order" value to the recipient, which means all data and documents are analyzed to ensure all the recipients required documents have been submitted and are available before releasing the package to Internet eXpress for delivery.

There can be no assurance that the Company's products will achieve broader market acceptance or result in significant revenue to the Company.

The Systems

The Systems allow users of personal computers and personal computer networks to scan, file, retrieve, display, print and route documents and other software objects (collectively "Documents"), such as word processing files, spreadsheets and electronic mail. The Systems can be integrated with many personal computer applications with little or no programming and can file and retrieve Documents without the time consuming step of manually labeling or indexing each Document. The Systems range from single user, stand-alone products to enterprise-wide document management solutions.

Electronic "file folders" of Documents can be accessed at any time by the user with only one key stroke combination. Minimal training is required. Moreover, all Documents previously attached to an electronic file folder are accessible as soon as each of the Systems is activated. If a Document is not so attached, it can be located by searching a Document list or by entering exact or partial identifying information into the folder's index fields. Multiple Documents can be viewed simultaneously in any of the Systems.

Images displayed through any of the Systems are facsimiles of the Documents that have been scanned, and the Systems allow Documents to be scrolled through (i.e., moved on a display screen to search for a particular line or section), enlarged, reduced, and rotated. The Systems also allow stored Documents to be reproduced through a locally connected laser printer, or through shared laser print servers on a network.

Professional Edition

The Professional Edition allows users to create "folders" of Documents and attach or "clip" them to their existing application software. The additional features available include the ability to scan, index, retrieve, display, print, fax, import and export Documents. Storage of Documents is on multiple forms of media and, in addition, enables the user to store Documents on a large variety of optical disk and "jukebox" storage devices. A "jukebox" is a mechanical device which allows for multiple optical disk platters or tapes to be managed and accessed by software. This allows the storage of millions of Documents while maintaining a high level of performance. The Professional Edition works in conjunction with SQL database products from Microsoft and Sybase.

Workgroup Edition

Workgroup Edition provides users with all of the features of Professional Edition, and allows users to perform all of the functions at the same time, as well as to route Documents and folders to other users on a network.

Enterprise Edition

Enterprise Edition provides all the features of the Workgroup Edition and provides for Wide Area Network operation using a client/server architecture. The significant difference provided to users by the Enterprise Edition are the improved performance in networks with more than 20 users and the ability to manage a greater number of folders and documents. To operate Enterprise Edition, the user is required to obtain a license, which is readily available from various third parties, for the desired SQL server. The Enterprise Edition is suited to large departmental and enterprise installations. The Company presently offers its Enterprise Edition to work in conjunction with SQL Servers from Microsoft, Sybase and Oracle.

Capture Product Line - DECS

DECS (Document EDI Capture Suite) is a set of applications with which end users and business applications will collect electronic documents and / or Electronic Data Interchange (EDI) into an Electronic Document Exchange ("EDX") V2.0 Package for transmission to an IDM solution or EDI application or both. DECS provides the tools for collecting scanned images, documents printed to the DECS Print Driver, file import, keyed and file captured EDI. This data can be transformed, packaged and transported to the recipient for further processing as an EDX V2.0 Package. DECS is a remote electronic document EDX packaging system that provides scanning, printing, filing and Electronic Data Interchange ("EDI") capture producing capabilities, and creates EDX Packages for Internet Express ("IE"), eXpressLink ("XL"), the Systems and/or any EDX compliant solution.

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The Cold Product

PaperClip COLD captures formatted print data streams. Once the data is captured by the PaperClip COLD Extract Engine, it is automatically imported into the user's PaperClip System and made available to the users by viewing through the PaperClip system. Users can access folders containing COLD data by simply pressing a designated key from the applications that they choose. They can also access folders of diverse information through PaperClip's intuitive file cabinet/folder interface. PaperClip COLD can print to any standard Windows printers or fax and can display documents on conventional 80-column monitors in 132 column format. To further facilitate the retrieval and review of COLD documents, PaperClip COLD supports full text searching of COLD documents and forms overlay, and can add colored lines to the display to simulate green bar paper viewing.

The Noss Product Line

NOSS is the subsystem for optical storage and jukebox management. When combined with the Workgroup and Enterprise Editions, it provides a powerful system that manages a range of mass storage devices. The acquisition of the NOSS product line (a portion of which is subject to an exclusive, royalty free, perpetual license from Cheyenne) allows PaperClip to fully take advantage of NOSS's high-end functionality to further develop powerful document imaging solutions for client/server network environments.

Internet Product Line - Webserver

WebServer(TM) is an add-on to the Systems. The product provides full security for documents stored on a PaperClip System and enables users to make documents available to anyone with a Web Browser and to make available the user's document repository to both Internet and private intranet users. WebServer allows users across the World Wide Web to retrieve documents and conduct simple workflow tasks from their thin client browser.

Internet Express

Internet Express (IE) is an extranet designed to exchange electronic documents as an Application Service Provider ("ASP"). The Company will derive revenue based on the movement of EDX packages across the Internet. IE has expanded to four delivery options, IE Client, Secure Email, Secure Hosting, and Secure Fax. Service traffic for the year increased by 50% compared to 2004.

Clipit Toolkit

ClipIt is designed to facilitate the integration of legacy applications with other applications. ClipIt's greatest demand is found in the new thin client services. By integrating ClipIt within thin client applications, users simply hit a "Hot Key" to quickly view important records and documents across the Web. ClipIt is a Tool-kit designed to leverage PaperClip's award winning Visual Context Processor (Clipping) technology allowing developers and integrators the ability to program ClipIt within their application or script within browsers.

PaperClip BarCode

PaperClip developed and released a BarCode recognition solution where bar-coded documents are automatically received and filed. The solutions includes the ability to create bar-coded cover sheets and a server engine capable of reading the same. Documents can be scanned or faxed directly to the recognition engine.

Expresslink Communications

PaperClip's eXpressLink (XL) is an electronic document package exchange solution designed to interconnect dissimilar Electronic Document Management solutions whereby they can exchange documents similar to electronic data interchange (EDI). Designed to transport electronic document packages across the corporate Intranet or Internet providing interoperability, security and tracking. Utilizing the public standard Electronic Document eXchange version 2.0 for packaging electronic documents, any EDX V2.0 compliant system can connect to the XL Server seamlessly with no programming. A company can now connect company workflow and integrate dissimilar document management solutions to business partners and branch offices attached to the corporate Intranet or Internet. XL significantly reduces document processing costs. Standards driven, XL cuts cost and reduces time to process.

eXpressLink is designed to exchange electronic documents among organizations that are members of the same private intranet and connect to IE. The Company provides XL as a product, not a service. This product expands the user's communications options while maintaining a consistent interface to a user's document management solution.

Mortgage Assistant

Mortgage Assistant (MA) is PaperClip's workflow application designed to manage users, stages, products, documents, alerts and reports. Mortgage Assistant manages document requirements and performs workflow features including rendezvous, sign-offs, process reports, notification alerts, data-feed integration and process audits. Mortgage Assistant is an add-on module to PaperClip32.

Objectives, Internal Sales Force And Risks

Management's marketing objectives for the Systems and the Company's other products are as follows: (i) develop strategic relationships with prominent software organizations; (ii) introduce the Systems and the Company's other products to customers through VARs, original equipment manufacturers ("OEMs"), distributors and other distribution networks; (iii) create brand name recognition of its products by advertising in appropriate trade magazines and publications, and by attending and participating in exhibitions, shows and seminars, engaging in public relations campaigns, and conducting its own seminars and direct mail campaigns; and (iv) support the sales efforts of its resellers through sales tools and training.

Training and technical support of VARs is a component of the Company's efforts with respect to its Workgroup and Enterprise Editions. Consequently, the Company provides technical support along with on-going communication to its VARs.

The Company has a sales force of three persons. The Company conducts selling efforts directly to the mortgage broker industry and life insurance brokers. The Company has one sales person focusing on each of those markets. While the Company attempts to encourage VARs, distributors and other resellers to focus on the Company's products, management is aware that VARs, distributors and other resellers also represent other lines of products, some of which may be, or are, competitive with those of the Company. Accordingly, the VARs, OEMs, distributors and other resellers may choose to give higher priority to products of other publishers, which would decrease potential sales by the Company.

Value Added Reseller Network

To date, revenue sources are approximately evenly divided between VAR sales and internal services. The Company currently has approximately 23 VARs, of which approximately 20 VARs are in the United States and approximately 3 are abroad.

Business Services

The Company's Business Services Department sells directly to major accounts that want to work on a direct basis with the Company. It also offers users of its products and VARs, post-contract support, consulting services and assistance in the form of training, product education and technical support, when requested. The Business Services Department currently consists of 1 employee.

Customers And Sales

The Company had net sales of $1,739,394 in 2005 and $1,420,637 in 2004. ImageTek, a VAR, Bisys and NISC accounted for 9%, 10%, and 9%, respectively, of the Company's sales in 2005. Lumtron, an OEM, and ImageTek, a VAR, Bisys and NISC accounted for 10%, 11%,11%, and 10%, respectively, of the Company's sales in 2004. In 2004, the Company commenced a lawsuit against Lumtron in the Superior Court of the State of New Jersey for payment of delinquent accounts receivable approximating $ 93,000. The Company has set up what it believes is an adequate bad debt reserve to cover this dispute. An arbitration proceeding relating to this dispute is currently scheduled for July 2006. Three customers (ImageTek, Summit and Valmark) represented 47% of accounts receivable at December 31, 2005. Three customers (Companion, ImageTek, and Lumtron) represented 58% of accounts receivable at December 31, 2004.

Customer Support And Service

The Company presently provides telephone support to its VARs and OEMs and customers it deals with directly. The majority of the Company's service and support activities involve responses to customer inquiries regarding use of the Workgroup, Enterprise and Professional Editions, which are provided by telephone support directly from the Company's technical support center.

Product Development

At present, the Company's systems are being developed by a combination of in house staff and, when necessary, outside consultants. PaperClip expended approximately $503,000 and $ 421,800 on research and development in 2005 and 2004, respectively.

Existing and future competing products that may be offered at lower prices, or that may have superior technological and performance characteristics, could adversely affect sales of the Systems and/or other products offered by the Company. Management expects that growing demand for efficient and cost-effective solutions for document management and imaging will continue to drive the developments of new technologies that may be more sophisticated than the Company's products and that the Company's ability to continue to compete depends upon its ability to continue to enhance successfully its existing products and to develop new products that meet the changing needs of end-users. If the Company is unable to successfully enhance its existing products or to develop new products, it may have a material adverse effect on the Company's operations and profitability.

Production

The Company has produced a set of master CD's and documentation for all of its products. Depending on the product, the Company will either duplicate the CD's and ship the Systems from its headquarters or provide the customer with a download of the file. The Company has also engaged various sources to produce and assemble the product and documentation (including packaging for the Systems on terms management believes are commercially reasonable).

Product Protection

The Company relies on a combination of copyright, trade secret and trademark laws and license agreements to protect its proprietary rights in its technology. The Company was issued a Certificate of Registration for the Trademark Paperclip on November 20, 2001. Although to the best of Company's knowledge no other person or entity owns any U.S. registered trademark for the mark "PaperClip" in connection with software or imaging products, there is a registration filed by a third party for "Technology As Easy To Use As A PaperClip"(tm) for consulting on computer hardware, software and systems in the fields of sales automation, order processing, voicemail, paging, dictation, transcription and telecommunications and off-site employee programs and businesses. While the Company does not believe there is any likelihood of confusion raised by the use of such mark, if such confusion were alleged, the Company would rely on its prior common law rights. If any claim is asserted, the Company may be forced to expend significant effort, time and funds to defend against it. If the Company is not successful in defending against such a claim, the Company would be required to adopt a different name and would incur costs as a result thereof.

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The Company owns registrations for the trademark PAPERCLIP IMAGING SOFTWARE & DESIGN in Canada, but does not now own registrations or pending applications for trademark registration in other countries in which the Systems and the Company's other products are sold.

The Company distributes its products under signed software license agreements, which grant customers perpetual licenses to use, rather than ownership of, the Company's products and which contain restrictions on copying, disclosure, reverse engineering and transferability. The source code for all of the Company's products is protected as a trade secret and as an unpublished copyrighted work. In addition, the Company has entered into nondisclosure agreements with its employees. There can be no assurance that the steps taken by the Company in this regard will be adequate to deter misappropriations or independent third-party development of its technology.

The Company has no patents on its proprietary software technology and existing copyright laws afford only limited practical protection. In addition, the laws of some foreign countries do not protect the Company's proprietary rights in its products and technology to the same extent as U.S. laws.

Although management believes that the Company's products, trademarks and other proprietary rights do not infringe on any existing proprietary right of others, there can be no assurance that third parties will not assert infringement claims in the future.

Components Provided By Others

The Systems require licenses, which the Company has obtained, from, Merant AccuSoft Corporation, and Snowbound Software and may require licenses from Pegasus Imaging Corporation and Sybase Inc.

Competition

The document management software market is intensely competitive. Buyer preferences can shift quickly, and rapid changes in technology provide opportunities for new entrants into the market. Management is not aware of any product line which offers all of the features and functions of the Systems. However, a number of software companies offer products which compete with one or more of the functions of the Systems.

There are numerous companies that sell either stand-alone, network and Web based systems with which the Company competes. Competition for the Company's products include, among others, Hyland Software, Optika Imaging Systems Incorporated, OTG (a division of EMC) and LaserFiche Document Imaging. The Company also competes with more expensive turnkey solutions such as those produced by FileNet Corp. Many of these companies have greater financial strength and resources than the Company, and there can be no assurance that these competitors will not modify their existing systems, develop new products or systems or acquire other competitors of the Company to better compete with the Systems. In addition, there can be no assurance that new companies will not introduce new systems with better features and functions than the Systems. There are a few competitors in the electronic document exchange market. This is a new extension of the Internet services collectively known as the Business to Business Electronic Commerce (B2B/ec). Current competition is focused on electronic mail (Email) based exchange solutions, which is different from the methodology the Company has adopted. In the life insurance industry, one competitor has emerged utilizing a central repository for document exchange. Intellisys and Hooper Holmes each provides a central repository and sells retrieval and communications with selected carriers as their service. Each contracts with the smaller brokers where outsourcing to the broker makes more sense. PaperClip's document management customers are the larger volume brokers. Intellisys is an Internet Express customer. In the mortgage broker industry, PaperClip competes with a number of companies, such as Virpak, Advectis, SwiftView Inc. and Del Mar. In addition to computer software for document management and imaging, there is also a diverse range of alternative types of tools and methods for storing and retrieving documents, including microfilm, microfiche and computer output microfilm and microfiche machines. Moreover, management expects that the growing demand for efficient and cost-effective solutions for document management and computer imaging will continue to drive the development of new technologies that may be more sophisticated and cost-effective than the Systems. Many existing and potential competitors have considerably greater financial, technological, marketing and personnel resources than the Company.

Management believes that the principal competitive factors in the market for the Company's products include product performance, technology, quality of customer support, availability of training and consulting services, price, sales and marketing strength, corporate reputation and ongoing responsiveness to user needs.

Employees

As of March 21, 2006, the Company's full-time staff of sixteen (compared to seventeen a year ago) employees includes seven employees engaged in development and systems testing, three engaged in sales, two in training and technical support, one in Business Services and three engaged in administration. The Company has no collective bargaining agreements, and no employee is represented by a labor union. The Company has never had a work stoppage and considers its relationship with its employees to be satisfactory. The Company intends to utilize consultants to supplement its systems development, sales and marketing efforts, when necessary.

The Company's success depends to a significant extent upon a number of key management and technical employees. The loss of services of one or several of these key employees could have a material adverse effect on the Company. Management believes that the future success of the Company will also depend in large part upon the Company's ability to attract and retain highly skilled technical, managerial and marketing personnel. Competition for such personnel in the software industry is intense.

Capital Raising Initiatives

On October 29, 2004, the Company engaged Sloan Securities Corp. (together with its affiliates, "Sloan") to provide financial advisory services, which may include assistance in seeking to raise additional capital. In connection with such engagement, the Company issued two-year warrants to Sloan to purchase 500,000 shares of the Company's Common Stock at an exercise price of $.10 per share. The Warrants vested as to 425,000 shares on the date of issuance of such warrants and as to the remaining 75,000 shares at such time that a financing is consummated in which at least 1,400,000 shares of common stock or common stock equivalents are issued to investors introduced to the Company by Sloan.

On March 30, 2005 and April 8, 2005, the Company received funds from a group of accredited investors in the net amounts of $100,000 and $57,500, respectively, in anticipation of the execution of definitive documentation with such investors. Documents had been fully negotiated in anticipation of a financing for gross proceeds of between $500,000 and $1,200,000. While the Company executed certain documents prior to its receipt of the funds, the documents were to be held in escrow pending a final transaction and the Company never received countersigned agreements from the investors. Under the terms of the negotiated transaction, the invested funds were to be in the form of a two year loan, secured by a lien on the Company's assets, with interest at the rate of 12% per annum prepaid for the entire period, and financing fees due to Sloan in an aggregate amount equal to 13% of the gross proceeds raised. Warrants to purchase 200,000 shares and 50,000 shares were also to be issued to the investors and Sloan, respectively, for each $100,000 of the financing. One half of such warrants were to be exercisable at $0.20 per share, and the other half of such warrants were to be exercisable at $0.25 per share. In a letter agreement dated March 31, 2005, Sloan and the investors agreed that they would not enforce their registration rights related to shares of common stock issuable upon exercise of the warrants until such time as the Company has received an aggregate of $500,000 of gross proceeds through the issuance of notes. The Company has recorded a $250,000 loan payable on its December 31, 2005 balance

sheet based on its understanding of the intent of the parties that such $157,500 aggregate amount represents net proceeds to the Company, after prepaid interest and financing costs, of a $250,000 loan to the Company by such investors. The Company has also reserved 625,000 shares for issuance upon exercise of the warrants that were to be issued in connection with the $250,000 financing. The Company has been unable to obtain executed documents from the investors or Sloan or definitive confirmation of their intent regarding the funds. Accordingly, there can be no assurance that the investors will not seek to treat the funding as an incomplete investment and demand return of the funds. The Company has accounted for the loan as short-term indebtedness.

ITEM 2. Description of Property.

The Company's principal administrative, sales and marketing, product development and support facilities are located in Hackensack, New Jersey, and comprise approximately 2,100 square feet. The Company occupies these premises pursuant to a lease, the term of which expires on February 28, 2011. The fixed rent is approximately $4,000 per month plus utilities, plus its proportionate share of any increase in operating costs.

ITEM 3. Legal Proceedings.

In 2004, the Company commenced a lawsuit against Lumtron, one of the largest customers of the Company, in the Superior Court of the State of New Jersey for payment of delinquent accounts receivable approximating $93,000. The Company has set up what it believes is an adequate bad debt reserve to cover this dispute. An arbitration proceeding relating to this dispute is currently scheduled for July 2006.

Except as set forth above, the Company is not a party to any material pending legal proceedings.

ITEM 4. Submission Of Matters To A Vote Of Security Holders.

No matters were submitted to a vote of security holders during 2005.

PART II

ITEM 5. Market For Common Equity and Related Stockholder Matters.

	Common Stock	
2005	High	Low
First	0.14	0.04
Second	0.07	0.05
Third	0.08	0.04
Fourth	0.06	0.03
2004	High	Low
First	0.10	0.04
Second	0.18	0.09
Third	0.12	0.06
Fourth	0.14	0.07

The above prices per share were the bid prices during such periods as reported by Bloomberg News Service for OTC market quotations. Such quotations reflect interdealer prices without retail mark-up, mark-down or commission and may not necessarily represent actual transactions.

The Company's securities are presently traded on the OTC Bulletin Board. As of December 31, 2005, there were approximately 160 holders of record of the Company's shares of Common Stock. The Company has not paid cash dividends since its organization and does not anticipate the declaration or the payment of cash dividends in the foreseeable future. In addition, the Company's Series A Preferred Stock Certificate of Designation restricts the declaration, payment and setting aside of any dividends without the consent of the holders of the Requisite Percentage (as defined in such Certificate) of Series A Preferred Stock.

ITEM 6. Management's Discussion and Analysis or Plan of Operation.

RESULTS OF OPERATIONS

Year Ended December 31, 2005 Compared to Year Ended December 31, 2004

Net sales increased by $318,757 or 22.4% to $1,739,394 for the year ended December 31, 2005 from $1,420,637 for the year ended December 31, 2004. The increase was due to an increase in revenues from annual support and upgrade assurances and an increase in sales of the Company's products.

Research and development expenses increased by $81,182 or 19% to $ 502,979 for the year ended December 31, 2005 from $421,797 for the year ended December 31, 2004. The increase was due to an increase in salaries related to research and development.

Selling expenses increased by $43,447 or 6% to $796,039 for the year ended December 31, 2005 from $752,592 for the year ended December 31, 2004. The increases resulted from an increase in sales salaries, partially offset by a decrease in travel expenses.

General and administrative expenses increased by $75,374 or 14% to $600,839 for the year ended December 31, 2005 from $525,465 for the year ended December 31, 2004. The increase was due to an increase in professional fees and moving expense to relocate the Company's offices.

Other income (expense) decreased by $44,331 to $(23,064) for the year ended December 31, 2005 from income of $21,267 for the year ended December 31, 2004. The decrease was primarily due to an increase in interest expense resulting from loans payable to a group of investors.

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There was no current provision for income taxes in 2005 or 2004 as the Company had losses in both years and the Company has provided a full valuation allowance for net deferred tax assets.

Net loss decreased by $74,423 to $(183,527) for the year ended December 31, 2005 from $(257,950) for the year ended December 31, 2004. The decrease was primarily due to an increase in sales, offset by an increase in salaries professional fees, and an increase in other expenses.

LIQUIDITY AND CAPITAL RESOURCES

For the year ended December 31, 2005, the Company's net loss was $183,527. For the year ended December 31, 2004, the Company's operations resulted in a net loss of $(257,950). The Company reported an operating loss of approximately $160,463 during fiscal year 2005. As of December 31, 2005 and 2004, the Company had an accumulated deficit of $20,946,008 and $20,762,481, respectively. Net cash (used for) provided by operating activities was $(130,028) and $46,990 for the years ended December 31, 2005 and December 31, 2004, respectively. As of December 31, 2005, the Company had a working capital deficit of $(601,781), with $626,388 in current assets and $1,228,169 in current liabilities. As of December 31, 2004, the Company had a working capital deficit of $(454,674), with $535,562 in current assets and $990,236 in current liabilities.

Presently, the Company funds working capital from revenues it receives from the sale of its products. Over the preceding five fiscal years, the Company received an aggregate of approximately $1,500,000 from the sale of its tax losses, but does not anticipate any additional proceeds from such sales in the future. As of December 31, 2005, the Company had aggregate liabilities approximately $2.1 million. Such amount of aggregate liabilities includes approximately (i) $400,000 in annual support contracts, which are recorded as deferred revenue, a non-cash item, for accounting purposes and reclassified, on a pro rata basis to sales as such contracts expire and income is earned, (ii) $435,000 in accounts payable and accrued expenses, and (iii) $380,000 in notes and loans payable of which $130,000 was issued more than six years ago. Such liabilities also include accrued compensation-related party, which relates to deferred compensation of approximately $868,000 payable to Mr. Weiss. Mr. Weiss has entered into a written agreement with the Company in which he agreed not to demand payment of his deferred compensation until subsequent to April 1, 2007.

At December 31, 2005, the Company had net Federal operating loss carry forwards ("NOL") of approximately $20,000,000 for financial reporting purposes, which are due to expire from 2007 through 2025. Due to losses sustained by the Company for both financial and tax reporting through 2005, management was unable to determine that realization of the tax asset related to the NOL was more likely than not and, thus, has provided a valuation allowance of $6,197,500 against the potential tax deferred tax asset of $6,197,500. The Company's NOL that would be available to offset future income may be subject to annual limitations. However, due to a provision under the laws of the State of New Jersey, the Company realized $623,135, $ 351,335, $223,000, $191,000 and $127,000 in 1999, 2000, 2001, 2002 and 2003, respectively, from the sale of its New Jersey net operating losses and research tax credits. As noted above, no additional proceeds are anticipated from such sales in the future.

For 2006, the Company anticipates that it will need approximately $1,800,000 in order to fund its operations. The Company's management believes that the Company will be able to meet its anticipated cash requirements through the end of 2006 through a combination of cash from the sale of its products, cost reduction initiatives to be implemented as necessary (which initiatives the Company expects would be primarily related to the Company's sales and marketing activities), and cash on hand.

The Company's ability to fund its operations is subject to broader acceptance of its product lines, its ability to continue to realize revenues from its largest customers, product performance, competitive forces, sales efforts of resellers, the absence of unanticipated expenses and other factors identified herein. There can be no assurance that the Company will generate enough cash from the sale of its products, or that the Company will be successful in implementing any cost reduction initiatives that may be undertaken, to meet its anticipated cash requirements for the next 12 months. If the Company does not generate enough cash to meet its requirements for the next 12 months, the Company will not have sufficient working capital to satisfy its liabilities, develop new products or implement its marketing and sales initiatives, which may result in a loss of sales and would have a material adverse effect on the Company.

See "Business-Capital Raising Initiatives" for a description of certain capital raised by the Company during 2005. As described in greater detail therein, on March 30, 2005 and April 8, 2005, the Company received funds from a group of accredited investors in the net amounts of $100,000 and $57,500, respectively, in connection with an investment in the Company in the aggregate principal amount of $250,000. Under the terms of the negotiated transaction, definitive documentation for which was never received, the amount invested would have been treated as a loan becoming due in 2007 on the second anniversaries of such dates and secured by a lien on the Company's assets. If the Company does not repay this amount in 2007 and if the investors were determined to have an enforceable loan and an enforceable security interest in the Company's assets, the investors could foreclose upon the Company's assets and apply the proceeds from the sale of such assets to the repayment of such amount. Any such foreclosure or other disposition of the Company's assets would have a material adverse effect on the Company.

Statement Regarding Critical Accounting Policies

The financial statements of the Company are prepared in accordance with accounting principles generally accepted in the United States of America that require the Company to make estimates and assumptions. The Securities and Exchange Commission ("SEC") has recently issued disclosure guidance for "critical accounting policies." The SEC defines critical accounting policies as those that require application of management's most difficult, subjective or complex judgments that are inherently uncertain and may change in subsequent periods.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Notwithstanding the foregoing, the Company believes that the Company's operations are of such a nature that management is not required to make estimates and assumptions about highly uncertain matters such that differences in such estimates would have a material impact on the presentation of the Company's financial statements. Accordingly, the Company believes that none of its significant accounting policies (see Note 2 in the Notes to the Financial Statements) require additional disclosure as being "critical accounting policies."

ITEM 7. Financial Statements.

The Financial Statements can be found following Part III of this Report.

ITEM 8. Changes In And Disagreements With Accountants On Accounting And Financial Disclosure.

None

ITEM 8A CONTROLS AND PROCEDURES.

Disclosure Controls and Procedures

The Chief Executive Officer/Principal Financial Officer of the Company has concluded, based on his evaluation as of the end of the fiscal period covered by this Report, that the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in the reports filed or submitted by it under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and include controls and procedures designed to ensure that information required to be disclosed by the Company in such reports is accumulated and communicated to the Company's management, including the Chief Executive Officer/Principal Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Internal Control over Financial Reporting.

During the year ended December 31, 2005, there has been no change in the Company's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

ITEM 8B. OTHER INFORMATION

None.

PART III

ITEM 9. Directors and Executive Officers of the Registrant

Executive Officers and Directors

The directors and executive officers of the Company are as follows:

Name	Age	Position
William Weiss	62	Chief Executive Officer; Treasurer; Director
D. Michael Bridges	51	President, Director
Michael Suleski	45	Vice President, Engineering; Secretary; Director

WILLIAM WEISS, a founder of the Company, has been Chief Executive Officer and a director of the Company since its formation in October 1991. From January 1980 until March 31, 2003 Mr. Weiss had also been an executive officer and President of Medical Registry Services, Inc., a computer software company which sells and services a computerized system for cancer record keeping in hospitals. Mr. Weiss devotes approximately 40 hours per week to the Company. Mr. Weiss received a B.S. from the Wharton School of the University of Pennsylvania and a J.D. from New York Law School.

D. MICHAEL BRIDGES, President, rejoined the Company in March, 2000 after providing consulting services to the Company from August 1998 to March 2000. He has been a director of the Company since March 2000. Mr. Bridges served as the Company's Vice President of Marketing & Sales and Director of Corporate Services from February 1995 to August 1998. Mr. Bridges received a B.S. from Rowan University and served as a Captain in the United States Marine Corps.

MICHAEL SULESKI, a founder of the Company, has been Vice President, Engineering of the Company since August 1992, and its Director of Research and Development from its inception in October 1991 to August 1992. He has been a director of the Company since May 1995, and Secretary of the Company since July 1995. He received a B.S. and a M.S. degree from Fairleigh Dickenson University College of Science and Engineering.

The Company's directors were elected at the last annual meeting of stockholders and hold office until the next annual meeting of the stockholders or until their successors are elected and qualified. Directors are not currently compensated or reimbursed for expenses incurred by them in connection with their services as directors, except for travel to Board of Directors meetings.

The Company does not have any independent directors and therefore does not have an audit committee. The full Board of Directors is performing the functions of the audit committee.

There are no family relationships among any of the directors or officers.

The Company's officers are chosen by the Board of Directors and serve at the pleasure of the Board. The loss of the services of any one of William Weiss, D. Michael Bridges or Michael Suleski could have a material adverse effect on the Company.

Board of Advisors

In January 2004, the Company formed an Advisory Board consisting of distinguished professionals and entrepreneurs who will provide guidance and advice to the Company and serve as a sounding board for the management team. The Advisory Board members will share experiences with colleagues and voice opinions on the technologies transforming electronic document management and its end communications. The Company believes that the input of its Board of Advisors will influence the development of new products and improve existing technologies. During 2004, the Company revamped its Advisory Board to reflect the direction that the Company was taking in focusing on the mortgage and life insurance industries. To that end the Company replaced the three members of the advisory board with two others. See "2004 Stock Incentive Plan" below for a description of stock options available for issuance to members of the Advisory Board. The current Advisory Board members are as follows:

A.W. Pickel, III, CMC, president of Leader Mortgage Company, is the former president of the National Association of Mortgage Brokers. Leader Mortgage Company ("Leader"), is based in Lenexa, Kansas, with a branch office in St. Louis, Missouri. Leader has been in business since 1992, primarily in the Midwest. A.W. Pickel, III as a mortgage brokerage, founded Leader. Over time Leader has grown and evolved into a regional mortgage banker. Leader offers in-house processing, underwriting and closing. Leader is a full service mortgage lender, approved to provide conventional as well as government loans.

Mr. Nachmany is the Chief Operating Officer of International Object Technology (IOT). Prior to joining International Object Technology Mr. Nachmany was the President and CEO of bCompliant, Inc., a company he established in order to conduct the collection, review, validation, and approval of electronic and paper transaction documents for the mortgage industry in an efficient and convenient fashion regardless of the number of participants and their geographic dispersion. From 1990 to 1997, Mr. Nachmany was the President and CEO of Image Integration Corp. From 1985-1990, Mr. Nachmany acted as the CEO of Image Communication Systems, a company which was responsible for the development and support of a joint venture between McDonnell Douglas Computer Systems Company and the Bell & Howell Company, in the Computer Aided Retrieval (CAR) market for the banking industry.

Limitation of Liability and Indemnification Matters

Insofar as indemnification for liabilities arising under the Securities Act of 1933, as amended, may be permitted to directors, officers, or persons controlling the Company pursuant to the foregoing provisions, the Company has been informed that in the opinion of the Securities and Exchange Commission such indemnification is against public policy as expressed in the Act and is therefore unenforceable.

Audit Committee Financial Expert

The Board of Directors has determined that William Weiss, the Company's Chief Executive Officer, is the Board's "audit committee financial expert" within the meaning of Item 401(e)(2) of Regulation S-B. The Company does not have any independent directors and therefore does not have an audit committee. The full Board of Directors is performing the functions of the audit committee.

Compliance with Section 16

Section 16(a) of the Exchange Act requires certain persons, including the Company's directors and executive officers, and beneficial owners of more than 10% of the Company's equity securities, to file reports with the Securities and Exchange Commission regarding beneficial ownership of equity securities of the Company. Based on material provided to the Company by such directors, officers and beneficial owners of more than 10% of the Company's equity securities, the Company believes that during the fiscal year ended December 31, 2005, there was compliance with all such filing requirements.

Code of Ethics

The Company has adopted a code of ethics (the "Code") that applies to our directors, officers and employees. The Code is designed to deter wrongdoing on the part of such persons and to promote: (1) honest and ethical business conduct, including the ethical handling of actual or apparent conflicts of interest between personal and provisional relationships, (2) full, fair, accurate, timely and understandable disclosure in reports and documents that we file with, or submit to the SEC and in other public communications made by us, (3) compliance with applicable governmental laws, rules and regulations, (4) the prompt internal reporting of violations of the Code to an appropriate person or persons identified in the Code, and (5) accountability for adherence to the

Code. The Code is designed to foster the highest standards of ethics and conduct in all of our business relationships. The Code will be available on the Company's website, www.paperclip.com, and copies will be mailed upon written request to Secretary, 1 University Plaza, Hackensack, NJ 07601 or by calling (201) 525-1221. The Company intends to disclose any amendments to or waivers of the Code on behalf of its Chief Executive Officer, Chief Financial Officer, and persons performing similar functions on the Company's website, at www.paperclip.com, promptly following the date of such amendment or waiver. To date, there are no such amendments.

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ITEM 10. Executive Compensation.

The Summary Compensation Table below sets forth compensation paid by the Company for the last three fiscal years ended December 31, 2005 for all services in all capacities for its Chief Executive Officer and each of its principal executive officers whose total annual salary and bonus exceeded $100,000. The Board determines the compensation of the Company's executive officers, none of whom received increases in their salaries, or a bonus, in 2005.

Summary Compensation Table

		Annual Compensation			Long Term Compensation	
Name and Other Position Compensation	Year	Salary ($)	Bonus ($)	Other Annual Compensation	Restricted Stock Awards ($)	Securities Underlying Options/SARs (#
William Weiss	2005	120,000	0	0	0	0
	2004	120,000	0	0	0	0
CEO (1)(2)	2003	120,000	0	0	0	0
Michael Suleski	2005	105,000	0	0	0	0
	2004	105,000	0	0	0	0
Vice President Engineering (1)	2003	105,000	0	0	0	0
D Michael Bridges	2005	107,800	0	0	0	0
	2004	107,800	0	0	0	0
President	2003	107,800	0	0	0	0

(1) The Company presently has no employment contract with William Weiss or Michael Suleski.

(2)As of December 31, 2005, approximately $868,000 is owed to William Weiss for past salaries accrued but not paid.

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Option/SAR Grants

During the fiscal year ended December 31, 2005, there were no options granted to either the Company's Chief Executive Officer or any of its principal officers.

The table below indicates that no options/SARs were exercised during fiscal year 2005 by the Company's Chief Executive Officer and each of its principal executive officers and shows the value of their unexercised options/SARs.

AGGREGATED OPTION/SAR EXERCISES IN FISCAL YEAR 2005
AND OPTION/SAR VALUES AT DECEMBER 31, 2005

Name	Shares Acquired On Exercise (#)	Value Realized ($)	Number of Securities Underlying Unexercised Options/SARs at FY-end Exercisable/ Unexercisable (#) (1)	Val I O S F E U
William Weiss	0	0	770,921/0	
D. Michael Bridges	0	0	405,000/0	
Michael Suleski	0	0	744,921/0	

(1) The Company does not have a stock appreciation rights ("SAR") plan and does not have any SARs outstanding.

The Company presently has no employment contracts with William Weiss or Michael Suleski. The Company does not have any pension, profit sharing, or bonus plan, other than a 2004 Stock Incentive Plan for consultants and members of the Board of Advisors, which is described below.

The Company entered into an Employment Agreement with David Michael Bridges effective as of January 1, 2000 (the "Employment Agreement"). The Employment Agreement provides that Mr. Bridges will serve as the Company's President and as a member of the Company's Board of Directors, subject to stockholder vote, for a term of three years, subject to automatic one year extensions and early termination, at an initial base salary of $107,800. The Employment Agreement provides that Mr. Bridges shall not compete with the Company in the product lines under development by the Company or use or disclose any trade secrets of the Company during the term of the Employment Agreement. In addition, the Employment Agreement provides that Mr. Bridges shall not solicit employees of the Company or induce any employee to terminate his or her relationship with the Company during the term and for a period of 24 months after termination of the

Employment Agreement unless the Company terminates Mr. Bridges without cause (as defined in the Employment Agreement), the Company fails to satisfy certain conditions or if William Weiss or Michael Suleski shall leave the employment of the Company other than by reason of death or disability. Mr. Bridges may not be terminated prior to the end of the term except with cause (as defined in the Employment Agreement) and Mr. Bridges may terminate the Employment Agreement prior to the end of the term by giving the Company at least 90 days written notice. In the event that there is a transfer of control, defined as 50%, of the Company within 6 months of the termination of Mr. Bridges, Mr. Bridges shall be entitled to his base salary, vacation and other benefits for the remainder of the term of the Employment Agreement and any difference in value of the Company's capital stock owned by Mr. Bridges at the time of his termination and the value of such stock after transfer of control as valued in accordance with the terms of the Employment Agreement. The Employment Agreement also provided for the grant of options to purchase 400,000 shares of the Company's common stock. Mr. Bridges is also entitled to indemnification to the fullest extent permitted under New Jersey law. In the event that Mr. Bridges' employment is terminated without cause prior to the end of the term or any extension of the term or because of a disability (as defined in the Employment Agreement), he is entitled to receive his base salary for 6 months, at his then current annual rate paid in a lump sum within 10 days of termination, plus a payment for unused vacation. The Employment Agreement also provides that Mr. Bridges may independently develop intellectual property outside of his regular hours of employment with the Company and maintain full ownership of such intellectual property but provides for the Company's use of certain intellectual property owned by Mr. Bridges. The Employment Agreement restricts Mr. Bridges from using certain intellectual property owned by him to compete with the Company during the term of the Employment Agreement.

2004 Stock Incentive Plan

In February 2004, the Board of Directors of the Company adopted a stock incentive plan (the "2004 Stock Incentive Plan"). Only consultants and members of the Board of Advisors are eligible to participate in this plan. The 2004 Stock Incentive Plan provides that the aggregate number of shares of common stock for which options may be granted thereunder is 600,000 shares. The 2004 Stock Incentive Plan provides that it shall be administered by a committee (the "Committee") consisting of either the full Board of Directors or a committee consisting of at least two directors.

The Committee has the full power and authority, subject to the provisions of the 2004 Stock Incentive Plan, to designate participants, grant options and determine the terms of all options. The terms of specific options granted under the 2004 Stock Incentive Plan are determined by the Committee. The term of each option is also determined by the Committee, but no option may be exercisable after ten years have elapsed from the date upon which the option is granted. As of December 31, 2005, 100,000 options under the 2004 Stock Incentive Plan were outstanding.

1993 Stock Option Plan

In March 1993, the Company adopted its 1993 Stock Option Plan (the "1993 Stock Plan") covering 68,912 shares of Common Stock, pursuant to which employees (other than directors) of the Company were eligible to receive stock options. The 1993 Stock Plan expired on February 1, 2003, and all the outstanding options expired in 2005.

1995 Stock Option Plan

In May 1995, the Company adopted a stock option plan (the "1995 Stock Plan"), pursuant to which officers, directors and employees of the Company and certain other persons conferring benefit upon the Company were eligible to receive stock options. The 1995 Stock Plan terminated on March 1, 2005. All options thereunder outstanding at the time of such termination shall continue in full force and effect according to the terms of the option agreements governing such options. As of December 31, 2005, options to acquire 3,969,222 shares of Common Stock had been granted under the 1995 Stock Plan. At such date, 892,872 options had expired, 95,508 options had been exercised and 2,980,842 options were outstanding.

Long-Term Incentive Plan

The Company did not grant any awards to executive officers under any long-term incentive plan during fiscal year 2005.

Compensation of Directors

Directors are not currently compensated or reimbursed for expenses incurred by them in connection with their services as directors, except for travel to Board of Directors meetings.

ITEM 11. Security Ownership of Certain Beneficial Owners and Management And Related Stockholder Matters.

The following table sets forth, as of March 21, 2006, the number of shares of Common Stock and Series A Preferred Stock beneficially owned by each director, by the directors and executive officers of the Company as a group and by each holder of at least five percent of Common Stock or the Series A Preferred Stock, as the case may be, known to the Company and the respective percentage ownership of the outstanding Common Stock and Series A Preferred Stock held by each such holder and group:

	Common shares		Series Preferred A shar	
Name and Address of Beneficial Owner	Number of Shares (1)	Percentage of Class	Number of Shares	Percenta of Clas
William Weiss (2) PaperClip Software, Inc. 1 University Plaza Hackensack , New Jersey 07601	3,569,643(3)	31.04%	2,533,869	69.4%
Michael Suleski (2) PaperClip Software, Inc. 1 University Plaza Hackensack , New Jersey 07601	780,936(4)	8.73%		
D. Michael Bridges PaperClip Software, Inc. 1 University Plaza Hackensack , New Jersey 07601	556,500(5)	6.38%	150,000	4.1%

All Officers and Directors as a group (3 persons)	4,911,079	38.35%	2,683,869	73.5%

(1) Unless otherwise indicated below, all shares are owned beneficially and of record.

(2) William Weiss and Michael Suleski are founders of the Company.

(3) Includes (a) 770,921 shares of Common Stock issuable upon the exercise of options currently exercisable under the 1995 Stock Option Plan, and (b) 2,533,869 shares of Common Stock issuable upon the conversion of 2,533,869 shares of Series A Preferred Stock.

(4) Includes 744,921 shares of Common Stock issuable upon the exercise of options currently exercisable under the 1995 Stock Option Plan.

(5) Includes 405,000 shares of Common Stock issuable upon the exercise of options currently exercisable under the 1995 Stock Option Plan, and 150,000 shares of Common Stock issuable upon the conversion of 150,000 shares of Series A Preferred Stock.

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EQUITY COMPENSATION PLAN INFORMATION

The following table provides information, as of December 31, 2005, about the Company's 1995 Stock Option Plan and 2004 Stock Incentive Plan, the material features of which are described in this report under "Item 10-Executive Compensation." Although the 1995 Stock Option Plan expired on March 1, 2005, the options with unexercised terms remain outstanding under such plan and are included in the table below.

All outstanding awards relate to the Company's common stock.

	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 remaining availa issuance under plans (exclu reflec
Equity compensation plans approved by security holders	2,980,842(1)	.31	
Equity compensation plans not approved by security holders	100,000 (3)		
Total	3,080,842		

(1) Represents 2,980,842 shares of Common Stock issuable upon the exercise of outstanding options previously granted under the 1995 Stock Option Plan

(2) The 1995 Stock Option Plan expired on March 1, 2005.

(3) Represents 100,000 shares of Common Stock issuable upon the exercise of outstanding options granted under the 2004 Stock Incentive Plan.

(4) Represents 500,000 shares of Common Stock available for future issuance under the 2004 Stock Incentive Plan.

ITEM 12 CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS.

Mr. Weiss receives compensation of $10,000 per month as part of an oral employment arrangement. However, in lieu of receiving current compensation payments, Mr. Weiss has agreed to the deferred payment of such compensation. During 2002 and for the first three months ended March 31, 2003, Mr. Weiss has assigned payment of the compensation to another company he is affiliated with. At December 31, 2005, the Company had accrued $867,749 in deferred compensation to Mr. Weiss, or his affiliated company which is recorded as long term accrued compensation- related party on the balance sheet. Mr. Weiss has entered into a written agreement with the Company in which he agreed not to demand payment of his deferred compensation until subsequent to April 1, 2007.

Item 13. Exhibits .

(a) Exhibits:

3.1 Certificate of Incorporation of Registrant, as amended.(1)
3.1(a) Certificate of Amendment to Certificate of Incorporation.(3)
3.1(b) Series A Preferred Stock Certificate of Designations.(3)
3.2 By-Laws of Registrant, as amended. (1)
3.3 Registrant's Authorization to do Business in New Jersey. (1)
3.5 Form of Common Stock Certificate. (1)
10.2 1995 Stock Option Plan, as amended (2)
10.3 2004 Stock Incentive Plan (5)
10.4 Form of End User License. (1)
10.5 (a) Reschedule Agreement with NCC Export Systems 1995 LTD ("NCC"), dated as of October 21, 1996 (incorporated by reference from Exhibit 10 of the Registrant's Form 10-QSB for the quarter ended September 30, 1996), (b) Receipt of full payment and termination of the Reschedule Agreement from NCC, dated January 29 , 1997.(2)
10.6 License Agreement with Cheyenne Software, Inc., dated November 10, 1995 (incorporated by reference from Exhibit 10.12(c) of the Registrant's Form 10-KSB for the fiscal year ended December 31, 1995)
10.11 Employment Agreement dated as of January 1, 2000 between Paperclip Software, Inc. and D. Michael Bridges. (3)

10.13 Agreement, dated December 31, 2005 , by and between PaperClip Software, Inc. and William Weiss

14. Code of Ethics (5)

23.1 Consent of Sobel & Co., LLC
31.1 Certification Pursuant to Rule 13a-14(a) Promulgated under the Securities Exchange Act of 1934.
32.1 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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(1) Incorporated by reference from the Registrant's Registration Statement on Form SB-2 (File No. 33-92768NY).
(2) Incorporated by reference from the Registrant's Form 10-KSB for the fiscal year ended December 31, 1997 (File No. 000-26598).
(3) Incorporated by reference from the Registrant's Form 10-KSB for the Fiscal year December 31, 2000 (File No. 000-26598)
(4) Incorporated by reference from the Registrant's Form 10-KSB for the Fiscal year December 31, 2002 (File No. 000-26598)
(5) Incorporated by reference from the Registrant's Form 10-KSB for the Fiscal year December 31, 2004 (File No. 000-26598)

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ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

Sobel & Co., LLC ("Sobel") was the Company's principal accountant for the fiscal years ended December 31, 2005 and 2004.

The following is a summary of the fees billed to the Company by Sobel for professional services rendered for the fiscal years ended December 31, 2005 and December 31, 2004:

Fee Category	Fiscal 2005 Fees	Percentage of 2005 Fees Approved by the Board	Fiscal 2004 Fees	Percentage of 2004 Fees Approved by the Board
Audit Fees	$30,734	100%	$27,600	100%
Audit-Related Fees	5,780		-	
Tax Fees	-		-	
All Other Fees	-		-	
Total Fees	$36,514		$27,600	

Audit Fees. Consists of fees billed for professional services rendered for the audit of the Company's annual financial statements and review of the interim financial statements included in the Company's quarterly reports on Form 10-QSB and related services.

Audit-Related Fees. Consists of fees billed for assurance and related services that are reasonably related to the performance of the audit or review of the Company's financial statements and are not reported under "Audit Fees."

The audit-related fees of $5,780 relate to professional services rendered in conjunction with research, assistance and discussions in assisting the Company preparing responses to SEC letters.

Tax Fees. Consists of fees billed for professional services for tax compliance, tax advice and tax planning.

All Other Fees. Consists of fees for services other than the services reported above.

The Company does not have any independent directors and therefore does not have an audit committee. The full Board of Directors is performing the functions of the audit committee. The Board of Director's policy is to pre-approve all audit and permissible non-audit services provided by the independent auditors. These services may include audit services, audit-related services, tax services and other services. Pre-approval is generally provided for up to one year and any pre-approval is detailed as to the particular service or category of services and is generally subject to a specific budget. The independent auditors and management are required to periodically report to the Board of Directors regarding the extent of services provided by the independent auditors in accordance with this pre-approval, and the fees for the services performed to date. The Board of Directors may also pre-approve particular services on a case-by-case basis. As illustrated in the table set forth above, the Board of Directors pre-approved each audit and non-audit service rendered to the Company by its independent Auditors and no services were approved using the de minimus exception afforded by Rule 2-01(c)(7)(i)(C) of Regulation S-X.

SIGNATURES

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

PAPERCLIP SOFTWARE, INC.

By: /s/ William Weiss
William Weiss, Chief Executive Officer

Date: March 30, 2006

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

Signature	Title	Date
/s/ William Weiss William Weiss	Director and Chief Executive Officer (Principal Executive, Financial and Accounting Officer)	March 30, 2006
/s/ D. Michael Bridges D. Michael Bridges	Director, President	March 30, 2006
/s/ Michael Suleski Michael Suleski	Director, Vice President, Engineering and Secretary	March 30, 2006

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PAPERCLIP SOFTWARE, INC.

FINANCIAL STATEMENTS

DECEMBER 31, 2005 AND 2004

PAPERCLIP SOFTWARE, INC.

DECEMBER 31, 2005 AND 2004

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Report of Independent Registered Public Accounting Firm

To the Board of Directors
PaperClip Software, Inc.

We have audited the accompanying balance sheet of PaperClip Software, Inc. (a Delaware corporation) (the "Company") as of December 31, 2005 , and the related statements of operations, change in stockholders' deficiency, and cash flows for each of the years ended December 31, 2005 and 2004. 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 is not required to have, nor were we engaged to perform, an audit of its internal control 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, 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 PaperClip Software, Inc. as of December 31, 2005, and the results of its operations and its cash flows for the years ended December 31, 2005 and 2004, in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 3 to the financial statements, the Company has a significant loss from operations; current liabilities exceed current assets by approximately $202,000 (after adjusting for approximately $400,000 of deferred revenues, a non-cash item); deficiencies in working capital and net worth. These factors raise substantial doubt about the Company's ability to continue as a going concern. Management's plans regarding those matters are also described in Note 3. These financial statements do not include any adjustments that might result from the outcome of this uncertainty.

/s/ Sobel & Co., LLC
Certified Public Accountants

March 13, 2006
Livingston, New Jersey

PAPERCLIP SOFTWARE, INC.
BALANCE SHEET

		DECEMBER 31, 2005
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$	384,539
Accounts receivable (net of allowance for doubtful accounts of $89,000)		200,053
Other current assets		41,796
Total Current Assets		626,388
EQUIPMENT, FURNITURE AND FIXTURES:		
Computer and office equipment		42,932
Furniture and fixtures		6,056
		48,988
Less- Accumulated depreciation		14,008
Equipment, Furniture, and Fixtures, Net		34,980
OTHER ASSETS		22,006
DEFERRED FINANCING COSTS, NET		35,314
Total assets	$	718,688
LIABILITIES AND STOCKHOLDERS' DEFICIENCY		
CURRENT LIABILITIES:		
Accounts payable and accrued expenses	$	435,278
Taxes payable		13,500
Deferred revenue		399,700
Notes payable		129,691
Loans payable		250,000
Total Current Liabilities		1,228,169
Accrued compensation- related party		867,749
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS' DEFICIENCY:		
Convertible Series A, preferred stock, authorized 10,000,000 shares; $.01 par value; 3,649,543 shares issued and outstanding		36,495
Common stock, authorized 30,000,000 shares; $.01 par value; issued and outstanding 8,196,521 shares		81,965
Additional paid-in capital		19,450,318
Accumulated deficit		(20,946,008)
Total Stockholders' Deficiency		(1,377,230)
Total liabilities and stockholders' deficiency	$	718,688

See report of independent registered public accounting firm and notes to financial statements

PAPERCLIP SOFTWARE, INC.
STATEMENTS OF OPERATIONS

	YEAR ENDED DECEMBER 31, 2005	2004
NET SALES	$ 1,739,394	$ 1,420,637
OPERATING EXPENSES:		
Research and development expenses	502,979	421,797
Selling expenses	796,039	752,592
General and administrative expenses	600,839	525,465
Total operating expenses	1,899,857	1,699,854
LOSS FROM OPERATIONS	(160,463)	(279,217)
OTHER INCOME (EXPENSE):		
Extinguishment of accounts payable	35,090	36,127
Interest expense	(59,186)	(15,600)
Interest income	1,032	740
Total other (expense) income, net	(23,064)	21,267
NET LOSS BEFORE PROVISION FOR INCOME TAXES	$ (183,527)	$ (257,950)
Provision for income taxes	0	0
NET LOSS	$ (183,527)	$ (257,950)
BASIC AND FULLY DILUTED LOSS PER COMMON SHARE	$ (0.02)	$ (0.03)
WEIGHTED AVERAGE NUMBER COMMON SHARES OUTSTANDING	8,196,521	8,196,521

See report of independent registered public accounting firm and notes to financial statements

PAPERCLIP SOFTWARE, INC.
STATEMENTS OF CHANGES IN STOCKHOLDERS' DEFICIENCY
FOR THE YEARS ENDED DECEMBER 31, 2005 AND 2004

	Preferred Stock Number of Shares	Preferred Stock Par value	Common Stock Number of Shares	Common Stock Par value	Additional Paid-In Capital	Accumulated Deficit
BALANCE, December 31, 2003	3,649,543	$36,495	8,196,521	$81,965	$19,426,318	($20,504,53
Deferred financing costs					24,000	
NET LOSS, 2004						(257,95
BALANCE, December 31, 2004	3,649,543	$36,495	8,196,521	81,965	19,450,318	(20,762,48
NET LOSS, 2005						(183,52
BALANCE, December 31, 2005	3,649,543	$36,495	8,196,521	$81,965	$19,450,318	($20,946,00

See report of independent registered public accounting firm and notes to financial statements

PAPERCLIP SOFTWARE, INC.
STATEMENTS OF CASH FLOWS

	YEAR ENDED DECEMBER 31, 2005	2004
OPERATING ACTIVITIES:		
Net loss	$ (183,527)	$ (257,950)
Adjustments to reconcile net income to net cash provided by (used for) operating activities-		
Depreciation	10,066	7,843
Extinguishment of accounts payable	(35,090)	(36,127)
Accrued interest on convertible note	15,500	15,600
Increase in accrued compensation to related party	64,038	93,592
Amortization of prepaid interest & deferred financing costs	43,686	-
Tax deferred asset	-	11,600
Change in operating assets and liabilities:		
Accounts receivable	(39,422)	107,018
Other current assets	(4,296)	-
Other assets	(8,506)	-
Accounts payable and accrued expenses	26,223	(9,836)
Taxes payable	-	(27,000)
Deferred revenue	(18,700)	142,250
Net cash (used for) provided by operating activities	(130,028)	46,990

INVESTING ACTIVITIES -- Purchases of

equipment, furniture and fixtures	(17,864)	(25,067)
FINANCING ACTIVITIES:		
Net proceeds from loans payable	157,500	-
Net cash provided by financing activities	157,500	-
Net increase in cash and cash equivalents	9,608	21,923
CASH AND CASH EQUIVALENTS		
Beginning of year	374,931	353,008
End of year	$ 384,539	$ 374,931

See report of independent registered public accounting firm and notes to financial statements

PAPERCLIP SOFTWARE, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2005 AND 2004

NOTE 1 - ORGANIZATION:

PaperClip Software, Inc. (formerly known as PaperClip Imaging Software, Inc.),located in Hackensack, NJ, (the "Company"), a Delaware corporation, incorporated in October, 1991,is engaged in the development and distribution of computer software for document management and transport of electronic document packages across the public Internet or a private Intranet with interoperability, security and tracking capabilities. The Company's systems allow users of personal computer networks to scan, file, retrieve, display, print and route documents and other software objects (such as word processing files, spreadsheets and electronic mail), while continuing to use their existing application software. The systems can be integrated with many personal computer applications with little or no programming and can file and retrieve documents without the time consuming step of manually labeling or indexing each document.

The Company sells its products worldwide to twenty three Value Added Resellers ("VAR's") and original equipment manufacturers ("OEM's") of personal computers and personal computer networks utilized on a corporate level.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Basis of Accounting:

The Company's policy is to prepare its financial statements on the accrual basis of accounting.

Revenue Recognition:

The Company generates revenues from licensing the rights to use its software products directly to distributors, resellers, original equipment manufacturers, and end users. The Company's delivery and payment arrangements do not include extended payment terms and are generally net 30 days.

Revenues from licenses are recognized upon shipment of the software if there are no significant post delivery obligations, if collection is probable and if payment is due within one year. The Company provides post contract services, which includes telephone support, software version upgrades and consulting and training services related to installation and implementation of the Company's products at no additional charge for periods not exceeding one year. The estimated cost of providing such support is not significant. Revenues from consulting services are recognized as services are performed.

In addition to the above-referenced post contract services provided at no additional charge, the Company offers additional contractual support services that are billed separately. Revenues paid by the customer prior to performance of such contractual support services are deferred and recognized over the term of the contract service agreement, usually one year. The underlying calculation for deferred services are generally not complex (i.e., deferred revenues are generally recognized as income over the course of the applicable contract on a formulaic basis).

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Reclassification:

Certain reclassifications have been made to the 2004 financial statements to conform to the 2005 financial statement presentation.

Use of Estimates:

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

Significant estimates have been made by management in the areas of the allowance for bad Debts (See Note 9)and the recognition/realization of deferred revenues. Actual results could differ materially from these estimates, making it reasonably possible that a change in these estimates could occur in the near term.

Advertising:

Advertising costs are expensed as incurred, and amounted to approximately $17,000 in 2005 and $32,000 in 2004.

Cash and Cash Equivalents:

Cash and cash equivalents consist primarily of cash at banks and highly liquid investments with original maturities of three months or less.

Accounts Receivable:

The Company carries its accounts receivable at cost less an allowance for doubtful accounts. On a periodic basis, the Company evaluates its accounts receivable and adjusts the allowance for doubtful accounts, based on a history of past write-offs and collections and current credit conditions. At December 31, 2005 and 2004, the Company believes the allowance for doubtful accounts is adequate.

Equipment, Furniture and Fixtures:

Equipment, furniture and fixtures are stated at cost, less accumulated depreciation. Depreciation expense is computed using the straight-line method over the estimated useful lives of the assets which range from five to seven years.

Accounting for Stock-Based Compensation:

The Company has elected to follow Accounting Principles Board Opinion No. 25,"Accounting for Stock Issued to Employees"(APB25). If the option price under the Stock Option plans equals or exceeds the fair market value of the common shares on the date of the grant, no compensation cost is recognized under the provisions of APB 25 for stock options. If the option price under the Stock Option Plans is less than the fair market value of the common stock on the date of grant, compensation cost is recognized for the difference.

The Company adopted only the disclosure part of Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" (SFAS 123 as amended by SFAS 123R). The adoption of this pronouncement had no impact on the Company's financial condition or results of operations for 2005 and 2004, however, additional disclosures have been included in the financial statements.

Deferred Financing Costs:

Expenditures incurred in conjunction with debt or equity capital issuances are deferred as other assets. Such costs will be offset against equity proceeds, amortized over the life of the debt, or expensed if the transaction is not completed.

Deferred Rent:

The Company recognizes rent expense on a straight line basis for financial reporting purposes. The difference between cash payments and expenses will be included in deferred rent. Deferred rent will commence January 1, 2006.

Federal Income Taxes:

The Company has adopted Statement of Financial Accounting Standards Board No. 109, "Accounting for Income Taxes" (SFAS 109), which provides for the recognition of deferred tax assets, net of an applicable valuation allowance, related to net operating loss carryforwards and certain temporary differences.

Income (Loss) Per Common Share:

Income per common share-basic is computed based upon the weighted average number of common shares and common share equivalents outstanding, if dilutive. 2005 and 2004 fully diluted loss per share does not reflect the conversion of Series A Preferred Stock or common stock equivalents as the result would be anti-dilutive.

Research and Development Costs:

The costs incurred in establishing the technological feasibility of a computer software product that is to be sold, leased or otherwise marketed by the Company is accounted for as Research & Development costs and expensed in the period incurred. The amount charged against income was $502,979 and $421,797 for the years ended December 31, 2005 and 2004, respectively.

Recent Accounting Pronouncements:

The Financial Accounting Standards Board ("FASB") has issued several new standards during 2005 and 2004. In December 2004, the FASB issued SFAS 123(R), "Share-Based Payment," which revises SFAS 123, "Accounting for Stock-Based Compensation," and supersedes APB Opinion No. 25, "Accounting for Stock Issued to Employees." SFAS 123(R) requires fair value recognition of stock option grants in the income statement as an expense and is effective for the first interim reporting period beginning after December 15, 2005. This pronouncement may have a material impact on the Company's operating results. The Company is in the process of evaluating the impact of this pronouncement on its financial statements.

NOTE 3-GOING CONCERN:

The accompanying financial statements have been prepared assuming the Company is a going concern, which assumption contemplates the realization of assets and satisfaction of liabilities in the normal course of business. The Company has suffered a loss from operations, current liabilities exceed current assets by approximately $202,000 (after adjusting for approximately $400,000 of deferred revenues, a non-cash item), and the Company lacks sufficient liquidity to continue its operations. Management's 2006 forecast indicates positive trends for sales, but it may not result in an increase in operating income, net income, and positive cash flows.

These factors raise substantial doubt about the Company's ability to continue as a going concern. The financial statements do not include any adjustments related to the recoverability and classification of recorded asset amounts or the amount of liabilities that might be necessary should the Company be unable to continue in existence.

Continuation of the Company as a going concern is dependent upon achieving profitable operations . Management's plans to achieve profitability include developing new products, obtaining new customers, increasing sales to existing customers and implementing certain cost reduction initiatives as necessary. There can be no assurance that the Company will generate enough cash from the sale of its products, or that cost reduction initiatives will be successful to meet anticipated cash requirements.

NOTE 4 - INCOME TAXES:

For tax return purposes, the Company has the following net operating loss carry forwards as of December 31, 2005 and 2004 for Federal purposes:

Federal Net Operating Loss	Year Incurred	Expiration Date
$1,474,595	December 31, 1992	December 31, 2007
$2,790,034	December 31, 1993	December 31, 2008
$2,880,756	December 31, 1994	December 31, 2009
$3,648,749	December 31, 1995	December 31, 2010
$4,660,613	December 31, 1996	December 31, 2011
$2,707,112	December 31, 1997	December 31, 2017
$ 880,373	December 31, 1998	December 31, 2018
$ 35,944	December 31, 1999	December 31, 2019
$ 633,601	December 31, 2000	December 31, 2020
$ 43,371	December 31, 2001	December 31, 2021
$ 161,000	December 31, 2004	December 31, 2024
$ 183,000	December 31, 2005	December 31, 2025

The Company also has tax credits related to research activities of approximately $400,000 for Federal purposes at December 31, 2005.

As stated in Note 13, the State of New Jersey has allowed in recent years the sale of state net operating losses and research tax credits. The Company has sold all of its net operating losses and research tax credits available through 2003. The Company has a state net operating loss carryforward for 2004 and 2005 approximately $200,000, which will expire through 2012.

The Company's total deferred tax liabilities, deferred tax assets, which are comprised principally of net operating loss carry forwards, and valuation allowance consists of the following at December 31:

	2005	2004
Total deferred tax liabilities	$ -	$ -
Total deferred tax assets	6,197,500	6,140,000
Total valuation allowance	6,197,500	6,140,000
Current deferred tax asset	$ -	$ -

A reconciliation of the statutory tax rates are as follows:

	Year Ended December 31, 2005	2004
Statutory rate	(34%)	(34%)
State income tax	(6%)	(6%)
	(40%)	(40%)
Current year valuation allowance	40%	40%
Benefit for income tax	0%	0%

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Note 5- INVESTMENT BANKING AGREEMENT AND LOAN PAYABLE:

On October 29, 2004, the Company signed an investment banking agreement with Sloan Securities Corp. ("Sloan") to raise capital for the Company. In connection with such engagement, the Company issued two-year warrants to Sloan to purchase 500,000 shares of the Company's Common Stock at an exercise price of $.10 per share. The Warrants vested as to 425,000 shares on the date of issuance and as to the remaining 75,000 shares at such time that a financing is consummated in which at least 1,400,000 shares of common stock or common stock equivalents are issued to investors introduced to the Company by Sloan. The Company recorded the 425,000 warrants on the balance sheet as deferred financing costs at a value of $24,000.

On March 31, 2005 and April 8, 2005 the Company received funds from a group of accredited investors in the amounts of $100,000 and $57,500, respectively, in anticipation of the execution of definite documentation with such investors. Documents had been fully negotiated in anticipation of a financing for gross proceeds of between $500,000 and $1,200,000. While the Company executed certain documents prior to its receipt of the funds, the documents were to be held in escrow pending a final transaction and the Company never received countersigned agreements from the investors. Under the terms of the negotiated transaction, the invested funds were to be in the form of a two year loan, secured by a lien on the Company's assets, with interest at the rate of 12% per annum prepaid for the entire period, and financing fees to Sloan in the aggregate amount equal to 13% of the gross proceeds raised. Warrants to purchase 200,000 shares and 50,000 shares were also to be issued to the investors and Sloan, respectively, for each $100,000 of the financing. One half of such warrants were to be exercisable at $0.20 per share, and the other half of such warrants were to be exercisable at $0.25 per share. In a letter agreement dated March 31, 2005, Sloan and the investors agreed that they would not enforce their registration rights related to shares of common stock issuable upon exercise of the warrants until such time as the Company has received an aggregate of $500,000 of gross proceeds through the issuance of notes. The Company has recorded a $250,000 loan payable on its December 31, 2005 balance sheet based on its understanding of the intent of the parties that such $157,000 aggregate amount represents net proceeds to the Company, after prepaid interest and financing costs, of a $250,000 loan to the Company, by such investors. The Company has also reserved 625,000 shares for issuance upon exercise of the warrants that were to be issued in connection with the $250,000 financing. The Company has been unable to obtain executed documents from the investors or Sloan or definite confirmation of their intent regarding the funds. Accordingly, there can be no assurance that the investors will not seek to treat the funding as an incomplete investment and demand return of the funds. The Company has accounted for the loan as short-term indebtedness.

NOTE 6 - CONVERTIBLE DEBT:

Notes payable, convertible into common stock at $.30 per share, 12% interest, matured December 31, 1999, and as of December 31, 2005, the notes remain in default.	$129,691

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Note 7 - EXTINGUISHMENT OF ACCOUNTS PAYABLE:

During the years ended December 31, 2005 and 2004, the Company wrote down its accounts payable by $35,090 and $36,127, respectively, relating to debts which were incurred over six years ago, for which the statute of limitations has expired and the vendors can no longer institute a claim against the Company. The write down was included in the statement of operations as an extinguishment of accounts payable.

NOTE 8 - PREFERRED STOCK:

The Company has ten million shares of preferred stock $.01 par Value authorized. The Company has designated Series A Preferred Stock, with 3,649,543 shares issued on November 2, 2000, 3,649,543 shares issued and outstanding as of December 31, 2005. Each share of Series A Preferred Stock is convertible into one share of common stock subject to adjustment and anti-dilution protection upon certain events.

NOTE 9 - COMMITMENTS AND CONTINGENCIES:

In 2004, the Company commenced a lawsuit against a customer in the Superior Court of the State of New Jersey for payment of delinquent accounts receivable approximating $50,000. The Company has set up what it believes is an adequate bad debt reserve to cover this dispute.

NOTE 10 - LEASES:

The Company leases its office space under a non-cancelable operating lease. which expires in 2011. Rent expense was approximately $56,000 and $51,000 for the years ended December 31, 2005 and 2004, respectively.

Future minimum rental payments required under this lease are as follows:

Year Ended December 31,	
2006	$40,275
2007	$48,778
2008	$49,315
2009	$49,852

2010	$50,389
2011	$ 8,413

NOTE 11 - EMPLOYMENT AGREEMENT:

The Company has an employment agreement with Michael Bridges, the Company's President who is also a member of the Board of Directors, subject to automatic one-year extensions and early terminations at a base salary of $107,800. The agreement also provides for options to purchase 400,000 shares of common stock at $0.25 per share with immediate vesting, which was subsequently granted at the fair market value of the Company's stock at the time of issuance which was $.25 per share. In addition, the agreement has specific clauses including not limited to covenants not to compete with the Company's product line, solicitation of employees of the Company upon termination and a severance package if there is a transfer of control.

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NOTE 12 - CONCENTRATION OF RISK:

The Company maintains its cash balances and certificates of deposit at one financial institution. This account is insured by the FDIC (Federal Deposit Insurance Corporation) up to $100,000. The Company routinely maintains balances in excess of $100,000 in the ordinary course of business.

NOTE 13 - MAJOR CUSTOMERS:

The Company sells its products primarily through mass distributors and approximately 23 independent VARS. The VARS sell and install these products at end user sites.

Sales to three major customers for the year ended December 31, 2005 were approximately 28%. Sales to four major customers for the year ended December 31, 2004 was approximately 42%.

Four and three customers make up 47% and 58% of accounts receivable at December 31, 2005 and 2004, respectively.

NOTE 14 - STOCK OPTIONS:

1993 Stock Option Plan

The Company adopted a stock option plan (the "1993 Stock Option Plan"), effective March 8, 1993, pursuant to which employees of the Company were eligible to receive incentive stock options. The 1993 Stock Option Plan expired on February 1, 2003, and all outstanding options thereunder expired in 2005. Stock option transactions for the 1993 Stock Option Plan are summarized as follows:

	Year Ended December 31,			
	2005	Exercise Price	2004	Exercise Price
Outstanding, beginning of year	20,183	$2.60	20,183	$2.60
Granted	-	-	-	-
Exercised	-	-	-	-
Cancelled, settled or expired	20,183	$2.60	-	-
Outstanding, end of year	-	-	20,183	$2.60

1995 Stock Option Plan -

In May 1995, the Company adopted a stock option plan (the "1995 Stock Option Plan"), pursuant to which officers, directors and employees of the Company and certain other persons conferring benefit upon the Company were eligible to receive stock options. The 1995 Stock Option Plan expired on March 1, 2005. All options thereunder outstanding at the time of such termination shall continue in full force and effect according to the terms of the option agreements governing such options.

Stock option transactions for the 1995 Stock Option Plan are summarized as follows:

	Year Ended December 31, 2005	Exercise Price	2004	Exercise Price
Outstanding, beginning of year	3,183,842	$.06-2.50	3,133,842	$.06-2.50
Granted	-	-	150,000	$.05-$.07
Exercised	-	-	-	-
Cancelled or expired	(203,000)	$.05-2.50	(100,000)	$.25
Outstanding, end of year	2,980,842	$.05-2.50	3,183,842	$.06-2.50

In February 2004, the Board of Directors of the Company adopted a stock incentive plan(the "2004 Stock Incentive Plan"). Only consultants and members of the Board of Advisors are eligible to participate in this plan. The 2004 Stock Incentive Plan provides that the aggregate number of shares of common stock for which options may be granted thereunder is 600,000 shares. In 2004, the Board awarded options for an aggregate of 525,000 shares to the members of the Board of Advisors under the 2004 Stock Incentive Plan at an exercise price of $.07 to $.10 per share, the market price of the Common Stock on the date of grant. Such options are not included in the tables above.

Stock option transactions for the 2004 Stock Incentive Option Plan are summarized as follows:

	Year Ended December 31, 2005	Exercise Price	2004	Exercise Price
Outstanding, beginning of year	175,000	$.07-$.10		
Granted	-		525,000	$.07-$.10
Exercised	-	-	-	-
Cancelled,repurchased or expired	(75,000)	$.07-$.10	(350,000)	$.07
Outstanding, end of year	100,000	$.07	175,000	$.07-$.10

SFAS 123 disclosure:

During the year ended December 31, 2004, the Board of Directors authorized the issuance of options to purchase 675,000 shares at an average exercise price of $.06 per share. The Board did not authorize the granting of any options in 2005. The fair value of each option grant was estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions used for grants: expected volatility of 175% and 190% for 2005 and 2004, respectively; risk-free interest rate of 4.5% and 4% for 2005 and 2004, respectively; and expected lives of 10 years.

Had compensation cost for the Company's stock option plan been recognized based on the fair value at the grant date for awards consistent with the provisions of SFAS No. 123, as amended by SFAS No. 123R, the Company's net income and income per share for the year ended December 31, 2005 and 2004 would have been as follows:

	2005	2004
Net loss as reported	$(183,527)	$(257,950)
Required adjustment to loss	(6,300)	(10,500)
Net loss pro forma	$(189,827)	$(268,450)

	Basic	Fully diluted
Loss per common share - as reported 2005	$(.02)	$(.02)
Loss per common share - pro forma 2005	$(.02)	$(.02)
Loss per common share - as reported 2004	$(.03)	$(.03)
Loss per common share - pro forma 2004	$(.03)	$(.03)

NOTE 15 - RELATED PARTY TRANSACTIONS:

Mr. William Weiss, ("Weiss"), Chief Executive Officer and Treasurer of the Company, receives compensation of $10,000 per month as part of an oral employment arrangement. In lieu of receiving current compensation payments, Mr. Weiss has agreed to the deferred payment of such compensation. During 2002 and for the first three months ended March 31, 2003, Mr. Weiss has assigned payment of the compensation to another company he is affiliated with. At December 31, 2005, the Company has accrued $867,749 in deferred compensation to Mr. Weiss, which is recorded as accrued compensation - related party on the balance sheet. Mr. Weiss has entered into a written agreement with the Company in which he agreed not to demand payment of his deferred compensation until subsequent to April 1, 2007.

NOTE 16 - ROYALTIES:

During 2005 and 2004, the Company had licensing agreements with five vendors to distribute various software products. The agreements require royalty payments to vendors based on sales volume. At December 31, 2005, all amounts outstanding in regards to these agreements have been included in the accompanying financial statements. For the years ended December 31, 2005 and 2004, the Company paid royalties of $8,535 and $11,752, respectively. As of December 31, 2005, the Company's accrued royalties of approximately $49,000, which is included as accrued expenses on the balance sheet.

NOTE 17 - EXPORT SALES:

Export sales were approximately 1% and 2% of the Company's net sales for the years ended December 2005 and 2004, respectively. The foreign countries that the Company primarily deals with are Italy, Nigeria and various other countries.

NOTE 18 - SUPPLEMENTAL DISCLOSURE OF CASH FLOWS INFORMATION:

	2005	2004
Cash paid for interest	$ -	$ -
Cash paid for state income taxes	$ -	$ -
Non cash financing activity- Prepaid interest and deferred costs	$92,500	$ -
Non cash issuance of warrants for services	$ -	$24,000

Note 19 - Fair Value of Financial Instruments:

SFAS No.107" Disclosure About the Fair Value of Financial Instruments", requires disclosure of fair value information about financial instruments. The carrying amounts reported in the balance sheet for cash, accounts receivable, accounts payable and accrued expenses approximate fair value because of their short term nature. The carrying amounts of notes payable and long term debt approximates fair value because those financial instruments bear interest at rates that approximate current market rates for loans with similar maturities and credit quality. None of these financial instruments are held for trading purposes.

Exhibit 10.12

Agreement, dated December 31, 2005, by and between
PaperClip Software, Inc. and William Weiss

WILLIAM WEISS

December 31, 2005

PaperClip Software, Inc.
1 University Plaza
Hackensack , New Jersey 07601

Reference is hereby made to the $867,749 in "accrued compensation-related party" recorded on the balance sheet appearing in the Annual Report on Form 10-KSB of PaperClip Software, Inc. for the year ended December 31, 2005. Such payables relate to deferred compensation for services previously performed by William Weiss ("Weiss") as an officer of the Company pursuant to an oral employment arrangement and are payable to Weiss and/or his affiliated company. Weiss hereby agrees that neither Weiss nor such affiliated company shall demand payment of such payables prior to April 1, 2007.

Sincerely,

/s/ William Weiss
William Weiss

Exhibit 23.1

CONSENT OF INDEPENDENT REGISITERED PUBLIC ACCOUNTING FIRM

We consent to the incorporation by reference in the Registration Statement on Form S-8 (Registration No. 333-04245) of our report dated March 13, 2006, with respect to the financial statements of PaperClip Software, Inc. included in the Annual Report on Form 10-KSB of PaperClip Software, Inc. for the year ended December 31, 2005.

/s/ Sobel & Co., LLC
Certified Public Accountants

March 13, 2006
Livingston, New Jersey

Exhibit 31.1 CERTIFICATION

I, William Weiss, certify that:

1. I have reviewed this annual report on Form 10-KSB of PaperClip Software, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the small business issuer as of, and for, the periods presented in this report;

4. The small business issuer's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the small business issuer and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) [Reserved];

(c) Evaluated the effectiveness of the small business issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the small business issuer's internal control over financial reporting that occurred during the small business issuer's most recent fiscal quarter (the small business issuer's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the small business issuer's internal control over financial reporting; and

5. The small business issuer's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the small business issuer's auditors and the audit committee of the small business issuer's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the small business issuer's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the small business issuer's internal control over financial reporting.

Date: March 30, 2006

By: /s/ William Weiss
William Weiss
Chief Executive Officer
Principal Financial Officer

Exhibit 32.1

CERTIFICATION OF

CHIEF EXECUTIVE OFFICER AND PRINCIPAL FINANCIAL OFFICER OF
PAPERCLIP SOFTWARE, INC.

(Pursuant to Section 1350 of Chapter 63 of Title 18 of the United States Code)

The undersigned, William Weiss, Chief Executive Officer and Principal Financial Officer of PaperClip Software, Inc. (the "Company"), certifies that:

- the Annual Report on Form 10-KSB of the Company for the year ended December 31, 2004 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934;

- and the information contained in the Annual Report on Form 10-KSB of the Company for the year ended December 31, 2005 fairly presents, in all material respects, the financial condition and results of operations of the Company.

March 30, 2006 By: /s/ William Weiss