

INFORMATION ANALYSIS INC  
Form DEF 14A  
April 19, 2006

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

**SCHEDULE 14A**

**Proxy Statement Pursuant to Section 14(a) of the**  
**Securities Exchange Act of 1934**  
**(Amendment No. \_\_)**

Filed by the Registrant

Filed by a Party other than the Registrant

Check the appropriate box:

Preliminary Proxy Statement

**Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**

Definitive Proxy Statement

Definitive Additional Materials

Soliciting Material Under Rule 14a-12

**Information Analysis Incorporated**

(Name of Registrant as Specified In Its Charter)

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(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

No fee required.

Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

1) Title of each class of securities to which transaction applies:

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2) Aggregate number of securities to which transaction applies:

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3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

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1) Amount previously paid:

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2) Form, Schedule or Registration Statement No:

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3) Filing party:

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4) Date Filed:

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(703) 383-3000

(800) 829-7614

Fax: (703) 293-7979

11240 Waples Mill Road, Suite 201, Fairfax, Virginia 22030

www.infoa.com  
April 17, 2006

Dear Stockholder,

We cordially invite you to attend our 2006 annual meeting of stockholders to be held at 10:00 AM on Thursday, May 18, 2006, at our offices at 11240 Waples Mill Road, Suite 201, Fairfax, Virginia 22030. The attached notice of annual meeting and proxy statement describe the business we will conduct at the meeting and provide information about Information Analysis Incorporated that you should consider when you vote your shares.

When you have finished reading the proxy statement, please promptly vote your shares by marking, signing, dating and returning the proxy card in the enclosed envelope. We encourage you to vote by proxy so that your shares will be represented and voted at the meeting, whether or not you can attend.

Sincerely,

/s/ Sandor Rosenberg  
Sandor Rosenberg  
Chairman of the Board and  
Chief Executive officer

(703) 383-3000

(800) 829-7614

Fax: (703) 293-7979

11240 Waples Mill Road, Suite 201, Fairfax, Virginia 22030

www.infoa.com  
**April 17, 2006**

**NOTICE OF 2006 ANNUAL MEETING OF STOCKHOLDERS**

TIME: 10:00 AM

DATE: May 18, 2006

PLACE: Information Analysis Incorporated  
11240 Waples Mill Road, Suite 201  
Fairfax, Virginia 22030

PURPOSES:

1. To elect Four directors to serve terms expiring at the 2007 Annual Meeting.
2. To ratify the appointment of Reznick Group, P.C. as the company's independent public accountants for the fiscal year ending December 31, 2006.
3. To approve the IAI 2006 Stock Incentive Plan.
4. To consider any other business that is properly presented at the meeting.

WHO MAY VOTE:

You may vote if you were the record owner of Information Analysis Incorporated stock at the close of business on April 12, 2006. A list of stockholders of record will be available at the meeting and, during the 10 days prior to the meeting, at the office of the Secretary at the above address.

BY ORDER OF THE BOARD OF DIRECTORS

/s/ Richard S. DeRose  
Richard S. DeRose  
Secretary

Information Analysis Incorporated

2006 Proxy Statement

**INFORMATION ANALYSIS INCORPORATED**

**11240 WAPLES MILL ROAD, SUITE 201**

**FAIRFAX, VIRGINIA 22030**

**PROXY STATEMENT FOR THE INFORMATION ANALYSIS INCORPORATED**

**2006 ANNUAL MEETING OF STOCKHOLDERS TO BE HELD ON**

**MAY 18, 2006**

**GENERAL INFORMATION ABOUT THE ANNUAL MEETING**

**Why Did You Send Me this Proxy Statement?**

We sent you this proxy statement and the enclosed proxy card because Information Analysis Incorporated's (IAI) Board of Directors is soliciting your proxy to vote at the 2006 annual meeting of stockholders and any adjournments of the meeting to be held at 10:00 AM on Thursday, May 18, 2006, at our offices at 11240 Waples Mill Road, Suite 201, Fairfax, Virginia 22030. This proxy statement along with the accompanying Notice of Annual Meeting of Stockholders summarizes the purposes of the meeting and the information you need to know to vote at the annual meeting.

On April 17, 2006, we began sending this proxy statement, the attached notice of annual meeting and the enclosed proxy card to all stockholders entitled to vote at the meeting. Although not part of this proxy statement, we are also sending along with this proxy statement, our 2006 annual report, which includes our financial statements for the fiscal year ended December 31, 2005. You can also find a copy of our 2005 Annual Report on Form 10-KSB on the Internet through the SEC's electronic data system called EDGAR at [www.sec.gov](http://www.sec.gov) or through the Investor Relations section of our website at [www.infoa.com](http://www.infoa.com).

**Who Can Vote?**

Only stockholders who owned IAI common stock at the close of business on April 12, 2006, are entitled to vote at the annual meeting. On this record date, there were 10,906,515 shares of IAI common stock outstanding and entitled to vote. Information Analysis Incorporated common stock is our only class of voting stock.

You do not need to attend the annual meeting to vote your shares. Shares represented by valid proxies, received in time for the meeting and not revoked prior to the meeting, will be voted at the meeting. A stockholder may revoke a proxy before the proxy is voted by delivering to our Secretary a signed statement of revocation or a duly executed proxy card bearing a later date. Any stockholder who has executed a proxy card but attends the meeting in person may revoke the proxy and vote at the meeting.

**How Many Votes Do I Have?**

Each share of IAI common stock that you own entitles you to one vote.

**How Do I Vote?**

Whether you plan to attend the annual meeting or not, we urge you to vote by proxy. Voting by proxy will not affect your right to attend the annual meeting. If your shares are registered directly in your name through our stock transfer agent, American Stock Transfer, or you have stock certificates, you may vote:

**By mail.** Complete and mail the enclosed proxy card in the enclosed postage prepaid envelope. Your proxy will be voted in accordance with your instructions. If you sign the proxy card but do not specify how you want your shares voted, they will be voted as recommended by our Board of Directors.



**In person at the meeting.** If you attend the meeting, you may deliver your completed proxy card in person or you may vote by completing a ballot, which will be available at the meeting.

If your shares are held in street name (held in the name of a bank, broker or other nominee), you must provide the bank, broker or other nominee with instructions on how to vote your shares and can do so as follows:

**By mail.** You will receive instructions from your broker or other nominee explaining how to vote your shares.

**In person at the meeting.** Contact the broker or other nominee who holds your shares to obtain a broker's proxy card and bring it with you to the meeting. You will not be able to vote at the meeting unless you have a proxy card from your broker.

**How Does the Board of Directors Recommend That I Vote on the Proposals?**

The board of directors recommends that you vote as follows:

**FOR** the election of the nominees for director;

**FOR** ratification of the selection of independent public accountants for our fiscal year ending December 31, 2006.

**FOR** approval of the IAI 2006 Stock Incentive Plan;

If any other matter is presented, the proxy card provides that your shares will be voted by the proxy holder listed on the proxy card in accordance with his or her best judgment. At the time this proxy statement was printed, we knew of no matters that needed to be acted on at the annual meeting, other than those discussed in this proxy statement.

**May I Revoke My Proxy?**

If you give us your proxy, you may revoke it at any time before the meeting. You may revoke your proxy in any one of the following ways:

signing a new proxy card and submitting it as instructed above;

notifying IAI's Secretary in writing before the annual meeting that you have revoked your proxy; or

attending the meeting in person and voting in person. Attending the meeting in person will not in and of itself revoke a previously submitted proxy unless you specifically request it.

**What if I Receive More Than One Proxy Card?**

You may receive more than one proxy card or voting instruction form if you hold shares of our common stock in more than one account, which may be in registered form or held in street name. Please vote in the manner described under "How Do I Vote?" for each account to ensure that all of your shares are voted.

**Will My Shares be Voted if I Do Not Return My Proxy Card?**



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If your shares are registered in your name or if you have stock certificates, they will not be voted if you do not return your proxy card by mail or vote at the meeting as described above under "How Do I Vote?"

If your shares are held in street name and you do not provide voting instructions to the bank, broker or other nominee that holds your shares as described above under "How Do I Vote?", the bank, broker or other nominee has the authority to vote your unvoted shares on both Proposals 1 and 2 even if it does not receive instructions from you. We encourage you to provide voting instructions. This ensures your shares will be voted at the meeting in the

manner you desire. If your broker cannot vote your shares on a particular matter because it has not received instructions from you and does not have discretionary voting authority on that matter or because your broker chooses not to vote on a matter for which it does have discretionary voting authority, this is referred to as a broker non-vote .

### What Vote is Required to Approve Each Proposal and How are Votes Counted?

#### Proposal 1: Elect Directors

The nominees for director who receive the most votes (also known as a plurality of the votes) will be elected. Abstentions are not counted for purposes of electing directors. You may vote either FOR all of the nominees, WITHHOLD your vote from all of the nominees or WITHHOLD your vote from any one or more of the nominees. Votes that are withheld will not be included in the vote tally for the election of directors. Brokerage firms have authority to vote customers' unvoted shares held by the firms in street name for the election of directors. If a broker does not exercise this authority, such broker non-votes will have no effect on the results of this vote.

#### Proposal 2: Ratify Selection of Auditors

The affirmative vote of a majority of the votes present or represented by proxy and entitled to vote at the annual meeting is required to ratify the selection of independent auditors. Abstentions will be treated as votes against this proposal. Brokerage firms have authority to vote customers' unvoted shares held by the firms in street name on this proposal. If a broker does not exercise this authority, such broker non-votes will have no effect on the results of this vote. We are not required to obtain the approval of our stockholders to select our independent accountants. However, if our stockholders do not ratify the selection of Reznick Group, P.C. as our independent accountants for 2006, our Audit Committee of our Board of Directors will reconsider its selection.

#### Proposal 3: Approval of IAI 2006 Stock Incentive Plan

The affirmative vote of a majority of the votes present or represented by proxy and entitled to vote at the annual meeting is required to approve the IAI 2006 Stock Incentive Plan. Abstentions will be treated as votes against this proposal. Brokerage firms do not have authority to vote customers' unvoted shares held by the firms in street name on this proposal, therefore, any shares not voted by a customer will be treated as a broker non-vote, such broker non-votes will have no effect on the results of this vote.

### Is Voting Confidential?

We will keep all the proxies, ballots and voting tabulations private. We only let our Inspectors of Election American Stock Transfer examine these documents. We will not disclose your vote to management unless it is necessary to meet legal requirements. We will, however, forward to management any written comments you make, on the proxy card or elsewhere.

### What Are the Costs of Soliciting these Proxies?

We will pay all of the costs of soliciting these proxies. Our directors and employees may solicit proxies in person or by telephone, fax or email. We will pay these employees and directors no additional compensation for these services. We will ask banks, brokers and other institutions, nominees and fiduciaries to forward these proxy materials to their principals and to obtain authority to execute proxies. We will then reimburse them for their expenses.

**What Constitutes a Quorum for the Meeting?**

The presence, in person or by proxy, of the holders of a majority of the outstanding shares of our common stock is necessary to constitute a quorum at the meeting. Votes of stockholders of record who are present at the meeting in person or by proxy, abstentions, and broker non-votes are counted for purposes of determining whether a quorum exists.

**SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT**

The following table sets forth certain information with respect to the beneficial ownership of our common stock as of April 4, 2006, for (a) the executive officers named in the Summary Compensation Table on page 9 of this proxy statement, (b) each of our directors and director nominees, (c) all of our current directors and executive officers as a group and (d) each stockholder known by us to own beneficially more than 5% of our common stock. Beneficial ownership is determined in accordance with the rules of the SEC and includes voting or investment power with respect to the securities. We deem shares of common stock that may be acquired by an individual or group within 60 days of April 4, 2006, pursuant to the exercise of options or warrants to be outstanding for the purpose of computing the percentage ownership of such individual or group, but are not deemed to be outstanding for the purpose of computing the percentage ownership of any other person shown in the table. Except as indicated in footnotes to this table, we believe that the stockholders named in this table have sole voting and investment power with respect to all shares of common stock shown to be beneficially owned by them based on information provided to us by these stockholders. Percentage of ownership is based on 10,854,015 shares of common stock outstanding on April 4, 2006.

**TITLE OF CLASS: INFORMATION ANALYSIS INCORPORATED COMMON STOCK**

Name and Address of Beneficial Owner (1)	Amount and Nature of Beneficial Ownership (2)	Percent Of Class
Sandor Rosenberg, Chairman, CEO, and Director	1,832,800	16.9
Richard S. DeRose, Executive Vice President	440,900(3)	4.0
Stanley A. Reese, Senior Vice President	275,750(4)	2.5
Charles A. May, Jr., Director	66,000(5)	*
Bonnie K. Wachtel, Director	132,800(6)	1.2
James D. Wester, Director	329,355(7)	3.0
Traditions LP, 5% shareholder	1,000,000	9.2
All directors and executive officers as a group	3,077,605(8)	26.5

\* *represents less than 1%*

- (1) The address of all beneficial holders is in care of the Company, except Ms. Wachtel, whose address of record is 1101 14<sup>th</sup> St. NW, Washington, DC 20001, and Traditions, LP, whose address of record is 924 Ridge Drive, McLean, VA 22101.
- (2) All shares are held outright by the individuals listed.
- (3) Includes 242,900 shares issuable upon the exercise of options to purchase common stock
- (4) Includes 253,750 shares issuable upon the exercise of options to purchase common stock
- (5) Includes 26,000 shares issuable upon the exercise of options to purchase common stock

- (6) Includes 23,000 shares issuable upon the exercise of options to purchase common stock
  
- (7) Includes 200,000 shares issuable upon the exercise of options to purchase common stock
  
- (8) Includes 745,650 shares issuable upon the exercise of options to purchase common stock

## MANAGEMENT

**The Board of Directors**

Our Bylaws provide that our business is to be managed by or under the direction of our Board of Directors. All Directors are elected at each annual meeting of stockholders to serve until the next annual meeting of stockholders and until their successors have been elected and qualified. Our Board of Directors currently consists of four (4) members.

Our Board of Directors voted to nominate Charles A. May, Jr, Sandor Rosenberg, Bonnie K. Wachtel and James D. Wester for election at the annual meeting to serve until the 2007 annual meeting of stockholders, and until their respective successors have been elected and qualified.

Set forth below are the names of the persons nominated as directors, their ages, their offices in the Company, if any, their principal occupations or employment for the past five years, the length of their tenure as directors and the names of other public companies in which such persons hold directorships.

Name of Nominee	Age	Director Since	Position with the Company
Charles A. May, Jr.	68	1997	Director
Sandor Rosenberg	59	1979	Chairman of the Board, Chief Executive Officer and President
Bonnie K. Wachtel	50	1992	Director
James C. Wester	67	1985	Director

**Charles A. May, Jr.**, 68, is a consultant focusing on national security and defense conversion issues. In 1992, he retired as a Lt. General from the Air Force where he last served as Assistant Vice Chief of Staff, Headquarters US Air Force, Washington, D.C. He is a graduate of the U.S. Air Force Academy, where he once served as an Associate Professor of Political Science. General May has also graduated from the NATO Defense College and has completed the University of Pittsburgh's Management Program for Executives.

**Sandor Rosenberg**, 59, is the founder of the Company and has been Chairman of the Board and Chief Executive Officer of the Company since 1979, and President since 1998. Mr. Rosenberg holds a B.S. degree in Aerospace Engineering from Rensselaer Polytechnic Institute, and has done graduate studies in Operations Research at George Washington University.

**Bonnie K. Wachtel**, 50, has served as vice president and general counsel of Wachtel & Co., Inc., a Washington, D.C.-based brokerage and investment banking firm, since 1984. Ms. Wachtel holds BA and MBA degrees from the University of Chicago and a JD from the University of Virginia. Ms. Wachtel is a Certified Financial Analyst. She is a director of Integral Systems, Inc., a provider of computer systems and software for the satellite communications market; and VSE Corporation, a provider of technical services to the federal government.

**James D. Wester**, 67, has been a computer services marketing consultant for more than 16 years. Since 1984, he has been president of Results, Inc., a computer services marketing firm. Mr. Wester holds a BME degree from Auburn University and an MBA from George Washington University.

Our Board has determined that the following members of the Board qualify as independent under the definition promulgated by the NASDAQ Stock Market:

Charles A. May, Jr.

Bonnie K. Wachtel

James D. Wester

There are no family relationships between any directors or executive officers of the Company.



### Committees of the Board of Directors and Meetings

*Meeting Attendance.* During the fiscal year ended December 31, 2005 there were two meetings of our Board of Directors. No director attended fewer than 75% of the total number of meetings of the Board and of committees of the Board on which he or she served during fiscal 2006, except for James D. Wester, who did not attend either of the meetings of the Board in fiscal 2006. The Board has adopted a policy under which each member of the Board is strongly encouraged to attend each annual meeting of our stockholders.

*Audit Committee.* Our Audit Committee met two times during 2005. This committee currently has two members, Bonnie K. Wachtel (Chairman) and Charles A. May, Jr. Our Audit Committee has the authority to retain and terminate the services of our independent accountants, reviews annual financial statements, considers matters relating to accounting policy and internal controls and reviews the scope of annual audits. All members of the Audit Committee satisfy the current independence standards promulgated by the Securities and Exchange Commission and by the NASDAQ Stock Market, as such standards apply specifically to members of audit committees. The Board has determined that Ms. Wachtel is an audit committee financial expert, as the Securities and Exchange Commission has defined that term in Item 401 of Regulation S-B. Please also see the report of the Audit Committee set forth elsewhere in this proxy statement.

*Compensation Committee.* Our Compensation Committee met one time during 2005. This committee currently has two members, Ms. Wachtel (Chairman) and Mr. May. Our Compensation Committee reviews, approves and makes recommendations regarding our compensation policies, practices and procedures to ensure that legal and fiduciary responsibilities of the Board of Directors are carried out and that such policies, practices and procedures contribute to our success. The Compensation Committee is responsible for the determination of the compensation of our Chief Executive Officer, and shall conduct its decision-making process with respect to that issue without the chief executive officer present. All members of the Compensation Committee qualify as independent under the definition promulgated by the NASDAQ Stock Market.

*Nominating Committee.* Our Nominating Committee met one time during 2005 and has four members, Mr. Rosenberg (Chairman), Ms. Wachtel, and Messrs. May and Wester. This committee's role is to make recommendations to the full Board as to the size and composition of the Board and its committees, and to evaluate and make recommendations as to potential candidates. All members of the Nominating Committee qualify as independent under the definition promulgated by the NASDAQ Stock Market except for Mr. Rosenberg. The Nominating Committee may consider candidates recommended by stockholders as well as from other sources such as other directors or officers, third party search firms or other appropriate sources. For all potential candidates, the Nominating Committee may consider all factors it deems relevant, such as a candidate's personal integrity and sound judgment, business and professional skills and experience, independence, knowledge of the industry in which we operate, possible conflicts of interest, diversity, the extent to which the candidate would fill a present need on the Board, and concern for the long-term interests of the stockholders. In general, persons recommended by stockholders will be considered on the same basis as candidates from other sources. If a stockholder wishes to nominate a candidate to be considered for election as a director at the 2007 Annual Meeting of Stockholders, it must follow the procedures described in Stockholder Proposals and Nominations For Director.

### Shareholder Communications to the Board

Generally, shareholders who have questions or concerns should contact our Investor Relations department at (703) 383-3000. However, any shareholders who wish to address questions regarding our business directly with the Board of Directors, or any individual director, should direct his or her questions in writing to:

Board of Directors of Information Analysis Incorporated

ATTN: (Chairman of the Board/Board member name)

11240 Waples Mill Road, Suite 201

Fairfax, Virginia 22030

**Compensation of Directors**

The Company may pay each non-employee director an annual fee of \$2,000 to serve on the Board, payable quarterly. Expenses incurred in attending Board of Director meetings and committee meetings may be reimbursed.

**Executive Officers**

The following table sets forth certain information regarding our executive officers who are not also directors.

Name	Age	Position
Richard S. DeRose	67	Executive Vice President, Secretary, and Chief Financial Officer
Stanley A. Reese	49	Senior Vice President and Chief Operating Officer

**Richard S. DeRose**, 67, has been Executive Vice President since 1991. Prior to that, he served as the President and CEO of DHD, Inc., a company he founded, from 1979 until DHD's acquisition by the Company in 1991. Prior to DHD, Mr. DeRose held several management positions in the information technology and telecommunications industries at RCA, Burroughs, and MCI. Mr. DeRose holds a BS degree in Science from the US Naval Academy and an MS degree in Computer Systems Management from the US Naval Postgraduate School, Monterey.

**Stanley A. Reese**, 49, joined the Company in 1993. Mr. Reese has been Senior Vice President since 1997 and Chief Operating Officer since March 1999. From 1992 to 1993, he served as Vice President, Technical Services at Tomco Systems, Inc. Prior to Tomco Systems, he served as Senior Program manager at ICF Information Technology, Inc. Mr. Reese has over 19 years experience managing and marketing large scale mainframe and PC-based applications. Mr. Reese holds a BA in History from George Mason University.

**EXECUTIVE COMPENSATION**

The Summary Compensation Table below sets forth individual compensation information for the Chief Executive Officer and the other executive officers serving as executive officers as of December 31, 2005 (collectively "Named Executive Officers"):

**Summary Compensation Table**

Name and Principal Position	Year	Annual Compensation		Long Term Compensation Awards Securities Underlying
		Salary	Bonus	Options (#)
Sandor Rosenberg Chairman of the Board and Chief Executive Officer	2005	\$ 129,375	20,000	
	2004	\$ 114,987	16,000	
	2003	\$ 93,994		
Richard S. DeRose Executive Vice President Chief Financial Officer	2005	\$ 129,375	25,314	25,000
	2004	\$ 114,987	16,000	
	2003	\$ 93,994		50,000
Stanley A. Reese Senior Vice President and Chief Operating Officer	2005	\$ 129,375	20,000	25,000
	2004	\$ 114,987	16,000	
	2003	\$ 95,076		50,000

No Named Executive Officer has received any perquisite or benefit, securities, or property that exceeded the lesser of \$50,000 or 10% of the total annual salary and bonus reported for such executive officer.



## Information Analysis Incorporated

## 2006 Proxy Statement

## Option Grants in Our Last Fiscal Year

The following named executive officers were awarded options during the year ended December 31, 2005. The exercise prices of the options issued were at the closing prices on the dates of issue. These options vested on December 31, 2005.

## Option Grants in Last Fiscal Year

[Individual Grants](1)

Name (a)	Number of securities underlying options granted (b)	Percent of total options granted to employees in fiscal year (c)	Exercise or base price (\$/Sh) (d)	Expiration Date (e)
Richard S. DeRose	25,000	20.5%	0.42	10/27/2015
Stanley A. Reese	25,000	20.5%	0.42	10/27/2015

(1) The options were granted pursuant to our 1996 Stock Option Plan, and are incentive stock options.

## Aggregated Option Exercises in Last Fiscal Year and Fiscal Year-End Option Values

The following table depicts option exercise activity in the last fiscal year and fiscal year-end option values with respect to each of the Named Executive Officers. The value of unexercised in-the-money options at December 31, 2005 equals the market value of the underlying common stock at December 31, 2005 minus the option exercise price. The fair market value of the Company's common stock at December 31, 2005 was \$0.69.

Name	Value		Number of Securities		Value of Unexercised	
	Shares Acquired on Exercise (#)	Realized	Underlying Unexercised		In-the-Money	
			Options at 12/31/2005 Exercisable	Options at 12/31/2005 Unexercisable	Options at 12/31/2005 Exercisable	Options at 12/31/2005 Unexercisable
Richard S. DeRose		\$	242,900		\$ 67,541	\$
Stanley A. Reese		\$	253,750		\$ 58,903	\$

## Equity Compensation Plan Information

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

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants, and rights	Weighted average exercise price of outstanding options, warrants, and rights	Number of securities remaining available for future issuance
Equity compensation plans approved by security holders	1,963,350	\$ 0.87	81,800
Equity compensation plans not approved by security holders	0		

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Total	1,963,350	\$	0.87	81,800
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**Employment Contracts, Termination of Employment and Change-in-Control Arrangements**

On June 18, 1997, the Company agreed in writing to provide to Richard S. DeRose, Executive Vice President, Chief Financial Officer, and Secretary, twelve months severance pay of his base salary, payable in normal payroll increments, in the event of the termination of his employment other than for cause. In the event of a change of control or the sale or transfer of substantially all of the Company's assets, the Company agreed that in the event of Mr. DeRose's termination, substantial reduction of duties, or requirement to be based at a location outside of a 30-mile radius of Fairfax, Virginia, he will receive a twelve month severance payment of base salary, payable in lump sum or monthly, at the Company's discretion.

**Changes In and Disagreements With Accountants on Accounting and Financial Disclosure**

On April 4, 2005, on the recommendation of the Audit Committee of the Board of Directors, Information Analysis Incorporated (the Company) notified Reznick Group, P.C. that they have been engaged to serve as the Company's independent public accountants, and notified Rubino & McGeehin, Chartered that they have been dismissed as the Company's independent public accountants, effective immediately.

Rubino & McGeehin, Chartered performed audits of the financial statements for the years ended December 31, 2004 and 2003. Their reports did not contain an adverse opinion or a disclaimer of opinion and were not qualified or modified as to uncertainty, audit scope, or accounting principles, except as follows: Rubino & McGeehin, Chartered's report on the financial statements of Information Analysis Incorporated for the years ended December 31, 2004 and 2003, contained a separate paragraph, stating:

The accompanying consolidated financial statements have been prepared assuming Information Analysis Incorporated and subsidiary will continue as a going concern. As discussed in Note 15, the Company has suffered recurring losses from operations and has cash flows problems and financing requirements that raise substantial doubt about its ability to continue as a going concern. Management's plans in regards to these matters are described in Note 15. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

During the two years ended December 31, 2004, and from December 31, 2004 through the effective date of Rubino & McGeehin, Chartered's termination, there had been no disagreements between the Company and Rubino & McGeehin, Chartered on any matter of accounting principles or practice, financial statement disclosure, or auditing scope of procedure, which disagreements would have caused Rubino & McGeehin, Chartered to make reference to the subject matter of such disagreements in connection with its report.

Rubino & McGeehin, Chartered has furnished a letter to the SEC dated April 7, 2005, stating that it agrees with the above statements.

**REPORT OF AUDIT COMMITTEE**

The Audit Committee of the Board of Directors, which consists entirely of directors who meet the independence and experience requirements of the NASDAQ stock market, has furnished the following report:

The Audit Committee assists the Board in overseeing and monitoring the integrity of our financial reporting process, compliance with legal and regulatory requirements and the quality of internal and external audit processes. This committee's role and responsibilities are set forth in a our charter adopted by the Board. This committee reviews and reassesses our charter annually and recommends any changes to the Board for approval. The Audit Committee is responsible for overseeing our overall financial reporting process, and for the appointment, compensation, retention, and oversight of the work of Reznick Group, P.C. In fulfilling its responsibilities for the financial statements for fiscal year December 31, 2005, the Audit Committee took the following actions:

Reviewed and discussed the audited financial statements for the fiscal year ended December 31, 2005, with management and Reznick Group, P.C., our independent auditors;

Discussed with Reznick Group, P.C. the matters required to be discussed by Statement on Auditing Standards No. 61 relating to the conduct of the audit; and

Received written disclosures and the letter from Reznick Group, P.C., regarding its independence as required by Independence Standards Board Standard No. 1. The Audit Committee further discussed with Reznick Group, P.C., their independence. The Audit Committee also considered the status of pending litigation, taxation matters and other areas of oversight relating to the financial reporting and audit process that the committee determined appropriate.

Based on the Audit Committee's review of the audited financial statements and discussions with management and Reznick Group, P.C., the Audit Committee recommended to the Board that the audited financial statements be included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2005, for filing with the SEC.

Members of the Information Analysis Incorporated Audit Committee  
Bonnie K. Wachtel  
Charles A. May, Jr.

#### SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE

Section 16(a) ( Section 16(a) ) of the Securities Exchange Act of 1934, as amended (the Exchange Act ), requires executive officers and Directors and persons who beneficially own more than ten percent (10%) of the Company's Common Stock to file initial reports of ownership and reports of changes in ownership with the Securities and Exchange Commission (the Commission ) and any national securities exchange on which the Company's securities are registered. Executive officers, Directors and greater than ten percent (10%) beneficial owners are required by the Commission's regulations to furnish the Company with copies of all Section 16(a) forms they file.

Based solely on a review of the copies of such forms furnished to the Company, the following executive officers, Directors and 10% beneficial owners failed to file on a timely basis the forms required under Section 16(a) of the Exchange Act:

Name	Year	Number of	Number of Transactions	Known Failure
		Late Reports	Not Reported on a Timely Basis	To File a Form
Richard DeRose	2005	1	1	
Stanley A. Reese	2005	1	1	

#### CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

Our Audit Committee reviews and approves in advance all related-party transactions. There were no such transactions in either of the last two fiscal years.

**ELECTION OF DIRECTORS**

**(Notice Item 1)**

The Board of Directors nominated Charles A. May, Jr., Sandor Rosenberg, Bonnie K. Wachtel and James D. Wester for election at the Annual Meeting. If they are elected, they will serve on our Board of Directors until the 2007 Annual Meeting of Stockholders and until their respective successors have been elected and qualified.

Unless authority to vote for any of these nominees is withheld, the shares represented by the enclosed proxy will be voted **FOR** the election as directors of Charles A. May, Jr., Sandor Rosenberg, Bonnie K. Wachtel and James D. Wester. In the event that any nominee becomes unable or unwilling to serve, the shares represented by the enclosed proxy will be voted for the election of such other person as the Board of Directors may recommend in his/her place. We have no reason to believe that any nominee will be unable or unwilling to serve as a director.

All nominees are currently Directors of the Company and have served continuously since the dates of their elections as shown on page 7.

A plurality of the shares voted affirmatively or negatively at the Meeting is required to elect each nominee as a director.

**The Board Of Directors Recommends The Election Of Charles A. May, Jr., Sandor Rosenberg, Bonnie K. Wachtel and James D. Wester As Directors, And Proxies Solicited By The Board Will Be Voted In Favor Thereof Unless A Stockholder Has Indicated Otherwise On The Proxy.**

## INDEPENDENT PUBLIC ACCOUNTANTS

## (Notice Item 2)

The Audit Committee has appointed Reznick Group, P.C., independent public accountants, to audit our financial statements for the fiscal year ending December 31, 2006. The Board proposes that the stockholders ratify this appointment. Reznick Group, P.C., audited our financial statements for the fiscal year ended December 31, 2005. We expect that representatives of Reznick Group, P.C., will not be present at the meeting, will therefore be unable to make a statement, and will not be available to respond to appropriate questions.

The following table presents fees for professional audit services rendered by Reznick Group, P.C., and Rubino & McGeehin, Chartered, for the audit of the Company's annual financial statements for the years ended December 31, 2005 and 2004, respectively, and fees billed for other services rendered by our principal accountants during those periods.

Fee Category	Fiscal 2005 Fees	Fiscal 2004 Fees
Audit Fees	\$ 46,510	\$ 45,500
Audit-Related Fees		
Out of Pocket Expenses	935	1,249
Communication with subsequent auditors	4,620	
Tax Fees	4,109	2,939
Other Fees		
Meeting with management to discuss accounting for stock options, including tax impact to IAI and employees	565	
Audit of Information Analysis Incorporated Profit Sharing Plan for the year ended December 31, 2003		8,500
General consulting and related research pertaining to SBA qualifications, pension and benefit plans, and stock options		1,345
Total Fees and Services	\$ 56,739	\$ 59,533

The Audit Committee directly engages the Independent Certified Public Accountants as it relates to the audit of the Company's fiscal year and the reviews of its fiscal quarters and the associated fees. The percentages of services other than Audit Fees that were approved by the audit committee in 2005 and 2004 are 94.5% and 39.4% respectively.

Although stockholder approval of the Board of Directors' selection of Reznick Group is not required by law, the Board of Directors believes that it is advisable to give stockholders an opportunity to ratify this selection.

In the event the stockholders do not ratify the appointment of Reznick Group, P.C., as our independent public accountants, the Audit Committee will reconsider its appointment.

The affirmative vote of a majority of the shares present or represented and entitled to vote at the Meeting is required to ratify the appointment of the independent public accountants.

**The Board Of Directors Recommends A Vote To Ratify The Appointment Of Reznick Group, P.C., As Independent Public Accountants, And Proxies Solicited By The Board Will Be Voted In Favor Of Such Ratification Unless A Stockholder Indicates Otherwise On The Proxy.**

**2006 STOCK INCENTIVE PLAN****(Notice Item 3)**

On April 12, 2006, the Board of Directors adopted the Information Analysis, Inc. 2006 Stock Incentive Plan (the *Plan*) subject to approval by the Company's shareholders. The Plan was adopted to provide for the grant of equity based, long-term incentives to attract and retain key employees, officers, directors and other third parties who provide personal services of substantial benefit or value to the Company. The maximum number of shares of common stock that may be issued pursuant to the Plan is 950,000 shares. The following review of certain provisions of the Plan is not, nor is it intended to be an exhaustive description of the Plan. A copy of the Plan is attached hereto as Exhibit A and is incorporated by reference. Shareholders are encouraged to review the Plan in its entirety.

**General**

Equity awards are an important and critical element of compensation in the technology industries without which we will have difficulty retaining and recruiting valuable employees. Our 1996 Plan expires on May 29, 2006. Without approval of the 2006 Plan, we will not have any shares available for equity awards to grant to current and future employees, including employees of recently acquired or to be acquired entities.

**Participation**

The intent of the Plan is to provide the Company with a means of attracting and retaining the services of highly motivated and qualified key personnel. Accordingly, the Plan is limited to the Company's employees, executive officers, directors, independent advisors and consultants. If the Company's shareholders do not approve the 2006 Plan as proposed, no awards will be made pursuant to the Plan.

The Company's proposed Stock Incentive Plan is limited to two classes of individuals: (a) Company employees and employee directors (*Employees*) and (b) non-employee directors, consultants and advisors (*Selected Persons*). The number of Employees and Selected persons that are potentially eligible for participation in the Plan at present are approximately forty-eight (48) and twenty-one (21), respectively.

**Principal Features of the Plan**

The Plan permits the Company to grant incentive (statutory) stock options and non-statutory stock options (*Options*) and restricted common stock (*Restricted Stock*). Its purpose is to promote the Company's interests and the interests of the shareholders by motivating key employees to work towards achieving the Company's long-range goals and by attracting and retaining exceptional employees, directors, independent advisors and consultants. By motivating these persons to share in the Company's long-term growth, their interests are more closely aligned with those of the shareholders.

**Administration**

The Plan will be administered by the Company's Board of Directors or by a committee appointed by the Board (the *Committee*). The term *Board* as used in this section refers to the Board of Directors or if the Board has delegated authority, the Committee. The Company intends that the Plan conform in all respects with the requirements of Rule 16b-3 of the Securities and Exchange Commission under the Securities Exchange Act of 1934, as amended. To the extent that any aspect of the Plan or its administration shall at any time be viewed as inconsistent with the requirements of Rule 16b-3 or, such aspect shall be deemed to be modified, deleted or otherwise changed as necessary to ensure continued compliance with such provision.

*Duties of Board*

In accordance with the provisions of the Plan, the Board shall (i) select those eligible persons to whom Restricted Stock or Options shall be granted (*Optionees*); (ii) determine the time or times at which each Option shall be granted, whether an Option is an Incentive Stock Option (*ISO*) or a Non-statutory Stock Option (*NSO*) and the

number of shares to be subject to each Option; and (iii) fix the time and manner in which the Option may be exercised, the Option exercise price, and the Option period all subject to the limitations and guidelines of the Plan.

The Board shall determine the form of option agreement to evidence the terms and conditions of each Option. The Board, from time to time, may adopt such rules and regulations for carrying out the purposes of the Plan as it may deem proper and in the best interests of the Company. The Board shall keep minutes of its meetings and records of its actions. A majority of the members of the Board shall constitute a quorum for the transaction of any business by the Board. The Board may act at any time by an affirmative vote of a majority of those members voting. Such vote may be taken at a meeting (which may be conducted in person or by any telecommunication medium) or by written consent of the Board or Committee members without a meeting. The Board shall resolve all questions arising under the Plan and option agreements entered into pursuant to the Plan. Each determination, interpretation, or other action made or taken by the Board shall be final and conclusive and binding.

### **Stock Options**

A stock option award grants to the Optionee the right to buy a specified number of shares of the Company's common stock at a fixed price, subject to such terms and conditions as the Board may determine.

#### *Exercise Price*

The Board determines the exercise price of all options at the time of grant, but the exercise price of any ISO may not be less than 100% of the fair market value of the underlying stock on the date of the grant.

#### *Payment*

Each Option may be exercised in whole, at any time, or in part, from time to time, within the period for exercise set forth in the related option agreement. Optionees are not required to pay cash in return for the grant of an option (except as may be required by law). However, consideration equal to the exercise price must be paid to exercise an option. At the discretion of the Board, Options may be exercised by payment of the exercise price either in cash, certified check, by tendering of shares of the Company's common stock having a fair market value equal to the exercise price, or other such consideration as the Board deems appropriate.

#### *Transferability*

An Option shall be exercisable only by the Optionee, or other legal representative(s) during the Optionee's lifetime, or in the event of death, by the Optionee's guardian(s) or conservator(s). No Option may be transferred by the Optionee, either voluntarily or involuntarily, except by will of the laws of descent and distribution or pursuant to a qualified domestic relations order as defined by the Plan.

#### *Restricted Stock*

The Board may grant Restricted Stock awards that result in shares of common stock being issued to a participant subject to restrictions against disposition during a restricted period established by the Board. The Board may condition the grant of Restricted Stock upon the attainment of specified performance goals or service requirements. The provisions of Restricted Stock awards need not be the same with respect to each recipient. The Company will hold the Restricted Stock in custody until the restrictions thereon have lapsed. During the period of the restrictions, a participant has the right to vote the shares of restricted stock and to receive dividends and distributions unless the Board requires such dividends and distributions to be held by the Company subject to the same restrictions as the Restricted Stock. If a participant terminates employment or service during the period of the restrictions, all shares still subject to restrictions will be forfeited and returned to the Company, subject to the right of the Board to waive such restrictions in the event of a participant's death, total disability, retirement or under special circumstances approved by the Board.



*Vesting and Expiration*

The Board has the authority to determine the vesting and expiration of the stock option grants and vesting of Restricted Stock awards. However, in the event of a participant's death, all unexercised Options may be exercised by the Optionee's legal guardian(s), conservator(s), or other legal representative(s) within twelve months after the Optionee's death or before the expiration of the option, whichever shall first occur. In the event of a termination of employment, except for events set forth in the Plan, all exercisable options shall terminate.

*Change of Control*

In the event of a reorganization or change in control of the Company such as a merger, consolidation, share exchange or other business combination, the Board has the authority to accelerate the exercisability or termination of any unexercised options, subject to any terms and conditions provided by the reorganization.

*Amendment*

The Board of Directors may amend, alter or terminate the Plan at any time. The Company must obtain shareholder approval for any change that would (i) require such approval under any regulatory or tax requirement, (ii) materially impair any option previously granted, (iii) materially increase the number of shares subject to the plan, (iv) materially increase the benefits accruing to Optionees under the plan, or (v) materially modify the requirements as to eligibility to participate in the Plan or the method for determining the option exercise price.

**Tax Consequences**

The Federal income tax consequences of an Optionee's participation in the Plan are complex and subject to change. The following is only a summary of the general rules applicable to the Plan. The summary is based on current provisions of the Internal Revenue Code and does not cover any state or local tax consequences of participation in the Plan. Participants in the Plan are advised to consult their own tax advisors as a taxpayer's particular situation may be such that some variation of the rules described below will apply.

The exercise of a non-statutory option generally results in immediate recognition of ordinary income by the Optionee and a corresponding tax deduction for the Company in the amount by which the fair market value of the shares of common stock purchased, on the date of such exercise, exceeds the aggregate option price. Any appreciation or depreciation in the fair market value of such shares after the date of such exercise will generally result in a capital gain or loss to the Optionee at the time he or she disposes of such shares.

In general, the exercise of an incentive stock option is exempt from income tax (although not from the alternative minimum tax) and does not result in a tax deduction for the Company at any time unless the Optionee disposes of the common stock purchased thereby within two years of the date such incentive stock option was granted or one year of the date of such exercise (known as a "disqualifying disposition"). If these holding period requirements under the Internal Revenue Code are satisfied, and if the Optionee has been an employee of us at all times from the date of grant of the incentive stock option to the day three months before such exercise (or twelve months in the case of termination of employment due to disability), then such Optionee will recognize any gain or loss upon disposition of such shares as capital gain or loss. However, if the Optionee makes a disqualifying disposition of any such shares, he or she will generally be obligated to report as ordinary income for the year in which such disposition occurs the excess, with certain adjustments, of the fair market value of the shares disposed of, on the date the incentive stock option was exercised, over the option price paid for such shares. The Company would be entitled to a tax deduction in the same amount so reported by such Optionee. Any additional gain realized by such Optionee on such a disqualifying disposition of such shares would be capital gain. If the total amount realized in a disqualifying disposition is less than the exercise price of the incentive stock option, the difference would be a capital loss for the Optionee.

The grant of Restricted Stock should not result in immediate income for the participant or in a deduction for the Company for federal income tax purposes, assuming the shares are nontransferable and subject to restrictions which would result in a "substantial risk of forfeiture" as intended by the Company and as defined in applicable Treasury regulations. If the shares are transferable or there are no such restrictions, the participant will realize compensation income upon receipt of the award. Otherwise, a participant generally will realize taxable compensation when any such

restrictions lapses. The amount of such income will be the value of the common stock on that date less any amount paid, if any, for the shares. Dividends paid on the common stock and received by the participant during the restricted period also will be taxable compensation income to the participant. In any event, the Company will be entitled to a tax deduction to the extent, and at the time, the participant realizes compensation income. A participant may elect, under Section 83(b) of the Code, to be taxed on the value of the stock at the time of award. If the election is made, the fair market value of the stock at the time of the award is taxable to the participant as compensation income and the Company is entitled to a corresponding deduction.

#### **Benefits to Directors and Executive Officers**

Awards under the Plan are made at the Board's discretion. Accordingly, future awards under the Plan, particularly to directors and executive officers, are not determinable at this time.

Pursuant to Item 10(a)(2)(iii) of Schedule 14A, if future awards to directors and executive officers under the proposed 2006 Stock Incentive Plan described herein are not presently determinable, the Company is obligated to provide in tabular format the benefits or amounts that participants would have received if the Stock Incentive Plan had been in effect during fiscal year 2005. As of this date, the Company has not made any determinations with respect to grants of Options or Restricted Stock.

The affirmative vote of a majority of the votes present or represented and entitled to vote at the Meeting is required to approve the increase in the aggregate number of shares of common stock available under the Plan.

**The Board Of Directors Recommends Approval Of The Adoption the IAI 2006 Stock Incentive Plan, And Proxies Solicited By The Board Will Be Voted In Favor Of The Amendment Unless A Stockholder Indicates Otherwise On The Proxy.**

**CODE OF CONDUCT AND ETHICS**

We have adopted a code of conduct and ethics that applies to all of our employees, including our chief executive officer and chief financial and accounting officers. The text of the code of conduct and ethics is posted on our website at [www.infoa.com](http://www.infoa.com) and will be made available to stockholders without charge, upon request, in writing to the Corporate Secretary at Information Analysis Incorporated, 11240 Waples Mill Road, Suite 201, Fairfax, Virginia 22030. Disclosure regarding any amendments to, or waivers from, provisions of the code of conduct and ethics that apply to our directors, principal executive and financial officers will be included in a Current Report on Form 8-K within four business days following the date of the amendment or waiver.

**OTHER MATTERS**

The Board of Directors knows of no other business which will be presented to the Annual Meeting. If any other business is properly brought before the Annual Meeting, proxies in the enclosed form will be voted in accordance with the judgment of the persons voting the proxies.

**STOCKHOLDER PROPOSALS AND NOMINATIONS FOR DIRECTOR**

To be considered for inclusion in the proxy statement relating to our Annual Meeting of Stockholders to be held in 2007, stockholder proposals must be received no later than December 18, 2005. If we do not receive notice of any matter to be considered for presentation at the Annual Meeting, although not included in the proxy statement, by March 3, 2006, management proxies may confer discretionary authority to vote on the matters presented at the Annual Meeting by a stockholder in accordance with Rule 14a-4 under the Securities Exchange Act. All stockholder proposals should be marked for the attention of Richard S. DeRose, Secretary, Information Analysis Incorporated, 11240 Waples Mill Road, Suite 201, Fairfax, Virginia 22030.

**Fairfax, Virginia**

**April 17, 2006**

**Our Annual Report on Form 10-KSB for the fiscal year ended December 31, 2005 (other than exhibits thereto) filed with the SEC, which provides additional information about us, is available on the Internet at [www.infoa.com](http://www.infoa.com) and is available in paper form to beneficial owners of our common stock without charge upon written request to Richard S. DeRose, Secretary, Information Analysis Incorporated, 11240 Waples Mill Road, Suite 201, Fairfax, Virginia 22030.**

IN WITNESS WHEREOF, the Corporation has caused this Certificate to be signed by Sandor Rosenberg, President and Chief Executive Officer, and attested to by Richard S. DeRose, Secretary, this 17<sup>th</sup> day of April, 2006.

**INFORMATION ANALYSIS INCORPORATED**

By: /s/ Sandor Rosenberg  
Sandor Rosenberg  
President and Chief Executive Officer

ATTEST:

/s/ Richard S. DeRose  
Richard S. DeRose  
Secretary

**INFORMATION ANALYSIS INCORPORATED**

**2006 STOCK INCENTIVE PLAN**

**ARTICLE 1**

**GENERAL PROVISIONS**

**1.1 Purpose.**

This Stock Incentive Plan (the Plan) is intended to allow designated officers, employee-directors and employees (all of whom are sometimes collectively referred to herein as Employees) and certain non-employee directors, independent advisors and consultants (all of whom are sometimes collectively referred to as Selected Persons) of Information Analysis, Inc. (IAI) and its Subsidiaries which it may have from time to time (IAI, and such Subsidiaries are referred to herein as the Company) to receive certain options (Stock Options) to purchase IAI common stock, \$0.01 par value (Common Stock), and to receive grants of Common Stock subject to certain restrictions (Awards). As used in this Plan, the term Subsidiary shall mean each corporation which is a subsidiary corporation of IAI, within the meaning of Section 424(f) of the Internal Revenue Code of 1986, as amended (the Code).

The main purpose of this Plan is to provide Employees and Selected Persons with equity-based compensation incentives to make significant and extraordinary contributions to the long-term performance and growth of the Company, and to attract and retain Employees and Selected Persons of exceptional ability.

**1.2 Administration.**

The Plan shall be administered by IAI's Board of Directors (the Board) and/or by a duly appointed Compensation Committee (the Committee) having such powers as shall be specified by the Board. The provisions of IAI's Charter, By-Laws and of applicable Virginia law shall govern the Board and/or Committee, except as otherwise provided herein or determined by the Board. Any subsequent references to the Board shall also mean the Committee if it has been appointed.

In the case of an appointed Committee, a combination of two or more officers and/or directors of the Company, including individuals who may be both officers and directors of the Company, will administer the Plan within any limitations determined by the Board. The Committee shall select one of its members as Chairman and shall act by vote of a majority of a quorum, or by unanimous written consent. A majority of its members shall constitute a quorum. The Committee shall keep records of its meetings and shall make such rules for the conduct of its business as the Board shall deem advisable.

The Board shall have full and complete authority, in its discretion, but subject to the express provisions of the Plan to: (i) approve the Employees and Selected Persons nominated by the management of the Company to be granted Awards or Stock Options; (ii) to determine the number of Awards or Stock Options to be granted to an Employee or Selected Person; (iii) to determine the time or times at which Awards or Stock Options shall be granted; (iv) to establish the terms and conditions upon which Awards or Stock Options may be exercised; (v) to remove or adjust any restrictions and conditions upon Awards or Stock Options; (vi) to specify, at the time of grant, provisions relating to exercisability of Stock Options and (vii) to accelerate or otherwise modify the exercisability of any Stock Options; (viii) and to adopt such rules and regulations and to make all other determinations deemed necessary or desirable for the administration of the Plan. All interpretations and constructions of the Plan by the Board, and all of its actions hereunder, shall be binding and conclusive on all persons for all purposes.

If the Company is to be consolidated with or acquired by another entity in a merger, sale of all or substantially all of the Company's assets other than a transaction to merely change the state of incorporation (a

Corporate Transaction ), the Board or the board of directors of any entity assuming the obligations of the Company hereunder (the Successor Board ), shall, as to outstanding Options, either (i) make appropriate provision for the continuation of such Options by substituting on an equitable basis for the Shares then subject to such Options either the consideration payable with respect to the outstanding shares of Common Stock in connection with the Corporate Transaction or securities of any successor or acquiring entity; or (ii) upon written notice to the Participants, provide that all Options must be exercised (either to the extent then exercisable or, at the discretion of the Board or, upon a change of control of the Company, all Options being made fully exercisable for purposes of this Subparagraph), within a specified number of days of the date of such notice, at the end of which period the Options shall terminate; or (iii) terminate all Options in exchange for a cash payment equal to the excess of the Fair Market Value of the Shares subject to such Options (either to the extent then exercisable or, at the discretion of the Board, all Options being made fully exercisable for purposes of this Subparagraph) over the exercise price thereof.

The Company hereby agrees to indemnify and hold harmless each Board member and each employee of the Company, and the estate and heirs of such Board member or employee, against all claims, liabilities, expenses, penalties, damages or other pecuniary losses, including legal fees, which such Board member or employee, his or her estate or heirs may suffer as a result of his or her responsibilities, obligations or duties in connection with the Plan, to the extent that insurance, if any, does not cover the payment of such items. No member of the Committee or the Board shall be liable for any action or determination made in good faith with respect to the Plan or any Award or Stock Option granted pursuant to the Plan.

### **1.3 Eligibility and Participation.**

Individuals eligible under the Plan shall be approved by the Board from those Employees and Selected Persons who, in the opinion of the management of the Company, are in positions that enable them to make significant and extraordinary contributions to the long-term performance and growth of the Company. In selecting Employees and Selected Persons to whom Stock Options or Awards may be granted, consideration shall be given to such factors including but not limited to employment position, duties and responsibilities, ability, productivity, length of service, morale, interest in the Company and recommendations of supervisors.

The Board will, in its sole discretion, approve the participants in the Plan, provided, however, that each participant must be an Employee or Selected Person of the Company or subsidiary at the time an Option is granted. Notwithstanding the foregoing, the Committee may authorize the grant of an Option to a person not then an Employee of the Company; provided, however, that the actual grant of such Option shall be conditioned upon such person becoming eligible to become a participant at or prior to the time of the execution of the Option Agreement evidencing such Option. Statutory Stock Options (Incentive Stock Options) may be granted only to Employees. Non-statutory Stock Options (Non-qualified Options) may be granted to any Employee or Selected Person of the Company. The granting of any Option to any individual shall neither entitle that individual to, nor disqualify him or her from, participation in any other grant of stock options.

### **1.4 Shares Subject to the Plan.**

Subject to adjustment as provided in Section 4.1, the maximum number of shares of Common Stock that may be issued pursuant to the Plan shall be nine hundred and fifty thousand (950,000). If shares of Common Stock awarded or issued under the Plan are reacquired by the Company due to forfeiture or for any other reason, such shares shall be cancelled and thereafter shall again be available for purposes of the Plan. If a Stock Option expires, terminates or is cancelled for any reason without having been exercised in full, the shares of Common Stock not purchased thereunder shall again be available for purposes of the Plan.

ARTICLE 2

**PROVISIONS RELATING TO STOCK OPTIONS**

**2.1 Grants of Stock Options.**

The Board may grant Stock Options in such amounts, at such times, and to such Employees and Selected Persons nominated by the management of the Company as the Board, in its discretion, may determine. Stock Options granted under the Plan shall constitute Incentive Stock Options within the meaning of Section 422 of the Code, if so designated by the Board on the date of grant. The Board shall also have the discretion to grant Stock Options, which do not constitute Incentive Stock Options, and any such Stock Options shall be designated Non-statutory stock options by the Board on the date of grant.

The aggregate fair market value (determined as of the time an Incentive Stock Option is granted) of the Common Stock with respect to which incentive stock options are exercisable for the first time by any Employee during any one calendar year (under all plans of the Company and any parent or Subsidiary of the Company) may not exceed the maximum amount permitted under Section 422 of the Code (currently \$100,000.00). Non-statutory stock options shall not be subject to the limitations relating to incentive stock options contained in the preceding sentence.

Each Stock Option shall be evidenced by a written agreement (the Option Agreement ) in a form approved by the Board, which shall be executed on behalf of the Company and by the Employee or Selected Person to whom the Stock Option is granted, and which shall be subject to the terms and conditions of this Plan. In the discretion of the Board, Stock Options may include provisions (which need not be uniform), authorized by the Board in its discretion, that accelerate an Employee's rights to exercise Stock Options following a Change in Control , upon termination of such Employee employment by the Company without Cause or by the Employee for Good Reason, as such terms are defined in Section 3.1 hereof. The holder of a Stock Option shall not be entitled to the privileges of stock ownership as to any shares of Common Stock not actually issued to such holder.

**2.2 Purchase Price.**

The purchase price (the Exercise Price ) of shares of Common Stock subject to each Stock Option ( Option Shares ) shall be fixed by the Board. In regard to the grant of an Incentive Stock Option, the exercise price shall not be less than one hundred percent (100%) of the Fair Market Value per share of Common Stock on the issuance date. Notwithstanding the foregoing, the Exercise Price of Option Shares subject to an Incentive Stock Option granted to an Employee who at the time of grant owns stock possessing more than 10% of the total combined voting power of all classes of stock of the Company or of any parent or Subsidiary shall be at least equal to 110% of the Fair Market Value of such shares on the date of grant of such Stock Option. The exercise price for Non-statutory Options shall be determined by the Board and may be less than Fair Market Value.

Fair Market Value means, as of any date, the value of Common Stock determined as follows: (i) If the Common Stock is listed on a national securities exchange or traded in the over-the-counter market and sales prices are regularly reported for the Common Stock, its Fair Market Value shall be the closing or last price of the Common Stock on the Composite Tape or other comparable reporting system for the trading day immediately preceding the date of determination;

or (ii) If the Common Stock is not traded on a national securities exchange, but is traded on the over-the-counter market, and if sales prices are not regularly reported for the Common Stock for the trading day and if bid and asked prices for the Common Stock are regularly reported, then its Fair Market Value shall be the mean between the bid and the asked price for the Common Stock at the close of trading in the over-the-counter market for the trading day on which Common Stock was traded immediately preceding the date of determination; or (iii) If the Common Stock is neither listed on a national securities exchange nor regularly traded in the over-the-counter market in such volume so as to reasonably establish true marketable value, the Fair Market Value shall be determined in good faith by the Board consistent with past practice.

### **2.3 Option Period.**

The Stock Option period (the Term) shall commence on the date of grant of the Stock Option and shall be ten (10) years or such shorter period as is determined by the Board. Notwithstanding the foregoing, the Term of an Incentive Stock Option granted to an Employee or Selected Person who at the time of grant owns stock possessing more than 10% of the total combined voting power of all classes of stock of the Company or of any parent or Subsidiary shall not exceed five (5) years.

Each Stock Option shall provide that it is exercisable over its term in such periodic installments as the Board in its sole discretion may determine. Such provisions need not be uniform. Unless otherwise provided for by the Board in the grant of the Stock Option, any Stock Option granted hereunder shall be exercisable in full immediately upon grant. Notwithstanding the foregoing, but subject to the provisions of Sections 1.2 and 2.1, Stock Options granted to Employees and Selected Persons who are subject to the reporting requirements of Section 16(a) of the Exchange Act (Section 16 Reporting Persons) shall not be exercisable until at least six months and one day from the date the Stock Option is granted unless the Board adjusts the waiting period as they deem appropriate. The adjustment of the waiting period is to give the Company an ability to attract and retain qualified individuals.

### **2.4 Exercise of Options.**

Each Stock Option may be exercised in whole or in part (but not as to fractional shares) by delivering it for surrender or endorsement to the Company, attention of the President, at the principal office of the Company, together with payment of the Exercise Price and an executed Notice and Agreement of Exercise in a form prescribed by the following paragraph. Payment may be made (i) in cash, (ii) by cashier's or certified check, (iii) by surrender of previously owned shares of the Company's Common Stock valued pursuant to Section 2.2 (if the Board authorizes payment in stock in its discretion), or (iv) in the discretion of the Board, by the delivery to the Company of the Optionee's promissory note secured by the Option Shares, bearing interest at a rate sufficient to prevent the imputation of interest under Sections 483 or 1274 of the Code, and having such other terms and conditions as may be satisfactory to the Board.

Exercise of each Stock Option is conditioned upon the agreement of the Employee or Selected Person to the terms and conditions of this Plan and of such Stock Option as evidenced by the Employee's or Selected Person's execution and delivery of a Notice and Agreement of Exercise in a form to be determined by the Board in its discretion. Such Notice and Agreement of Exercise shall set forth the agreement of the Employee or Selected Person that: (a) no Option Shares will be sold or otherwise distributed in violation of the Securities Act of 1933 (the Securities Act) or any other applicable federal or state securities laws, (b) each Option Share certificate may be imprinted with legends reflecting any applicable federal and state securities law restrictions and conditions, (c) the Company may comply with said securities law restrictions and issue stop transfer instructions to its Transfer Agent and Registrar without liability, (d) if the Employee or Selected Person is a Section 16 Reporting Person, said person will furnish to the Company a copy of each Form 4 or Form 5 filed by said Employee or Selected Person and will timely file all reports required under federal securities laws, and (e) the Employee or Selected Person will report all sales of Option Shares to the Company in writing on a form prescribed by the Company.

No Stock Option shall be exercisable unless and until any applicable registration or qualification requirements of federal and state securities laws, and all other legal requirements, have been fully complied with. The Company will use reasonable efforts to file and maintain the effectiveness of a Registration Statement under the Securities Act for the issuance of Stock Options and shares acquired thereunder, but there may be times when no such Registration Statement will be currently effective. The Company shall have no obligation to file any Registration Statement, but may do so solely at the discretion of the Board. The exercise of Stock Options may be temporarily suspended without liability to the Company during times when no such Registration Statement is currently effective, or during times when, in the reasonable opinion of the Board, such suspension is necessary to preclude violation of any requirements of applicable law or regulatory bodies having jurisdiction over the Company. If any Stock Option would expire for any reason except the end of its term during such a suspension, then if exercise of such Stock Option is duly tendered before its expiration, such Stock Option shall be exercisable and exercised (unless the attempted exercise is withdrawn) as of the first day after the end of such suspension.

**2.5 Continuous Employment.**

Except as provided in Section 2.7 below, an Employee may not exercise a Stock Option unless from the date of grant to the date of exercise such Employee remains continuously in the employ of the Company. For purposes of this Section 2.5, the period of continuous employment of an Employee with the Company shall be deemed to include (without extending the term of the Stock Option) any period during which such Employee is on leave of absence with the consent of the Company, provided that such leave of absence shall not exceed three months and that such Employee returns to the employ of the Company at the expiration of such leave of absence. If such Employee fails to return to the employ of the Company at the expiration of such leave of absence, such Employee's employment with the Company shall be deemed terminated as of the date such leave of absence commenced. The continuous employment of an Employee with the Company shall also be deemed to include any period during which such Employee is a member of the Armed Forces of the United States, provided that such Employee returns to the employ of the Company within 90 days (or such longer period as may be prescribed by law) from the date such Employee first becomes entitled to discharge. If an Employee does not return to the employ of the Company within 90 days (or such longer period as may be prescribed by law) from the date such Employee first becomes entitled to discharge, such Employee's employment with the Company shall be deemed to have terminated as of the date such Employee's military service ended.

**2.6 Restrictions on Transfer.**

Each Stock Option granted under this Plan shall be transferable only by will or the laws of descent and distribution. No interest of any Employee or Selected Person under the Plan shall be subject to attachment, execution, garnishment, sequestration, the laws of bankruptcy or any other legal or equitable process. Each Stock Option granted under this Plan shall be exercisable during an Employee's or Selected Person's lifetime only by such Employee or Selected Person or by such Employee's or Selected Person's legal representative.

**2.7 Termination of Employment.**

Upon an Employee's or Selected Person's Retirement, Disability or death, (a) all Stock Options to the extent then presently exercisable shall remain in full force and effect and may be exercised pursuant to the provisions thereof, including expiration at the end of the fixed term thereof, and (b) unless otherwise provided by the Board, all Stock Options to the extent not then presently exercisable by such Employee or Selected Person shall terminate as of the date of such termination of employment or service and shall not be exercisable thereafter.

Upon the termination of the employment of an Employee or Selected Person with the Company for any reason other than the reasons set forth above, (a) all Stock Options to the extent then presently exercisable by such Employee or Selected Person shall remain exercisable only for a period of 90 days after the date of such termination of employment or service (except that the 90-day period shall be extended to 12 months if the Employee or Selected Person shall die during such 90-day period), and may be exercised pursuant to the provisions thereof, including expiration at the end of the fixed term thereof, and (b) unless otherwise provided by the Board, all Stock Options to the extent not then presently exercisable by such Employee or Selected Person shall terminate as of the date of such termination of employment or service and shall not be exercisable thereafter.

**For purposes of this Plan:**

Retirement shall mean an Employee's or Selected Person's retirement from the employ of the Company on or after the date on which such Employee or Selected Person attains the age of sixty-five (65) years; and

Disability shall mean total and permanent incapacity of an Employee or Selected Person, due to physical impairment or legally established mental incompetence, to perform the usual duties of such Employee's or Selected Person's employment with the Company, which disability shall be determined: (i) on medical evidence by a licensed physician designated by the Board, or (ii) on evidence that the Employee or Selected Person has become entitled to receive primary benefits as a disabled employee under the Social Security Act in effect on the date of such disability.



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ARTICLE 3

**PROVISIONS RELATING TO AWARDS**

**3.1 Grant of Awards.**

Subject to the provisions of the Plan, the Board shall have full and complete authority, in its discretion, but subject to the express provisions of this Plan, to (i) grant Awards pursuant to the Plan, (ii) determine the number of shares of Common Stock subject to each Award ( Award Shares ), (iii) determine the terms and conditions (which need not be identical) of each Award, including the consideration (if any) to be paid by the Employee or Selected Person for such Common Stock, which may, in the Board's discretion, consist of the delivery of the Employee's or Selected Person's promissory note meeting the requirements of Section 2.5, (iv) establish and modify performance criteria for Awards, and (v) make all of the determinations necessary or advisable with respect to Awards under the Plan.

Each award under the Plan shall consist of a grant of shares of Common Stock subject to a restriction period (after which the restrictions shall lapse), which shall be a period commencing on the date the award is granted and ending on such date as the Board shall determine (the Restriction Period ). The Board may provide for the lapse of restrictions in installments, for acceleration of the lapse of restrictions upon the satisfaction of such performance or other criteria or upon the occurrence of such events as the Board shall determine, and for the early expiration of the Restriction Period upon an Employee's or Selected Person's death, Disability or Retirement as defined in Section 2.7, or, following a Change of Control, upon termination of an Employee's or Selected Person's employment by the Company without Cause or by the Employee or Selected Person for Good Reason, as those terms are defined herein.

**For purposes of this Plan:**

Change of Control shall be deemed to occur (a) on the date the Company first has actual knowledge that any person (as such term is used in Sections 13(d) and 14(d) (2) of the Exchange Act) has become the beneficial owner (as defined in Rule 13(d)-3 under the Exchange Act), directly or indirectly, of securities of the Company representing 40% or more of the combined voting power of the Company's then outstanding securities, or (b) on the date the shareholders of the Company approve (i) a merger of the Company with or into any other corporation in which the Company is not the surviving corporation or in which the Company survives as a subsidiary of another corporation, (ii) a consolidation of the Company with any other corporation, or (iii) the sale or disposition of all or substantially all of the Company's assets or a plan of complete liquidation.

Cause, when used with reference to termination of the employment of an Employee or Selected Person by the Company for Cause, shall mean:

- a. the individual's continuing willful and material breach of his or her duties to the Company after he or she receives a demand from the Chief Executive of the Company or any other officer specifying the manner in which he or she has willfully and materially breached such duties, other than any such failure resulting from Disability of the individual or his or her resignation for Good Reason, as defined herein; or
- b. the conviction of a felony; or
- c. the commission of fraud in the course of his or her employment with the Company, such as embezzlement or other material and intentional violation of law against the Company; or
- d. the gross misconduct causing material harm to the Company.

Good Reason shall mean any one or more of the following, occurring following or in connection with a Change of Control and within 90 days prior to the Employee's or Selected Person's resignation, unless the Employee or Selected Person shall have consented thereto in writing:

- a. the assignment to the Employee of duties inconsistent with his or her executive status prior to the Change of Control or a substantive change in the officer or officers to whom he or she reports from the officer or officers to whom he or she reported immediately prior to the Change of Control; or



- b. the elimination or reassignment of a majority of the duties and responsibilities that were assigned to the Employee or Selected Person immediately prior to the Change of Control; or
- c. a reduction by the Company in the Employee's annual base salary as in effect immediately prior to the Change of Control; or
- d. the Company's requiring the Employee or Selected Person to be based anywhere outside a 35-mile radius from his or her place of employment immediately prior to the Change of Control, except for required travel on the Company's business to an extent substantially consistent with the Employee's or Selected Persons business travel obligations immediately prior to the Change of Control; or
- e. the failure of the Company to grant the Employee a performance bonus reasonably equivalent to the same percentage of salary the Employee normally received prior to the Change of Control, given comparable performance by the Company and the Employee; or

**3.2 Incentive Agreements.**

Each Award granted under the Plan shall be evidenced by a written agreement (an Incentive Agreement) in a form approved by the Board and executed by the Company and the Employee or Selected Person to whom the Award is granted. Each Incentive Agreement shall be subject to the terms and conditions of the Plan and other such terms and conditions as the Board may specify, including without limitation, terms that condition the issuance of Common Stock upon the achievement of one or more performance goals.

**3.3 Waiver of Restrictions.**

The Board may modify or amend any Award under the Plan or waive any restrictions or conditions applicable to such Awards; provided, however, that the Board may not undertake any such modifications, amendments or waivers if the effect thereof materially increases the benefits to any Employee or Selected Person, or adversely affects the rights of any Employee or Selected Person without his or her consent.

**3.4 Terms and Conditions of Awards.**

- a. Upon receipt of an Award of shares of Common Stock under the Plan, even during the Restriction Period, an Employee or Selected Person shall be the holder of record of the shares and shall have all the rights of a shareholder with respect to such shares, subject to the terms and conditions of the Plan and the Award.
- b. Except as otherwise provided in this Section 3.4, shares of Common Stock received pursuant to the Plan shall not be sold, exchanged, transferred, pledged, hypothecated or otherwise disposed of during the Restriction Period applicable to such shares. Any purported disposition of such Common Stock in violation of this Section 3.4 shall be null and void.
- c. If an Employee's or Selected Persons employment with the Company terminates prior to the expiration of the Restriction Period for an Award, subject to any provisions of the Award with respect to the Employee's or Selected Persons death, Disability or Retirement, or Change of Control, all shares of Common Stock subject to the Award shall be immediately forfeited by the Employee or Selected Person and reacquired by the Company, and the Employee or Selected Person shall have no further rights with respect to the Award. In the discretion of the Board, an Incentive Agreement may provide that, upon the forfeiture by an Employee or Selected Person of Award Shares, the Company shall repay to the Employee or Selected Person the consideration (if any) which the Employee or Selected Person paid for the Award Shares on the grant of the Award. In the discretion of the Board, an Incentive Agreement may also provide that such repayment shall include an interest factor on such consideration from the date of the grant of the Award to the date of such repayment.

- d. The Board may require under such terms and conditions as it deems appropriate or desirable that (i) the certificates for Common Stock delivered under the Plan are to be held in custody by the Company or a person or institution designated by the Company until the Restriction Period expires, (ii) such certificates shall bear a legend referring to the restrictions on the Common Stock pursuant to the Plan, and (iii) the Employee or Selected Person shall have delivered to the Company a stock power endorsed in blank relating to the Common Stock.
- e. Shares of Common Stock issued under the Plan may, in the discretion of the Board, be fully and immediately vested upon issuance or may vest in one or more installments over the participant's period of employment or service or upon attainment of specified performance objectives. The Board shall determine the elements of the vesting schedule applicable to any unvested shares of Common Stock issued under the Plan. The participant shall have full stockholder rights with respect to any shares of Common Stock issued to the participant under the Plan, whether or not the participant's interest in those shares is vested. Accordingly, the participant shall have the right to vote such shares and to receive cash dividends, if any, paid on such shares.
- f. The Board may in its discretion waive the surrender and cancellation of one or more unvested shares of Common Stock, which would otherwise occur upon the cessation of the Participant's Service or the non-attainment of the performance objectives applicable to those shares. Such waiver shall result in the immediate vesting of the participant's interest in the shares of Common Stock as to which the waiver applies. Such waiver may be effected at any time, whether before or after the participant's cessation of employment or service or the attainment or non-attainment of the applicable performance objectives.

#### ARTICLE 4

#### MISCELLANEOUS PROVISIONS

##### 4.1 Adjustments Upon Change in Capitalization.

The number and class of shares subject to each outstanding Stock Option, the Exercise Price thereof (but not the total price), the maximum number of Stock Options that may be granted under the Plan, the minimum number of shares as to which a Stock Option may be exercised at any one time, and the number and class of shares subject to each outstanding Award, may be proportionately adjusted in the event of any increase or decrease in the number of the issued shares of Common Stock which results from a stock split or reverse stock split, payment of a stock dividend exceeding a total of 10% for which the record dates occur in any one fiscal year, a recapitalization (other than the conversion of certain convertible securities according to their terms), a combination of shares or other like capital adjustment, or any other increase or decrease in the number of issued Common Stock effected without receipt of consideration by the Company so that:

- (i) upon exercise of the Stock Option, the Employee or Selected Person shall receive the number and class of shares such Employee or Selected Person would have received had such Employee or Selected Person been the holder of the number of shares of Common Stock for which the Stock Option is being exercised upon the date of such change or increase or decrease in the number of issued shares of the Company, and
- (ii) upon the lapse of restrictions of the Award Shares, the Employee or Selected Person shall receive the number and class of shares such Employee or Selected Person would have received if the restrictions on the Award Shares had lapsed on the date of such change or increase or decrease in the number of issued shares of the Company. Notwithstanding the above, the Board may in its discretion, not subject the employee's stock options and/or awards to any decreases in the in the number of shares issued resulting from stock splits, dividends, recapitalization and/or any other actions of the Company that reduce the number of shares outstanding. In the event of adjustments that increase the number of shares outstanding, the employee's stock options and/or awards will be proportionately adjusted.

Upon a reorganization, merger or consolidation of the Company with one or more corporations as a result of which IAI is not the surviving corporation or in which IAI survives as a wholly-owned subsidiary of another

corporation, or upon a sale of all or substantially all of the property of the Company to another corporation, or any dividend or distribution to shareholders of more than 25% of the Company's assets, adequate adjustment or other provisions may be made by the Company or other party to such transaction so that there shall remain and/or be substituted for the Option Shares and Award Shares provided for herein, the shares, securities or assets which would have been issuable or payable in respect of or in exchange for such Option Shares and Award Shares then remaining, as if the Employee or Selected Person had been the owner of such shares as of the applicable date. Any securities so substituted shall be subject to similar successive adjustments.

The Board may in its discretion, not subject the number of shares allocated to the Plan to any changes in the number of shares issued resulting from stock splits, dividends, recapitalization and/or any other action of the Company that affect the number of shares outstanding.

#### **4.2 Withholding Taxes.**

The Company shall have the right at the time of exercise of any Stock Option, the grant of an Award, or the lapse of restrictions on Award Shares, to make adequate provision for any federal, state, local or foreign taxes which it believes are or may be required by law to be withheld with respect to such exercise ( Tax Liability ), to ensure the payment of any such Tax Liability. The Company may provide for the payment of any Tax Liability by any of the following means or a combination of such means, as determined by the Board in its sole and absolute discretion in the particular case: (i) by requiring the Employee or Selected Person to tender a cash payment to the Company, (ii) by withholding from the Employee's salary or Selected Person's payment, (iii) by withholding from the Option Shares which would otherwise be issuable upon exercise of the Stock Option, or from the Award Shares on their grant or date of lapse of restrictions, that number of Option Shares or Award Shares having an aggregate fair market value (determined in the manner prescribed by Section 2.2) as of the date the withholding tax obligation arises in an amount which is equal to the Employee's or Selected Person's Tax Liability or (iv) by any other method deemed appropriate by the Board. Satisfaction of the Tax Liability of a Section 16 Reporting Person may be made by the method of payment specified in clause (iii) above only if the following two conditions are satisfied:

- a. the withholding of Option Shares or Award Shares and the exercise of the related Stock Option occur at least six months and one day following the date of grant of such Stock Option or Award; and
- b. the withholding of Option Shares or Award Shares is made either (i) pursuant to an irrevocable election ( Withholding Election ) made by such Employee or Selected Person at least six months in advance of the withholding of Options Shares or Award Shares, or (ii) on a day within a ten-day window period beginning on the third business day following the date of release of the Company's quarterly or annual summary statement of sales and earnings.

Anything herein to the contrary notwithstanding, a Withholding Election may be disapproved by the Board at any time.

#### **4.3 Amendments and Termination.**

The Board of Directors may at any time suspend, amend or terminate this Plan provided, however, that any such earlier termination shall not affect any Option Agreements executed prior to the effective date of such termination. No amendment or modification of this Plan may be adopted, except subject to stockholder approval, which would: (a) materially increase the benefits accruing to Employees or Selected Persons and officers under this Plan, (b) materially increase the number of securities which may be issued under this Plan (except for adjustments pursuant to Section 4.1 hereof), or (c) materially modify the requirements as to eligibility for participation in the Plan.

#### **4.4 Successors in Interest.**

The provisions of this Plan and the actions of the Board shall be binding upon all heirs, successors and assigns of the Company and of Employees, Selected Persons and officers.

**4.5 Other Documents.**

All documents prepared, executed or delivered in connection with this Plan (including, without limitation, Option Agreements and Incentive Agreements) shall be, in substance and form, as established and modified by the Board; provided, however, that all such documents shall be subject in every respect to the provisions of this Plan, and in the event of any conflict between the terms of any such document and this Plan, the provisions of this Plan shall prevail.

**4.6 No Obligation to Continue Employment.**

This Plan and grants hereunder shall not impose any obligation on the Company to continue to employ any Employee or Selected Person. Moreover, no provision of this Plan or any document executed or delivered pursuant to this Plan shall be deemed modified in any way by any employment contract between an Employee (or other employee) or Selected Person and the Company.

**4.7 Misconduct of an Employee.**

Notwithstanding any other provision of this Plan, if an Employee or Selected Person commits fraud or dishonesty toward the Company or wrongfully uses or discloses any trade secret, confidential data or other information proprietary to the Company, or intentionally takes any other action materially inimical to the best interests of the Company, as determined by the Board, in its sole and absolute discretion, such individual shall forfeit all rights and benefits under this Plan.

**4.8 Term of Plan.**

The Plan shall become effective on the date of its adoption by the Board subject to the approval of the Plan by the holders of the majority of the voting shares of stock of the Company represented at a meeting of the shareholders, within twelve (12) months of the effective date. No Stock Options or Awards shall be awarded pursuant to the Plan after the expiration of the ten-year period beginning on the date the Plan is adopted by the Board.

**4.9 Governing Law.**

This Plan shall be construed in accordance with, and governed by, the laws of the State of Virginia.

**4.10 Shareholder Approval.**

No Stock Option shall be exercisable, or Award granted, unless and until the Shareholders of the Company have approved this Plan and all other legal requirements have been fully complied with.

**4.11 Notice to Company of Disqualifying Disposition**

Each Employee who receives an Incentive Stock Option must agree to notify the Company in writing immediately after the Employee makes a Disqualifying Disposition of any shares acquired pursuant to the exercise of an Incentive Stock Option. A Disqualifying Disposition is defined in Section 424(c) of the Code and includes any disposition (including any sale or gift) of such shares before the later of (a) two years after the date the Employee was granted the Incentive Stock Option, or (b) one year after the date the Employee acquired Shares by exercising the Incentive Stock Option, except as otherwise provided in Section 424(c) of the Code. If the Employee has died before such stock is sold, these holding period requirements do not apply and no Disqualifying Disposition can occur thereafter.

**4.12 Compliance With Rule 16B-3.**

Transactions under the Plan are intended to comply with all applicable conditions of Rule 16b-3. To the extent that any provision of the Plan or action by the Board fails to so comply, it shall be deemed null and void, to the extent permitted by law and deemed advisable by the Board.

**4.13 Other Considerations**

The Board may require each participant acquiring Common Stock pursuant to awards granted hereunder to represent to and agree with the Company in writing that such person is acquiring the Common Stock without a view to distribution thereof. The certificates for such Common Stock may include any legend that the Board deems appropriate to reflect any restrictions on transfer. All certificates for Common Stock issued pursuant to this Plan shall be subject to such stock transfer orders and other restrictions as the Board may deem advisable under the rules, regulations and other requirements of the Securities and Exchange Commission, any stock exchange upon which the Common Stock is then listed or interdealer quotation system upon which the Common Stock is then quoted, and any applicable federal or state securities laws. In the absence of an effective registration statement under the securities Act of 1933, as amended, the Board may place a legend or legends on any such certificates to make appropriate references to such restrictions.

**4.14 Limitation on Issuance of Certificate**

The Company shall not be required to issue any certificate or certificates for Common Stock with respect to awards granted under this Plan, or record any person as a holder of record of such Common Stock, without obtaining, to the complete satisfaction of the Board, the approval of all regulatory bodies deemed necessary by the Board, and without complying to the Board's complete satisfaction, with all rules and regulations, under federal, state or local law deemed applicable by the Board.

IN WITNESS WHEREOF, this Plan has been adopted as of April 12, 2006

INFORMATION ANALYSIS, INC.

By:  
Sandor Rosenberg, Chairman of the Board

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**INFORMATION ANALYSIS INCORPORATED**

**PROXY**

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THIS PROXY IS SOLICITED ON BEHALF OF THE BOARD OF DIRECTORS OF INFORMATION ANALYSIS INCORPORATED

The undersigned hereby appoints Richard S. DeRose with the power to appoint his substitute, and hereby authorizes him to represent and to vote, as designated below, all the shares of common stock of Information Analysis Incorporated held on record by the undersigned on April 12, 2006, at the annual meeting of the stockholders to be held on May 18, 2006 or any adjournment thereof.

Please sign, date, and return promptly in the enclosed envelope. Please mark your vote in blue or black ink as shown here    x

1. ELECTION OF DIRECTORS

..      FOR all nominees.

..      WITHHOLD AUTHORITY for all nominees.

..      FOR ALL EXCEPT (see instructions below)

**INSTRUCTION:**      To withhold authority to vote for any individual nominee(s), mark **FOR ALL EXCEPT** and fill the circle next to each nominee you wish to withhold, as shown here    n

..      Charles A. May, Jr

..      Sandor Rosenberg

..      Bonnie K. Wachtel

..      James D. Wester

2. RATIFICATION OF INDEPENDENT PUBLIC ACCOUNTANTS

..      FOR the ratification of Reznick Group, P.C. as the independent public accountants.

..      AGAINST the ratification of Reznick Group, P.C. as the independent public accountants.

..      ABSTAIN from ratification of Reznick Group, P.C. as the independent public accountants.



3. APPROVAL OF THE IAI 2006 STOCK INCENTIVE PLAN

“ FOR the approval of the IAI 2006 Stock Incentive Plan.

“ AGAINST the approval of the IAI 2006 Stock Incentive Plan.

“ ABSTAIN from the approval of the IAI 2006 Stock Incentive Plan.

4. In his discretion, the proxy is authorized to vote upon such other business as may properly come before the meeting. **THIS PROXY WHEN PROPERLY EXECUTED WILL BE VOTED IN THE MANNER DIRECTED HEREIN BY THE UNDERSIGNED STOCKHOLDER. IF NO DIRECTION IS MADE, THIS PROXY WILL BE VOTED IN FAVOR OF THE ELECTION OF EACH OF THE NOMINEES FOR DIRECTOR AND FOR THE SELECTION OF REZNICK GROUP, P.C. AS INDEPENDENT PUBLIC ACCOUNTANTS.**

Note: Please sign exactly as your names appear on this Proxy. When shares are held jointly, each holder should sign. When signing as executor, administrator, attorney, trustee, or guardian, please give full title as such. If the signer is a corporation, please sign full corporate name by duly authorized officer, giving full title as such. If signer is a partnership, please sign in partnership name by authorized person.

PLEASE DATE, SIGN, AND MAIL YOUR PROXY CARD IN THE ENVELOPE PROVIDED AS SOON AS POSSIBLE.

Signature of Stockholder

Date

Signature of Stockholder

Date