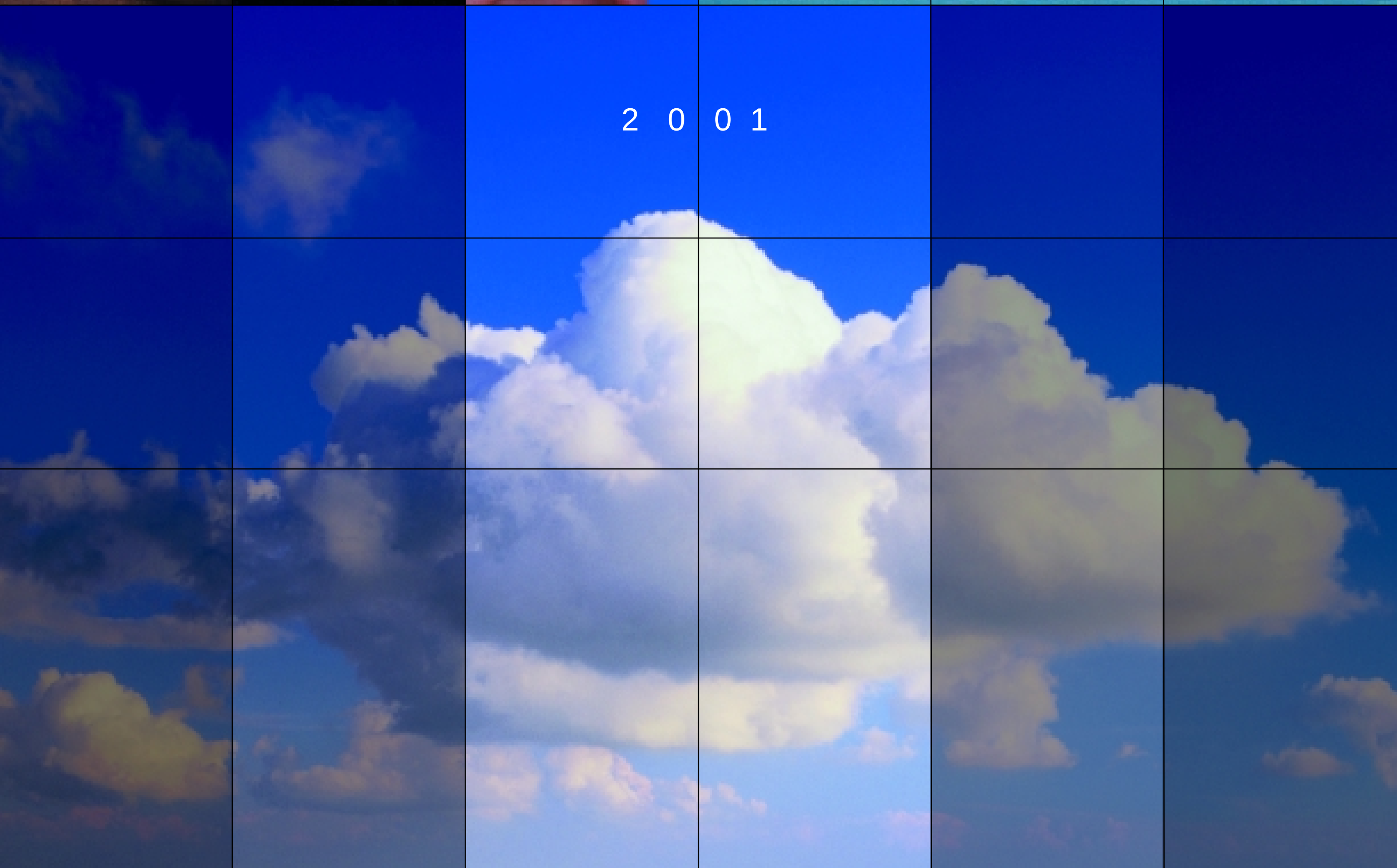
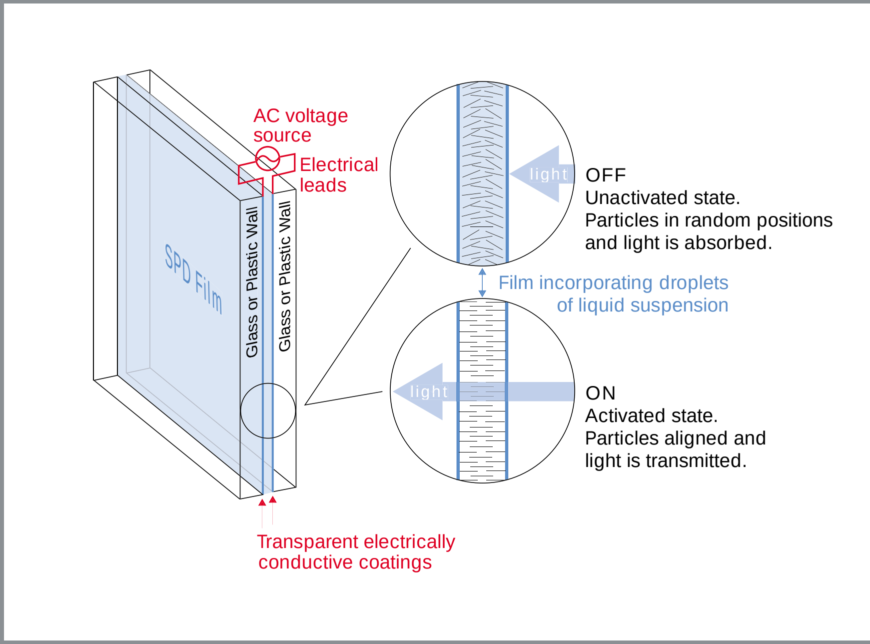
RESEARCH FRONTIERS

ANNUAL REPORT

2001



C O N T E N T S



The illustration above 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.

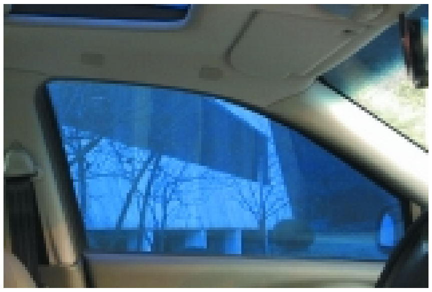
“Research Frontiers is no longer a ‘concept company’.”

—Letter to Shareholders
Research Frontiers
2001 Annual Report

LETTER TO OUR SHAREHOLDERS

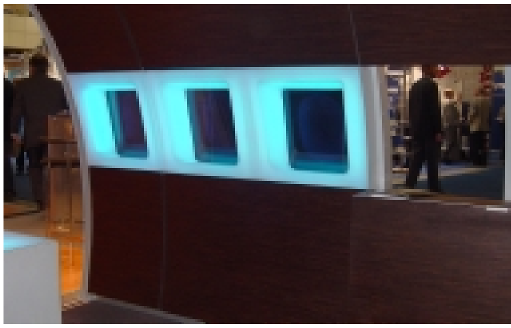
Since our letter to you in last year's Annual Report, there have been some dramatic and exciting changes at Research Frontiers and in the various industries that our SPD light-control technology serves. In 2001 the Company's most important long-term goal—commercialization of SPD technology—was successfully accomplished! The supply infrastructure that we have been building over the years continues to grow and now consists of 15 companies licensed to make SPD emulsions, films and end-products. And now that SPD Inc.'s factory in Incheon, South Korea is in production, SPD-Smart™ products are beginning to be sold for a variety of applications worldwide.

In January 2001, our licensee, Hankuk Glass Industries (HGI) announced the creation of SPD Inc. as a subsidiary whose business is exclusively devoted to the manufacture and sale of SPD film and end-products. Three months later in April, SPD Inc. announced acquisition of a manufacturing plant located in Incheon, South Korea. SPD Enterprises, Inc., a subsidiary of Research Frontiers, purchased a minority interest in SPD Inc. for 1 billion won (about $750 thousand). Several of Korea's leading venture capital firms and major banks also purchased minority interests. Plant capacity is about 4.3 million square feet per year, and can be expanded if necessary. We are extremely pleased to report that mass production of SPD film began during the first quarter of 2002 and SPD Inc. is now offering shipment one month after receiving orders from its customers. SPD Inc. now offers laminated glass with SPD film already incorporated into it, as well as energy-efficient insulating glass units (IGUs) which are windows consisting of SPD-Smart™ laminated glass, an air gap, and a separate glass sheet having low emissivity (heat reflecting) and UV blocking coatings. These products have electrical connections in place and can be readily placed in a frame and electrically activated. SPD Inc. has reported that the number of daily inquiries they receive from customers has increased sevenfold after attending their first major trade show of the



PHOTOGRAPH COURTESY OF HANKUK GLASS INDUSTRIES/SPD INC.

Left: SPD-Smart™ automobile side window. Right: Research Frontiers licensee, InspecTech Aero Service, Inc., in conjunction with their customer, Aircabin GmbH, showcase SPD-Smart™ aircraft windows in the ACJ (Airbus Corporate Jet) display at the Aircraft Interiors International Expo held in April 2002 in Hamburg, Germany.



PHOTOGRAPH COURTESY OF INSPECTECH AERO SERVICE, INC.

year (GlassTech Asia) held in Singapore in late February, and business has increased again for them after their North American debut of an SPD-Smart™ House at this year's National Glass Association show in Houston, Texas in late March.

Recently, the world's largest glass company, Saint-Gobain, increased its ownership position in our licensee HGI to over 35%. The two companies have had close business relations for many years, and we regard their alliance as potentially very promising for the worldwide dissemination of SPD technology.

On August 15, 2001, the sale of the world's first product using SPD technology was announced by our licensee InspecTech Aero Service, Inc. Incorporating SPD film purchased from SPD Inc. into plastic, InspecTech obtained FAA certification, and announced to the world that it had equipped the world's first executive jet (a Learjet 25C) with SPD-Smart™ windows. Subsequently, InspecTech has also announced installing SPD-Smart™ windows in two Bell/Textron helicopters, one of which was offered as original equipment and even featured in the Neiman Marcus 2001 Christmas catalog, and subsequently sold. In addition to these announced installations, InspecTech has reported that they have been filling other customer orders, including orders for SPD aircraft windows from some of the world's largest jet manufacturers. In April 2002, InspecTech and Aircabin GmbH, a wholly-owned subsidiary of Airbus, exhibited the interior of an Airbus Corp. Jetliner (ACJ) with innovative interior lighting systems, including SPD windows. This aircraft mock-up was featured at the Hamburg Airshow and received very favorable customer and media attention.

InspecTech plans to achieve its announced sales goal of reaching 5,000 SPD aircraft windows per month in 2002 by selling and installing these windows through various market channels, including manufacturers, completion centers, aftermarket suppliers, as well as selling directly to end-users such as airlines, charter fleets and fractional ownership companies. InspecTech is partnering with various companies to supply

Near right: Interior of Bell 430 Helicopter featuring SPD-Smart™ windows and specially-designed touch switch below window. Far right: Exterior of Neiman Marcus Limited Edition Bell 430 Helicopter equipped with SPD-Smart™ windows.

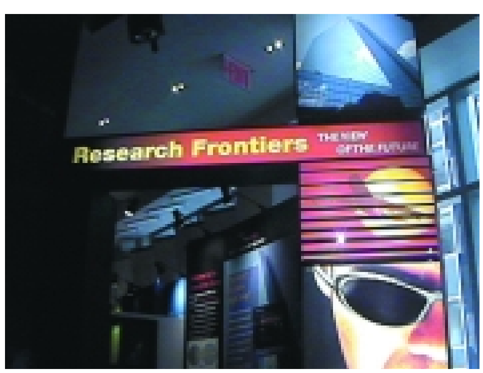
PHOTOGRAPHS COURTESY OF INSPECTECH AERO SERVICE, INC.

components to be used in SPD window systems, an example of which is its recently announced alliance with Goodrich Corporation which will be producing power supplies and switch circuitry for elegant touch-control switches specially designed for InspecTech's SPD-Smart™ aircraft windows.

Depending on the type of aircraft, SPD-Smart™ aircraft windows generally sell in the range of about $400–$1,500 per window, and Research Frontiers will receive from InspecTech a royalty of 10% of net sales. Worldwide, it is estimated that there are approximately 2,000,000 conventional aircraft windows in existence, and it is expected that in future years many of these windows, along with their shades, will be replaced with SPD-Smart™ windows, because the lighter weight and non-mechanical construction of SPD windows should enable aircraft to reduce fuel consumption, maintenance, downtime and operating cost while at the same time enhancing customer enjoyment and control of their lighting environment.

Our licensee ThermoView Industries, Inc., one of the largest publicly traded companies dedicated to the home improvement and renovation industry, announced in June, 2001 that it was developing a new line of "smart" SPD windows, and planned to begin manufacturing and selling them to residential home customers in 2002. "We expect these smart windows will offer value to homeowners who want to control light and glare while retaining their picturesque views," Charles L. Smith, President of ThermoView Industries, commented. The General Electric Company, which has a film-making license from Research Frontiers, is a part-owner of ThermoView Industries, and supplies some materials to them. ThermoView has partnered with Winchester Industries to manufacture SPD-Smart™ windows, and currently expects to begin selling SPD windows in the third quarter of 2002.

Research Frontiers sponsored an important survey of 50 U.S. window manufacturers by the Townsend Research Group. The manufacturers questioned in the survey expect



Entrance to Research Frontiers' "Experience the View of the Future" Exhibit at Nasdaq MarketSite in Times Square, New York City. This interactive exhibit featured SPD-Smart™ products for homes, offices, aircraft and automotive use.

6.2% of the windows in commercial buildings and 3.6% of windows in residential homes to use some type of "smart" window technology by 2005. Three possible types of "smart" windows were included within the survey's scope, namely liquid crystal, electrochromic and SPD. Liquid crystal windows, because of their haze, high price, lack of tunability and inability to block light well, have only garnered a small niche market position, mainly for indoor use or uses where privacy is important. Moreover, several major companies have reportedly abandoned electrochromic window projects because of very high costs, slow response time and other technical problems. This appears to now leave SPD technology in a dominant position as the only cost-effective, available technology for most "smart" window applications.

Based on market research published by The Freedonia Group, worldwide flat glass production was about 37 billion square feet in 1999 and is now approaching 40 billion square feet annually. Flat glass sales growth is expected to be strong, particularly in Asia. In addition, Research Frontiers estimates that 150-300 billion square feet of windows exist worldwide from cumulative past production, which constitutes a gigantic potential market for retrofitting (modification) with SPD-Smart™ films and windows.

On June 29, 2001, at the invitation of NASDAQ, Research Frontiers had the distinct honor of officially opening trading for the NASDAQ stock market in a Market Open Ceremony at the NASDAQ MarketSite in Times Square, New York City. Employees of Research Frontiers, senior executives from several of our licensees, and friends of the Company attended the special ceremony, while the Company's name was prominently displayed in huge letters on the outside of the building. The fact that we were invited is perhaps an indication or portent of our Company's increasing importance in the world of technology.

From July 1 through October 31, 2001, again at NASDAQ's request, Research Frontiers' SPD technology was showcased in a substantial exhibit at the NASDAQ

Left: SPD-Smart™ windows are perfect for preserving magnificent views in your home or office. US window manufacturers expect smart windows to be in 3.6% of residential windows and 6.2% of commercial windows by 2005. Right: SPD-Smart™ sunroof increases comfort of vehicle occupants and gives them better control over their driving environment.

PHOTOGRAPH COURTESY OF HANKUK GLASS INDUSTRIES/SPD INC.

MarketSite. Frequent tours through the site gave members of the public an opportunity to experience for themselves the "View of the Future," which featured SPD-Smart™ windows and other SPD products for aircraft, home and automotive use.

Several new license agreements were entered into during 2001. In February AP Technoglass, a subsidiary of Asahi Glass Co. Ltd., Japan's largest flat glass company, was granted a non-exclusive license to make SPD-Smart™ sunroof glass. AP Technoglass is the leading automotive glass and sunroof glass supplier in North America. In 2000 an estimated 6.2 million sunroofs were manufactured worldwide or 11.6% of the estimated 53.8 million cars and SUVs produced annually. SPD-Smart™ glass could expand this market since it will enable vehicle occupants to be more comfortable and have better control over their environment. SPD technology will also enable car manufacturers to continue the trend towards increasing glass content in their vehicles. Interest by the world's automakers in SPD sunroofs and other products remains high, and SPD Inc. currently reports that Mercedes Benz is testing SPD sunroofs on their vehicles as well.

In March 2001, Film Technologies International Inc. (FTI) was granted a non-exclusive license to make and sell SPD films to our current and future SPD end-product licensees. FTI is reported to be the world's fifth largest manufacturer of specialty films for windows.

During 2001, N.V. Bekaert S.A. of Belgium took over the non-exclusive license previously held by Material Sciences Corp., to make and sell SPD film as part of Bekaert's acquisition of MSC Specialty Films Inc. Bekaert Specialty Films is reported to be the world's second largest producer of specialty window films. Bekaert is also a major producer of films including the electrically-conductive transparent plastic film used in SPD film.

In December, Research Frontiers granted a non-exclusive license to Avery Dennison Corporation covering certain display products. Although Avery Dennison is better known for its office products, adhesives and sealants technologies, it has an interest in the display area as well. SPD displays can be used in a wide variety of applications because of their high brightness, excellent contrast and wide angle of view. Since year end, Research Frontiers also licensed BOS Automotive for SPD sunshades and sunvisors, and the Italian glass company, Isoclima S.p.A. for SPD architectural and automotive windows.

Considerable progress was made during 2001 by two of our emulsion-making licensees, Hitachi Chemical Co., Ltd. and Dainippon Ink and Chemicals Incorporated. The emulsions will be used as material from which SPD film can be made. These companies have already delivered samples to other Research Frontiers licensees and are working with these companies to supply larger quantities as well as more advanced materials.

We also sadly note that our close friend and colleague, Dr. Bernard Gold, who served as a Director of the Company since June 1991, passed away in September, 2001. His great faith in the Company, staunch support, wisdom and excellent advice will be sorely missed.

Victor F. Keen, who has served as the Company's Secretary since 1987, was appointed a Director in June, 2001. Victor is thoroughly familiar with the activities of Research Frontiers and is a Partner and Chairman of the Tax Department of Duane Morris & Heckscher LLP, a law firm of 475 attorneys with offices in 20 cities throughout the United States and Europe. We are most pleased to have Victor continue his involvement with Research Frontiers by joining our Board.

Our net loss for 2001 of $4.5 million or $.38 per share was sharply lower than comparable figures of $7.6 million and $.63 per share for 2000, primarily as a result of reduced non-cash charges. Our financial position at year-end 2001 remained strong with working capital of $8.0 million, $7.9 million in cash, cash equivalents and marketable securities, and no debt. During 2001, institutions increased their ownership in Research Frontiers from about 3% to 10.4% of our outstanding shares.

Research Frontiers is no longer a "concept company." Now that commercial production and sales of SPD film and end-products has begun, we anticipate a rising tide of licensee sales and rapid growth of earned royalties as our licensees sell products using SPD light-control technology. In February 2002 Joe Harary was promoted to the position of President to help lead Research Frontiers as it embarks on this new and exciting phase with SPD-Smart™ products being introduced for many applications throughout the world. In March 2002, we promoted Mike LaPointe to the position of Vice President–Marketing to head our expanding marketing department to expedite penetration of the numerous markets for SPD light-control technology, as well as to coordinate our worldwide marketing efforts with those of our licensees.

We warmly thank our employees, licensees, shareholders and many friends for their hard work and faith in our Company, and we pledge to continue to work diligently to make SPD technology known and respected throughout the world.

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 National Market. As of March 27, 2002, there were 12,130,395 shares of common stock outstanding.

The table at right 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, 2000	14.6250	40.0000
June 30, 2000	9.6875	32.0000
September 30, 2000	14.7500	31.7500
December 31, 2000	13.7500	22.4375
March 31, 2001	10.5000	24.2500
June 30, 2001	17.0000	30.0000
September 30, 2001	9.0000	29.0000
December 31, 2001	13.1500	19.0000

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 27, 2002, there were 606 holders of record of the Company's common stock. The Company estimates that there are approximately 10,675 beneficial holders of the Company's common stock.

Dividends The Company did not pay dividends on its common stock in 2001 and does not expect to pay any cash dividends in the foreseeable future. There are no restrictions on the payment of dividends.

Selected Financial Data

The table below 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		2001	2000	1999	1998	1997
Statement of Operations Data:	Fee income	$142,002	$333,652	$128,096	$108,735	$60,000
	Operating expenses	2,744,059	3,027,655	1,605,028	1,631,179	1,884,038
	Research and development (1)	2,634,671	2,618,567	1,971,341	1,647,448	1,831,397
	Non-recurring non-cash compensation expense (2)	—	3,133,748	671,052	—	—
		5,378,730	8,779,970	4,247,421	3,278,627	3,715,435
	Operating loss	(5,236,728)	(8,446,318)	(4,119,325)	(3,169,892)	(3,655,435)
	Net investment income (3)	696,058	878,518	386,303	460,572	425,990
	Other income	—	—	—	91,379	—
	Net loss	(4,540,670)	(7,567,800)	(3,733,022)	(2,617,941)	(3,229,445)
	Basic and diluted net loss per common share	(.38)	(.63)	(.34)	(.24)	(.32)
	Dividends per share	—	—	—	—	—

As of December 31		2001	2000	1999	1998	1997
Balance Sheet Data:	Total current assets	$8,272,677	$15,358,819	$9,695,137	$ 6,728,453	$9,728,285
	Total assets	9,324,902	15,729,127	10,037,063	7,021,291	10,033,663
	Long-term debt, including accrued interest	—	—	—	—	—
	Total shareholders' equity	9,049,920	14,737,917	9,507,736	6,740,489	9,621,979

(1) Research and development expenses for 1999 include $289,177 paid by the Company for 74 patents and patent applications acquired from Glaverbel, SA.

(2) During 1999, the Company granted 237,800 contingent performance options to employees, which vested only, if a certain performance milestone in the price of the Company's common stock was achieved during 2000. The charges recorded as a result of the issuance of these performance options were calculated based upon changes in the Company's stock price as of the end of each quarter until the vesting date, and are non-cash compensation charges.

(3) Net investment income for 2001, 2000, 1999, 1998, and 1997 includes $0, $0, $95,001, $50,968, and $68,810, respectively, of interest income received from officers of the Company upon payment of notes receivable, and $6,382 of unrealized loss on investments in 1997. Prior to July 1997, the Company classified its investments as trading securities which resulted in the unrealized gains and losses recorded in the statement of operations.

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."

We have entered into a number of license agreements covering potential products using the Company's SPD technology. Under these agreements, we generally recognize income from royalties when earned in accordance with the terms of the agreements.

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 research-related overhead expenses.

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 EITF 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 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

2001 vs. 2000 The Company's fee income from licensing activities for 2001 was $142,002 as compared to $333,652 for 2000. 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 $283,596 for 2001 to $2,744,059 from $3,027,655 for 2000. This decrease was primarily the result of a lower non-cash accounting charge of $43,596 which was recorded by the Company during 2001 compared to a non-cash accounting charge of $598,758 which was recorded by the Company during 2000, relating to the vesting of warrants based upon performance criteria being achieved or services performed, which expense was based upon the fair value of such warrants on the date the warrants vested as determined using a Black-Scholes option pricing model. Partially offsetting this decrease were increases with respect to payroll, marketing, public relations and insurance expenses.

Research and development expenditures increased modestly in 2001 to $2,634,671 from $2,618,567 for 2000. This increase was primarily the result of higher patent, payroll and insurance expenses, offset partially by lower costs of materials and lower consulting expenses.

Operating expenses and research and development expenses listed above included amounts paid under a performance bonus plan of $496,790 and $288,710, respectively during 2001 and $477,500 and $277,500, respectively during 2000. The Company also recorded a non-cash compensation charge of $3,133,748 during 2000 which did not recur during 2001 which is related to the non-recurring grant of certain contingent performance options issued to employees and directors during 1999. Because of the performance milestones which must have been achieved in order for these options to vest, the Company was required to account for these options as variable plan under APB Opinion No. 25. Without taking into account the non-cash accounting charge associated with the contingent performance options described above and the performance warrants described above, the Company's net loss would have been $4,497,074 ($0.37 per share) for 2001 as compared to $3,835,294 ($0.32 per share) for 2000.

The Company's net gain from its investing activities for 2001 was $696,058, as compared to a net gain from its investing activities of $878,518 for 2000. This difference was primarily due to a lower level of average investment balances in 2001 compared to 2000, and lower prevailing interest rates in the U.S. Treasury markets.

As a consequence of the factors discussed above, the Company's net loss was $4,540,670 ($0.38 per share) for 2001 as compared to $7,567,800 ($0.63 per share) for 2000. Without taking into account the non-cash accounting charge associated with the contingent performance options described above and the performance warrants described above, the Company's net loss would have been $4,497,074 ($0.37 per share) for 2001 as compared to $3,835,294 ($0.32 per share) for 2000.

2000 vs.1999 The Company's fee income from licensing activities for 2000 was $333,652 as compared to fee income of $128,096 for 1999. The increase in fee income was due to the Company entering into additional license agreements during the year and scheduled increases in the minimum annual royalties payable thereunder. 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.

Operating expenses increased by $1,422,627 for 2000 to $3,027,655 from $1,605,028 for 1999. This increase was primarily the result of increased compensation (primarily as a result of certain non-cash charges associated with performance options and warrants issued to consultants described below, the addition of two new employees during the first quarter of 2000, and the payment to employees for certain performance bonuses), marketing, insurance, stock listing fees, depreciation, general expenses, and travel expenses, offset by lower investor and public relations expenses, legal and accounting fees. During 2000, the Company incurred non-cash operating expenses of $598,758 in connection with the issuance of options to certain consultants valued by the Black-Scholes pricing model at $70,560, and a non-cash compensation charge of $528,198 relating to the vesting of certain performance based warrants issued to another consultant for services performed.

Research and development expenditures increased by $647,226 to $2,618,567 for 2000 from $1,971,341 for 1999. This increase was primarily the result of higher research-related salaries and performance bonuses, and higher materials costs, patent and depreciation expenses.

Operating expenses and research and development expenses listed above included amounts accrued under a performance bonus plan of $477,500 and $277,500, respectively. These performance bonuses in the amount accrued for were paid by the Company during the third quarter of 2000 because the applicable performance milestones were achieved. In addition to these performance bonus accruals, the Company also recorded a non-cash compensation charge of $3,133,748 and $671,052 with respect to 2000 and 1999, respectively, which is related to the non-recurring grant of certain contingent performance options issued to employees and directors during 1999.

The Company's net gain from its investing activities for 2000 was $878,518, as compared to a net gain from its investing activities of $291,302 for 1999. This difference was primarily due to a higher level of average investment balances in 2000 compared to the same period in 1999 as a result of proceeds received from the exercise of the Class A Warrant and employee stock options. In addition, during 1999 the Company recorded $95,001 of interest income on notes receivable from one of its officers which was paid through the delivery of shares of common stock to the Company.

As a consequence of the factors discussed above, the Company's net loss was $7,567,800 ($0.63 per share) for 2000 as compared to $3,733,022 ($0.34 per share) for 1999. As more fully described above, during 2000, the Company incurred non-cash accounting charges of $3,732,506 in connection with contingent performance options issued to employees of the Company in 1999 and the issuance of options and warrants to non-employees when these options and warrants vested. Without taking into account these non-cash accounting charges of $3,732,506, the Company's net loss would have been $3,835,294 ($0.32 per share) for 2000 as compared to $3,061,970 ($0.28 per share) for 1999.

Financial Condition, Liquidity and Capital Resources

During 2001, the Company's cash and cash equivalent balance decreased by $2,952,962 principally as a result of the $6,614,721 of proceeds received, net of expenses, from the issuance of common stock upon the exercise of options and warrants, the proceeds of which have been invested by the Company primarily in U.S. Treasury notes, offset by cash used to fund the Company's operating activities of $4,938,397, and the purchase of 407,065 shares of treasury stock for $8,144,693 (which shares were subsequently retired). At December 31, 2001, the Company had working capital of $7,997,695 and its shareholders' equity was $9,049,920.

On October 1, 1998, the Company announced that Ailouros Ltd., a London-based institutional money management fund, has committed to purchase up to $15 million worth of common stock of the Company through December 31, 2001. This commitment is in the form of a Class A Warrant issued to Ailouros Ltd. which gives 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 has now been eliminated by mutual agreement so that the Company may put stock to Ailouros at selling prices in excess of $15 per share. However, the Company is 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 determines the amount of common stock that the Company wishes to issue during such three-month period. The Company also sets the minimum selling or "floor" price, which can 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 will determine how much common stock, if any, is to be sold (the amount of which can 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 does 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.

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 is dedicated exclusively to the production of suspended particle device (SPD) light-control film and a wide variety of end-products using SPD film.

In December 2000, the Company's Board of Directors approved a performance bonus plan which provides for a bonus to be paid on or after July 2, 2001 and on or after January 2, 2002 equal to 1% of the increase, if any, in the Company's market value during the first and second halves of 2001. Bonuses are capped at a recipient's salary in the case of employees of the Company, and are currently capped at $57,222 in the case of non-employee directors of the Company. During 2000, the Company had a similar performance plan in place. The Company recorded $785,500 and $755,000 of expenses in connection with these plans for the years ended December 31, 2001 and 2000, respectively. The Company's Board of Directors approved a similar bonus plan for 2002 but with higher thresholds to be met before a bonus is payable under such plan. In addition to the payment caps described above, under the current plan, in order to insure that bonuses are not paid based upon temporary fluctuations in the market value of the Company, bonuses under this plan will only be paid to the various participants under this plan if and when the market value of the Company exceeds $280,489,009 (and in the case of any bonus paid to Robert L. Saxe, if and when the market value of the Company exceeds $304,207,362).

The Company expects to use 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, 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 expenditures, assumed ten percent annual increases therein, existing cash reserves and budgeted revenues, the Company believes that it would not require additional funding for the next two years (without giving effect to any new financing raised). 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.

Inflation

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

New Accounting Standards

In July 2001, the FASB issued Statement of Financial Accounting Standards No. 141, *Business Combinations* which supersedes Accounting Principles Board (APB) Opinion No. 16, *Business Combinations*. SFAS 141 eliminates the pooling-of-interests method of accounting for business combinations and modifies the application of the purchase accounting method. The elimination of the pooling-of-interests method is effective for transactions initiated after June 30, 2001. The remaining provisions of SFAS 141 will be effective for transactions accounted for using the purchase method that are completed after June 30, 2001.

In July 2001, the FASB also issued Statement of Financial Accounting Standards No. 142, *Goodwill and Intangible Assets* which supersedes APB Opinion No. 17, *Intangible Assets*. SFAS 142 eliminates the current requirement to amortize goodwill and indefinite-lived intangible assets, addresses the amortization of intangible assets with a defined life and addresses the impairment testing and recognition for goodwill and intangible assets. SFAS 142 will apply to goodwill and intangible assets arising from transactions completed before and after the Statement's effective date. SFAS 142 is effective for the Company beginning January 1, 2002. Management of the Company does not believe that the implementation of SFAS 141 or SFAS 142 will have a significant impact on its financial position or results of operations.

In October 2001, the FASB also issued Statement of Financial Accounting Standards No. 144, *Accounting for the Impairment of Long-Lived Assets,*which addresses financial accounting and reporting for the impairment or disposal of long-lived assets. This statement supersedes SFAS No. 121, *Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of*, while retaining the fundamental recognition and measurement provisions of that statement. SFAS No. 144 requires that a long-lived asset to be abandoned, exchanged for a similar productive asset or distributed to owners in a spinoff to be considered held and used until it is disposed of. However, SFAS No. 144 requires that management consider revising the depreciable life of such long-lived asset. With respect to long-lived assets to be disposed of by sale, SFAS No. 144 retains the provisions of SFAS No. 121, and therefore, requires that discontinued operations no longer be measured on a net realizable value basis and that future operating losses associated with such discontinued operations no longer be recognized before they occur. SFAS 144 is effective for the Company beginning January 1, 2002. Management of the Company does not believe that the implementation of SFAS 144 will have a significant impact on its financial position or results of operations.

Related Party Transactions

Statement of Financial Accounting Standards No. 57, *"Related Party Disclosures"* requires the Company to identify and describe material transactions involving related persons or entities and to disclose information necessary to understand the effects of such transactions on our consolidated financial statements. The Company has loaned two officers an aggregate of $152,961. Each of the aforementioned loans were made in April 1997 or prior thereto; are due in January 2003; relate to the purchase of common stock of the Company; are collateralized by the pledge of shares of common stock of the Company; may be prepaid in part or in full without notice or penalty; are represented by a promissory note which bears interest at a rate per annum equal to the broker call rate in effect on the first day of each calendar quarter; and permit repayment of the loan by delivery of securities of the Company having a fair market value equal to the balance of the loan outstanding.

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

The Company invests available cash and cash equivalents 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

BALANCE SHEETS

December 31			2001	2000
Assets	*Current assets*	Cash and cash equivalents	$ 853,210	3,806,172
		Marketable investment securities held-to-maturity	—	11,307,752
		Marketable investment securities-available for sale	7,083,606	3,906
		Receivable from warrant exercise pending settlement	164,311	—
		Royalty receivable	37,500	—
		Prepaid expenses and other current assets	134,050	240,989
		Total current assets	8,272,677	15,358,819
		Investment in SPD Inc., at cost	750,002	—
		Fixed assets, net	279,618	347,703
		Deposits and other assets	22,605	22,605
		Total assets	$9,324,902	15,729,127
Liabilities and Shareholders' Equity	*Current liabilities*	Accounts payable	$79,197	203,787
		Deferred revenue	37,500	37,502
		Accrued expenses and other	158,285	749,921
		Total liabilities	274,982	991,210
	Shareholders' equity	Common stock, par value $0.0001 per share; authorized 100,000,000 shares, issued and outstanding 12,108,195 and 12,103,683 shares for 2001 and 2000	1,211	1,210
		Additional paid-in capital	51,359,036	52,594,293
		Accumulated other comprehensive income (loss)	41,835	(46,094)
		Accumulated deficit	(42,199,201)	(37,658,531)
			9,202,881	14,890,878
		Notes receivable from officers	(152,961)	(152,961)
		Total shareholders' equity	9,049,920	14,737,917
		Commitments and contingency		
		Total liabilities and shareholders' equity	$9,324,902	15,729,127

See accompanying notes to consolidated financial statements.

STATEMENTS OF OPERATIONS

Years ended December 31	2001	2000	1999
Fee income	$ 142,002	333,652	128,096
Operating expenses	2,744,059	3,027,655	1,605,028
Purchase of patents	—	—	289,177
Research and development	2,634,671	2,618,567	1,682,164
Non-recurring non-cash compensation expense	—	3,133,748	671,052
	5,378,730	8,779,970	4,247,421
Operating loss	(5,236,728)	(8,446,318)	(4,119,325)
Net investment income	696,058	878,518	291,302
Interest income on notes receivable from officers	—	—	95,001
Net loss	$(4,540,670)	(7,567,800)	(3,733,022)
Basic and diluted net loss per common share	$ (0.38)	(0.63)	(0.34)
Weighted average number of common shares outstanding	12,085,609	12,096,108	11,100,196

See accompanying notes to consolidated financial statements.

Years ended December 31, 2001, 2000 and 1999

	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Accumulated Deficit	Treasury Stock, at Cost	Accumulated Other Comprehensive Income (Loss)	Notes Receivable	Total
Balance, December 31, 1998	10,929,041	$1,093	33,982,066	(26,357,709)	—	—	(884,961)	6,740,489
Issuance of common stock	664,214	66	5,805,358	—	—	—	—	5,805,424
Purchase of treasury stock	—	—	—	—	(345,837)	—	—	(345,837)
Repayment of note by officer	—	—	—	—	(482,001)	—	732,000	249,999
Retirement of treasury stock	(78,667)	(8)	(827,830)	—	827,838	—	—	—
Net loss	—	—	—	(3,733,022)	—	—	—	(3,733,022)
Issuance of performance options	—	—	671,052	—	—	—	—	671,052
Issuance of stock and warrants for services performed	9,312	1	119,630	—	—	—	—	119,631
Balance, December 31, 1999	11,523,900	$ 1,152	39,750,276	(30,090,731)	—	—	(152,961)	9,507,736
Issuance of common stock	758,945	76	12,172,093	—	—	—	—	12,172,169
Purchase of treasury stock	—	—	—	—	(3,314,169)	—	—	(3,314,169)
Retirement of treasury stock	(182,600)	(18)	(3,314,151)	—	3,314,169	—	—	—
Issuance of performance options	—	—	3,133,748	—	—	—	—	3,133,748
Comprehensive loss:								
Net loss	—	—	—	(7,567,800)	—	—	—	(7,567,800)
Unrealized loss on available for sale securities	—	—	—	—	—	(46,094)	—	(46,094)
Total Comprehensive Loss								(7,613,894)
Issuance of stock and warrants for services performed	3,438	—	852,327	—	—	—	—	852,327
Balance, December 31, 2000	12,103,683	$1,210	52,594,293	(37,658,531)	—	(46,094)	(152,961)	14,737,917
Issuance of common stock	407,175	41	6,778,991	—	—	—	—	6,779,032
Purchase of treasury stock	—	—	—	—	(8,144,693)	—	—	(8,144,693)
Retirement of treasury stock	(407,065)	(40)	(8,144,653)	—	8,144,693	—	—	—
Comprehensive loss:								
Net loss	—	—	—	(4,540,670)	—	—	—	(4,540,670)
Unrealized gain on available for sale securities	—	—	—	—	—	87,929	—	87,929
Total Comprehensive Loss								(4,452,741)
Issuance of stock and warrants for services performed	4,402	—	130,405	—	—	—	—	130,405
Balance, December 31, 2001	12,108,195	$1,211	51,359,036	(42,199,201)	—	41,835	(152,961)	9,049,920

See accompanying notes to consolidated financial statements..

Years ended December 31	2001	2000	1999
Cash flows from operating activities			
Net loss	$(4,540,670)	(7,567,800)	(3,733,022)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization	118,657	109,137	93,472
Interest income on officer notes receivable	—	—	(95,001)
Expense relating to issuance of contingent performance options	—	3,133,748	671,052
Marketable securities received as license fee	—	(50,000)	—
Cashless exercise of options and warrants	17,588	—	82,481
Expense relating to issuance of stock and warrants for services performed	112,817	852,327	37,150
Changes in assets and liabilities:			
Salary advance to officer	—	66,445	39,122
Royalty receivable	(37,500)	—	—
Prepaid expenses and other current assets	106,939	(223,498)	13,875
Deferred revenue	(2)	(8,652)	(10,096)
Accounts payable and accrued expenses	(716,226)	470,535	258,621
Net cash used in operating activities	(4,938,397)	(3,217,758)	(2,642,346)
Cash flows from investing activities			
Proceeds from sale and maturity of held-to-maturity securities	1,319,572	2,526,363	2,405,181
Proceeds from sale of available-for-sale securities	2,996,409	—	—
Purchases of held-to-maturity treasury securities	—	(12,588,032)	(2,461,878)
Investment in SPD, Inc., at cost	(750,002)	—	—
Purchases of fixed assets	(50,572)	(137,519)	(143,709)
Net cash provided by (used in) investing activities	3,515,407	(10,199,188)	(200,406)
Cash flows from financing activities			
Repayment of principal on officer's loans	—	—	345,000
Proceeds from issuances of common stock and warrants	6,614,721	12,394,718	5,582,875
Purchase of treasury stock	(8,144,693)	(3,314,169)	(345,837)
Net cash (used in) provided by financing activities	(1,529,972)	9,080,549	5,582,038
Net increase (decrease) in cash and cash equivalents	(2,952,962)	(4,336,397)	2,739,286
Cash and cash equivalents at beginning of year	3,806,172	8,142,569	5,403,283
Cash and cash equivalents at end of year	$853,210	3,806,172	8,142,569

See accompanying notes to consolidated financial statements..

1 Business

Research Frontiers Incorporated (the "Company" or "Research Frontiers") 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.

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 is dedicated exclusively to the production of suspended particle device (SPD) light-control film and a wide variety of end-products using SPD film.

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.

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, 2001 and 2000.

Marketable Investment Securities The Company accounts for its investments in marketable securities under the provisions of Statement of Financial Accounting Standards No. 115, *"Accounting for Certain Investment in Debt and Equity Securities"* ("Statement 115"). During the second quarter of 2001, the Company determined that it may sell its marketable investment securities prior to their maturity dates in order to invest in other marketable securities, repurchase and retire its common stock, and for general working capital purposes. Accordingly, as of June 30, 2001, the Company transferred its classification of marketable securities from held-to-maturity to available-for-sale. In accordance with Statement 115, available-for-sale securities 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.

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 10) relating to technology developed by the Company.

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, 2001 because all common stock equivalents (i.e., options and warrants) were antidilutive in those periods. The number of options and warrants that was not included because their effect is antidilutive was 2,542,576, 2,224,201, and 1,995,363 for 2001, 2000 and 1999, 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 Management of the Company has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these financial statements in conformity with accounting principles generally accepted in the United States of America. 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.

The fair value of the notes receivable from officers approximates the carrying value as their stated interest rate, the broker call rate, is similar to other rates currently offered by local brokerage institutions for loans of similar terms to individuals with comparable credit risk.

Stock Option Plan The Company applies the intrinsic value-based method of accounting prescribed by Accounting Principles Board ("APB") Opinion No. 25 *"Accounting for Stock Issued to Employees,"* and related interpretations, in accounting for its fixed plan stock options. As such, compensation expense would be recorded on the date of grant only if the current market price of the underlying stock exceeded the exercise price.

Accumulated Other Comprehensive Income (loss) The unrealized gains on available-for-sale securities of $87,929 for the year ended December 31, 2001 is comprised of $168,985 of unrealized holding gains arising during the period less reclassification adjustments for gains realized in net income of $81,056 during the period. The unrealized loss on available-for-sale securities of $46,094 for the year ended December 31, 2000 represents unrealized holding losses arising during the period.

Deferred Revenue The Company has entered into a number of license agreements covering potential products. The Company receives minimum annual royalties under certain license agreements and records fee income for the amounts earned by the Company. Certain of the fees are paid to the Company in advance of the period in which they are earned resulting in deferred revenue.

3 Supplemental Cash Flow Information

The following is supplemental information relating to the Company's consolidated statement of cash flows:

	2001	2000	1999
Non-cash financing activities:			
Principal payment on officer's note receivable by surrendering of common stock	$ —	—	387,000
Receivable from warrant exercise	$164,311	—	222,549

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 securities at December 31, 2001 and 2000 were as follows:

	Amortized Cost	Gross Unrealized Holding Gains	Gross Unrealized Holding (Losses)	Fair Value
At December 31, 2001				
Available-for-sale securities:				
U.S. treasury securities	$ 6,991,771	80,960	—	7,072,731
Equity securities	50,000	—	(39,125)	10,875
At December 31, 2000				
U.S. treasury securities (held-to-maturity)	$11,307,752	151,360	—	11,459,112
Available-for-sale securities	50,000	—	(46,094)	3,906

Maturities of all U.S. treasury securities were less than two years at December 31, 2001 and 2000.

5 Notes Receivable from Officers

In 1996, the Company loaned several officers an aggregate of $350,000. In March and April 1997, the Company loaned several officers an aggregate of $1,390,000. During 1997, officers made aggregate principal payments of $592,353 against such loans of which $39,810 was paid in cash and $552,543 was paid through the surrender of the Company's common stock. During 1998, officers made aggregate principal payments of $542,186 against such loans of which $40,000 was paid in cash and $502,186 was paid through the surrender of the Company's common stock. During 1999, officers made aggregate principal payments of $732,000 against such loans of which $345,000 was paid in cash and $387,000 was paid through the surrender of the Company's common stock. In connection with the aforementioned loan repayments, the Company recorded $95,001 and $50,968, in interest income in 1999 and 1998, respectively, of which $95,001 and $43,367, was paid through the surrender of the Company's common stock in 1999 and 1998, respectively. It is the Company's policy to record interest income on these notes as received.

In a settlement agreement dated June 30, 1999, the Company settled a declaratory judgment action brought on March 25, 1999 in the Supreme Court of the State of New York, County of Nassau, by Jean Thompson in her individual capacity and as Executrix of the estate of Robert I. Thompson, a former officer and director of the Company. The action did not seek monetary damages and essentially sought a declaration that certain common stock of the Company securing loans made to Mr. Thompson was not available as collateral to secure such loans. Under the settlement agreement, among other things, the parties agreed that Jean Thompson and the estate of Robert I. Thompson would pay the $732,000 in loans made by the Company from 1993 to 1997 by paying the Company $345,000 in cash, and delivering to the Company for cancellation 38,467 shares of common stock and options to purchase 181,447 shares of common stock. This payment and delivery of the shares and stock options for cancellation were made in August 1999, resulting in the payment in full of all outstanding loans, and the Company recording interest income on such loans of $95,001.

Each of the aforementioned loans are due in January 2003. The loans relate to the purchase of common stock of the Company; are collateralized by the pledge of shares of common stock of the

Company; may be prepaid in part or in full without notice or penalty; are represented by a promissory note which bears interest at a rate per annum equal to the broker call rate (3.5% at December 31, 2001 and 8.25% at December 31, 2000) in effect on the first day of each calendar quarter; and permit repayment of the loan by delivery of securities of the Company having a fair market value equal to the balance of the loan outstanding.

6 Fixed Assets

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

	2001	2000	Estimated useful life
Equipment and furniture	$1,057,126	1,019,324	5 years
Leasehold improvements	269,360	256,590	Life of lease or estimated life if shorter
	1,326,486	1,275,914	
Less accumulated depreciation and amortization	1,046,868	928,211	
	$279,618	347,703	

7 Accrued Expenses and Other

Accrued expenses at December 31, 2001 and 2000 are as follows:

	2001	2000
Settlement of treasury stock repurchase	$ —	509,974
Payroll, bonuses and related benefits	91,942	73,006
Professional services	34,285	152,167
Other	32,058	14,774
	$158,285	749,921

8 Income Taxes

There was no income tax expense in 2001, 2000 and 1999 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, 2001 and 2000 are presented below.

		2001	2000
Deferred tax assets	Net operating loss carryforwards	$12,922,000	11,002,000
	Research and other credits	860,000	673,000
	Total gross deferred tax assets	13,782,000	11,675,000
	Less valuation allowance	13,782,000	11,675,000
		—	—

The Company has recorded a 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, 2001, the Company had a net operating loss carryforward for federal income tax purposes of approximately $32,306,000, varying amounts of which will expire in each year from 2002 through 2021. Research and other credit carryforwards of $860,000 are available to the Company to reduce income taxes payable in future years principally through 2021. Net operating loss carryforwards of $825,825 and research and other credit carryforwards of $9,556 are scheduled to expire during fiscal 2002, if not utilized.

9 Shareholders' Equity

Sale of Common Stock and Warrants During 1999, the Company received $5,805,424 of net cash proceeds from the issuance of 664,214 shares of common stock from the exercise of options and warrants, as follows: the issuance of 53,025 shares of common stock issued upon the exercise of options resulting in net proceeds of $321,532 and the issuance of 611,189 shares of common stock issued upon the exercise of warrants, principally related to the Class A Warrant, resulting in net proceeds of $5,483,892. In addition, 2,850 shares were issued to an investor relations firm through the cancellation of 33,250 warrants, resulting in public relations expense of $21,820; 6,048 shares were issued to an officer through the cancellation of 17,000 options resulting in compensation expense of $60,661; and 414 shares were issued to a director in payment of $3,000 in directors fees.

The Company recorded a receivable of $222,549 representing a warrant exercise that occurred prior to the end of 1999, that was scheduled to settle in January 2000. The Company received the cash for the settlement of this warrant in January 2000.

During 2000, the Company received $12,172,169 of net cash proceeds from the issuance of 758,945 shares of common stock from the exercise of options and warrants, as follows: the issuance of 95,962 shares of common stock issued upon the exercise of options resulting in net proceeds of $706,299 and the issuance of 662,983 shares of common stock issued upon the exercise of warrants, principally related to the Class A Warrant, resulting in net proceeds of $11,465,870. In addition, 3,438 shares were issued to a director in payment of $68,000 in directors fees.

During 2001, the Company received $6,614,721 of net cash proceeds from the issuance of 407,175 shares of common stock from the exercise of options and warrants, as follows: (i) the issuance of 48,175 shares of common stock issued upon the exercise of options resulting in net proceeds of $385,472 and (ii) 359,000 shares of common stock issued upon the exercise of warrants, principally related to the Class A Warrant, resulting in net proceeds (inclusive of a receivable described below of $164,311) of $6,393,560. In addition, 3,715 shares were issued to directors in payment of $69,221 in directors fees, and 687 shares were issued through the cancellation of 1,000 warrants, resulting in non-cash consulting expense of $17,588 being recorded.

The Company recorded a receivable of $164,311 representing a warrant exercise that occurred prior to the end of 2001, that was scheduled to settle in January 2002. The Company received the cash for the settlement of this warrant in January 2002.

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.

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 2000, the Company's shareholders approved an additional 600,000 shares for issuance under this Plan. As of December 31, 2001, awards for 196,322 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.

Activity in stock options is summarized below:

	Number of Shares Subject to Option	Weighted Average Exercise Price
Balance at December 31, 1998	1,495,159	$7.79
Granted	485,600	$8.38
Cancelled	(203,023)	$8.15
Exercised	(59,073)	$6.11
Balance at December 31, 1999	1,718,663	$7.98
Granted	332,500	$19.80
Cancelled	(6,700)	$14.85
Exercised	(95,962)	$7.36
Balance at December 31, 2000	1,948,501	$10.00
Granted	416,550	$20.20
Cancelled	—	—
Exercised	(48,175)	$8.00
Balance at December 31, 2001	2,316,876	$11.88

The following table summarizes information about stock options at December 31, 2001:

Range of Exercise Price	Options Outstanding	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	Shares Exercisable	Weighted Average Exercise Price
$3.00—$6.00	122,177	4.46	$ 5.75	122,177	$ 5.75
$6.01—$7.50	696,326	5.91	7.27	696,326	7.27
$7.51—$9.00	553,501	6.72	8.35	553,501	8.35
$9.01—$12.00	321,775	6.87	9.87	154,525	9.67
$12.01—$15.00	171,797	6.87	14.24	171,797	14.24
$15.01—$19.00	113,000	8.92	18.99	106,000	19.00
$19.01—$37.03	338,300	9.21	27.70	34,000	37.03
	2,316,876	6.86	$11.88	1,838,726	$ 9.57

Options to purchase 436,550 shares become exercisable during 2002.

During 2000, the Company granted 14,000 options to consultants which vested immediately. In accordance with EITF 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 recorded consulting expenses of $246,961 based upon the fair value of such options on the date the options vested as determined using a Black-Scholes option pricing model.

During 1999, the Company granted 237,800 contingent performance options to employees, which vest only, if a certain performance milestone in the price of the Company's common stock is achieved during 2000. This milestone was achieved during 2000 and these options vested. The Company is required to account for these options as a variable plan under APB Opinion No. 25. Accordingly, from the point in time that it appears probable that such milestone will be achieved, the Company is required to recognize non-cash compensation expense each period from the date of grant through the vesting date based on the quoted market price of the stock at the end of each period. Non-cash compensation expense recognized during 1999 and 2000 in connection with these options was $671,052 and $3,133,748, respectively. The charges recorded as a result of the issuance of these performance options are calculated based upon changes in the Company's stock price as of the end of each quarter, and are non-cash compensation charges.

The per share weighted average fair value of warrants issued to directors and stock options granted during 2001, 2000, and 1999 was approximately $12.41, $9.00, and $3.65, 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
September 2001	0 %	3.787%	90.190%	3.62
June 2001	0 %	4.768%	85.170%	3.62
December 2000	0 %	5.200%	64.659%	3.62
October 2000	0 %	5.760%	65.076%	3.62
June 2000	0 %	6.290%	64.532%	3.62
February 2000	0 %	6.600%	56.400%	3.62
December 1999	0 %	6.090%	53.698%	3.62
June 1999	0 %	5.940%	50.853%	3.60

The Company applies APB Opinion No. 25 in accounting for its stock option plans and, accordingly, no compensation cost has been recognized for its stock options and warrants in the financial statements as the exercise price of such instruments were equal to the fair value of the Company's common stock at the date of grant. Had the Company determined compensation cost based on the fair value at the grant date for its stock options under SFAS No. 123 *"Accounting for Stock Based Compensation,"* the Company's net loss and net loss per share would have been increased to the pro forma amounts indicated below:

		2001	2000	1999
Net loss	As reported	$(4,540,670)	$(7,567,800)	$(3,733,022)
	Pro forma	$(6,552,355)	$(7,843,116)	$(4,641,784)
Basic and diluted net loss per common share	As reported	$(0.38)	$(0.63)	$(0.34)
	Pro forma	$(0.54)	$(0.65)	$(0.42)

Pro forma net loss reflects only options and warrants granted since January 1, 1995. Therefore, the full impact of calculating compensation cost for stock options and warrants under SFAS No. 123 is not reflected in the pro forma net loss amounts presented above because compensation costs for options and warrants granted prior to January 1, 1995 were not considered.

Options and Warrants/Warrants Activity in warrants is summarized below, excluding the effect of the redeemable prepaid warrant (note 9 (d)) and the Class A Warrant (note 9 (d)):

	Number of Shares Underlying Warrants Granted		Exercise Price
Balance at December 31, 1998	306,339		5.88–13.50
Exercised	(49,239)		7.00–11.63
Terminated	(40,400)		7.50–7.67
Issued	60,000	(a)	8.98–21.00
Balance at December 31, 1999	276,700		$ 5.88–21.00
Exercised	(1,000)		9.00–10.00
Terminated	—		—
Issued	—		—
Balance at December 31, 2000	275,700		$5.88–21.00
Exercised	(30,000)		7.99–11.00
Terminated	(20,000)		16.00–21.00
Issued	—		—
Balance at December 31, 2001	225,700		$5.88–13.50

(a) Represents warrants to purchase 10,000 shares at $8.98 per share issued to two consultants for research and development work performed for the Company, 50% of which is currently vested and 50% of which vests if certain additional milestones are achieved as a result of the work performed by the consultants; and warrants to purchase 10,000 shares at $9.00 per share, 10,000 shares at $10.00 per share, 10,000 shares at $11.00 per share, 10,000 shares at $16.00 per share, and 10,000 shares at $21.00 per share, issued in payment for investor relations services provided to the Company which resulted in public relations expense of $9,168 and $34,150 during 2000 and 1999, respectively, which warrants vest 10,000 shares per quarter commencing April 1, 1999. These latter warrants were either exercised or expired in 2001.

Warrants generally expire from two to ten years from the date of issuance. At December 31, 2001, the number of warrants exercisable was 218,700 at a weighted average exercise price of $8.13 per share.

During 2001 and 2000, certain warrants granted to consultants in 1995 and 1994 to purchase 7,000 and 25,000 shares, respectively of common stock became vested due to services performed and performance criteria being met. In accordance with EITF 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 recorded consulting expense of $43,596 and $528,198, respectively, based upon the fair value of such warrants on the date the warrants vested as determined using a Black-Scholes option pricing model.

Treasury Stock During 2001, the Company purchased in the open market and subsequently retired 407,065 shares of treasury stock with an aggregate cost of $8,144,693. During 2000, the Company purchased in the open market and subsequently retired 182,600 shares of treasury stock with an aggregate cost of $3,314,169. During 1999, the Company purchased in the open market and subsequently retired 40,200 shares of treasury stock with an aggregate cost of $345,837. Also during 1999, the Company received 38,467 shares of common stock valued at $482,001 as partial payment of notes receivable from an officer pursuant to a settlement agreement as discussed above. Such shares were also subsequently retired.

Class A and Class B Warrants On October 1, 1998, the Company announced that Ailouros Ltd., a London-based institutional money management fund, has committed to purchase up to $15 million worth of common stock of the Company through December 31, 2001. This commitment is in the form of a Class A Warrant issued to Ailouros Ltd. which gives 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 has now been eliminated by mutual agreement so that the Company may put stock to Ailouros at selling prices in excess of $15 per share. However, the Company is 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 determines the amount of common stock that the Company wishes to issue during such three-month period. The Company also sets the minimum selling or "floor" price, which can 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 will determine how much common stock, if any, is to be sold (the amount of which can 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 does 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 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 at $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 Warrant's issuance. The Class B Warrant is exercisable into 65,500 shares. Ailouros paid the Company $10,000 upon issuance of the Class A Warrant and the Class B Warrant.

10 License and Other Agreements

The Company has entered into a number of license agreements covering various products using the Company's SPD technology. Although the Company may receive minimum annual royalties under certain of these licenses, to date although products have been sold resulting in earned royalties under some these license agreements, these earned royalty payments were offset by such minimum advance payments made by the applicable licensees. The table below summarizes Research Frontiers' existing license agreements and lists the year these agreements were entered into.

Licensees of Research Frontiers who incorporate SPD technology into end products will pay Research Frontiers a royalty of 5-10% of net sales of licensed products under license agreements currently in effect, and may also be required to pay Research Frontiers minimum annual royalties. 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. The license granted to Hankuk Glass Industries is exclusive within Korea for certain applications through December 2004. Global Mirror's license restricts new licenses from being granted in the truck mirror original equipment market for a period of time if certain sales milestones are met with respect to commercial vehicles in Classes 5 through 8 with gross vehicle weights in excess of 16,000 pounds.

Licensee or Optionee	*Products Covered*	*Territory*
AP Technoglass Co.	Sunroof glass for other licensees (2001)	Worldwide
Avery Dennison Corp.	SPD displays (2001)	Worldwide
BOS GmbH	Variable light transmission SPD sunshades and sunvisors. (2002)	Worldwide
Dainippon Ink and Chemicals Incorporated	SPD emulsions for other licensees (1999)	Worldwide
Film Technologies Int'l	SPD film for other licensees and prospective licensees (2001)	Worldwide
General Electric Company	SPD film for other licensees and prospective licensees (1995)	Worldwide
Glaverbel, S.A.	Automotive vehicle rear-view mirrors, transportation vehicle sunvisors, and architectural and automotive windows (1996)	Worldwide (except Korea for windows)
Global Mirror GmbH	Rear-view mirrors and sunvisors (1999)	Worldwide
Hankuk Glass Industries Inc.	Broad range of SPD light control products including windows, flat panel displays, automotive vehicle rear-view mirrors and sunvisors (installed as original equipment on Korean-made cars), and sunroofs; SPD film for licensees and prospective licensees (1997)	Worldwide
Hitachi Chemical Co., Ltd.	SPD emulsions and films for other licensees (1999)	Worldwide
InspecTech Aero Service, Inc.	Aircraft windows and cabin dividers (2001)	Worldwide (except Korea)
Isoclima S.p.A.	Architectural and automotive windows (2002)	Worldwide (except Korea)
N.V. Bekaert S.A (acquired from Material Sciences Corp.)	Architectural and automotive windows, SPD film for other licensees, prospective licensees and architectural and automotive window companies (1997)	Worldwide
Polaroid Corporation	SPD emulsions and films for other licensees (2000)	Worldwide
ThermoView Industries, Inc.	Architectural windows (2000)	Worldwide (except Korea)

11 Commitments

The Company has an employment agreement with one of its officers which provides for an annual base salary of $384,948 through December 31, 2002.

In December 2000, the Company's Board of Directors approved a performance bonus plan which provides for a bonus to be paid on or after July 2, 2001 and on or after January 2, 2002 equal to 1% of the increase, if any, in the Company's market value during the first and second halves of 2001. Bonuses are capped at a recipient's salary in the case of employees of the Company, and are currently capped at $57,222 in the case of non-employee directors of the Company. During 2000, the Company had a similar performance plan in place. The Company recorded $785,500 and $755,000 of expenses in connection with these plans for the years ended December 31, 2001 and 2000, respectively. The Company's Board of Directors approved a similar bonus plan for 2002 but with higher thresholds to be met before a bonus is payable under such plan. In addition to the payment caps described above, under the current plan, in order to insure that bonuses are not paid based upon temporary fluctuations in the market value of the Company, bonuses under this plan will only be paid to the various participants under this plan if and when the market value of the Company exceeds $280,489,009 (and in the case of any bonus paid to Robert L. Saxe, if and when the market value of the Company exceeds $304,207,362).

The Company occupies premises under an operating lease agreement which expires on January 31, 2004 and requires minimum annual rent which rises over the term of the lease to approximately $143,500. Rent expense, including other expenses, amounted to approximately $152,000, $142,000, and $143,000, for 2001, 2000, and 1999, respectively.

12 Selected Quarterly Financial Data (Unaudited)

Quarter		First	Second	Third	Fourth
2001	Fee income	$68,752	$12,500	$28,656	$32,094
	Operating loss	(1,187,734)	(1,909,782)	(1,177,408)	(961,804)
	Net loss	(993,822)	(1,748,444)	(985,529)	(812,875)
	Basic and diluted net loss per common share (1)	(.08)	(.14)	(.08)	(.07)
2000	Fee income	$98,774	$99,960	$99,959	$34,959
	Operating loss (2)	(4,736,168)	(1,539,962)	(767,146)	(1,403,042)
	Net loss (2)	(4,547,939)	(1,311,204)	(539,942)	(1,168,715)
	Basic and diluted net loss per common share (1) (2)	(.38)	(.11)	(.04)	(.10)

(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.

(2) The first quarter of 2000 has been restated to include a non-cash accounting charge of $528,198 relating to a warrant which was issued during 1994 and vested during the first quarter of 2000. (see note 9).

Independent Auditors' Report
The Shareholders and Board of Directors
Research Frontiers Incorporated:

We have audited the accompanying consolidated balance sheets of Research Frontiers Incorporated and subsidiary as of December 31, 2001 and 2000, and the related consolidated statements of operations, shareholders' equity and cash flows for each of the years in the three-year period ended December 31, 2001. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 at December 31, 2001 and 2000 and the results of its operations and cash flows for each of the years in the three-year period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States of America.

KPMG LLP

Melville, New York
March 1, 2002

Officers and Directors	***Robert L. Saxe*** Chairman of the Board of Directors Chief Executive Officer and Treasurer (E-Mail: Saxe@refr-spd.com)
	Joseph M. Harary Director, President and Chief Operating Officer General Counsel, Assistant Secretary (E-Mail: Harary@refr-spd.com)
	Michael R. LaPointe Vice President–Marketing (E-Mail: LaPointe@refr-spd.com)
	Robert M. Budin Director
	Victor F. Keen Director, Secretary
Investor Relations	***Patricia A. Bryant*** Manager of Investor Relations (E-Mail: Bryant@refr-spd.com)
Automotive Applications	***John N. Tobias*** Director of Automotive Marketing (E-Mail: Tobias@refr-spd.com)
Patent Counsel	***Cooper & Dunham LLP*** 1185 Avenue of the Americas New York NY 10036
Auditors	***KPMG LLP*** 1305 Walt Whitman Road Melville NY 11747
Transfer Agent and Registrar	***Continental Stock Transfer & Trust Company*** 17 Battery Place, 8th floor New York NY 10004 http://www.continentalstock.com
Headquarters	***Research Frontiers Incorporated*** 240 Crossways Park Drive Woodbury NY 11797-2033
Telephone	***516 364 1902 / 888 SPD REFR***
Facsimile	***516 364 3798***
E-mail	***info@refr-spd.com***
Web	***http://www.refr-spd.com***

RESEARCH FRONTIERS INCORPORATED
240 CROSSWAYS PARK DRIVE, WOODBURY NY 11797-2033