

NEW MEXICO SOFTWARE, INC
Form 10-K
March 30, 2012

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES

EXCHANGE ACT OF 1934

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2011

COMMISSION FILE #333-30176

NEW MEXICO SOFTWARE, INC.

(Exact name of registrant as specified in its charter)

NEVADA

(State or other jurisdiction of incorporation or organization)

91-1287406

(I.R.S. Employer Identification No.)

5021 INDIAN SCHOOL RD., SUITE 100

ALBUQUERQUE, NEW MEXICO 87110

(Address of principal executive offices)(Zip code)

(505) 255-1999

(Issuer's telephone number)

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT: NONE

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT: NONE

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act
YES NO

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the
Act YES NO

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company.

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company [X]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
YES NO [X]

AGGREGATE MARKET VALUE OF THE VOTING COMMON STOCK HELD BY NON-AFFILIATES OF THE REGISTRANT ON DECEMBER 31, 2011 WAS: \$3,527,388

THE NUMBER OF SHARES OUTSTANDING OF THE ISSUER'S COMMON STOCK AT MARCH 21, 2012 WAS: 146,974,488.

DOCUMENTS INCORPORATED BY REFERENCE

None

PART I

ITEM 1. DESCRIPTION OF BUSINESS

Our History and Background

Our business was incorporated in New Mexico in 1996 under the name of New Mexico Software, Inc. We were acquired by Raddatz Exploration, Inc., a publicly traded Delaware corporation, in 1999. At that time, Raddatz changed its name to NMXS.com, Inc., and operated New Mexico Software, Inc. as a wholly-owned subsidiary. On January 1, 2006, NMXS.com, Inc. merged into its newly incorporated, wholly-owned subsidiary, New Mexico Software, Inc., a Nevada corporation, for the sole purpose of changing its state of incorporation and its name. In May 2008, we created a wholly-owned subsidiary called Telerad Service, Inc. to provide radiological services.

Our primary address on the World Wide Web is www.nmxc.com. Additional web addresses also are available, www.nmxc.net and www.netmedical.com, which broadcast the same information as www.nmxc.com. The information at that web site is not part of our annual report, and we specifically disclaim any liability under federal securities law related to the web site.

Our Business

We currently operate under three business units.

The parent company, New Mexico Software, now operating under the trade name of Net Medical Xpress Solutions, primarily provides Picture Archiving and Communication System (PACS) hardware and software to hospitals and other medical facilities. We have received a 510k-clearance from the federal Food and Drug Administration for our PACs, which is HIPAA-compliant. We sell our PACS, trade named XR-Express, to medical facilities and also provide it as a hosted Software as a Service (SaaS), where the customer is billed on a monthly basis according to usage. The SaaS option allows our customers to optimize their operations without investing significant time and money on upfront costs for hardware, software, tech support and training.

Our wholly-owned subsidiary, Telerad Service, Inc., now operating under the trade name Net Medical Xpress Services, provides medical diagnostic reading services. We provide reports for X-rays, echocardiograms, EKGs, CTs, MRIs, and other diagnostic modalities for over 15,600 facilities in the U.S. We have forty radiologists and fifteen cardiologists providing services 24 hours per day, seven days per week, 365 days per year.

The parent company, New Mexico Software, now operating in part under the trade name Net Medical Xpress Specialists, provides telemedicine services to remote hospitals and other medical entities. At this time, we have specialists credentialed to provide services for neurology and stroke evaluation and cardiology. In addition, we anticipate providing specialists in the areas of orthopedics, infectious disease, renal exams, retinal scans, psychology and dermatology. The specialist program began pilot operations in neurology and stroke evaluation at a hospital in New Mexico in November 2011. We currently expect to provide this service to a number of other hospitals during the first half of 2012. This program has been in development since 2010 and will provide patient care 24 hours per day, seven days per week, 365 days per year, initially in New Mexico and Arizona, followed by additional states later in 2012.

Our Products and Services

XR-EXpress: XR-EXpress is our flagship software system. It enables medical providers to examine multiple types of medical images over the Internet. The originating medical facility or service provider uploads medical images as high-resolution DICOM (digital imaging and communications in medicine) files to our secure servers. The DICOM files are tagged with patient information. The radiologist then accesses the images on our secure servers through his or her own computer and returns the diagnostic report to our secure server for access by the treating physician.

XR-EXpress significantly reduces the time between the imaging events and report delivery. Our workflow technology provides scheduling, dispatching, monitoring and reporting functions, which boosts the customer's efficiency and productivity while enhancing patient care. The 501(k) clearance as a Class II Medical Device allows us to market XR-EXpress in the United States under FDA general control provisions, including requirements for annual registration of devices, good manufacturing practice, labeling, and prohibitions against misbranding and adulteration.

We believe that this will provide increased assurance to potential new customers regarding the quality of XR-EXpress, which will result in increased marketing opportunities for us in the future.

XR-Express is also the platform used for our Net Medical Xpress Services and Net Medical Xpress Specialists business units. In the Specialist division, XR-Express enables a referring hospital to instantly transmit digital diagnostic images and reports to a consulting physician, providing a means for the consulting physician to aid the attending physician in applying the appropriate care. We believe XR-EXpress is especially useful when the patient is located a substantial distance from a Level I Trauma Facility and transport decisions must be made quickly and effectively, while keeping costs down. XR-EXpress enables remote hospitals to avoid unnecessary transports, more effectively utilize resources, make better triage and management decisions, and keep patients in their local facilities, thus saving money and facilitating superior patient care.

Cardiology PACS: We are collaborating with the New Mexico Heart Institute to develop cardiology and vascular extensions to our XR-EXpress software. By working with the experts at NMHI, we have added comprehensive and customizable support for cardiology services, including visualization, automated data collection, measurement tools, and report writing. These software extensions now allow the system to support echocardiograms, stress echocardiograms, dobutamine stress tests, exercise stress tests, nuclear exams, upper and lower venous and arterial exams, carotid exams, renal artery exams, and vascular wellness screening. The extensions run onsite at NMHI and backup to New Mexico Software cloud servers.

Net Medical Xpress Services: Net Medical Xpress Services is a full service telemedicine provider. We specialize in diagnosing all types of studies: plain film, ultrasound, CT, MRI, echocardiogram, nuclear bone scan, EKG, and fluoroscopy. The studies are read and diagnosed within a web-based environment using our XR-EXpress software. There is no overhead impact, and data integrity, security and HIPAA compliance are maintained. We are able to provide either final or preliminary reports depending on the customer's need. We have forty board-certified radiologists and fifteen board-certified cardiologists reading for us, and our operations team manages the workload for over 15,600 facilities on our system. Our response time averages fifteen minutes for plain film stats and eighteen minutes for most routine plain film exams.

Net Medical Xpress Neuro : Net Medical Xpress Neuro is one of the services offered in our Net Medical Xpress Specialists business unit. It is a web-based clinical telemedicine solution that eliminates unnecessary transport of patients from one medical facility to another by facilitating the real-time assessment of patients through a virtual examination. Our software converts CT scans and MRI's into 3-D images that reveal details not otherwise available. The specialist program can save lives by reducing the time required to diagnose and treat patients. Combined with real-time video conferencing, the *Net Medical Xpress Neuro* program enables neurologists in urban areas to diagnose and treat stroke patients at remote medical service areas. The high definition imaging and video system maintenance costs are part of the service and are maintained by us, minimizing costs for the customer.

Our Technology

Our technology is the key to our product differentiation. We engineer our products around a central core of unique Internet technology. This proprietary technology makes it possible to rapidly view, distribute and manage a variety of media files such as documents, graphic images, animation sequences, film clips, audio files, x-rays, other medical images and high-definition media streams. The value of our core technology is that it provides maximum flexibility in the presentation of digital images to the customer, and integrates general browsing capabilities with specific search capabilities in one product.

All of our products are accessed via the Internet. This means that the customer needs only a PC with browser capability to be able to use our products. No additional expensive equipment, software or tech support is required, and training is accomplished smoothly and quickly. The customer's data is available 24 hours per day, so that the customer can work according to his or her own schedule with productivity available around the clock. Additionally, documents and images can be viewed from or distributed anywhere in the world at any time.

Business Strategy

Our greatest growth over the preceding five years has been in the medical arena. Both the federal government and numerous state governments continue to allocate funds to initiate and improve telemedicine programs, particularly in underserved rural areas. We are confident that telemedicine will continue to be part of the solution to the growing health care costs in the country, and that our web-based products and services can contribute to this solution.

Telemedicine can provide safe, effective services while reducing costs in a wide variety of medical applications, such as avoiding unnecessary patient transports, providing support for hospital overflows, providing increased services in remote or rural areas, providing services in jails and prisons, decreasing the length of some patient stays, providing increased home management of chronic diseases, and increasing access to specialized services. Digital diagnostics systems in particular have demonstrated significantly improved image quality over the last few years, while costs continue to decrease. By providing enhanced diagnostic capabilities with quick turn-around times, telemedicine can potentially increase patient safety and reduce costs.

Because of the potential opportunities in telemedicine in the coming years, we will continue to focus the majority of our efforts in this area. We believe that we can continue to take advantage of the growth in the telemedicine market during the next few years to further expand our customer base and our revenues.

We expect that the restructuring of our business into the three business units of Net Medical Xpress Solutions, Net Medical Xpress Services and Net Medical Xpress Specialists will clarify our products and services and will facilitate our expansion into new service areas. Net Medical Xpress Solutions will continue to offer hosted software solutions for medical entities as well as offer XR-EXpress for sale to hospitals. Net Medical Xpress Services will continue to provide diagnostic reports for a variety of medical imaging studies 24 hours per day, seven days per week, 365 days per year. Net Medical Xpress Specialists will provide remote diagnostic services for several medical specialties, including stroke and other neurological assessments, cardiology, orthopedics, renal exams, dermatological and psychological assessments.

Our current strategy involves the following factors:

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Continue to emphasize the flexibility and affordability of our hosted applications. Our customers who prefer this service do not need extensive hardware, software or technology staff to use our products. Also, we are usually able to get new customers and doctors operational within days, sometimes within hours, including training.

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Expand our software product offerings by implementing strategies to sell XR-EXpress directly to hospitals.

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Continue to expand the services we offer. During 2012, we will be focusing on growing our Net Medical Xpress Specialist business unit by fine-tuning and expanding the stroke and neurological assessment program. We also are in the process of adding cardiological and orthopedic services, and we anticipate adding renal consults and dermatological and psychological assessments later in the year.

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Continue to offer exceptionally prompt and thorough customer service, with outstanding quality.

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Invest in our future by recruiting superior engineering and management personnel.

Competition

Other, better-financed companies may be developing similar products that could compete with our products. Such competition could have a material adverse effect on our business, financial condition, performance and prospects. While the Internet technology marketplace is extremely competitive, we believe we have a first-to-market advantage with our particular combination of products. In addition, although the current market for telemedicine and teleradiology is growing rapidly, they are also exceptionally competitive. Other highly capitalized companies that have recognized the potentials of digital image management products and telemedicine could overwhelm our advantage with expensive and expansive media blitzes that create the perception of a dominant market presence and/or superior products. If we are unsuccessful in addressing these risks and uncertainties, our business, results of operations, and financial condition will be materially and adversely affected. The risk factor inherent in the use of Open Source software development tools is the fact that a sophisticated competitor might be able to imitate our work and produce similar functionality. Any such imitation, should it occur, could have material adverse effects on our business, financial condition, performance and prospects.

Marketing and Customers

During the last several years we have concentrated nearly all of our efforts on developing and growing our medical services business. During this time, our most effective marketing tool has been customer referrals and direct sales. During 2012, we plan to continue this approach, along with targeted trade shows and occasional direct marketing to potential XR-Express and Net Medical Xpress Services customers, to further build our customer base and to sustain our progress in growing our revenues. Overall, we anticipate that our customer base will continue to broaden in the next year as we expand our services, particularly for Net Medical Xpress Specialists, giving more stability, steady growth, and predictability to our revenues.

Our Intellectual Properties

We have several proprietary aspects to our software that we believe make our products unique and desirable in the marketplace. We believe the compiled object code that is accessible to our customers makes it difficult to discover the source code needed to create other similar programs, even though the code we use originates from Open Source. Because we maintain our enterprise software code on dedicated servers in our Albuquerque data center, it provides better protection and security of our products.

We have entered into confidentiality and non-disclosure agreements with our employees and contractors in order to limit access to, and disclosure of, our proprietary information. There is no assurance that these contractual arrangements or the other steps we have taken to protect our intellectual property will prove sufficient to prevent misappropriation of our technology or to deter independent third-party development of similar technologies.

Although we do not believe that we infringe the proprietary rights of third parties, there is no assurance that third parties will not claim infringement by us with respect to past, current, or future technologies. We expect that participants in our markets will be increasingly subject to infringement claims as the number of services and competitors in our industry grows. Any such claim, whether meritorious or not, could be time-consuming, result in costly litigation, cause service upgrade delays, or require us to enter into royalty or licensing agreements. Such royalty or licensing agreements may not be available on terms acceptable to us or at all. As a result, any such claim could have a material adverse effect upon our business, results of operations, and financial condition.

Government Regulation

Our operations, products, and services are all subject to regulations set forth by various federal, state and local regulatory agencies. We take measures to ensure our compliance with all such regulations as promulgated by these agencies from time to time. The Federal Communications Commission sets certain standards and regulations regarding communications and related equipment.

The Health Insurance Portability and Accountability Act (HIPAA) imposes standards for the use, dissemination and disclosure of protected health information. Protected health information is any information about health status, provision of health care, or payment for health care that can be linked with an individual. The act applies to any company that transmits health care data. The act encourages the use of electronic transmission of data within the U.S. healthcare system, and provides three types of security safeguards that are required for compliance: administrative, physical and technical. For each of these types, HIPAA identifies various security standards

which must be adopted and administered by any entity covered by the act. Our software strictly adheres to the privacy and security standards dictated by HIPAA.

There are currently few laws and regulations directly applicable to the Internet. It is possible that a number of laws and regulations may be adopted with respect to the Internet covering issues such as user privacy, pricing, content, copyrights, distribution, antitrust and characteristics and quality of products and services. The growth of the market for online commerce may prompt calls for more stringent consumer protection laws that may impose additional burdens on companies conducting business online. Tax authorities in a number of states are currently reviewing the appropriate tax treatment of companies engaged in online commerce, and new state tax regulations may subject us to additional state sales and income taxes.

We have received 510(k) clearance from the FDA for our XR-Express product. XR-Express is the foundation of all our medically related products and services.

Employees

As of March 1, 2012, we had nineteen full-time and three part-time staff, including five in systems engineering and quality assurance; eleven in customer support; and six in administration. We also have forty radiologists, fifteen cardiologists and two neurologists on contract.

Item 1A. Risk Factors

A small number of customers represent a large amount of our revenues and the loss of such customers will result in a significant decrease in revenues and threaten our ongoing operations.

During the year ended December 31, 2011, one customer accounted for 35% of our revenue. During the year ended December 31, 2010, one customer accounted for 29% of our revenues. The loss of such customers would result in a significant decrease in our revenues. Such decrease will negatively impact our growth and threaten our ongoing operations.

A small number of customers represent a large amount of our accounts receivable and the failure to collect those balances will result in a significant decrease in cash flow and threaten our ongoing operations.

As of December 31, 2011, balances due from one customer comprised 43% of total accounts receivable. Failure to collect this balance would result in a significant decrease in our working cash flow. Such decrease will negatively impact our growth and threaten our ongoing operations.

Our business depends on a limited number of key personnel, the loss of whom could negatively affect us.

Richard F. Govatski and Teresa B. Dickey, our senior executives and major stockholders, are important to our success. If they become unable or unwilling to continue in their present positions, our business and financial results could be materially negatively affected.

If we fail to adequately manage our growth, we may not be successful in growing our business and becoming profitable.

We expect our business and number of employees to continue to grow over the next twelve months, particularly as Net Medical Xpress Specialists continues to add new customers. Our growth may place significant stress on our operations, management, employee base, and particularly on our ability to meet capital requirements necessary to support our growth. Any failure to address the needs of our growing business successfully could have a negative impact on our chance of success.

Our occasional reliance on issuances of shares of our common stock for services performed for us in lieu of paying for such services will result in dilution of your ownership percentage and could depress the market.

Occasionally, we have paid for services by issuing shares of our common stock, in lieu of paying cash, to our employees and other service providers. We may find it necessary to continue this practice from time to time. In the event we issue stock for services in the future, the issuance of such shares will result in the dilution of your investment in us.

Our ability to grow our medical services in order to achieve profitability depends on our ability to contract with qualified medical specialists. Inability to locate and attract licensed and qualified providers, or the loss of those under contract, could have a material negative impact on our future growth and profitability.

The current market for highly qualified medical specialists is competitive, with potential decreases in the coming years. If we are unable to locate and attract licensed and qualified medical specialists, we could have difficulty growing, or maintaining our medical services business, which would negatively impact our revenues and operations, as well as reducing our opportunities for becoming profitable.

The current telemedicine and teleradiology markets are competitive, and they are projected to become significantly more competitive in the next few years, which may make it difficult to attract and retain customers.

The markets for telemedicine in general and teleradiology in particular are exceptionally competitive and volatile at this time, and potential government intervention in the form of health care reform may increase these factors. In addition, the technology used in these industries is rapidly changing. If we are not able to continually adapt to the changing market conditions, we may experience difficulties attracting and retaining customers, which could have a materially adverse effect on our revenues and operations.

ITEM 1B. UNRESOLVED STAFF COMMENTS

We do not have any unresolved staff comments.

ITEM 2. DESCRIPTION OF PROPERTY

We currently lease a 3,000 square foot facility in Albuquerque, New Mexico, at a cost of approximately \$4,820 per month. The lease expires on April 30, 2014. The facility houses our administrative, marketing and engineering offices, and provides adequate room for expansion. It also contains an advanced telephone system which will provide the capability needed to provide adequate customer telephone support. We house our primary servers in a separate facility downstairs from ours, at a cost of approximately \$1,700 per month on a month-to-month basis. The two locations are networked together by fiber optics. In this facility we have access to a large power generator, which enables our servers to continue operating during power outages.

ITEM 3. LEGAL PROCEEDINGS

On January 23, 2012, the US District Court in Albuquerque, New Mexico entered judgment in favor of New Mexico Software in the case of Premier Medical Enterprise Solutions, Inc. v. New Mexico Software, Inc. and Richard Govatski, Case No. Civ 09-165. The judgment brings to conclusion the suit initiated by Premier Medical in early 2009, alleging breach of breaches of (i) fiduciary duty, (ii) covenant of good faith and fair dealing and (iii) contract, along with claims of conversion and tortious interference and seeks an accounting. The suit sought compensatory, punitive and exemplary damages in excess of \$75,000, together with injunctive relief against unfair competition and attorney's fees. The court awarded judgment to New Mexico Software in the amount of \$636,606.

Premier Medical had been an early client of our XR-Express services. Premier Medical withheld payment for services provided prior to filing suit and after suit until we terminated service in June 2010. In December 2010, we wrote off as uncollectible all accounts receivable from Premier Medical.

We are evaluating with the advice of counsel whether to pursue collection of our judgment against Premier Medical, its principals and its successor which appears to have taken an assignment of Premier Medical's business without consideration.

ITEM 4. MINE SAFETY DISCLOSURE

Not applicable.

PART II

ITEM 5. MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Market Information

Our stock is quoted on the OTC Bulletin Board under the symbol NMXC. The table below sets forth, for the periods indicated below, high and low bids for our common stock. These quotations reflect inter-dealer prices, without retail mark-up, mark-down or commission, and may not necessarily represent actual transactions. The source of this information is Big Charts: www.bigcharts.com.

| | <u>Quarter</u> | <u>High</u> | <u>Low</u> |
|-------------------|-----------------------|--------------------|-------------------|
| FISCAL YEAR ENDED | First | \$0.040 | \$0.030 |
| DECEMBER 31, 2010 | Second | \$0.035 | \$0.020 |
| | Third | \$0.051 | \$0.014 |
| | Fourth | \$0.045 | \$0.030 |
| FISCAL YEAR ENDED | First | \$0.048 | \$0.032 |
| DECEMBER 31, 2011 | Second | \$0.040 | \$0.026 |
| | Third | \$0.030 | \$0.019 |
| | Fourth | \$0.040 | \$0.017 |
| FISCAL YEAR ENDED | First | \$0.030 | \$0.020 |
| DECEMBER 31, 2012 | (Through March 5) | | |

Recent Sales of Unregistered Securities

The following table sets forth information about our unregistered sales of common stock during the year ended December, 2011:

| <u>Class of Purchaser</u> | <u>Aggregate Number of Shares</u> | <u>Consideration</u> |
|----------------------------------|--|-----------------------------|
| Contractors (1 person) | 338,894 | \$10,000 |
| Contract Doctors (3 persons) | 2,012,818 | \$64,000 |

All shares issued to contractors were in payment of invoices. Of the shares issued to our contract doctors, 512,818 were payment for additional services, and 1,500,000 were in return for cash.

We did not pay and to our knowledge no one acting on our behalf or paid any commissions of other compensation with respect to the sales identified in the foregoing table. We made the sale directly to each purchaser for the consideration stated in the table. We used any cash proceeds and any cash which would have been used to pay bonuses and contractor fees, but for the issue of the shares, for working capital in payment of current obligations. Each purchaser acknowledged the investment nature of the transaction and a legend was placed on each certificate, prohibiting public resale of the shares, except in compliance with Rule 144. We believe each purchaser has either (a) such relationship with us or (b) such knowledge and experience in business and financial transactions that he or she is able to understand and evaluate the risks and merits of investment in our common stock. We relied upon the exemption from the registration requirement of the Securities Act of 1933, as amended (the Act) provided in Section 4(2) of the Act and the rules and regulations thereunder, on grounds that these sales did not involve a public offering within the meaning of the Act.

No shares were issued in 2011 pursuant to stock issuance plans and related registration statements on Form S-8.

Shareholders

As of March 9, 2012, there were 364 holders of record of our common shares.

Dividends

We did not declare any cash dividends on our common stock during the year ended December 31, 2011. We have no plans to pay any dividends to the holders of our common stock in 2012.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS

The following discussion and analysis of financial condition and results of operations should be read in conjunction with the Consolidated Financial Statements and Notes thereto included elsewhere in this Form 10-K.

OVERVIEW

To more accurately reflect the range of our services and our commitment to the telemedicine market we are using the following trade names for our services: Net Medical Xpress Solutions, Net Medical Xpress Services and Net Medical Xpress Specialists.

Through December 31, 2011, we have realized revenues from four primary sources:

1.
radiological services
2.
software usage fees
3.
software hosting and maintenance services
4.
cardiology services

We also occasionally realize revenues from software sales, scanning services, custom programming services, hardware sales associated with the sales of our software products and other services.

Gross profit is our key indicator of operating progress. Net Medical Xpress Services generated a gross profit percentage of 17.3% during 2011 as compared to 19.0% during 2010. Approximately 81% of the cost of services for Net Medical Xpress Services is doctor fees, which are directly related to revenues. Therefore, we expect this percentage to remain relatively stable during 2012. Net Medical Xpress Services accounted for approximately 87% of our gross revenues during 2011. Net Medical Xpress Solutions generated a gross profit percentage of 47% during 2011 as compared to 50% during 2010. As a result, our overall gross profit percentage was 21.1% during 2011 as compared to 22% during 2010.

Our normal general and administrative expenses (including depreciation, R&D and interest expense, but not including legal fees related to the legal proceedings described in Part II) continue to be approximately \$200,000 to \$250,000 per quarter.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of our financial statements in conformity with accounting principles generally accepted in the United States requires our management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. As such, in accordance with the use of accounting principles generally accepted in the United States of America, our actual realized results may differ from management's initial estimates as reported. A summary of our significant accounting policies is detailed in the notes to the financial statements, which are an integral component of this filing.

Revenue Recognition

According to FASB ASC Topic 605, *Revenue Recognition*, revenue is recognized when a transaction occurs and 1) the revenue is realized or realizable and 2) the revenue is earned. Revenue from a transaction must meet both criteria in order to be recognized. Revenue is generally considered realized when cash is received for the sale of a product or performance of a service. Revenue generally becomes realizable when a promise to pay is received in exchange for the sale of a product or performance of a service.

The Company invoices its customers for radiological review services rendered by its contracted licensed radiology staff upon full completion and closure of the case review process.

With each sale of our enterprise-level products, the end user enters into a license agreement for which an initial license fee is paid. The license agreement also provides that in order to continue the license, the licensee must pay an annual software maintenance fee for which the party receives access to product upgrades and bug fixes or product patches. Software maintenance consists primarily of hosting and managing our customers' data on our servers, as well as technical support programs for our products. Software usage comprises any charges for actual usage of our software.

Currently, software usage consists of XR-EXpress report fees.

Our software recognition policies are in accordance with the ASC Topic 985, *Software Revenue Recognition* as amended. Revenue is recognized when (a) persuasive evidence of an arrangement exists, (b) delivery has occurred, (c) the fee is fixed or determinable, and (d) collectibility is probable. We follow the guidance in ASC Topic 605, *Accounting for Performance of Construction-Type and Certain Production-Type Contracts* for custom software development arrangements that require us to provide significant production, customization or modification to our core software. Revenue is generally recognized for such arrangements under the percentage of completion method. Amounts collected prior to satisfying the above revenue recognition criteria are included in deferred revenue.

We follow the guidance provided by SEC Staff Accounting Bulletin (SAB) No. 101, *Revenue Recognition in Financial Statements* and SAB No. 104 *Revenue Recognition* which provide guidance on the recognition, presentation and disclosure of revenue in financial statements filed with the SEC. Revenue from radiological services, software installation, training and consulting services is recognized when the services are rendered.

Software Development Costs

We account for software development costs in accordance with ASC Topic 985, *Accounting for Costs of Computer Software to be Sold, Leased, or Otherwise Marketed*. Product research and development expenses consist primarily of personnel, outside consulting and related expenses for development, and systems personnel and consultants and are charged to operations as incurred until technological feasibility is established. We consider technological feasibility to be established when all planning, designing, coding and testing have been completed to design specifications. After technological feasibility is established, costs are capitalized. Historically, product development has been substantially completed with the establishment of technological feasibility and, accordingly, no costs have been capitalized.

See Note B to our Consolidated Financial Statements for a full discussion of our critical accounting policies and estimates.

RESULTS OF OPERATIONS

Revenues:

For the Year Ended December 31,

| <u>2011</u> | <u>2010</u> | <u>Increase (Decrease)</u> | <u>Percent Inc (Dec)</u> |
|-------------|-------------|----------------------------|--------------------------|
| \$3,207,000 | \$3,485,000 | \$(278,000) | (8.0)% |

These changes are a result of the following factors:

1. Radiological services:

For the Year Ended December 31,

| <u>2011</u> | <u>2010</u> | <u>Increase (Decrease)</u> | <u>Percent Inc (Dec)</u> |
|-------------|-------------|----------------------------|--------------------------|
| \$2,708,000 | \$2,942,000 | \$(234,000) | (8.0)% |

The decrease in radiological services during 2011 as compared to 2010 is primarily due to the loss of two customers during the year, one to bankruptcy and one to another service. The volume of reads from our current customers continues to expand and contract somewhat as their businesses change, but overall we anticipate that this revenue will increase slightly during 2012.

2. Software usage fees:

For the Year Ended December 31,

| <u>2011</u> | <u>2010</u> | <u>Increase (Decrease)</u> | <u>Percent Inc (Dec)</u> |
|-------------|-------------|----------------------------|--------------------------|
| \$338,000 | \$370,000 | \$(32,000) | (8.6)% |

The decrease in software usage fees during 2011 as compared to 2010 is primarily due to the loss of one customer. We will be expanding the services that we offer in this revenue category with the addition of the cardiology PACS system that began pilot operations at the end of 2011. As a result, we anticipate that this revenue will increase moderately during 2012.

3. Cardiology services:

For the Year Ended December 31,

| <u>2011</u> | <u>2010</u> | <u>Increase (Decrease)</u> | <u>Percent Inc (Dec)</u> |
|-------------|-------------|----------------------------|--------------------------|
| \$83,000 | \$27,000 | \$56,000 | 207.4% |

We began offering cardiology services during the first quarter of 2010, and we are still adding new customers each quarter. Therefore, we expect this revenue category to continue to increase slightly during 2012.

4. Software hosting and maintenance:

For the Year Ended December 31,

| <u>2011</u> | <u>2010</u> | <u>Increase (Decrease)</u> | <u>Percent Inc (Dec)</u> |
|-------------|-------------|----------------------------|--------------------------|
| \$60,000 | \$125,000 | \$(65,000) | (52.0)% |

This decrease is a result of our continued focus on our medical division and our decreased focus on our older software applications that were developed prior to XR-EXpress. At this point, nearly all of our customers are using our medically related services, with no customers remaining on the earlier enterprise systems, which we are no longer offering. Software maintenance consists mainly of hosting and managing our customers' data on our systems, and to a lesser extent includes technical support programs associated with our products. We expect revenues in this category to decrease further during the coming year, as we continue to focus our efforts on building our medical division.

5. Software sales and licenses:

For the Year Ended December 31,

| <u>2011</u> | <u>2010</u> | <u>Increase (Decrease)</u> | <u>Percent Inc (Dec)</u> |
|-------------|-------------|----------------------------|--------------------------|
| \$10,000 | \$2,000 | \$8,000 | 400.0% |

This increase is due to a software upgrade for one customer and is not likely to be repeated during 2012. We anticipate focusing some efforts on the sale of PACS systems to hospitals during the coming year. However, because these would be major sales, we are unable to project the volume or timing of any impact on revenues at this time.

6. Custom programming:

For the Year Ended December 31,

| <u>2011</u> | <u>2010</u> | <u>Increase (Decrease)</u> | <u>Percent Inc (Dec)</u> |
|-------------|-------------|----------------------------|--------------------------|
| \$7,000 | \$19,000 | \$(12,000) | (63.2)% |

We performed one custom programming project for a new cardiology customer during the fourth quarter of 2010. The revenue for 2011 was related to the setup of a new division for an existing customer. We anticipate undertaking a few small and medium-sized projects that will generate a moderate increase in revenues in this category during 2012. We continue to offer programming services for customer database integration, and for other projects for our existing and new customers.

Cost of services:

For the Year Ended December 31,

| <u>2011</u> | <u>2010</u> | <u>Increase (Decrease)</u> | <u>Percent Inc (Dec)</u> |
|-------------|-------------|----------------------------|--------------------------|
| \$2,529,000 | \$2,670,000 | \$(141,000) | (5.3)% |

Approximately 91% of the cost of services for the year ended December 31, 2011 is related to Net Medical Xpress Services. These costs consist of radiologist and cardiologist fees, management fees, professional credentialing and professional liability insurance. The majority of these costs are directly related to revenues. The majority of the decrease in these costs during 2011 as compared to 2010 is primarily due to two factors: doctor fees decreased approximately \$77,000 due to decreased volume of reads during 2011 as compared to 2010, and a reduction in engineering staff during 2011 accounts for most of the remaining decrease.

General and administrative expenses:

For the Year Ended December 31,

| | <u>2011</u> | <u>2010</u> | <u>Increase (Decrease)</u> | <u>Percent Inc (Dec)</u> |
|--------------------|-------------|-------------|----------------------------|--------------------------|
| Legal expenses | \$45,000 | \$146,000 | \$(101,000) | (69.2)% |
| Other G&A expenses | \$736,000 | \$706,000 | \$30,000 | 4.2% |

The decrease in legal expenses is due to the legal proceedings described in Part I, Item 3 above nearing the end of proceedings. The increase in general and administrative expenses is primarily due to the addition of administrative staff for Net Medical Xpress Specialist program.

Research and development costs:

For the Year Ended December 31,

| | <u>2011</u> | <u>2010</u> | <u>Increase (Decrease)</u> | <u>Percent Inc (Dec)</u> |
|--|-------------|-------------|----------------------------|--------------------------|
| | \$66,000 | \$60,000 | \$6,000 | 10.0% |

During 2011, over 86% of our research and development costs were directly associated with staffing. The increase in costs for 2011 as compared to 2010 is primarily related to computer supplies while developing the neurology/stroke program. In the software industry it is common for research and development costs to be ongoing, since development of the next version of the software begins as soon as the current version is completed. In addition, we are constantly developing new applications for our existing software that require modification. Management anticipates that research and development costs in the future will focus both on the upgrading of our existing products and the continued development of new products using our core technology; therefore they will remain relatively stable or perhaps increase slightly during the coming year.

Depreciation and bad debt expense:

For the Year Ended December 31,

| | <u>2011</u> | <u>2010</u> | <u>Increase (Decrease)</u> | <u>Percent Inc (Dec)</u> |
|----------------------|-------------|-------------|----------------------------|--------------------------|
| Depreciation expense | \$18,000 | \$18,000 | \$0 | 0.0% |
| Bad debt expense | \$27,000 | \$210,000 | \$(183,000) | (87.1)% |

The decrease in bad debt expense is primarily due to the write-off of the account involved in the legal proceedings described in Part I, Item 3 above during 2010.

Other income (expense):

For the Year Ended December 31,

| | <u>2011</u> | <u>2010</u> | <u>Increase (Decrease)</u> | <u>Percent Inc (Dec)</u> |
|------------------------------------|-------------|-------------|----------------------------|--------------------------|
| Interest income | \$0 | \$14,000 | \$(14,000) | (100.0)% |
| Gain on sale of obsolete inventory | \$0 | \$1,000 | \$(1,000) | (100.0)% |
| Interest expense | \$10,000 | \$14,000 | \$(4,000) | (28.6)% |

The decrease in interest income is primarily due to the termination during 2011 of the customer account associated with the legal proceedings described in Part I, Item 3 above.

The gain on sale of obsolete inventory is due to the sale during 2011 of certain inventory items on hand that were written off during 2010.

The decrease in interest expense is related to a reduction in lease obligations during 2011 as compared to 2010.

REPORTABLE SEGMENTS

We have identified reportable segments based on separate lines of business. The segment identified as Software derives revenues from the development and marketing proprietary internet technology-based software and the segment identified as Services provides medical image diagnostic services. Information related to our reportable segments for 2011 is as follows:

| | Software | Services | TOTAL |
|----------------------------|------------|--------------|--------------|
| Revenue | \$ 416,000 | \$ 2,791,000 | \$ 3,207,000 |
| Cost of services | 221,000 | 2,309,000 | 2,529,000 |
| General and administrative | 319,000 | 418,000 | 736,000 |
| Legal fees | 43,000 | - | 45,000 |
| Depreciation | 11,000 | 7,000 | 18,000 |
| Research and development | 66,000 | - | 66,000 |
| Bad debt expense | - | 27,000 | 27,000 |

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| | | | |
|-------------------------|--------------|------------|--------------|
| Operating income (loss) | \$ (244,000) | \$ 30,000 | \$ (214,000) |
| Total assets | \$ 139,000 | \$ 544,000 | \$ 683,000 |

A reconciliation of the segments' operating loss to the consolidated net loss/comprehensive loss is as follows:

| | |
|--------------------------|--------------|
| Segment s operating loss | \$ (214,000) |
| Other income (expense) | (10,000) |
| Consolidated net loss | \$ (224,000) |

LIQUIDITY AND CAPITAL RESOURCES

As of December 31, 2011, cash and cash equivalents totaled \$100,000, representing a \$88,000 decrease from the beginning of the period. The decrease in available cash was due to a combination of several factors during the year:

Operating activities:

For the Year Ended December 31,

| <u>2011</u> | <u>2010</u> | <u>Inc (Dec) in available cash</u> |
|----------------|-------------------|------------------------------------|
| used \$101,000 | provided \$98,000 | \$(199,000) |

The increase in available cash from operations during 2011 as compared to 2010 is mainly due to a combination of the following major factors:

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Accounts receivable increased by \$60,000 during 2011 as compared to decreasing by \$96,000 during 2010, providing a decrease in available funds of \$156,000.

.

Bad debt expense was \$27,000 during 2011 as compared to \$210,000 during 2010, resulting in a decrease in available funds of \$183,000.

.

Net loss during 2011 was \$224,000 as compared to \$324,000 during 2010, constituting an increase in available funds of \$100,000 during 2011.

Investing activities:

For the Year Ended December 31,

| <u>2011</u> | <u>2010</u> | <u>Inc (Dec) in available cash</u> |
|---------------|---------------|------------------------------------|
| used \$43,000 | used \$18,000 | \$(25,000) |

We leased additional computer and office equipment during 2011 for infrastructure upgrades.

Financing activities:

For the Year Ended December 31,

| <u>2011</u> | <u>2010</u> | <u>Inc (Dec) in available cash</u> |
|-------------------|--------------|------------------------------------|
| provided \$56,000 | used \$3,000 | \$59,000 |

We received \$44,000 for stock purchases during 2011 as compared to \$0 during 2010.

We do not currently have material commitments for capital expenditures and do not anticipate entering into any such commitments during the next twelve months. Our current commitments consist primarily of lease obligations for office space and office equipment.

At December 31, 2011 we had a working capital deficit of \$92,000 as opposed to a working capital deficit of \$20,000 at the end of 2010. This decrease is primarily due to a reduction in cash balance of \$88,000. We may continue to sell equity securities and incur debt as needed to meet our operating needs during 2011.

We anticipate that our primary uses of cash in the next year will continue to be for general operating purposes. We anticipate our operating cash requirements for the next twelve months again to be in the range of \$4,000,000 to \$5,000,000. This level of cash flow will allow us to maintain our current level of operations and allow for modest growth. Profitability remains our primary goal.

ITEM 8. FINANCIAL STATEMENTS

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and

Stockholders of New Mexico Software, Inc.

Albuquerque, New Mexico

We have audited the accompanying consolidated balance sheet of New Mexico Software, Inc. as of December 31, 2011, and the related statements of operations, stockholders' deficit, and cash flows for the year then ended. New Mexico Software Inc.'s management is responsible for these financial statements. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of New Mexico Software, Inc. as of December 31, 2011, and the results of its operations and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note A to the financial statements, the Company has an accumulated deficit of \$15,346,000 since inception, which raises substantial doubt about its ability to continue as a going concern. Management's plans concerning these matters are also described in Note A. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

/s/ L.L. Bradford & Company, LLC

L.L. Bradford & Company, LLC

March 30, 2012

Las Vegas, Nevada

SEALE AND BEERS, CPAs

www.sealebeers.com

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of

New Mexico Software, Inc.

Albuquerque, New Mexico

We have audited the accompanying consolidated balance sheet of New Mexico Software, Inc. as of December 31, 2010, and the related statements of income, stockholders' equity and comprehensive income, and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of New Mexico Software, Inc. as of December 31, 2010, and the related statements of operations, stockholders' equity and cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note A to the financial statements, the Company has an accumulated deficit of \$15,122,000 since inception, which raises substantial doubt about its ability to continue as a going concern. Management's plans concerning these matters are also described in Note A. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

/s/ Seale and Beers, CPAs

Las Vegas, Nevada

March 31, 2011

50 S. Jones Blvd. Suite 202 Las Vegas, NV 89107 Phone: (888)727-8251 Fax: (888)782-2351

New Mexico Software, Inc.
Consolidated Balance Sheets
(Rounded to the nearest thousand)

| | December 31, 2011 | December 31, 2010 |
|---|----------------------|----------------------|
| Assets | | |
| Current assets: | | |
| Cash and equivalents | \$ 100,000 | \$ 188,000 |
| Accounts receivable, net | 463,000 | 430,000 |
| Prepaid expenses and other assets | 41,000 | 53,000 |
| Total current assets | 604,000 | 671,000 |
| Furniture, equipment and improvements, net | 75,000 | 57,000 |
| Security deposits | 4,000 | 4,000 |
| Total Assets | \$ 683,000 | \$ 732,000 |
| Liabilities and Stockholders' (Deficit) Equity | | |
| Current liabilities: | | |
| Accounts payable | \$ 634,000 | \$ 647,000 |
| Accrued expenses | 31,000 | 31,000 |
| Customer deposits | 3,000 | 3,000 |
| Deferred revenue | 15,000 | 6,000 |
| Capital lease | 13,000 | 4,000 |
| Total current liabilities | 696,000 | 691,000 |
| Long-term liabilities | | |
| Note payable | 2,000 | - |
| Capital lease - long-term portion | 4,000 | 3,000 |
| Total long-term liabilities | 6,000 | 3,000 |
| Total liabilities | 702,000 | 694,000 |
| Stockholders' (deficit) equity: | | |
| Preferred stock, \$0.001 par value, 500,000 shares authorized, 0 shares issued and outstanding as of 12/31/11 and 12/31/10, respectively | - | - |
| Common stock, \$0.001 par value, 200,000,000 shares authorized, 147,187,307 and 144,835,595 shares issued and outstanding as of 12/31/11 and 12/31/10, respectively | 147,000 | 145,000 |
| Paid-in capital | 15,159,000 | 15,054,000 |
| Subscriptions payable | 21,000 | 21,000 |
| Deferred compensation | - | (60,000) |
| Accumulated deficit | (15,346,000) | (15,122,000) |
| Total stockholders' (deficit) equity | (19,000) | 38,000 |

| | | | | |
|---|----|---------|----|---------|
| Total Liabilities and Stockholders' (Deficit) Equity | \$ | 683,000 | \$ | 732,000 |
|---|----|---------|----|---------|

The accompanying notes are an integral part of these financial statements.

New Mexico Software, Inc.
Consolidated Statements of Operations
(Rounded to the nearest thousand)

| | For the year ended December 31, | |
|---|------------------------------------|--------------|
| | 2011 | 2010 |
| Revenues | | |
| Radiological services | \$ 2,708,000 | \$ 2,942,000 |
| Software usage fees | 338,000 | 370,000 |
| Cardiology services | 83,000 | 27,000 |
| Software hosting and maintenance | 60,000 | 125,000 |
| Software sales and licenses | 10,000 | 2,000 |
| Custom programming | 7,000 | 19,000 |
| Other | 1,000 | - |
| Gross revenues | 3,207,000 | 3,485,000 |
| Cost of services | 2,529,000 | 2,670,000 |
| Gross profit | 678,000 | 815,000 |
| Operating costs and expenses: | | |
| General and administrative | 736,000 | 706,000 |
| Legal fees | 45,000 | 146,000 |
| Depreciation and amortization | 18,000 | 18,000 |
| Research and development | 66,000 | 60,000 |
| Bad debt | 27,000 | 210,000 |
| Total operating costs and expenses | 892,000 | 1,140,000 |
| Net operating loss | (214,000) | (325,000) |
| Other income (expense): | | |
| Interest expense | (10,000) | (14,000) |
| Interest income | - | 14,000 |
| Gain on sale of obsolete inventory | - | 1,000 |
| Total other income (expense) | (10,000) | 1,000 |
| Net loss | \$ (224,000) | \$ (324,000) |
| Loss per share - basic | \$ (0.00) | \$ (0.00) |
| Weighted average number of common shares outstanding - basic | | |
| | 145,460,651 | 138,293,912 |

The accompanying notes are an integral part of these financial statements.

New Mexico Software, Inc.
Consolidated Statements of Cash Flows
(Rounded to the nearest thousand)

| | For the year ended December 31, | |
|--|------------------------------------|--------------|
| | 2011 | 2010 |
| Cash flows from operating activities | | |
| Net loss | \$ (224,000) | \$ (324,000) |
| Adjustments to reconcile net loss to net cash used by operating activities: | | |
| Common stock issued for services | 30,000 | 93,000 |
| Common stock issued for services to board members and officers | 60,000 | 60,000 |
| Executive services donated | 33,000 | - |
| Bad debt expense | 27,000 | 210,000 |
| Depreciation and amortization | 18,000 | 18,000 |
| Depreciation and amortization allocated to cost of services | 7,000 | 8,000 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (60,000) | 96,000 |
| Prepaid expenses and other assets | 12,000 | (7,000) |
| Accounts payable | (13,000) | (8,000) |
| Customer deposits | - | (18,000) |
| Accrued expenses | - | (19,000) |
| Deferred revenue | 9,000 | (11,000) |
| Net cash provided (used) by operating activities | (101,000) | 98,000 |
| Cash flows from investing activities | | |
| Acquisition of fixed assets | (43,000) | (18,000) |
| Net cash used by investing activities | (43,000) | (18,000) |
| Cash flows from financing activities | | |
| Proceeds from note payable | 2,000 | - |
| Net repayment of principal under capital lease | 10,000 | (3,000) |
| Net proceeds from the issuance of common stock | 44,000 | - |
| Net cash (used) provided by financing activities | 56,000 | (3,000) |
| Net increase in cash equivalents | (88,000) | 77,000 |
| Cash equivalents - beginning | 188,000 | 111,000 |
| Cash equivalents - ending | \$ 100,000 | \$ 188,000 |
| Supplemental disclosures: | | |
| Interest paid | \$ - | \$ 5,000 |
| Shares issued for exercise of options | \$ - | \$ - |
| Assets acquired under capital lease | \$ 10,000 | \$ 8,000 |

The accompanying notes are an integral part of these financial statements.

New Mexico Software, Inc.
Consolidated Statements of Stockholders' Equity (Deficit)
(Rounded to the nearest thousand)

| | Preferred Stock Shares | Common Stock Shares | Common Stock Amount | Additional Paid-in Capital | Deferred Compensation | Subscriptions Payable | Accumulated (Deficit) | Total Stockholders' Equity |
|---|------------------------------|------------------------|------------------------|----------------------------------|--------------------------|--------------------------|--------------------------|----------------------------------|
| Balance, December 31, 2009 | - | 134,192,738 | \$134,000 | \$14,852,000 | \$ - | 21,000 | \$(14,798,000) | \$ 209,000 |
| Issuance of common stock for services | | 2,642,857 | 3,000 | 90,000 | | | | 93,000 |
| Issuance of common stock to board members and officers for future services | | 8,000,000 | 8,000 | 112,000 | (120,000) | | | - |
| Compensation earned by board members and officers | | | | | 60,000 | | | 60,000 |
| Net (loss) For the year ended December 31, 2010 | | | | | | | (324,000) | (324,000) |

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| | | | | | | | | | | | |
|--|-------|-------------|-----------|--------------|----|----------|----|--------|----------------|----|-----------|
| Balance, December 31, 2010 | - \$- | 144,835,595 | \$145,000 | \$15,054,000 | \$ | (60,000) | \$ | 21,000 | \$(15,122,000) | \$ | 38,000 |
| Issuance of common stock for services | | 851,712 | | 30,000 | | | | | | | 30,000 |
| Issuance of common stock for cash | | 1,500,000 | 2,000 | 42,000 | | | | | | | 44,000 |
| Executive time donated | | | | 33,000 | | | | | | | 33,000 |
| Compensation earned by board members and officers | | | | | | 60,000 | | | | | 60,000 |
| Net (loss) For the year ended December 31, 2011 | | | | | | | | | (224,000) | | (224,000) |
| Balance, December 31, 2011 | - \$- | 147,187,307 | \$147,000 | \$15,159,000 | \$ | - \$ | | 21,000 | \$(15,346,000) | \$ | (19,000) |

The accompanying notes are an integral part of these financial statements.

New Mexico Software, Inc.

Notes to Consolidated Financial Statements

NOTE A - ORGANIZATION AND OPERATIONS

[1] Description of business and history

New Mexico Software, Inc., a Nevada corporation, (the Company), develops and markets proprietary Internet technology-based software for the management of digital high-resolution graphic images, documents, video clips and audio recordings. The Company provides its software products in the form of Software-as-a-Service (SaaS) solutions, primarily for medical industries.

The Company was incorporated in New Mexico in 1996 under the name of New Mexico Software, Inc. It was acquired by Raddatz Exploration, Inc., a publicly traded Delaware corporation, in 1999. At that time, Raddatz changed its name to NMXS.com, Inc., and operated New Mexico Software, Inc. as a wholly-owned subsidiary. On January 1, 2006, NMXS.com, Inc. merged into its newly incorporated, wholly-owned subsidiary, New Mexico Software, Inc., a Nevada corporation, for the sole purpose of changing its state of incorporation and its name.

In May 2008, the Company formed Telerad Service Inc. as a wholly-owned subsidiary of New Mexico Software, Inc., to provide radiological services to hospitals, mobile and portable x-ray providers, prisons, urgent care facilities, and assisted living facilities. Telerad Service utilizes the Company's XR-EXpress software in providing these services. In January 2012 Telerad Service Inc. began doing business under the trade name of Net Medical Xpress Services to more accurately reflect the diversity of services offered.

[2] Going concern

The accompanying financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. The Company has incurred cumulative net losses of approximately \$15,346,000 since its inception and requires capital for its contemplated operational and marketing activities to take place. The Company's ability to raise additional capital through the future issuances of common stock is unknown. The obtainment of additional financing, the successful continuation of the Company's contemplated plan of operations, and its transition, ultimately, to the attainment of profitable operations are necessary for the Company to continue operations. The ability to successfully resolve these factors raise substantial doubt about the Company's ability to continue as a going concern. The consolidated financial statements of the Company do not include any adjustments that may result from the outcome of these aforementioned uncertainties.

[3] Principles of Consolidation

The consolidated financial statements include the accounts of the Company's wholly owned subsidiary, TeleRad Services, Inc. All significant inter-company balances and transactions have been eliminated in consolidation.

New Mexico Software, Inc.

Notes to Consolidated Financial Statements

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

[1] Revenue recognition:

According to FASB ASC Topic 605, *Revenue Recognition*, revenue is recognized when a transaction occurs and 1) the revenue is realized or realizable and 2) the revenue is earned. Revenue from a transaction must meet both criteria in order to be recognized. Revenue is generally considered realized when cash is received for the sale of a product or performance of a service. Revenue generally becomes realizable when a promise to pay is received in exchange for the sale of a product or performance of a service.

The Company invoices its customers for radiological review services rendered by its contracted licensed radiology staff upon full completion and closure of the case review process.

The Company's revenues are generally classified into four main categories: radiological services, software usage fees, cardiology services, and software hosting and maintenance. The Company also occasionally derives revenue from hardware sales associated with sales of its various software products, fees for customization or modification to its core software product, scanning services and other services such as consulting, training and installation. The Company recognizes revenue on its software and hosting revenue in accordance with Statement of Position ASC Topic 985 *Software Revenue Recognition* as amended.

Revenue from proprietary software sales that does not require further commitment from the Company is recognized upon persuasive evidence of an arrangement as provided by agreements executed by both parties, delivery of the software, and determination that collection of a fixed or determinable fee is probable. These sales are generally direct purchases of a software product and there is no other involvement by the Company.

The Company offers with certain sales of its software products, software maintenance, upgrade and support arrangements. These contracts may be elements in a multiple-element arrangement or may be sold in a stand-alone basis. Revenues from maintenance and support services are recognized ratably on a straight-line basis over the term that the maintenance service is provided. The Company typically charges 17% to 21% of the software purchase price for a 12-month maintenance contract with discounts available for longer-term agreements. The complexity of the software determines the percentage that is charged to any individual customer, and that percentage remains consistent upon renewal unless there is a change in the software or the terms of the agreement.

Charges for hosting are likewise spread ratably over the term of the hosting agreement, with the typical hosting agreement having a term of 12 months, with renewal on an annual basis. The Company sells some hosting contracts in conjunction with the sale of software, and some hosting contracts without an associated software sale. When the hosting arrangement is sold in conjunction with a software sale, the Company allocates a portion of the fee to the software license. Hosting services do not require the customer to purchase the software license, and for those hosting contracts that are sold without an associated software sale, the customer has neither the right nor the ability to operate the software on its own.

New Mexico Software, Inc.

Notes to Consolidated Financial Statements

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

[1] Revenue recognition (Continued):

Should the sale of software involve an arrangement with multiple elements (for example, the sale of a software license along with the sale of maintenance and support to be delivered over the contract period), the Company allocates revenue to each component of the arrangement using the residual value method based on the fair value of the undelivered elements. The Company defers revenue from the arrangement equivalent to the fair value of the undelivered elements and recognizes the remaining amount at the time of the delivery of the product or when all other revenue recognition criteria have been met. Fair values for the ongoing maintenance and support obligations are based upon separate sales of renewals of maintenance contracts. Fair value of services, such as training or consulting, is based upon separate sales of these services to other customers. The Company follows the guidance in ASC Topic 605, *Accounting for Performance of Construction-Type and Certain Production-Type Contracts* for custom software development arrangements that require significant production, customization or modification to its core software. Revenue is generally recognized for such arrangements under the percentage-of-completion method.

Under percentage-of-completion accounting, both the product license and custom software development revenue are recognized as work progresses based on specific milestones in accordance with ASC 605-25. The Company believes that project milestones based on completion of specific tasks provide the best approximation of progress toward the completion of the contract. At December 31, 2011 and December 31, 2010, there were no custom software development arrangements in progress.

The Company also occasionally derives revenue from the sale of third party hardware, which is billed as a separate deliverable under consulting or custom development contracts. Revenue from radiological services, cardiology services, software installation, and any training or consulting services is recognized when the services are rendered. These revenues include services that are not essential to the functionality of the software. If these services are included in a software agreement with multiple elements, amounts are allocated to these categories based on the estimated number of hours required to complete the work, which is the same criteria used to bill for the services separately. License revenue is recognized ratably over the term of the license.

Amounts collected prior to satisfying the above revenue recognition criteria are included in deferred revenue.

The application of ASC 605, as amended, requires judgment, including a determination that collectibility is probable and the fee is fixed and determinable.

The Company follows the guidance provided by SEC Staff Accounting Bulletin (SAB) No. 101, *Revenue Recognition in Financial Statements* and SAB No. 104, *Revenue Recognition*, which provide guidance on the recognition, presentation and disclosure of revenue in financial statements filed with the SEC.

New Mexico Software, Inc.

Notes to Consolidated Financial Statements

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

[1] Revenue recognition (Continued):

Due to uncertainties inherent in the estimation process it is at least reasonably possible that completion costs for contracts in progress will be further revised in the near- term.

The cost of services, consisting of staff payroll, outside services, equipment rental, communication costs and supplies, is expensed as incurred.

[2] Cash and cash equivalents:

The Company considers all highly liquid instruments purchased with a maturity of three months or less to be cash equivalents. At December 31, 2011, the Company did not have cash and equivalents that exceeded federally insured limits.

[3] Trade Accounts Receivable:

The Company extends unsecured credit to customers under normal trade agreements which generally require payment within 30 - 45 days. Accounts not paid within 15 days after their original due date are considered delinquent. Unless specified by the customer, payments are applied to the oldest unpaid invoice. Accounts receivable are presented at the amount billed.

The Company also estimates an allowance for doubtful accounts, which amounted to \$32,000 and \$38,000 at December 31, 2011 and 2010, respectively. The estimate is based upon management's review of all accounts and an assessment of the Company's historical evidence of collections. Specific accounts are charged directly to the reserve when management obtains evidence of a customer's insolvency. Charge-offs, net of recoveries, for the years ended December 31, 2011 and 2010 totaled \$27,000 and \$210,000, respectively.

[4] Unbilled Accounts Receivable

At year end, certain completed cases are not invoiced to the Company's customers until a time subsequent to the yearend due to billing cycle timing issues. The unbilled cases are recorded on the Company's books as Unbilled Accounts Receivable. The balances of Unbilled Accounts Receivable included in Accounts Receivable, net on the Company's balance sheet at December 31, 2011 and 2010 were \$274,316 and \$287,843, respectively.

[5] Furniture, equipment and improvements:

Furniture, equipment and improvements are recorded at cost. The cost of maintenance and repairs is charged against results of operations as incurred. Depreciation is charged against results of operations using the straight-line method over the estimated economic useful life. Leasehold improvements are amortized on a straight-line basis over the life of the related lease.

New Mexico Software, Inc.

Notes to Consolidated Financial Statements

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

[6] Income taxes:

The Company recognizes deferred tax liabilities and assets for the expected future tax consequences of events that have been included in the financial statements or tax returns. Under this method, deferred tax liabilities and assets are determined on the basis of the differences between the tax basis of assets and liabilities and their respective financial reporting amount ("temporary differences") at enacted tax rates in effect for the years in which the differences are expected to reverse.

[7] Per share data:

The basic per share data has been computed on the basis of the net loss available to common stockholders for the period divided by the historic weighted average number of shares of common stock. All potentially dilutive securities have been excluded from the computations since they would be antidilutive, however, these dilutive securities could potentially dilute earnings per share in the future. Options exercisable for 10,962,250 and 11,262,250 shares of common stock have been excluded from the diluted loss per share calculation for the years ended December 31, 2011 and 2010, respectively, because inclusion of such would be antidilutive.

[8] Research and development expenses:

Costs of research and development activities are expensed as incurred.

[9] Advertising expenses:

The Company expenses advertising costs which consist primarily of direct mailings, promotional items and print media, as incurred. Advertising expenses amounted to \$0 and \$8,000 for the years ended December 31, 2011 and 2010, respectively.

[10] Presentation of financial statements:

The Company rounds the figures on the financial statements to the nearest thousand.

[11] Use of estimates:

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

New Mexico Software, Inc.

Notes to Consolidated Financial Statements

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

[12] Stock-based compensation:

The Company adopted ASC Topic 505, Share-Based Payment, effective January 1, 2006. ASC 505 requires the recognition of the fair value of stock-based compensation in net income. Stock-based compensation primarily consists of stock options. Stock options are granted to employees at exercise prices equal to the fair market value of the Company's stock at the dates of grant. The Company now recognizes the stock-based compensation expense over the requisite service period of the individual grantees, which generally equals the vesting period. The Company provides newly issued shares to satisfy stock option exercises. There were 0 and 0 option awards granted to employees and directors in the years ended December 31, 2011 and 2010, respectively. During the years ended December 31, 2011 and 2010, the Company recorded \$0 and \$0, respectively, in expense related to option grants to employees and directors.

[13] Software development:

The Company accounts for computer software development costs in accordance with ASC 985, "Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed". As such, all costs incurred prior to the product achieving technological feasibility are expensed as research and development costs. Technological feasibility is generally achieved upon satisfactory beta test results. Upon achieving technological feasibility, programming costs are capitalized and amortized over the economic useful life which is estimated to be two years. There were no capitalized software development costs as of December 31, 2011 and 2010.

[14] Fair value of financial instruments:

Financial accounting standards Statement No. 107, "Disclosure About Fair Value of Financial Instruments", requires the Company to disclose, when reasonably attainable, the fair market values of its assets and liabilities which are deemed to be financial instruments. The carrying amounts and estimated fair values of the Company's financial instruments approximate their fair value due to the short-term nature.

[15] Recent pronouncements:

The Company's management has reviewed recent accounting pronouncements issued through the date of the issuance of these financial statements. In management's opinion, no pronouncements apply or will have a material effect on the Company's financial statements.

New Mexico Software, Inc.

Notes to Consolidated Financial Statements

NOTE C - FURNITURE, EQUIPMENT, AND IMPROVEMENTS

Furniture, equipment, and improvements as of December 31, 2011 and 2010 consisted of the following:

| | 2011 | 2010 |
|-----------------------------------|------------|------------|
| Computers | \$ 474,000 | \$ 430,000 |
| Furniture, fixtures and equipment | 130,000 | 130,000 |
| Automobiles | 41,000 | 41,000 |
| Leasehold improvements | 20,000 | 20,000 |
| | 665,000 | 621,000 |
| Accumulated depreciation | (590,000) | (564,000) |
| | \$ 75,000 | \$ 57,000 |

Depreciation expense for the years ended December 31, 2011 and 2010 was \$18,000 and \$18,000, respectively.

NOTE D - STOCKHOLDERS EQUITYCommon stock:

During the year ended December 31, 2011, the Company effected the following stock transactions:

The Company issued a total of 851,712 shares of the Company's \$0.001 par value common stock to outside contractors in exchange for services rendered valued at \$30,000.

The Company issued a total of 1,500,000 shares of the Company's \$0.001 par value common stock to outside contractors in exchange for cash in the amount of \$44,000.

Earned compensation for the Board of Directors of \$60,000 is included in expense for the year ended December 31, 2011.

Donated time valued at \$33,000 for two executives is included in expense for the year ended December 31, 2011.

Treasury stock:

The Company effected no treasury stock transactions during the year ended December 31, 2011.

Warrants:

During the years ended December 31, 2011 and 2010, there were no warrants issued or exercised. No warrants are outstanding at December 31, 2011.

New Mexico Software, Inc.

Notes to Consolidated Financial Statements

NOTE D - STOCKHOLDERS EQUITY (CONTINUED)Stock options:

Stock options employees and directors - During the years ended December 31, 2011 and 2010, the Company made no grants of stock options to employees or directors.

Stock options non-employees - During the years ended December 31, 2011 and 2010, the Company made no grants of stock options for services.

Exercise prices and weighted-average contractual lives of stock options outstanding as of December 31, 2011 are as follows:

| Exercise Prices | Options Outstanding | | Options Exercisable | |
|-----------------|---------------------|---|---------------------|--------------------|
| | Number Outstanding | Weighted Average Remaining Contractual Life | Exercise Prices | Number Exercisable |
| \$0.01-\$0.04 | 9,500,000 | 4.86 | \$0.03 | 9,500,000 |
| \$0.05-\$0.30 | 1,462,250 | 1.20 | \$0.06 | 1,462,250 |

Summary of Options Granted and Outstanding:

| | For the Years Ended December 31, | | | |
|----------------------------------|----------------------------------|---------------------------------|------------|---------------------------------|
| | 2011 | | 2010 | |
| | Shares | Weighted Average Exercise Price | Shares | Weighted Average Exercise Price |
| Options: | | | | |
| Outstanding at beginning of year | 11,262,250 | \$0.03 | 11,489,250 | \$0.04 |
| Granted | 0 | \$0.00 | 0 | \$0.00 |
| Cancelled | (300,000) | \$0.06 | (227,000) | \$0.21 |
| Exercised | 0 | \$0.00 | 0 | \$0.00 |
| Outstanding at end of year | 10,962,250 | \$0.03 | 11,262,250 | \$0.03 |

During the year ended December 31, 2011, no options were granted.

NOTE E - INCOME TAXES

The Company accounts for income taxes using the liability method, under which deferred tax liabilities and assets are determined based on the difference between the financial statement carrying amounts and the tax basis of assets and liabilities using enacted tax rates in effect in the years in which the differences are expected to reverse.

New Mexico Software, Inc.

Notes to Consolidated Financial Statements

NOTE E - INCOME TAXES (CONTINUED)

As of December 31, 2010, the Company had net operating loss carry forwards of approximately \$15,346,000, which expire in varying amounts between 2017 and 2028. Realization of this potential future tax benefit is dependent on generating sufficient taxable income prior to expiration of the loss carry forward.

At December 31, 2010 and 2009, the Company had a federal operating loss carry forward of \$15,346,000 and \$15,122,000, respectively.

Components of net deferred tax assets, including a valuation allowance, are as follows at December 31:

| | 2011 | 2010 |
|----------------------------------|--------------|--------------|
| Deferred tax assets: | | |
| Net operating loss carry forward | \$ 4,809,000 | \$ 4,676,000 |
| Stock based compensation | 93,000 | 153,000 |
| Total deferred tax assets | 4,902,000 | 4,829,000 |
| Less: Valuation Allowance | (4,902,000) | (4,829,000) |
| Net Deferred Tax Assets | \$ -- | \$ -- |

The valuation allowance for deferred tax assets as of December 31, 2011 and 2010 was \$4,902,000 and \$4,829,000, respectively. In assessing the recovery of the deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income in the periods in which those temporary differences become deductible. Management considers the scheduled reversals of future deferred tax assets, projected future taxable income, and tax planning strategies in making this assessment. As a result, management determined it was more likely than not the deferred tax assets would be realized as of December 31, 2011 and 2010.

Reconciliation between the statutory rate and the effective tax rate is as follows at December 31:

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| | 2011 | 2010 |
|---|---------|---------|
| Federal statutory tax rate | (25.0)% | (25.0)% |
| State taxes, net of federal tax benefit | (5.0)% | (5.0)% |
| Permanent difference and other | 30.0% | 30.0% |
| Effective tax rate | 0% | 0% |

New Mexico Software, Inc.

Notes to Consolidated Financial Statements

NOTE F - MAJOR CUSTOMERS

During the year ended December 31, 2011, one customer accounted for 35% of the Company's revenue. During the year ended December 31, 2010, one customer accounted for 29% of the Company's revenue.

As of December 31, 2011, balances due from one customer comprised 43% of total accounts receivable.

NOTE G - REPORTABLE SEGMENTS

Management has identified the Company's reportable segments based on separate lines of business. New Mexico Software (NMS) derives revenues from the development and marketing proprietary internet technology-based software and Telerad Service (TRS) provides radiological services. Information related to the Company's reportable segments for 2011 is as follows:

| | NMS | TRS | TOTAL |
|----------------------------|--------------|--------------|--------------|
| Revenue | \$ 416,000 | \$ 2,791,000 | \$ 3,207,000 |
| Cost of services | 221,000 | 2,309,000 | 2,529,000 |
| General and administrative | 319,000 | 418,000 | 736,000 |
| Legal fees | 43,000 | - | 45,000 |
| Depreciation | 11,000 | 7,000 | 18,000 |
| Research and development | 66,000 | - | 66,000 |
| Bad debt expense | - | 27,000 | 27,000 |
| Operating income (loss) | \$ (244,000) | \$ 30,000 | \$ (214,000) |
| Total assets | \$ 139,000 | \$ 544,000 | \$ 683,000 |

A reconciliation of the segments' operating loss to the consolidated net loss/comprehensive loss is as follows:

| | |
|--------------------------|--------------|
| Segment s operating loss | \$ (214,000) |
| Other income (expense) | (10,000) |
| Consolidated net loss | \$ (224,000) |

NOTE H - COMMITMENTS AND CONTINGENCIES

Leases:

The Company leases office space in New Mexico expiring on April 30, 2014. The Company also leases one automobile. Future minimum lease payments as of December 31, 2011 are as follows:

New Mexico Software, Inc.

Notes to Consolidated Financial Statements

NOTE H - COMMITMENTS AND CONTINGENCIES (CONTINUED)

| <u>Year</u> | <u>Amount</u> |
|-------------|---------------|
| 2012 | 73,000 |
| 2013 | 63,000 |
| 2014 | 21,000 |

Rent expense for the years ended December 31, 2011 and 2010 amounted to \$64,000 and \$66,000, respectively.

Employment agreement:

The Company entered into an employment and non-competition agreement with a stockholder to act in the capacity of President and Chief Executive Officer (CEO). The term of the employment agreement is for three years commencing on January 1, 2010. The agreement allows for a one-year renewal option unless terminated by either party. Base salary is \$60,000 per annum with available additional cash compensation as defined in the agreement. Compensation under this agreement of \$60,000 is included in general and administrative expenses for the year ended December 31, 2011. The non-competition agreement commences upon the termination of the employment agreement for a period of one year. As of December 31, 2011, there was a total of \$0 in accrued payroll, and \$15,000 in donated capital, for unpaid salary, for this executive.

NOTE I - LEGAL PROCEEDINGS

On January 23, 2012, the US District Court in Albuquerque, New Mexico entered judgment in favor of New Mexico Software in the case of Premier Medical Enterprise Solutions, Inc. v. New Mexico Software, Inc. and Richard Govatski, Case No. Civ 09-165. The judgment brings to conclusion the suit initiated by Premier Medical in early 2009, alleging breaches of (i) fiduciary duty, (ii) covenant of good faith and fair dealing and (iii) contract, along with claims of conversion and tortious interference and seeks an accounting. The suit sought compensatory, punitive and exemplary damages in excess of \$75,000, together with injunctive relief against unfair competition and attorney's fees. The court awarded judgment to New Mexico Software in the amount of \$636,606.

Premier Medical had been an early client of our XR-Express services. Premier Medical withheld payment for services provided prior to filing suit and after suit until we terminated service in June 2010. In December 2010, we wrote off as uncollectible all accounts receivable from Premier Medical.

We are evaluating with the advice of counsel whether to pursue collection of our judgment against Premier Medical, its principals and its successor which appears to have taken an assignment of Premier Medical's business without consideration.

New Mexico Software, Inc.

Notes to Consolidated Financial Statements

NOTE J - SUBSEQUENT EVENTS

In January 2012, the Board of Directors approved the issuance of 8,000,000 shares of the Company's \$0.001 par value common stock valued at \$160,000 to the directors for services for 2012 and 2013.

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

During the two most recent fiscal years, there have been no disagreements with L.L. Bradford & Company, our independent auditor for the year ended December 31, 2011, or with Seale & Beers, LLP, our independent auditor for the year ended December 31, 2010, on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure.

ITEM 9A. CONTROLS AND PROCEDURES

307 - Disclosure controls and procedures: As of December 31, 2011, we carried out an evaluation of the effectiveness of our disclosure controls and procedures, with the participation of our principal executive and principal financial officers. Disclosure controls and procedures are defined in Exchange Act Rule 15d-15(e) as controls and other procedures of an issuer that are designed to ensure that information required to be disclosed by the issuer in the reports that it files or submits under the Act (15 U.S.C. 78a *et seq.*) is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms [and] include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Act is accumulated and communicated to the issuer's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. Based on our evaluation, our President/Chief Executive Officer and Chief Financial Officer have concluded that, as of December 31, 2011, such disclosure controls and procedures were not effective.

308(a)(1) - Management's responsibility: Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Exchange Act Rule 15d-15(f) as a process designed by, or under the supervision of, the issuer's principal executive and principal financial officers, or persons performing similar functions, and effected by the issuer's board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that: (1) Pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the issuer; (2) Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the issuer are being made only in accordance with authorizations of management and directors of the issuer; and (3) Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the issuer's assets that could have a material effect on the financial statements. Because of inherent limitations, internal control over financial reporting is not intended to provide absolute assurance that a misstatement of our financial statements would be prevented or detected.

308(a)(2) - Framework used for evaluation: In its evaluation of our internal control over financial reporting, our management has used the *Internal Control - Integrated Framework* (1992) and *Internal Control Over Financial Reporting Guidance for Smaller Public Companies* (2006), issued by the Committee of Sponsoring Organizations of

the Treadway Commission.

308(a)(3) - Evaluation of our internal control over financial reporting: Pursuant to Rule 15d-15 of the Exchange Act, our management conducted an evaluation of the effectiveness of our internal control over financial reporting as of December 31, 2011. Based on this evaluation, our management, with the participation of our principal executive and principal financial officers, concluded that our internal control over financial reporting was not effective as of December 31, 2011. Management has identified the following material weakness in our internal control over financial reporting:

.

We do not have adequate personnel and other resources to assure that significant and complex transactions are timely analyzed and reviewed.

.

We have limited personnel and financial resources available to plan, develop, and implement disclosure and procedure controls and other procedures that are designed to ensure that information required to be disclosed in our periodic reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms.

.

Our limited financial resources restrict our employment of adequate personnel needed and desirable to separate the various receiving, recording, reviewing and oversight functions for the exercise of effective control over financial reporting.

.

Our limited resources restrict our ability to ensure that information required to be disclosed in our periodic reports filed under the Exchange Act is accumulated and communicated to management to allow timely decisions regarding required disclosure.

308(c) - Changes in internal control over financial reporting: Based upon an evaluation by our management of our internal control over financial reporting, with the participation of our principal executive and principal financial officers, there were no changes made in our internal control over financial reporting during the year ended December 31, 2011 that have materially affected or are reasonably likely to materially affect our internal control over financial reporting.

Limitations on the Effectiveness of Internal Control: Our management does not expect that our disclosure controls and procedures or our internal control over financial reporting will necessarily prevent all fraud and material errors. An internal control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations on all internal control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake.

Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, and/or by management override of the control. The design of any system of internal control is also based in part upon certain assumptions about risks and the likelihood of future events, and there is no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in circumstances and the degree of compliance with the policies and procedures may deteriorate. Because of the inherent limitations in a cost-effective internal control system, financial reporting misstatements due to error or fraud may occur and not be detected on a timely basis.

ITEM 9B. OTHER INFORMATION

None

PART III**ITEM 10. DIRECTORS, EXECUTIVE OFFICERS, PROMOTERS, CONTROL PERSONS AND CORPORATE GOVERNANCE; COMPLIANCE WITH SECTION 16(A) OF THE EXCHANGE ACT**

Our directors and officers are set forth below. The directors hold office for a one-year term and until their successors are duly elected and qualified. The officers serve at the will of the board of directors.

| <u>Name</u> | <u>Age</u> | <u>Position</u> | <u>Director Since</u> |
|---------------------|------------|---|-----------------------|
| Richard F. Govatski | 67 | Chairman, President and Chief Executive Officer | 1999 |
| Teresa B. Dickey | 68 | Director, Secretary & Treasurer | 2002 |
| John E. Handley | 50 | Director | 2003 |
| Frank A. Reidy | 70 | Director | 2005 |

We do not have a separately designated audit committee, compensation committee or nominating committee.

However, Mr. Handley and Mr. Reidy, both qualify as audit committee financial experts because of their education and experience in business and accounting. Using the definition of independence contained in the NASDAQ listing rules, Mr. Handley and Mr. Reidy are also our independent directors. We have the authority under Nevada law and our bylaws to indemnify our directors and officers against certain liabilities. We have been informed by the U.S. Securities and Exchange Commission that indemnification against violations of federal securities law is against public policy and therefore unenforceable.

Set forth below is certain biographical information regarding our executive officers and directors:

RICHARD GOVATSKI has been our chairman, CEO, and President since 1996. Mr. Govatski founded New Mexico Software in 1996 after he identified market inefficiencies in how intellectual property owners managed their image assets. Prior to New Mexico Software, Mr. Govatski spent 18 years in systems integration and publishing, both in sales management and software development. Mr. Govatski led the sales teams for Popular Electronics, Computer Shopper, Shutterbug, and MacWeek. Later he sold numerous solutions for vendors, including Kodak, Apple Computer, and Sun Microsystems. Mr. Govatski also spent several years in systems development as President of Media Publishing Group and built graphic applications for companies including Ferrari Color, Time Magazine, New York Daily News, and Getty Images. He received a Bachelor of Science Degree in Communications from Butler University, located in Indianapolis, Indiana in 1968.

TERESA B. DICKEY has been our Secretary/Treasurer since August 1999. She became a member of our Board of Directors on December 19, 2002 and has held such position since such time. From 1988 until 1999 she was employed by Sandia National Laboratory as art director. Sandia National Laboratory is a U.S. Department of Energy national security laboratory. In 1964, Ms. Dickey received her Bachelor of Professional Arts from the Art Center College of

Design in Pasadena, California.

JOHN E. HANDLEY has been our director since January 2003. He has been self-employed since September 2002 as a telecommunications consultant. From August 1987 until August 2002 he was employed, as an associate partner (from September 1997 until August 2000) and as a partner (September 2000 until August 2002), by Accenture LLP, a business and technology consulting and outsourcing company. He received his Bachelor of Arts degree in Psychology and Business from Roanoke College in 1983. Thereafter, he received his Masters in Business Administration from Virginia Tech in 1987.

FRANK A. REIDY received his Bachelor of Science degree in Marketing from Oklahoma State University in 1964 and a Masters of Arts in Economics from the University of Toledo in 1972, where he taught micro and macro economics as an evening division adjunct professor for seventeen years. Full-time from 1973 - 1984 he was Chief Accountant for Tecumseh Products Company, Tecumseh, MI. From 1984 - 1989 he was Director of RETS Institute of Technology, Toledo, OH. From 1989 - 1998 he was the Business Manager for Plaza Medical Laboratory, Bartlesville, OK. Currently he is owner of a general construction business in Bartlesville.

Code of Ethics.

We have not adopted a code of ethics governing the conduct of our principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions.

Nomination of Candidates for Directors by Stockholders.

We have not adopted any procedures for nomination of candidates for directors by our stockholders.

Board Meeting Attendance.

Our board held two meetings during 2011, in person and by telephone. All directors attended both meetings.

Shareholder Communications.

We have not established any process for security holders to communicate with our board of directors. Our stockholders are welcome to contact our directors and executive officers individually at any time.

ITEM 11. EXECUTIVE COMPENSATION

Compensation of Executive Officers

Summary Compensation Table. The following table sets forth information concerning the annual and long-term compensation awarded to, earned by, or paid to the named executive officer for all services rendered in all capacities to us, or any of its subsidiaries, for the years ended December 31, 2011, 2010 and 2009. We did not pay any executive officer other than Mr. Govatski more than \$100,000 in the last three fiscal years.

| <u>Name and Principal Position</u> | <u>Year</u> | <u>Salary</u> | <u>Stock Awards</u> | <u>Total (\$)</u> |
|---------------------------------------|-------------|---------------|---------------------|-------------------|
| Richard F. Govatski | 2011 | \$60,000 | \$15,000 | \$75,000 |
| President and Chief Executive Officer | 2010 | \$60,000 | \$15,000 | \$75,000 |
| | 2009 | \$60,000 | \$17,000 | \$77,000 |
| Teresa B. Dickey | 2011 | \$60,000 | \$15,000 | \$75,000 |
| Chief Financial Officer | 2010 | \$60,000 | \$15,000 | \$75,000 |
| | 2009 | \$60,000 | \$17,000 | \$77,000 |

Aggregated Option Exercises In Last Fiscal Year And Fiscal Year-End Option/Par Values

The following table sets forth certain information regarding stock options exercised during fiscal 2011 and held as of December 31, 2011, by Mr. Govatski.

| <u>Name</u> | <u>Shares acquired on exercise</u> | <u>Value realized</u> | <u>Number of securities</u> | |
|---------------------|------------------------------------|-----------------------|--|---|
| | | | <u>underlying unexercised options at fiscal year-end</u> | <u>Value of unexercised in-the-money options at fiscal year-end (1)</u> |
| Richard F. Govatski | -0- | N/A | 3,500,000/0 | \$0/\$0 (2) |

(1) Value is based on the closing sale price of the Common Stock on December 30, 2011, the last trading day of fiscal 2011 (\$0.024), less the applicable option exercise price.

(2) Of these options, 500,000 were exercisable at \$0.044 per share and 3,000,000 were exercisable at \$0.03 per share.

Employment Contracts

We entered into an employment and non-competition agreement with Mr. Govatski to continue in the capacity of President and CEO for a term ending December 31, 2012. The agreement allows for a one-year renewal option unless terminated by either party. Base salary is \$60,000 per annum with available additional cash compensation as defined in the agreement. Additional cash compensation is based upon the achievement of target goals as approved by the Board of Directors, and is dependent on our available cash flow. The non-competition agreement commences upon the termination of the employment agreement for a period of one year.

We do not have an employment agreement with Ms. Dickey

Compensation of Directors

| Name | Shares Awards | 2011 Total |
|------------------|---------------|------------|
| Teresa B. Dickey | \$15,000 | \$15,000 |
| John Handley | \$15,000 | \$15,000 |
| Frank Reidy | \$15,000 | \$15,000 |

Directors are permitted to receive fixed fees and other compensation for their services. The Board of Directors has the authority to fix the compensation of directors. During the year ended December 31, 2010, the Board awarded 1,000,000 shares of our common stock to each Director for services performed during the fiscal year ended December 31, 2011.

Stock Option and Stock Issuance Plans

| Plan | Year | Options Outstanding and Exercisable (#) | Option Expiration Date |
|----------------------|------|--|------------------------|
| Stock Incentive Plan | 2005 | 500,000 | March 2, 2015 |
| Stock Incentive Plan | 2006 | 12,000,000 | October 17, 2016 |

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table sets forth certain information about the common stock ownership by (i) each director and executive officer; and (ii) directors and executive officers as a group. We do not know of any other person who owns more than five percent of our common stock.

| <u>Name and Address of Beneficial Owner</u> | <u>Amount and Nature of</u> | |
|---|-----------------------------|-----------------------------|
| | <u>Beneficial Owner (1)</u> | <u>Percent of Class (1)</u> |
| Richard F. Govatski | 21,664,043 (2) | 14.74% |
| Teresa B. Dickey | 7,175,510 (3) | 4.88% |
| John Handley | 7,983,170 (4) | 5.43% |
| Frank Reidy | 13,763,530 (5) | 9.36% |
| Executive Officers and Directors as a Group (4 Persons) | 50,586,253 | 34.42% |

(1) All of the persons are believed to have sole voting and investment power over the shares of common stock listed or share voting and investment power with his or her spouse, except as otherwise provided. Percentage is based on 146,974,488 shares outstanding as of March 9, 2012. Percentage includes amounts which the listed beneficial owner has the right to acquire within sixty days.

(2) This number of shares includes options to purchase 3,500,000 shares. These options have vested and are currently exercisable. The shares underlying these options are included in the table and are considered to be outstanding for purposes of computing the percentage interest held by Mr. Govatski.

(3) This number of shares includes options to purchase 3,000,000 shares. These options have vested and are currently exercisable. The shares underlying these options are included in the table and are considered to be outstanding for

purposes of computing the percentage interest held by Ms. Dickey.

(4) This number of shares includes options to purchase 1,500,000 shares. These options have vested and are currently exercisable. The shares underlying these options are included in the table and are considered to be outstanding for purposes of computing the percentage interest held by Mr. Handley.

(5) This number of shares includes options to purchase 1,500,000 shares. These options have vested and are currently exercisable. The shares underlying these options are included in the table and are considered to be outstanding for purposes of computing the percentage interest held by Mr. Reidy.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

We did not enter into any transactions with our directors and executive officers in 2011 and none are proposed.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The following table sets forth amounts we have been billed with respect to 2011 and 2010 for certain services provided by our independent accountant.

| Service | 2011 | 2010 |
|---|----------|----------|
| Audit | \$29,000 | \$29,000 |
| Review of unaudited financial statements | \$7,000 | \$7,000 |
| Audit-related fees | none | none |
| Tax compliance, tax advice and tax planning | none | none |
| All other services | none | none |

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

(a) The following documents are filed as part of this report:

1. Financial statements; see index to financial statement and schedules in Item 8 herein.
2. Financial statement schedules; see index to financial statements and schedules in Item 8 herein.
3. Exhibits: None

SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

New Mexico Software, Inc.

Date: March 30, 2012

/s/ Richard F. Govatski

Richard F. Govatski
President, Chief Executive Officer and Chairman
of the
Board of Directors

Date: March 30, 2012

/s/ Teresa B. Dickey

Teresa B. Dickey, Director, Secretary, Treasurer
and
Principal Financial Officer

Date: March 30, 2012

/s/ John Handley

John E. Handley, Director

Date: March 30, 2012

/s/ Frank A. Reidy

Frank A. Reidy, Director

