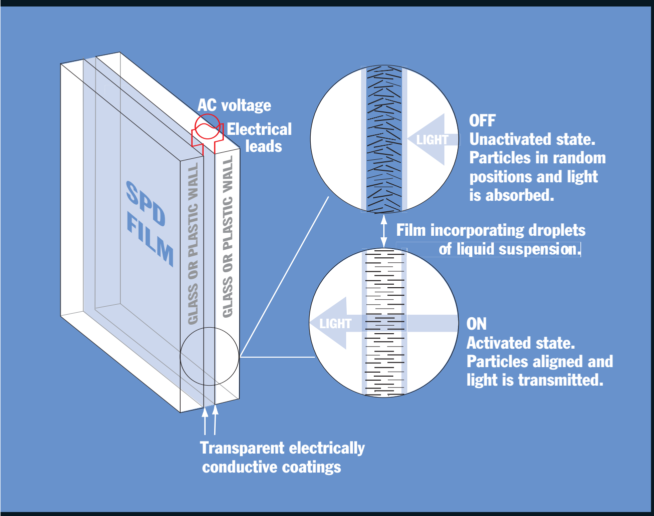
Research Frontiers Annual Report

2005



The illustration shows the structure and operation of a Suspended Particle Device (SPD).

Research Frontiers is the technological leader in the field of electrically operated light control devices which use films containing droplets of orientable particle suspensions. These devices are usually called either "light valves"or suspended particle devices ("SPDs"). When voltage is applied to the SPD, particles in the film align, enabling the operator to rapidly vary and control the amount of light transmitted through the device over a wide range. The amount of light transmitted depends on the voltage applied.

Research Frontiers Licensees

Air Products and Chemicals, Inc.
American Glass Products
Asahi Glass Company
Avery Dennison
BOS Automotive Products
BRG Group, Ltd.
Cricursa Cristales Curvados S.A.
Custom Glass Corporation
Dainippon Ink and Chemicals Inc.
DuPont
Film Technologies International, Inc.
General Electric Company
Glaverbel S.A.
Global Mirror GmbH & Co. KG
Hitachi Chemical Co., Ltd.
Innovative Glass Corporation
InspecTech Aero Service, Inc.
Isoclima S.p.A.
Kerros Ltd./IntelliTint
Laminated Technologies, Inc.
Leminur Ltd.
N.V. Bekaert S.A
Nippon Sheet Glass Co., Ltd.
Pilkington plc
Polaroid Corporation
Prelco Inc.
Saint-Gobain Glass France S.A.
SmartGlass Ireland Ltd.
SPD Control Systems Corp.
SPD Systems, Inc.
SPD Technologies, Inc.
ThermoView Industries, Inc.
Traco, Inc.
Vision Ltd.
(Environmental Innovation)

SPD-Smart™ skylight.
Photo courtesy of Vision (Environmental Innovation) Ltd.

There is a Haitian proverb: "Beyond the mountains are more mountains." This proverb applies to most companies involved in bringing a new technology to market. In R&D, after one issue is solved, others sometimes arise. It is appropriate to note that Haiti is an island nation, so that eventually, with perseverance and hard work, the mountains end, the goal is reached, and smooth sailing across the ocean of opportunity can begin. We are happy to report that we can see the ocean and some very large companies are preparing to bring SPD-Smart™ products to the world.

While we have always focused intensely on the development of our SPD light-control technology, this past year in particular, the Company has been working with extreme dedication and has made several very important new inventions to enable our film licensees to begin to successfully produce very attractive second generation SPD-Smart light-controlling film. A key part of our R&D strategy is to anticipate and find solutions for any potential problem or weakness relating to SPD emulsions, films or products. As discussed at our June 2005 Annual Meeting, part of this strategy is to gain further direct experience with commercially coating SPD emulsions into film, and the Company has now completed our own coating trials using the facilities of an outside toll coater.

At the Company's June 2005 Annual Meeting, we described in detail the kinds of technical challenges which, at that time, remained to be solved by our film-making licensees who were working to mass-produce SPD film on large coating machines. Most of these challenges were related to improving the physical appearance of the film, which, as we reported, was marred by numerous tiny bubbles in the film, as well as streaks, spots, haze and other defects which occurred when scaling up from the laboratory to the commercial film-making process.

We are very pleased to report that our licensees have substantially overcome these cosmetic problems. During the past nine months since our Annual Meeting, film samples made on commercial coating lines by these licensees have exhibited continual improvement in physical appearance, to the point where we, and key end-product licensees, now believe that the latest SPD films have reached a high level of quality and performance, and meet the needs expressed by potential customers in numerous markets.

With these cosmetic issues resolved, we and our licensees are currently working on improvements which will reduce the risk of film delamination, a situation which can potentially occur when the film or an end-product comprising the film is subjected to extreme environmental stresses such as large changes in temperature or pressure. In this regard, the Company has recently made what we believe to be an important invention, a new material which significantly increases film adhesion. We have filed a patent application on this invention, as well as others to enhance the overall quality and production efficiency of SPD emulsions and films, and have disclosed the details to our emulsion-making licensees.

The Company's research and development team has made several other major inventions of importance to our emulsion and film-making licensees. Materials have been invented for achieving and maintaining emulsions of high stability, for making films with an even wider range of light transmission, and for making films with improved adhesion characteristics mentioned above. Our R&D group has also furnished the SPD film-makers with valuable scientific information relating to reducing or eliminating film defects which can occur during the commercial coating process. In recognition of his outstanding accomplishments regarding these and other matters, the Company has promoted our long-time employee, Steven Slovak, to be Director of Film Development.

The Company continues to expand its patent portfolio, which provides a broad umbrella of protection for both the Company and its licensees. We now hold an aggregate of approximately 457 patents and patent applications worldwide.

Our marketing group has continued its long-term program of bringing the benefits of SPD light-control technology to the attention of people and companies who are in a position to manufacture, distribute, recommend or purchase SPD-Smart products. For example, presentations have been made to many premier international architectural firms, who are now enthusiastically awaiting availability of second-generation SPD-Smart products. The markets for SPD light-control products, particularly in the aerospace, automotive and architectural industries, have been developed to the point where a substantial need now exists for SPD-Smart products.

In response to growing interest in smart glass technology, and the increased levels of activities at our licensees at all levels, our marketing and investor relations departments have spearheaded a major effort to redesign our SmartGlass.com website to enable us to handle a much larger volume of consumer and business inquiries, and offer new information and services. We are pleased to inform you that our new website is scheduled to be launched during the second quarter of 2006.

Over the years Research Frontiers has built up a substantial infrastructure now comprising 34 companies which are licensed to make and sell SPD emulsions, films and end-products, as well as several companies that can laminate SPD films with other glass or plastic layers. This past year we further strengthened our infrastructure by granting a non-exclusive license to SPD Control Systems Corp., whose business objectives are to design, manufacture and sell electronic and total building control systems for powering SPD-Smart products. The availability of these control systems will simplify the marketing, installation and operation of SPD-Smart products, and greatly enhance their functionality and efficiency.

In early October, our licensee Isoclima showcased its new second-generation SPD-Smart light control film at the Vitrum 2005 Glass Show held in Milan, Italy. This event represented the first public display of second-generation SPD-Smart film, which had been produced by Isoclima on large-scale roll-to-roll coating equipment. Our licensee Hitachi continues its progress towards offering SPD film produced at its production facility, and has been working with end-product licensees to ensure that their upcoming commercial production runs meet the specifications of end-product manufacturers and their automotive, aerospace, marine and architectural customers.

With the permission and cooperation of the Company, our emulsion licensee Dainippon Ink & Chemicals (DIC) has been quietly working with toll coating companies in order to assure itself that its emulsions would be satisfactorily coatable into films. DIC's film samples have steadily improved with experience. Recently, DIC asked the Company if we would grant DIC a second license to make and sell film which would supplement its existing emulsion license, and in late March, they obtained a worldwide non-exclusive license which permits them to expand their business to manufacture and sell SPD films to our other licensees worldwide. The first shipments of DIC's next-generation SPD film from its production line have already begun, and DIC also plans to expand production capacity from current levels.

The continuing large investment by the Company and its licensees in SPD technology is being made with all of our eyes on the "prize" of product commercialization and growing sales volumes. In 2005 the Company's loss was $3.75 million ($0.27 per share), down from $4.26 million ($0.33 per share) in 2004, as a result of reduced R&D and operating expenses and an increase in investment income. At year-end 2005 the Company remained free of debt and had cash and cash equivalents of more than $3.6 million. Although this cash position is adequate until early 2007, the Company believes it would be prudent to increase its liquidity, and will therefore seek to raise additional funds during 2006.

The world is filled with windows—in homes, commercial buildings, automobiles, aircraft, boats and more, and a vast quantity of new and replacement windows are entering the market each year. SPD-Smart products will make it possible for people everywhere to aesthetically control their windows and their environment quickly and efficiently without losing their view. By using SPD technology the world is about to become a more beautiful and interesting place in which to live.

We warmly thank our licensees and our employees who have been working hard to make SPD-Smart products a commercial success. And we thank our loyal shareholders for their extraordinary patience as we progress together past the final mountain towards a rewarding future.

Sincerely,

Robert L. Saxe

Robert L. Saxe
Chairman and Chief Executive Officer

Joe Harary

Joseph M. Harary
President and Chief Operating Officer

Common Stock Information

Market Information

The Company's common stock is traded on the NASDAQ Capital Market. As of March 29, 2006, there were 13,812,559 shares of common stock outstanding.

The following table sets forth the range of the high and low selling prices (as provided by the National Association of Securities Dealers) of the Company's common stock for each quarterly period within the past two fiscal years:

Quarter ended	Low	High
March 31, 2004	8.28	13.98
June 30, 2004	6.94	11.55
September 30, 2004	5.13	7.60
December 31, 2004	5.65	7.96
March 31, 2005	5.00	6.59
June 30, 2005	2.76	5.75
September 30, 2005	2.55	3.50
December 31, 2005	3.18	7.00

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

Approximate Number of Security Holders

As of March 29, 2006, there were 610 holders of record of the Company's common stock. The Company estimates that there are approximately 8,200 beneficial holders of the Company's common stock.

Dividends

The Company did not pay dividends on its common stock in 2005 and does not expect to pay any cash dividends in the foreseeable future. There are no restrictions on the payment of dividends.

Issuer Purchases of Equity Securities

None.

Selected Financial Data

The following table sets forth selected data regarding the Company's operating results and financial position. The data should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and the consolidated financial statements and notes thereto, all of which are contained in this Annual Report to shareholders.

Year ended December 31	2005	2004	2003	2002	2001
Statement of Operations Data:					
Fee income	$ 138,742	$ 201,321	$ 258,187	$ 217,519	$ 142,002
Operating expenses (1)	2,624,379	2,633,534	2,537,317	2,631,139	3,155,305
Research and development (1)	1,391,657	1,682,624	1,908,753	1,859,030	2,223,425
Charge for reduction in value of investment in SPD Inc.(2)	–	165,501	615,200	–	–
	4,016,036	4,481,659	5,061,270	4,490,169	5,378,730
Operating loss	(3,877,294)	(4,280,338)	(4,803,083)	(4,272,650)	(5,236,728)
Net investment income (3)	129,762	17,597	30,775	321,534	696,058
Net loss	(3,747,532)	(4,262,741)	(4,772,308)	(3,951,116)	(4,540,670)
Basic and diluted net loss per common share	(.27)	(.33)	(.38)	(.33)	(.38)
Dividends per share	–	–	–	–	–

As of December 31	2005	2004	2003	2002	2001
Balance Sheet Data:					
Total current assets	$3,823,093	$2,716,964	$5,322,083	$5,293,629	$8,272,677
Total assets	3,957,205	2,860,673	5,690,270	6,267,051	9,324,902
Long-term debt, including accrued interest	–	–	–	–	–
Total shareholders equity	3,646,254	2,392,303	5,469,427	5,974,466	9,049,920

(1) During 2002, the Company reclassified costs associated with patents and patent applications from research and development expenses to operating expenses. The amount of patent costs reclassified from research and development expense to operating expense for the year ended December 31, 2001 was approximately $411,000. (2) Reflects a non-cash charge against income of $615,200 recorded by the Company in the first quarter of 2003 to reflect a reduction in the value of its investment in SPD Inc. determined based upon recent financing activity of SPD Inc. The Company also recorded a further non-cash charge against income of $209,704 during the first quarter of 2004. During the fourth quarter of 2004, the Company received a payment of $44,203 as part of a liquidation distribution made by SPD Inc. to its shareholders, resulting in a total net non-cash charge against income of $165,501 in 2004. (3) Net investment income for 2002 includes $64,608 of interest income received from officers of the Company upon payment of notes receivable.

Critical Accounting Policies

The following accounting policies are important to understanding our financial condition and results of operations and should be read as an integral part of the discussion and analysis of the results of our operations and financial position. For additional accounting policies, see note 2 to our consolidated financial statements, "Summary of Significant Accounting Policies."

The Company has entered into a number of license agreements covering potential products using the Company's SPD technology. The Company receives fees and minimum annual royalties under certain license agreements and records fee income on a ratable basis each quarter. In instances when sales of licensed products by its licensees exceed minimum annual royalties, the Company recognizes fee income as the amounts have been earned. Certain of the fees are accrued by, or paid to, the Company in advance of the period in which they are earned resulting in deferred revenue.

The Company expenses costs relating to the development or acquisition of patents due to the uncertainty of the recoverability of these items.

All of our research and development costs are charged to operations as incurred. Our research and development expenses consist of costs incurred for internal and external research and development. These costs include direct and indirect overhead expenses.

The Company has historically used the Black-Scholes option-pricing model to determine the estimated fair value of each option grant. The Black-Scholes model includes assumptions regarding dividend yields, expected volatility, expected lives, and risk-free interest rates. These assumptions reflect our best estimates, but these items involve uncertainties based on market conditions generally outside of our control. As a result, if other assumptions had been used in the current period, stock-based compensation expense could have been materially impacted. Furthermore, if management uses different assumptions in future periods, stock-based compensation expense could be materially impacted in future years.

On occasion, the Company may issue to consultants either options or warrants to purchase shares of common stock of the Company at specified share prices. These options or warrants may vest based upon specific services being performed or performance criteria being met. In accordance with Emerging Issues Task Force Issue 96-18, *Accounting for Equity Instruments that are Issued to Other than Employees for Acquiring, or in Conjunction with Selling, Goods or Services*, the Company would be required to record consulting expenses based upon the fair value of such options or warrants on the date that such options or warrants vest as determined using a Black-Scholes option pricing model. Depending upon the difference between the exercise price and the market price of the Company's common stock on the date that such options or warrants vest, the amount of non-cash expenses that could be recorded as a result of the vesting of such options or warrants can be material.

The Company applied the cost method of accounting for its minority equity interest in SPD Inc., a subsidiary of Hankuk Glass Industries, Inc. Because no public market existed for the common stock of SPD Inc., the Company reviewed the operating performance, financing and forecasts for such entity in assessing the net realizable value of this investment. During 2003, the Company recorded total non-cash accounting charges of $615,200 against income to reflect a reduction in the value of its investment in SPD Inc. These non-cash charges were determined as follows: During the first quarter of 2003, the Company recorded a non-cash charge against income of $255,200 to reflect a reduction in the value of its investment in SPD Inc. determined based upon recent financing activity of SPD Inc. The Company also recorded a further non-cash charge against income of $360,000 as of the end of 2003 to reflect a reduction in the value of its investment in SPD Inc. determined based upon its review of the financial position and results of operations of SPD Inc. as of and for the year ended December 31, 2003. On April 28, 2004, SPD Inc. informed the Company that it was planning to sell its equipment and other assets and cease its business activities. As a result, the Company wrote off its entire remaining investment in SPD Inc. of $209,704 in the first quarter of 2004. During the fourth quarter of 2004, the Company received a payment of $44,203 as part of a liquidation distribution made by SPD Inc. to its shareholders, resulting in a total net non-cash charge against income of $165,501 in 2004.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and reported amounts of revenues and expenses during the reporting periods. Actual results could differ from these estimates. An example of a critical estimate is the full valuation allowance for deferred taxes that was recorded based on the uncertainty that such tax benefits will be realized in future periods.

Results of Operations

2005 vs. 2004 The Company's fee income from licensing activities for 2005 was $138,742, as compared to $201,321 for 2004. This difference in fee income was primarily the result of the timing and amount of minimum annual royalties paid, and the date of receipt of such payment on certain license agreements, by end-product licensees. Certain license fees, which are paid to the Company in advance of the accounting period in which they are earned resulting in the recognition of deferred revenue for the current accounting period, will be recognized as fee income in future periods. Also, licensees may offset some or all of their royalty payments on sales of licensed products for a given period by applying these advance payments towards such earned royalty payments.

Operating expenses decreased by $9,155 for 2005 to $2,624,379 from $2,633,534 for 2004. This decrease was primarily the result of lower marketing, accounting, depreciation and insurance expenses, partially offset by higher payroll, consulting, and patent expenses, and higher stock listing fees and reserves for bad debts.

Research and development expenditures decreased by $290,967 to $1,391,657 for 2005 from $1,682,624 for 2004. This decrease was primarily the result of decreased payroll, depreciation, and other allocated office expenses partially offset by higher materials expense.

Investment income for 2005 was $129,762 as compared to a net gain from its investing activities of $17,597 for 2004. This difference was primarily due to higher interest rates during 2005 and higher cash balances due to the receipt of proceeds from the sale of common stock and warrants in February 2005. Investment income for 2004 was $30,097 prior to a write-down of $12,500 in the Company's investment in common stock of ThermoView Industries.

During 2004, the Company recorded total non-cash accounting charges of $165,501 against income to reflect a reduction in the value of its investment in SPD Inc.

As a consequence of the factors discussed above, the Company's net loss was $3,747,532 ($0.27 per share) for 2005 as compared to $4,262,741 ($0.33 per share) for 2004.

2004 vs. 2003 The Company's fee income from licensing activities for 2004 was $201,321, as compared to $258,187 for 2003. This difference in fee income was primarily the result of the timing and amount of minimum annual royalties paid, and the date of receipt of such payment on certain license agreements, by end-product licensees. Certain license fees, which are paid to the Company in advance of the accounting period in which they are earned resulting in the recognition of deferred revenue for the current accounting period, will be recognized as fee income in future periods. Also, licensees may offset some or all of their royalty payments on sales of licensed products for a given period by applying these advance payments towards such earned royalty payments.

Operating expenses increased by $96,217 for 2004 to $2,633,534 from $2,537,317 for 2003. This increase was primarily the result of higher accounting fees (representing a $201,050 increase), insurance, partially offset by lower payroll, marketing, legal, patent, depreciation, consulting and directors expenses.

Research and development expenditures decreased by $226,129 to $1,682,624 for 2004 from $1,908,753 for 2003. This decrease was primarily the result of decreased payroll and depreciation expenses, partially offset by higher insurance expenses, and rent.

Investment income for 2004 was $17,597 as compared to a net gain from its investing activities of $30,775 for 2003. Investment income for 2004 was $30,097 prior to a write-down of $12,500 in the Company's investment in common stock of ThermoView Industries.

During 2004, the Company recorded total non-cash accounting charges of $165,501 against income to reflect a reduction in the value of its investment in SPD Inc. Of this, the Company recorded a non-cash charge against income of $209,704 during the first quarter of 2004. During the fourth quarter of 2004, the Company received a payment of $44,203 as part of a liquidation distribution made by SPD Inc. to its shareholders, resulting in a total net non-cash charge against income of $165,501 in 2004. During 2003, the Company recorded total non-cash accounting charges of $615,200 against income to reflect a reduction in the value of its investment in SPD Inc. These non-cash charges were determined as follows: During the first quarter of 2003, the Company recorded a non-cash charge against income of $255,200 to reflect a reduction in the value of its investment in SPD Inc. determined based upon recent financing activity of SPD Inc. The Company also recorded a further non-cash charge against income of $360,000 as of the end of 2003 to reflect a reduction in the value of its investment in SPD Inc. determined based upon its review of the financial position and results of operations of SPD Inc. as of and for the year ended December 31, 2003.

As a consequence of the factors discussed above, the Company's net loss was $4,262,741 ($0.33 per share) for 2004 as compared to $4,772,308 ($0.38 per share) for 2003.

Financial Condition, Liquidity and Capital Resources

During 2005, the Company's cash and cash equivalent balance increased by $1,042,622 principally as a result of $5,000,000 of net proceeds received from the issuance of common stock and warrants, offset by cash used to fund the Company's operating activities of $3,920,835. At December 31, 2005, the Company had working capital of $3,512,142 and its shareholders' equity was $3,646,254.

The Company occupies premises under an operating lease agreement which expires on January 31, 2014 and requires minimum annual rent which rises over the term of the lease to approximately $176,669, plus tenant's share of applicable taxes. These lease obligations are summarized over time as of December 31, 2005:

	Payments due by period				
	<1 year	1–3 years	4–5 years	>5 years	Total
Operating lease obligations	159,000	493,000	340,000	365,000	1,357,000

In February 2005, the Company raised $5 million in net proceeds in connection with the registered sale to institutional investors of one million shares of its common stock and the issuance of five-year warrants to purchase 200,000 shares of common stock at an exercise price of $7.50 per share.

The Company expects to use its cash to fund its research and development of SPD light valves and for other working capital purposes. The Company's working capital and capital requirements depend upon numerous factors, including the results of research and development activities, competitive and technological developments, the timing and cost of patent filings, the development of new licensees and changes in the Company's relationships with its existing licensees. The degree of dependence of the Company's working capital requirements on each of the foregoing factors cannot be quantified; increased research and development activities and related costs would increase such requirements; the addition of new licensees may provide additional working capital or working capital requirements, and changes in relationships with existing licensees would have a favorable or negative impact depending upon the nature of such changes. Based upon existing levels of cash expenditures, existing cash reserves and budgeted revenues, the Company believes that it would not require additional funding until the first quarter of 2007. There can be no assurance that expenditures will not exceed the anticipated amounts or that additional financing, if required, will be available when needed or, if available, that its terms will be favorable or acceptable to the Company. Eventual success of the Company and generation of positive cash flow will be dependent upon the extent of commercialization of products using the Company's technology by the Company's licensees and payments of continuing royalties on account thereof.

Inflation

The Company does not believe that inflation has a significant impact on its business.

New Accounting Standards

In December 2004, the Financial Accounting Standards Board, or FASB, issued SFAS No. 123R "Share Based Payment," which replaces SFAS No. 123 and supersedes APB No. 25. SFAS No. 123R requires that the cost resulting from all share-based payment transactions be recognized in the consolidated financial statements. This statement applies to all share-based payment transactions in which an entity acquires goods or services by issuing its shares, options or other equity instruments. This statement establishes fair value as the measurement objective in accounting for share-based payment arrangements and requires all entities to apply a fair-value-based measurement method in accounting for share-based payment transactions with employees, except for equity instruments held by employee share ownership plans. This statement is effective as of the beginning of the first annual reporting period that begins after June 15, 2005, which will be the Company's next fiscal year beginning January 1, 2006. The Company expects that the adoption of SFAS No. 123R could have a material effect on the Company's consolidated financial statements, depending upon the number and terms of stock options issued by the Company in the future, since all options granted prior to January 1, 2006 are fully vested.

Related Party Transactions

None.

Forward Looking Statements

The information set forth in this Report and in all publicly disseminated information about the Company, including the narrative contained in Management's Discussion and Analysis of Financial Condition and Results of Operations above, includes forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, and is subject to the safe harbor created by that section. Readers are cautioned not to place undue reliance on these forward-looking statements as they speak only as of the date hereof and are not guaranteed.

Quantitative and Qualitative Disclosure About Market Risk

At times, the Company invests available cash and cash equivalents in money market funds or in short-term U.S. treasury securities with maturities that are generally two years or less. Although the rate of interest paid on such investments may fluctuate over time, each of the Company's investments, other than in money market funds whose interest yield varies, is made at a fixed interest rate over the duration of the investment. Accordingly, the Company does not believe it is materially exposed to changes in interest rates as it generally holds these treasury securities until maturity.

The Company does not have any sales, purchases, assets or liabilities determined in currencies other than the U.S. dollar, and as such, is not subject to foreign currency exchange risk.

Financial Statements and Supplementary Data

The consolidated financial statements are included in this Report beginning on page 8.

Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

Controls and Procedures

Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures As of the end of the period covered by this Annual Report on Form 10-K, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the CEO and CFO, of the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Exchange Act Rule 13a-15. Based upon that evaluation, the Company's CEO and CFO concluded that the Company's disclosure controls and procedures are effective in timely alerting them to material information relating to the Company (including its consolidated subsidiary) required to be included in the Company's periodic SEC filings. There were no changes in the Company's internal control over financial reporting during the quarterly period ended December 31, 2005 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

Balance Statements YEARS ENDED DECEMBER 31		2005	2004
Assets			
Current assets:	Cash and cash equivalents	$3,644,685	2,602,063
	Royalty receivables, net of reserves of $78,674 in 2005 and $82,522 in 2004	40,000	54,544
	Prepaid expenses and other current assets	138,408	60,357
	Total current assets	3,823,093	2,716,964
Fixed assets, net		111,507	121,104
Deposits		22,605	22,605
	Total assets	$3,957,205	2,860,673
Liabilities and shareholders equity			
Current liabilities:	Accounts payable	$132,584	116,440
	Deferred revenue	5,000	10,000
	Accrued expenses and other	173,367	341,930
	Total current liabilities	310,951	468,370
Shareholders equity:	Common stock, par value $0.0001 per share; authorized 100,000,000 shares, issued and outstanding 13,812,559 and 12,812,559 shares for 2005 and 2004	1,381	1,281
	Additional paid-in capital	62,577,771	57,576,388
	Accumulated deficit	(58,932,898)	(55,185,366)
	Total shareholders equity	3,646,254	2,392,303
Commitments (note 10)			
	Total liabilities and shareholders equity	$3,957,205	2,860,673

See accompanying notes to consolidated financial statements.

Statements of Operations YEARS ENDED DECEMBER 31	2005	2004	2003
Fee income	$ 138,742	201,321	258,187
Operating expenses	2,624,379	2,633,534	2,537,317
Research and development	1,391,657	1,682,624	1,908,753
Charge for reduction in value of investment in SPD Inc.	–	165,501	615,200
	4,016,036	4,481,659	5,061,270
Operating loss	(3,877,294)	(4,280,338)	(4,803,083)
Net investment income	129,762	17,597	30,775
Net loss	(3,747,532)	(4,262,741)	(4,772,308)
Basic and diluted net loss per common share	$ (0.27)	(0.33)	(0.38)
Weighted average number of common shares outstanding	13,692,011	12,792,091	12,436,879

See accompanying notes to consolidated financial statements.

Statements of Shareholders' Equity YEARS ENDED DECEMBER 31, 2005, 2004, 2003

	Common Stock				Accumulated	
	Shares	Amount	Additional Paid-in Capital	Accumulated Deficit	Comprehensive Income (Loss)	Total
Balance, December 31, 2002	12,215,879	$1,222	52,124,811	(46,150,317)	(1,250)	5,974,466
Issuance of common stock	460,025	46	4,201,711	–	–	4,201,757
Comprehensive loss:						
Net loss	–	–	–	(4,772,308)	–	(4,772,308)
Unrealized loss on available for sale securities	–	–	–	–	(3,375)	(3,375)
Total Comprehensive Loss						(4,775,683)
Issuance of stock, options and warrants for services performed	7,509	–	68,887	–	–	68,887
Balance, December 31, 2003	12,683,413	$1,268	56,395,409	(50,922,625)	(4,625)	5,469,427
Issuance of common stock	127,417	13	1,162,589	–	–	1,162,602
Comprehensive loss:						
Net loss	–	–	–	(4,262,741)	–	(4,262,741)
Unrealized loss on available for sale securities	–	–	–	–	4,625	4,625
Total Comprehensive Loss						(4,258,116)
Issuance of stock, options and warrants for services performed	1,729	–	18,390	–	–	18,390
Balance, December 31, 2004	12,812,559	$1,281	57,576,388	(55,185,366)	–	2,392,303
Issuance of Common Stock	1,000,000	100	4,999,900	–	–	5,000,000
Net Loss	–	–	–	(3,747,532)	–	(3,747,532)
Issuance of Options for services performed	–	–	1,483	–	–	1,483
Balance, December 31, 2005	13,812,559	$1,381	62,577,771	(58,932,898)	–	3,646,254

See accompanying notes to consolidated financial statements.

Statements of Cash Flows YEARS ENDED DECEMBER 31

	2005	2004	2003
Cash flows from operating activities:			
Net loss	$ (3,747,532)	(4,262,741)	(4,772,308)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization	46,140	82,736	112,092
Provision for uncollectible royalty receivables	(3,848)	32,522	50,000
Charge for reduction in value of investment in SPD Inc.	–	165,501	615,200
Expense relating to cashless exercise of stock options	–	15,707	40,987
Expense relating to issuance of stock, options and warrants for services performed	1,483	2,683	27,900
Impairment loss on marketable securities	–	12,500	–
Changes in assets and liabilities:			
Royalty receivables	18,392	72,825	(71,744)
Prepaid expenses and other current assets	(78,051)	21,670	(55,366)
Deferred revenue	(5,000)	(13,683)	11,683
Accounts payable and accrued expenses	(152,419)	261,210	(83,425)
Net cash used in operating activities	(3,920,835)	(3,609,070)	(4,124,981)
Cash flows from investing activities:			
Purchases of fixed assets	(36,543)	(67,962)	(47,155)
Proceeds from liquidation of SPD Inc.	–	44,203	–
Investment in SPD Inc., at cost	–	–	(74,902)
Net cash used in investing activities	(36,543)	(23,759)	(122,057)
Cash flows from financing activities:			
Proceeds from issuances of common stock and warrants	5,000,000	1,162,602	4,201,757
Net cash provided by financing activities	5,000,000	1,162,602	4,201,757
Net increase (decrease) in cash and cash equivalents	1,042,622	(2,470,227)	(45,281)
Cash and cash equivalents at beginning of year	2,602,063	5,072,290	5,117,571
Cash and cash equivalents at end of year	$ 3,644,685	2,602,063	5,072,290

See accompanying notes to consolidated financial statements.

December 31, 2005, 2004, 2003

1. Business

Research Frontiers Incorporated ("Research Frontiers" or the "Company") operates in a single business segment which is engaged in the development and marketing of technology and devices to control the flow of light. Such devices, often referred to as "light valves" or suspended particle devices (SPDs), use colloidal particles that are either incorporated within a liquid suspension or a film, which is usually enclosed between two sheets of glass or plastic having transparent, electrically conductive coatings on the facing surfaces thereof. At least one of the two sheets is transparent. SPD technology, made possible by a flexible light-control film invented by Research Frontiers, allows the user to instantly and precisely control the shading of glass/plastic manually or automatically. SPD technology has numerous product applications, including: SPD-Smart™ windows, sunshades, skylights and interior partitions for homes and buildings; automotive windows, sunroofs, sun-visors, sunshades, rear-view mirrors, instrument panels and navigation systems; aircraft windows; eyewear products; and flat panel displays for electronic products. SPD-Smart light control film is now being used in architectural, automotive, marine, aerospace and appliance applications.

The Company has historically utilized its cash and the proceeds from maturities of its investments to fund its research and development of SPD light valves and for other working capital purposes. The Company's working capital and capital requirements depend upon numerous factors, including the results of research and development activities, competitive and technological developments, the timing and cost of patent filings, and the development of new licensees and changes in the Company's relationships with its existing licensees. The degree of dependence of the Company's working capital requirements on each of the foregoing factors cannot be quantified; increased research and development activities and related costs would increase such requirements; the addition of new licensees may provide additional working capital or working capital requirements, and changes in relationships with existing licensees would have a favorable or negative impact depending upon the nature of such changes. There can be no assurance that expenditures will not exceed the anticipated amounts or that additional financing, if required, will be available when needed or, if available, that its terms will be favorable or acceptable to the Company. Eventual success of the Company and generation of positive cash flow will be dependent upon the commercialization of products using the Company's technology by the Company's licensees and payments of continuing royalties on account thereof. To date, the Company has not generated sufficient revenue from its licensees to fund its operations.

2. Summary of Significant Accounting Policies Cash and Cash Equivalents

The Company considers securities purchased with original maturities of three months or less to be cash equivalents. Cash equivalents consist of short-term investments in money market accounts at December 31, 2005 and 2004.

Marketable Investment Securities The Company classifies its securities (equity security) into available-for-sale which are recorded at fair value with unrealized holding gains and losses excluded from earnings and are reported as a separate component of shareholders' equity until realized. Dividend and interest income are recognized when earned. Cost is maintained on a specific identification basis for purposes of determining realized gains and losses on sales of investments. A decline in the market value of any available-for-sale security below cost that is deemed to be other than temporary results in a reduction in carrying amount to fair market value. The impairment is charged to earnings and a new cost basis for this security is established. During the fourth quarter of 2004, the Company reduced the investment balance to $0 based upon a continued reduction in the market price of this equity security, and recorded a charge to net investment income of $12,500.

Royalties Receivable Royalties receivable are recorded at the amounts specified within the license agreements when the collectibility of the receivable is reasonably assured. The receivables do not bear interest. The allowance for doubtful accounts is the Company's best estimate of the amount of probable credit losses in the Company's existing royalties receivable. The Company determines the allowance based on historical write off experience. The Company reviews its allowance for doubtful accounts periodically. Past due accounts are reviewed individually for collectibility. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote.

Fixed Assets Fixed assets are carried at cost. Depreciation and amortization are computed using the straight-line method over the estimated useful lives of the assets.

Fee Income Fee income represents amounts earned by the Company under various license and other agreements (note 9) relating to technology developed by the Company. During fiscal 2005, four licensees of the Company accounted for 36%, 14%, 13% and 11%, respectively of fee income recognized during the year. During fiscal 2004, four licensees of the Company accounted for 25%, 19%, 13% and 12%, respectively of fee income recognized during the year. During fiscal 2003, four licensees of the Company accounted for 19%, 19%, 19% and 15%, respectively of fee income recognized during the year.

Basic and Diluted Loss Per Common Share Basic earnings (loss) per share excludes any dilution. It is based upon the weighted average number of common shares outstanding during the period. Dilutive earnings (loss) per share reflects the potential dilution that would occur if securities or other contracts to issue common stock were exercised or converted into common stock. The Company's dilutive earnings (loss) per share equals basic earnings (loss) per share for each of the years in the three-year period ended December 31, 2005 because all common stock equivalents (*i.e.*, options and warrants) were antidilutive in those periods. The number of options and warrants that were not included because their effect is antidilutive was 3,075,593, 2,628,400, and 2,686,975, for 2005, 2004, and 2003, respectively.

Research and Development Costs Research and development costs are charged to expense as incurred.

Patent Costs The Company expenses costs relating to the development or acquisition of patents due to the uncertainty of the recoverability of these items.

Use of Estimates The preparation of the Company's consolidated financial statements requires management of the Company to make a number of estimates and assumptions relating to the reported amount of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during this period. Significant items subject to such estimates and assumptions include the valuation of deferred income tax assets. Actual results could differ from those estimates.

Income Taxes Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Fair Value of Financial Instruments The fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties. The carrying amounts of all financial instruments classified as a current asset or current liability are deemed to approximate fair value because of the short maturity of those instruments.

Stock-Based Compensation In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation —Transition and Disclosure." SFAS No. 148 provides alternative methods of transition for a voluntary change to the fair value method of accounting for stock-based employee compensation as originally provided by SFAS No. 123, "Accounting for Stock-Based Compensation." Additionally, SFAS No. 148 amends the disclosure provisions of SFAS No. 123 to require prominent disclosure in both the annual and interim financial statements about the method of accounting for stock-based compensation and the effect of the method used on reported results. The Company adopted the disclosure provisions of this statement in the fiscal quarter ended March 31, 2003.

The exercise price for stock options granted are generally set at the average of the high and low trading prices of the Company's common stock on the trading date immediately prior to the date of grant, and the related number of shares granted are fixed at the date of grant. Under the principles of APB Opinion No. 25, the Company does not recognize compensation expense associated with the grant of stock options. SFAS No. 123 requires the use of option valuation models to determine the fair value of options granted after 1995. Pro forma information regarding net loss and net loss per share shown below was determined as if the Company had accounted for its employee stock options and shares sold under its stock purchase plan under the fair value method set forth in SFAS No. 123.

The fair value of the options was estimated at the date of grant using a Black-Scholes option pricing model. For purposes of pro forma disclosures, the estimated fair value of the options is amortized over the options' vesting periods.

The following table illustrates the effect on net loss and earnings per share as if the fair value method had been applied:

	2005	2004	2003
Net loss, as reported	$ (3,747,532)	$ (4,262,741)	$ (4,772,308)
Add: Stock-based employee compensation expense included in reported net loss	1,483	18,390	40,987
Deduct: Total stock-based employee compensation determined under fair-value based method for all awards	(955,584)	(693,943)	(873,262)
Pro forma	$ (4,701,633)	$ (4,938,294)	$ (5,604,583)
Basic and diluted net loss per common share			
As reported	$ (0.27)	$ (0.33)	$ (0.38)
Pro forma	$ (0.34)	$ (0.38)	$ (0.45)

The per share weighted average fair value of stock options granted during 2005, 2004, and 2003, was approximately $2.22, $4.37, and $7.45, respectively, on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions:

Grant date	Expected dividend yield	Risk-Free interest rate	Expected stock volatility	Expected life in years
December 2005	0%	4.251%	68.910%	5.00
July 2005	0%	3.788%	70.800%	5.00
January 2004	0%	3.225%	79.580%	4.53
December 2004	0%	3.521%	70.650%	4.53
June 2003	0%	1.750%	82.050%	3.77

(l) Accumulated Other Comprehensive Income (loss)

The change in accumulated other comprehensive income (loss) was a reclassification adjustment of $4,625 for the year-ended December 31, 2004 reflecting the write off of an equity investment for an other than temporary impairment (see note 2(b)).

The change in accumulated other comprehensive income (loss) was $3,375 for the year-ended December 31, 2003 for the unrealized holding losses on available-for-sale securities for the period.

Revenue Recognition The Company has entered into a number of license agreements covering its light control technology. The Company receives minimum annual royalties under certain license agreements and records fee income on a ratable basis each quarter. In instances when sales of licensed products by its licensees exceed minimum annual royalties, the Company recognizes fee income as the amounts have been earned. Certain of the fees are accrued by, or paid to, the Company in advance of the period in which they are earned resulting in deferred revenue. Such excess amounts are recorded as deferred revenue and recognized into income in future periods as earned.

Impairment of Long-Lived Assets In accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," the Company reviews long-lived assets to determine whether an event or change in circumstances indicates the carrying value of the asset may not be recoverable. The Company bases its evaluation on such impairment indicators as the nature of the assets, the future economic benefit of the assets and any historical or future profitability measurements, as well as other external market conditions or factors that may be present. If such impairment indicators are present or other factors exist that indicate that the carrying amount of the asset may not be recoverable, the Company determines whether an impairment has occurred through the use of an undiscounted cash flows analysis at the lowest level for which identifiable cash flows exist. If impairment has occurred, the Company recognizes a loss for the difference between the carrying amount and the fair value of the asset. Fair value is the amount at which the asset could be bought or sold in a current transaction between a willing buyer and seller other than in a forced or liquidation sale and can be measured as the asset's quoted market price in an active market or, where an active market for the asset does not exist, the Company's best estimate of fair value based on discounted cash flow analysis. Assets to be disposed of by sale are measured at the lower of carrying amount or fair value less estimated costs to sell. The implementation of SFAS No. 144 had no impact on the Company's financial position or results of operations.

3. Investment in SPD Inc.

During the second quarter of 2001, the Company, through its wholly-owned subsidiary, SPD Enterprises, Inc., invested approximately $750,000 for a minority equity interest in SPD Inc., a subsidiary of Hankuk Glass Industries Inc., Korea's largest glass manufacturer, which was dedicated exclusively to the production of suspended particle device (SPD) light-control film and a wide variety of end-products using SPD film. In April 2003, the Company's wholly-owned subsidiary, SPD Enterprises, Inc., invested $74,902 in SPD Inc., raising its equity ownership from 6.67% to 6.91%. SPD Inc.'s parent company invested at the same time and at the same price, $748,931, raising its equity ownership in SPD Inc. from 66.67% to 69.09%. During 2003, the Company recorded total non-cash accounting charges of $615,200 against income to reflect a reduction in the value of its investment in SPD Inc. These non-cash charges were determined as follows: During the first quarter of 2003, the Company recorded a non-cash charge against income of $255,200 to reflect a reduction in the value of its investment in SPD Inc. determined based upon the April 2003 financing, and the Company recorded a further non-cash charge against income of $360,000 as of the end of 2003 to reflect a reduction in the value of its investment in SPD Inc. determined based upon its review of the financial position and results of operations of SPD Inc. as of and for the year ended December 31, 2003. On April 28, 2004, SPD Inc. informed the Company that it was planning to sell its equipment and other assets and cease its business activities. As a result, the Company wrote off its entire remaining investment in SPD Inc. of $209,704 in the first quarter of 2004. During the fourth quarter of 2004, the Company received a payment of $44,203 as part of a liquidation distribution made by SPD Inc. to its shareholders, resulting in a total net non-cash charge against income of $165,501 in 2004. The Company's license agreement with Hankuk Glass Industries provided for the payment of minimum annual royalties to the Company in 2002 and 2003. These amounts were all paid in full in 2004.

4. Marketable Investment Securities

The fair value of marketable investment securities is based upon quoted market prices. The amortized cost, gross unrealized holding gains and fair value for the Company's investment security at December 31, 2003 were as follows:

	Amortized cost	Gross unrealized holding Gains	(Losses)	Fair value
Available-for-sale securities:				
Equity security available-for-sale	$12,500	–	($4,625)	$7,875

During the fourth quarter of 2004, the Company charged the remaining value ($7,875) of this security to net investment income as the result of an impairment that was deemed other than temporary.

5. Fixed Assets

Fixed assets and their estimated useful lives, are as follows:

	2005	2004	Estimated useful life
Equipment and furniture	$1,181,824	1,167,771	5 years
Leasehold improvements	331,689	309,199	Life of lease or estimated life if shorter
	1,513,513	1,476,970	
Less accumulated depreciation and amortization	1,402,006	1,355,866	
	$ 111,507	121,104	

6. Accrued Expenses and Other

Accrued expenses consist of the following at December 31, 2005 and 2004:

	2005	2004
Payroll, bonuses and related benefits	$ 83,253	103,406
Professional services	47,777	206,674
Deferred rent	19,006	10,691
Other	23,331	21,159
	$173,367	341,930

7. Income Taxes

There was no income tax expense in 2005, 2004 and 2003 due to losses incurred by the Company.

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets at December 31, 2005 and 2004 are presented below.

	2005	2004
Deferred tax assets:		
Depreciation	$ 93,000	$ 100,000
Capital loss carryforward	66,000	312,000
Allowance for bad debts	32,000	33,000
Net operating loss carryforwards	18,307,000	17,118,000
Research and other credits	979,000	951,000
Other temporary differences	15,000	15,000
Total gross deferred tax assets	19,492,000	18,529,000
Less valuation allowance	19,492,000	18,529,000
	$ –	$ –

In assessing the realizability of deferred tax assets, the Company 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 future taxable income during the period in which those temporary differences become deductible. The Company considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. Based upon its historical operating losses, the Company believes that it is more likely than not that deferred tax assets will not be realized. Accordingly, the Company has recorded a full valuation allowance against the deferred tax assets, as they will not be realized unless the Company achieves profitable operations in the future.

At December 31, 2005, the Company had a net operating loss carryforward for federal income tax purposes of $45,800,000, varying amounts of which will expire in each year from 2006 through 2025. Research and other credit carryforwards of $979,000 are available to the Company to reduce income taxes payable in future years principally through 2025. Net operating loss carryforwards of $956,000 and research and other credit carryforwards of $40,000 are scheduled to expire during fiscal 2006, if not utilized.

8. Shareholders' Equity

During 2003, the Company received $4,201,757 of net cash proceeds from (i) the issuance of 25,000 shares of common stock of the Company (along with a ten-year warrant to purchase 25,000 shares of common stock of the Company at an exercise price of $9.00 per share) in a private placement to a director of the Company resulting in net proceeds of $165,000; (ii) 364,300 shares of common stock issued upon the exercise of warrants resulting in net proceeds of $3,527,148; and (iii) the issuance of 69,475 shares of common stock issued upon the exercise of options resulting in net proceeds of $509,590. In addition, 3,754 shares were issued through the cashless exercise of certain options and warrants, resulting in non-cash directors expense of $40,987 being recorded, and 9,995 shares with a value of $108,995 were delivered to the Company and immediately retired in payment of the exercise price of options to purchase 15,000 shares.

During 2004, the Company received $1,162,602 of net cash proceeds from the issuance of (i) 104,917 shares of common stock issued upon the exercise of warrants resulting in net proceeds of $987,037; and (ii) 22,500 shares of common stock issued upon the exercise of options resulting in net proceeds of $175,565. In addition, 1,729 shares were issued through the cashless exercise of an option to purchase 17,500 shares. In connection therewith, the Company recorded a non-cash compensation expense of $15,707 in 2004.

In February 2005, the Company raised $5 million in net proceeds in connection with the registered sale to institutional investors of one million shares of its common stock and the issuance of five-year warrants to purchase 200,000 shares of common stock at an exercise price of $7.50 per share.

Options and Warrants ***Options*** In 1992, the shareholders approved a stock option plan (1992 Stock Option Plan) which provides for the granting of both incentive stock options at the fair market value at the date of grant and nonqualified stock options at or below the fair market value at the date of grant to employees or non-employees who, in the determination of the Board of Directors, have made or may make significant contributions to the Company in the future. The Company initially reserved 468,750 shares of its common stock for issuance under this plan. In 1994 and 1996, the Company's shareholders approved an additional 300,000 shares and 450,000 shares, respectively, for issuance under this plan. As of December 31, 2001, no options were available for issuance under this Plan and this Plan expired during 2002.

In 1998, the shareholders approved a stock option plan (1998 Stock Option Plan) which provides for the granting of both incentive stock options at the fair market value at the date of grant and nonqualified stock options at or below the fair market value at the date of grant to employees or non-employees who, in the determination of the Board of Directors, have made or may make significant contributions to the Company in the future. The Company may also award stock appreciation rights or restricted stock under this plan. The Company initially reserved 540,000 shares of its common stock for issuance under this plan. In 1999, the Company's shareholders approved an additional 545,000 shares for issuance under this Plan, and in each of 2000 and 2002, the Company's shareholders approved an additional 600,000 shares for issuance under this Plan. As of December 31, 2005, awards for 15,379 shares of common stock were available for issuance under this Plan.

At the discretion of the Board of Directors, options expire in ten years or less from the date of grant and are generally fully exercisable upon grant but in some cases may be subject to vesting in the future. Full payment of the exercise price may be made in cash or in shares of common stock valued at the fair market value thereof on the date of exercise, or by agreeing with the Company to cancel a portion of the exercised options. When an employee exercises a stock option through the surrender of options held, rather than of cash for the option exercise price, compensation expense is recorded in accordance with APB Opinion No. 25. Accordingly, compensation expense is recorded for the difference between the quoted market value of the Company's common stock at the date of exchange and the exercise price of the option. During 2004 and 2003, the

Company recorded non-cash expenses of $15,707 and $40,987, respectively, related to cashless exercises of options.

Activity in stock options is summarized below:

	Number of shares subject to option	Weighted average exercise price
Balance at December 31, 2002	2,435,750	$12.04
Granted	86,500	$12.62
Cancelled	(3,000)	$15.41
Exercised	(84,475)	$ 7.32
Balance at December 31, 2003	2,434,775	$12.22
Granted	148,750	$ 7.34
Cancelled	(134,325)	$ 9.16
Exercised	(40,000)	$ 7.97
Balance at December 31, 2004	2,409,200	$12.16
Granted	430,193	$ 7.42
Cancelled	(148,400)	$11.27
Balance at December 31, 2005	2,690,993	$11.45

The following table summarizes information about stock options at December 31, 2005:

Range of exercise price	Options out-standing	Weighted average remaining contractual life (years)	Weighted average exercise price	Shares exercisable	Weighted average exercise price
$3.00–$ 6.00	388,433	7.86	$ 5.86	388,433	$ 5.86
$6.01–$ 7.50	650,250	3.44	$ 7.11	650,250	$ 7.11
$7.51–$ 9.00	465,800	3.44	$ 8.38	465,800	$ 8.38
$9.01–$12.00	413,960	5.98	$10.50	413,960	$10.50
$12.01–$15.00	332,250	6.17	$13.29	332,250	$13.29
$15.01–$19.00	109,000	4.91	$18.99	109,000	$19.00
$19.01–$37.03	331,300	5.20	$27.75	325,300	$27.75
	2,690,933	5.08	$11.46	2,684,993	$11.44

During 2005, 2004 and 2003, the Company issued options to a consultant to purchase 500, 750 and 5,000 shares of common stock at an exercise price of $5.60, $6.175 and $9.54 per share, respectively. The Company recorded $1,483, $2,683, and $27,900 of non-cash expense in connection with the issuance of these options.

Warrants Activity in warrants is summarized below, excluding the effect of the warrants discussed in note 8(c)):

	Number of shares underlying warrants granted	Exercise price
Balance at December 31, 2002	227,200	$5.88–13.50
Exercised	–	–
Terminated	–	–
Issued	25,000	9.00
Balance at December 31, 2003	252,200	5.88–13.50
Exercised	5,500	5.88
Terminated	(27,500)	5.88 –9.35
Issued	–	–
Balance at December 31, 2004	219,200	5.88–13.50
Exercised	–	–
Terminated	(34,600)	7.31–13.50
Issued	200,000	7.50
Balance at December 31, 2005	384,600	$5.88 –9.63

Warrants generally expire from two to ten years from the date of issuance. At December 31, 2005, the number of warrants exercisable was 379,600 at a weighted average exercise price of $7.64 per share.

During 2003, a warrant to purchase 25,000 shares of common stock at an exercise price of $9.00 per share was issued to a director of the Company in connection with a private placement.

Class A and Class B Warrants On October 1, 1998, the Company announced that Ailouros Ltd., a London-based institutional money management fund, committed to purchase up to $15 million worth of common stock of the Company through December 31, 2001. This commitment was in the form of a Class A Warrant issued to Ailouros Ltd. which gave the Company the option in any three-month period to deliver a put notice to Ailouros requiring them to purchase an amount of common stock specified by the Company at a price equal to the greater of (A) 92% of the seven-day average trading price per share of common stock, or (B) a minimum or floor price per share set by the Company from time to time. The pricing was initially subject to an overall cap of $15 per share, which cap was subsequently eliminated by mutual agreement so that the Company could put stock to Ailouros at selling prices in excess of $15 per share. The Company was not required to sell any shares under the agreement. Before the beginning of each of a series of three-month periods specified by the Company, the Company determined the amount of common stock that the Company wished to issue during such three-month period. The Company also set the minimum selling or floor price, which could be reset by the Company in its sole discretion prior to the beginning of any subsequent three-month period. Therefore, at the beginning of each three-month period, the Company could determine how much common stock, if any, was to be sold (the amount of which could range from $0 to $1.5 million during such three-month period), and the minimum selling price per share. In March 2000, Ailouros agreed to expand its commitment beyond the original $15 million, thereby giving the Company the right to raise additional funds from Ailouros so long as the Company did not have to issue more shares than were originally registered with the Securities and Exchange Commission, and in December 2001 the expiration date of the Class A Warrant was extended to December 31, 2003. In December 2003, this expiration date for the Class A Warrant was further extended to December 31, 2005. As of March 15, 2004, no shares remained registered for future issuance under the Class A Warrant.

In connection with the financing, the Company also issued Ailouros Ltd. a Class B Warrant which expires on September 30, 2008. The Class B Warrant is exercisable into 65,500 shares at an exercise price of $8.25 per share which represents 120% of average of the closing bid and ask price of the Company's common stock on the date of the Class B Warrants issuance. The Class B Warrant has not been exercised to date. Ailouros paid the Company $10,000 upon issuance of the Class A Warrant and the Class B Warrant.

9. License and Other Agreements

The Company has entered into a number of license agreements covering various products using the Company's SPD technology. Licensees of Research Frontiers who incorporate SPD technology into end products will pay Research Frontiers an earned royalty of 5-15% of net sales of licensed products under license agreements currently in effect, and may also be required to pay Research Frontiers fees and minimum annual royalties. To the extent that products have been sold resulting in earned royalties under these license agreements in excess of these minimum advance royalty payments, the Company has recorded additional royalty income. Licensees who sell products or components to other licensees of Research Frontiers do not pay a royalty on such sale and Research Frontiers will collect such royalty from the licensee incorporating such products or components into their own end-products. Research Frontiers license agreements typically allow the licensee to terminate the license after some period of time, and give Research Frontiers only limited rights to terminate before the license expires. Most licenses are non-exclusive and generally last as long as our patents remain in effect. To date, revenues from license agreements have not been sufficient to fund the Company's costs of operation.

10. Commitments

The Company has an employment agreement with one of its officers which provides for an annual base salary of $379,798 through December 31, 2006.

The Company has a defined contribution profit sharing (401K) plan covering employees who have completed one year of service. Contributions are made at the discretion of the Company. The Company did not make any contributions to this plan for 2005, 2004 or 2003.

The Company occupies premises under an operating lease agreement which expires on January 31, 2014. At December 31, 2005, the approximate minimum annual future rental commitment under this lease for the next five years are as follows:

2006:	$159,000
2007:	$162,000
2008:	$164,000
2009:	$167,000
20010:	$169,000
Thereafter:	$536,000

Rent expense, including other occupancy related expenses, amounted to approximately $175,000, $168,000, and $152,000, for 2005, 2004, and 2003, respectively.

11. Rights Plan

In February 2003, the Company's Board of Directors adopted a Stockholders' Rights Plan and declared a dividend distribution of one Right for each outstanding share of Company common stock to stockholders of record at the close of business on March 3, 2003. Subject to certain exceptions listed in the Rights Plan, if a person or group has acquired beneficial ownership of, or commences a tender or exchange offer for, 15% or more of the Company's common stock, unless redeemed by the Company's Board of Directors, each Right entitles the holder (other than the acquiring person) to purchase from the Company $120 worth of common stock for $60. If the Company is merged into, or 50% or more of its assets or earning power is sold to, the acquiring company, the Rights will also enable the holder (other than the acquiring person) to purchase $120 worth of common stock of the acquiring company for $60. The Rights will expire at the close of business on February 18, 2013, unless the Rights Plan is extended by the Company's Board of Directors or unless the Rights are earlier redeemed by the Company at a price of $.0001 per Right. The Rights are not exercisable during the time when they are redeemable by the Company.

12. Selected Quarterly Financial Data (Unaudited)

2005 by Quarter	First	Second	Third	Fourth
Fee income	$ 41,250	$ 36,992	$ 26,750	$ 33,750
Operating loss	(962,734)	(999,180)	(951,098)	(964,282)
Net loss	(940,498)	(962,104)	(914,867)	(930,063)
Basic and diluted net loss per common share (1)	(.07)	(.07)	(.07)	(.07)

2004 by Quarter	First	Second	Third	Fourth
Fee income	$ 37,319	$ 56,008	$ 41,648	$ 66,346
Operating loss	(1,335,797)	(1,013,267)	(879,020)	(1,052,254)
Net loss	(1,328,814)	(1,007,038)	(870,809)	(1,056,080)
Basic and diluted net loss per common share (1)	(.10)	(.08)	(.07)	(.08)

(1) Since per share information is computed independently for each quarter and the full year, based on the respective average number of common shares outstanding, the sum of the quarterly per share amounts does not necessarily equal the per share amounts for the year.

Report of Independent Registered Public Accounting Firms

The Shareholders and Board of Directors
Research Frontiers Incorporated:

We have audited the accompanying consolidated balance sheet of Research Frontiers Incorporated as of December 31, 2005 and the related consolidated statements of operations shareholders equity, and cash flows for the year then ended. Our audit also included the financial statement schedule for year ended December 31, 2005, as listed in Item 15(a). These financial statements and schedule 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 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 and financial statement schedule 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 audits 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 and financial statement schedule, 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 Research Frontiers Incorporated at December 31, 2005, 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. Also, in our opinion, the financial statement schedule presents fairly, in all material respects, the information set forth therein.

BDO Seidman, LLP

BDO Seidman, LLP
Melville, New York
March 3, 2006

The Shareholders and Board of Directors
Research Frontiers Incorporated:

We have audited the accompanying consolidated balance sheet of Research Frontiers Incorporated and subsidiary as of December 31, 2004, and the related consolidated statements of operations, shareholders equity and cash flows for each of the years in the two-year period ended December 31, 2004. In connection with our audits of the consolidated financial statements, we also have audited the information included in the financial statement schedule as listed in Item 15(a) for each of the years in the two-year period ended December 31, 2004. These consolidated financial statements and the financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements and the financial statement schedule based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Research Frontiers Incorporated and subsidiary as of December 31, 2004, and the results of their operations and their cash flows for each of the years in the two-year period ended December 31, 2004, in conformity with U.S. generally accepted accounting principles. Also in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein for each of the years in the two-year period ended December 31, 2004.

KPMG LLP

KPMG LLP
Melville, New York
March 15, 2005

Corporate Directory

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