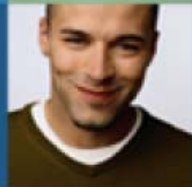




MatchNet® plc



HELPING PEOPLE CLICK



matchnet.de



MatchNet.co.uk

MatchNet.com.au

2004 Second Quarter Report

FINANCIAL HIGHLIGHTS

(Dollars are approximate and expressed in U.S. Dollars)

	Year Ended December 31,		Three Months Ended March 31,		Six Months Ended June 30,	
	2003	2002	2004	2003(1)	2004	2003(1)
Net revenues (in thousands)	\$ 36,941	\$ 16,352	\$ 15,050	\$ 7,036	\$ 30,862	\$ 15,459
Net (loss) (in thousands)	\$ (10,852)	\$ (524)	\$ (3,021)	\$ (591)	\$ (7,114)	\$ (1,328)
Net (loss) per share(2)	\$ (0.57)	\$ (0.03)	\$ (0.14)	\$ (0.03)	\$ (0.33)	\$ (0.07)
Employees	150	74	179	88	194	107

MEMBERSHIP HIGHLIGHTS

(Dollars are approximate and expressed in U.S. Dollars)

Business Metrics(3)	Year Ended December 31,		Three Months Ended March 31,		Six Months Ended June 30,	
	2003	2002	2004	2003	2004	2003
Active members(4) (in thousands)	9,500	5,900	9,500	6,700	9,800	7,100
Subscribers (in thousands)	190	80	220	110	235	125
Average revenue per subscriber(5)	\$ 85	\$ 102	\$ 74	\$ 88	\$ 74	\$ 84
Subscriber churn(6)	26%	20%	33%	28%	32%	29%
Average subscriber acquisition cost(7)	\$ 36	\$ 30	\$ 31	\$ 33	\$ 37	\$ 37

- 1) These amounts are restated amounts from previously filed quarterly reports with the Frankfurt Stock Exchange. See "Risk Factors—We Face Risks Related to Our Recent Accounting Restatements."
- 2) For information regarding the computation of per share amounts, refer to note 1 of our consolidated financial statements.
- 3) All business metrics are full period, except active members and subscribers, which are as of period end.
- 4) Represents individuals who posted a personal profile on one of our Web sites or logged on to that Web site at least once in the 12 months preceding the period end date.
- 5) Represents the inverse of subscriber churn, calculated as described in note (6) below, multiplied by the average monthly subscription price.
- 6) Subscriber churn represents a ratio, expressed as a percentage, of (i) subscriber cancellations in the period divided by the average of the subscribers at the beginning and end of the period and (ii) the number of months in the period. Subscriber cancellations represent the sum of subscribers at the beginning of the period and subscribers added during the period less subscribers at the end of the period.
- 7) Represents marketing expense divided by the gross number of subscribers added during the period.

BUSINESS AND OUTLOOK

Throughout this report, we refer to MatchNet, plc., an English company, and its subsidiaries as “we,” “us,” “our,” “our company,” and “MatchNet” unless otherwise indicated. MatchNet, JDate and AmericanSingles are our registered trademarks. Trade names, trademarks, and service marks of other companies appearing in this report are the property of the respective holders.

We are a leading provider of online personals services in the United States and internationally. We enable adults to meet online and participate in a community, become friends, date, form a long-term relationship or marry. In the first six months of 2004 we averaged approximately 5.3 million unique monthly visitors to our Web sites, which, according to comScore Media Metrix, ranked us as the second largest online personals property among United States Internet users. Currently, our key Web sites are AmericanSingles and JDate. Membership on our sites is free and allows a registered user to post a personal profile and to access our searchable database of member profiles and our 24/7 customer service. The ability to communicate with other members requires the payment of a monthly subscription fee, which represents our primary source of revenue.

As of June 30, 2004, we had approximately 9.8 million active members, which we define as members who have posted a personal profile or have logged on to any of our Web sites at least once in the last 12 months, and approximately 235,000 paying subscribers, representing increases of 38% and 88%, respectively, from June 30, 2003.

We intend to grow our business in the following ways:

- Expand our base of members in the United States and internationally;
- Increase the number and percentage of our members who become paying subscribers; and
- Add revenue opportunities through online advertising on our Web sites.

We believe that one of our key opportunities lies in our ability to significantly enhance our primary brand. To address this we intend to launch a rebranding campaign designed to heighten our brand recognition and attract additional active members and subscribers. We intend to change our name, establish the new company name as our primary consumer brand and consolidate our online personals services, except for JDate, under this umbrella brand name.

Our Industry

Overview

We believe that online personals fulfill significant needs for America’s 86 million single adults who are looking to meet a companion or date. Traditional methods such as printed personals advertisements, offline dating services and public social gathering places often do not meet the needs of time-constrained single people. Printed personals advertisements offer individuals limited personal information and interaction before meeting. Offline dating services are time-consuming, expensive, and offer a smaller number of potential partners. In contrast, online personals services facilitate interaction between singles by allowing them to screen and communicate with a large number of potential companions. This medium allows users to communicate with other singles at their convenience and affords them the ability to virtually meet multiple people in a safe and secure setting. Moreover, online personals services allow people to learn considerably more about someone prior to an in-person meeting, through detailed personal profiles, emails and instant messaging.

Growth Drivers

Internet growth and broadband adoption: In 2003, International Data Corporation, or IDC, estimated there were 700 million Internet users worldwide and projected the number of Internet users to grow to approximately 1.1 billion by 2007. It is estimated that this will be primarily driven by growth outside the United States. In the United States, users are migrating to broadband connections which enable faster delivery of complex content such as online photos and streaming media, as well as instant messaging. IDC projects that 61% of Internet households in the United States will have broadband connections by 2007, up from 35% in 2003.

Growth in e-commerce: We believe broadband users have a higher propensity to conduct e-commerce transactions including the purchase of content and services online, as these Internet connections provide a faster, more convenient transaction experience. According to IDC, worldwide consumer e-commerce spending is expected to grow from \$216 billion in 2003 to \$759 billion by 2007, implying a compound annual growth rate of 37%.

Mainstream acceptance of online personals services: Online personals services continue to gain mainstream acceptance. According to Jupiter Research, 21% of all United States Internet users browsed online personals and 13% posted their own profiles in 2003. In addition, according to comScore Media Metrix, in 2003 the average time spent on online personals sites per month by users rose 155%, from 44 minutes in January 2003 to 111 minutes in January 2004. Online personals services now represent the largest segment of content purchased online, growing 49% in 2003 to \$450 million, according to the Online Publishers Association.

Our Competitive Strengths

- *Critical mass of members:* We had over 9.8 million active members as of June 30, 2004. We believe that one of the reasons singles seeking friendship, dating or long-term relationships are attracted to our Web sites is because of our large pool of current members. We believe that increasing social interaction among members within our online community and generating strong word-of-mouth helps create additional interest in our services, add new members, convert members into paying subscribers, and retain members.
- *Web site functionality:* We continually evaluate the functionality of our Web sites to improve our members' online personals experience. We believe our matching technology gives us a competitive advantage over many of our competitors in the online personals industry. Our systems match members across a myriad of attributes, taking into account personal profile data, and preferences as well as additional proprietary parameters. In addition, many of the features that we offer increase the probability of communication between our members, which we believe increases the number and percentage of members who become paying subscribers. We believe our Web site functionality drives return visits to our Web sites and helps retain subscribers who might otherwise consider switching to our competitors' Web sites.
- *Customer service focus:* We believe that our customer service offers a competitive advantage and differentiates us from our major competitors. Our multi-lingual call center is staffed 24/7 with dating and technical consultants. These consultants help members with such matters as completing personal profiles and choosing photos for their profiles, as well as answering questions about billing and technical issues. We believe our quality customer service increases member satisfaction, which improves the number and percentage of members that become paying subscribers and retention of subscribers.

Our Web Sites

Our online personals services offer single adults a secure and private setting for meeting other singles. Visitors to our Web sites are encouraged to become registered members by posting profiles. Posting a profile is a multi-stage process, where visitors are asked various questions about themselves, including information such as their tastes in food, hobbies, and desired attributes of potential partners. Members are also urged to post photos, since this is likely to improve their chances of making a successful contact with another member. Once they are members they can make detailed searches of other profiles and save their preferences, and their profiles can be viewed by other members. In order for members to communicate with other members, they must purchase a subscription. A subscription affords access to the subscribers' on-site email and instant messaging, enabling them to communicate with other subscribers. Our subscription fees are charged on a monthly basis, with discounts for longer-term subscriptions ranging from three to twelve months.

We strive to offer traditional as well as new and different ways for our members to communicate. Examples of ways our members can communicate include:

- *On-site Email:* We provide all subscribers with private message centers, dedicated exclusively to communications with other subscribers. These personal on-site email boxes offer features such as customizable folders for storing correspondence, the ability to know when sent messages were read as well as block and ignore functions, which afford a subscriber the ability to control future messages from a specific subscriber.
- *Hot Lists and Favorites:* Among the most popular features on our Web sites, “Hot Lists” enable members to see who’s interested in them and to save those favorite members that they are interested in. Lists include who’s viewed your profile, your favorites, and who’s emailed you. Members can group their favorites into customized folders and add their own notes, including detail included in a member’s profile.
- *Real-time chat rooms:* Subscribers can utilize our exclusive chat rooms to mix and mingle in real-time, building community through one-to-many communication. Additional features enable users to add customized graphics such as emoticons to their conversations.
- *Ice Breakers (Flirt/Tease):* allow members to send “pre-packaged” opening remarks to other members or subscribers.
- *Instant messaging and Online Now:* enables real-time communication between subscribers, creating a real-time call to action. Audio/video functionality is offered on one of our Web sites, and we are in the process of implementing this feature on all of our sites.
- *Click!:* connects members who think they would be compatible with each other. A member simply clicks “yes,” “no” or “maybe” in another member’s profile. When two members click “yes” in each other’s profiles, our patented feature sends an email to both of them alerting them of a possible match.

We believe we are a unique company in the online personals markets because, in addition to servicing mass markets, we operate Web sites targeted at selected niche markets. We currently offer our services in English, German, and Hebrew. Our key Web sites are as follows:

- *AmericanSingles.com.* AmericanSingles is our mainstream U.S. online dating community, targeted at an audience of singles between 25 and 49 years old. The site caters to singles of all races, ethnicities, and interests. AmericanSingles members are primarily concentrated in major metropolitan areas across the United States. The current monthly subscription fee on AmericanSingles is \$24.95. As part of our emerging rebranding strategy, we intend to re-launch AmericanSingles.com under our new company name in late 2004.
- *JDate.com.* JDate was our first Web site and is solely dedicated to the Jewish community. Currently, JDate members represent approximately one third of all Jewish singles in the United States, based on data provided by the National Jewish Population Survey. JDate members are primarily concentrated in New York, Southern California, Miami, and Chicago. The current monthly subscription fee on JDate is \$34.95.

Business Strategy

We intend to grow subscription-based revenue by growing the number of our members, increasing the number and percentage of our members who convert to subscribers and enhancing our subscribers’ online experience. Our large base of members provides us with a significant amount of consumer data to evaluate areas for growth. We are able to analyze different groups of members by key metrics such as average conversion rates and average revenue per subscriber and identify those targeted groups that may prefer a dedicated service. In addition to growing our subscription-based business, we plan to generate revenue by monetizing our large online community through online advertising.

Grow memberships: We believe there are significant growth opportunities to build brand awareness, drive additional traffic to our Web sites, and identify new markets, where we can leverage our existing infrastructure to increase memberships.

- *Rebranding strategy.* We believe that significant opportunities lie in our ability to enhance our brands. We intend to launch a rebranding campaign designed to heighten our brand recognition and attract additional active members and subscribers. We plan to change our name and establish the new company name as the primary consumer brand for our services except for JDate. We believe that marketing the new company brand name as opposed to several distinct brands will allow us to gain marketing efficiencies and heighten our brand recognition.
- *Integrated and targeted marketing.* We believe that targeting potential members with consistent and compelling marketing messages, delivered through a broad mix of marketing channels, will be effective in driving more traffic and a higher percentage of relationship-oriented singles to our Web sites. We intend to use a variety of channels to increase our base of members including online and offline advertising, public relations, promotional alliances and special events.
- *Geographic expansion.* We plan to expand into new geographic markets where we can introduce one or more of our existing products in multiple languages. We believe that our recently introduced multicurrency payment system will aid the growth in our international member base.
- *Niche market expansion.* We intend to expand into new demographic markets in an effort to increase the number of our members. We believe there are a number of niche markets, or targeted demographics, which would prefer to interact within their own ethnic, lifestyle or religious group. We plan to target those groups that possess the scale to obtain the required critical mass of members.

Increase conversion rates: As of June 30, 2004, we had approximately 235,000 subscribers. We believe that a significant growth opportunity lies in our ability to convert more of our 9.8 million active members as of June 30, 2004 to paying subscribers. We plan to achieve this increase in conversion by focusing on:

- *Improved matching technology.* We believe that the more successful members are in finding matches in our database, the more likely they are to communicate with those members, which require that they become subscribers. We intend to continue to enhance our matching technology and the quality and relevance of search results to provide fast, relevant matching suggestions.
- *Leveraging strong customer service.* Each time a member or potential member contacts our customer service center by email or phone, it represents a potential new subscriber to our services. By training our customer service representatives on up-selling opportunities we believe they will continue to be successful in selling and building loyalty to our subscription-based services.
- *Improved member communications.* We believe that enhanced member communications is a key component to growing our business. We focus on improving and enhancing our Web site functionality and features to encourage communications between members, which requires that members become subscribers. We will also continue to inform members of new features and functions with the goal of improving our conversion ratios.

Pursue additional revenue through online advertising on our Web sites: Many advertisers target the mass audience and niche communities we serve. We believe we have the critical mass of unique monthly visitors to our Web sites necessary to attract interest from advertisers which will allow us to generate additional revenue. By expanding our membership base and offering improved Web site functionality and features designed to enhance the average time spent on our Web sites per month, we believe that we can generate additional advertising opportunities.

Customer Service

Our customer support and service function operates 24/7. As of June 30, 2004, we employed 79 customer service representatives at our Beverly Hills, California facility and 10 customer service representatives at our Israeli facility that serves our Hebrew-speaking members. Our team of customer service representatives helps members with matters such as completing personal essays and choosing photos for their profiles, as well as answering questions about billing and technical issues. Customer service representatives undergo comprehensive, ongoing training in an effort to better personalize the experience for members or subscribers that call in and to capitalize on up-selling opportunities. On average we receive 1,400 phone calls and 9,000 emails per day, and our average wait time for phone calls and response rate for emails is two minutes and four hours, respectively.

Marketing

Historically, we have engaged in a variety of marketing activities intended to drive consumer traffic to our Web sites and allow us the opportunity to introduce our products and services to prospective members. Our marketing efforts have been principally focused online, where we have employed a combination of banner and other display advertising on Web portals and other specialized sites. We have also relied on commercial search listings and direct e-mail campaigns to attract potential customers, and have utilized a network of online affiliates, through which we acquire traffic.

In order to drive broader awareness of our online personals services and brands, we expect to invest in an integrated and targeted marketing campaign and broaden the marketing channels we use. In addition to our current online marketing efforts, we expect to employ a variety of offline marketing activities. These may include broadcast, print, and outdoor advertising, public relations, event sponsorship, and promotional alliances. We believe that a more targeted marketing message, delivered through an array of available marketing channels, will improve consumer awareness of our brands and drive more traffic to our Web sites.

An essential component of our marketing strategy will be to establish our new company name as the primary consumer brand name for our properties. With the exception of JDate, which we believe has built significant brand equity and consumer awareness, we intend to consolidate our online dating properties under the umbrella brand of our new company name. We plan to change our name and intend to re-launch AmericanSingles.com under the new company name in late 2004.

Technology

Our software development team consists of 14 employees as of June 30, 2004, who are focused on expanding and improving the features and functionality of our Web sites. As feature and functionality development is an important element of our strategy, we plan to significantly expand our software development team. In addition to our development team, an additional 26 technology employees maintain our software and hardware infrastructure.

Our network infrastructure and operations are designed to deliver high levels of availability, performance, security and scalability in a cost-effective manner. The majority of our software architecture is based on standard modular Microsoft technology, and is designed for maximum flexibility and scalability, which we believe facilitates the addition of new Web sites and features.

Our scalable email system runs on four servers, with each server capable of sending approximately 2 million messages per hour. In addition to our email servers, we operate another 260 Web, database and other servers, which are co-located at a facility in El Segundo, California that is operated by a third party. We plan to add adequate redundant hardware and software systems supporting our services at an alternate site within the next 12 months.

Intellectual Property

We rely on a combination of patent, trademark, copyright, and trade secret laws in the United States and other jurisdictions as well as confidentiality procedures and contractual provisions to protect our

proprietary technology and our brands. We also enter into confidentiality and invention assignment agreements with our employees and consultants and confidentiality agreements with other third parties, and we rigorously control access to proprietary technology.

MatchNet, JDate, and AmericanSingles are our registered trademarks in the United States and several other countries; we have a number of other registered and unregistered trademarks. Our patent for *Click!* was granted in September of 1999 and pertains to an automated process for confidentially determining whether people feel mutual attraction or have mutual interests. The patent describes the method and apparatus for the identification of a person's level of attraction and the subsequent notification when the feeling or attraction is mutual.

Competition

We operate in a highly competitive environment with minimal barriers to entry. We believe that the primary competitive factors in creating a community on the Internet are functionality, brand recognition, critical mass of members, member affinity and loyalty, ease-of-use, quality of service, and reliability. We compete with a number of large and small companies, including vertically integrated Internet portals and specialty-focused media companies that provide online and offline products and services to the markets we serve. Our principal online personals services competitors include Match.com, Yahoo! Personals, eHarmony, LavaLife, and Tickle, which operate primarily in North America, and Meetic, in Europe. In addition, we face competition from social networking Web sites such as Friendster, MySpace, and Orkut. There are also several other companies offering online personals services that compete with us, but are smaller than we are in terms of paying subscribers and annual revenue generation.

Employees

As of June 30, 2004, we had 194 full-time employees. We are not subject to any collective bargaining agreements, and we believe that our relationship with our employees is good.

Facilities

Our headquarters are located in Beverly Hills, California, where we occupy approximately 25,000 square feet of office space that houses our technology department, customer service operations, and most of our corporate and administrative personnel. This lease expires on July 31, 2006. We also lease office space in England, Israel, and Germany. We believe that our facilities are adequate for our current needs, and suitable additional or substitute space will be available in the future to replace our existing facilities, if necessary, or accommodate expansion of our operations.

**MANAGEMENT DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following discussion of our financial condition and results of operations should be read in conjunction with our audited consolidated financial statements and the related notes thereto included elsewhere in this report. This discussion contains forward-looking statements about us which involve substantial risks and uncertainties. Forward-looking statements include information concerning possible or assumed future results of operations, and include statements preceded by, followed by or that otherwise include the words “believes,” “expects,” “anticipates,” “intends,” “estimates,” “may,” “will,” “continue,” “should,” “plan,” “predict,” “potential” or the negative of these terms or other similar expressions. We have based these forward-looking statements on our current expectations and projections about future events and financial trends that we believe may affect our financial condition, results of operations, business strategy, and financial needs. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including, but not limited to, those set forth below and elsewhere in this report, particularly under the heading “Risk Factors.”

Overview

We provide online personals services, which enable individuals to post information about themselves on our Web sites, and search and contact other individuals who have posted similar information. Our members reside primarily in the United States, and we presently have members located in over 200 countries.

Our revenues have grown from \$659,000 in 1999 to \$36.9 million in 2003. As of June 30, 2004 we had approximately 9.8 million active members and 235,000 subscribers. We define an active member as an individual who has posted a personal profile or logged on to one of our Web sites at least once in the last 12 months. We define subscribers as members who have upgraded to subscriber status by paying a monthly fee that enables them to communicate with other members. We offer a number of Web sites for singles, most of which are differentiated by age, religious preference, sexual preference, and geography. Our key Web sites are AmericanSingles, which targets the U.S. mainstream online singles community at a current subscription fee of \$24.95 per month, and JDate, which targets the Jewish singles community in the United States and internationally at a current subscription fee of \$34.95 per month. Our subscription fees are charged on a monthly basis, with discounts for longer-term subscriptions ranging from three to twelve months.

We have grown both internally and through acquisitions of entities and selected assets of entities offering online personals services and related businesses. As a result of each of these acquisitions, we have been able to combine the target entity’s existing database of online personals customers into one of our Web sites’ databases, with the goal of attracting these new members to our Web sites, retaining as many of them as possible, and converting them into paying subscribers. A summary of these business and/or asset acquisitions is as follows:

Name	Transaction Date	Strategic Rationale
Cupid’s Network, Inc.	May 1999	Expand into new markets, leverage an existing brand, AmericanSingles, and improve position within the market.
MeetMeOnline, Inc.	September 1999	Leverage the positioning and membership database of an existing online personals service, enhance and extend existing brands.
DoYouDo, Inc.	September 2000	Leverage the positioning and membership database of an existing online personals service, enhance and extend existing brands.
SocialNet, Inc.	February 2001	Leverage the positioning and membership database of an existing online personals service enhance and extend existing brands.
Agentscape AG (FlirtMaschine.de)	October 2001	Leverage the positioning and membership database of an existing online personals service, enhance and extend existing brands.

FaceLink Inc.	February 2002	Purchase member database and Web site to increase services provided, leverage market position for marketing existing MatchNet services.
Point Match Ltd.	January 2004	Purchase member databases and Web sites from a leading competitor of JDate in the United States and Israel.

Our future success will depend on many factors, including:

- continued acceptance of online personals services;
- our ability to increase brand awareness both domestically and internationally;
- our ability to attract a large number of new members, convert members into paying subscribers and retain our paying subscribers;
- our ability to sustain, and when possible, increase subscription rates for our services; and
- our ability to introduce new targeted Web sites, affiliate programs, fee-based services and advertising as additional sources of revenues.

We believe that one of our key opportunities lies in our ability to significantly enhance our primary brand. With the exception of JDate, which is widely known among Jewish singles, our brands are generally not as well known today as those of our principal competitors. To address this we intend to launch a rebranding effort designed to heighten our brand recognition and attract additional active members and subscribers. We intend to change our name, establish the new company name as our primary consumer brand, and consolidate our online personals services, excluding JDate, under this umbrella brand name.

In addition, our ability to compete effectively will depend on the timely introduction and success of our future Web sites, services and features, and the ability to address the needs of our members and subscribers, and respond to Web sites, services and features introduced by others. To address this challenge, we have invested and will continue to invest significant resources in order to enhance our existing services, and introduce new services, which will include new targeted Web sites, as well as new features designed to increase the probability of communication among our members and subscribers, and to enhance their online personals experiences.

We intend to diversify our sources of revenue by introducing online advertising. To date, substantially all of our revenue has been derived from our subscription-based services. We believe our large membership base positions us to earn revenues from advertisers that target the mass audience and niche communities we serve. We intend to leverage this opportunity by focusing our efforts within the next 12 months toward diversifying our revenue base through advertising.

Critical Accounting Policies, Estimates and Assumptions

Our discussion and analysis of our financial condition and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, we evaluate our estimates, including those related to revenue recognition, prepaid advertising, Web site, and software development costs, goodwill, intangible, and other long-lived assets, accounting for business combinations, contingencies, and income taxes. We base our estimates on historical experience and on various other assumptions that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Management has discussed the development and selection of our critical accounting policies, estimates and assumptions with our Board of Directors and the Board has reviewed these disclosures.

We believe the following critical accounting policies reflect our more significant judgments and estimates used in the preparation of our consolidated financial statements:

Revenue Recognition and Deferred Revenue

Substantially all of our revenues are derived from subscription fees. Revenues are presented net of credits and credit card chargebacks. We recognize revenue in accordance with accounting principles generally accepted in the United States, and with Securities and Exchange Commission Staff Accounting Bulletin No. 104, "Revenue Recognition." Recognition occurs ratably over the subscription period, beginning when there is persuasive evidence of an arrangement, delivery has occurred (access has been granted), the fees are fixed and determinable, and collection is reasonably assured. Subscribers pay in advance, primarily by using a credit card, and all purchases are final and nonrefundable. Subscription fees collected in advance are deferred and recognized as revenue using the straight-line method over the term of the subscription.

Prepaid Advertising Expenses

In certain circumstances, we pay in advance for Internet based advertising on other contracted Web sites, and expense the prepaid amounts over the contract periods as the contracted Web site delivers on their commitment. We evaluate the realization of prepaid amounts at each reporting period, and expense prepaid amounts if the contracted Web site is unable to deliver on their commitment.

Web Site and Software Development Costs

We capitalize costs related to developing or obtaining internal-use software. Capitalization of costs begins after the conceptual formulation stage has been completed. Product development costs are expensed as incurred or capitalized into property and equipment in accordance with Statement of Position 98-1 "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use" ("SOP 98-1"). SOP 98-1 requires that costs incurred in the preliminary project and post-implementation stages of an internal use software project be expensed as incurred, and that certain costs incurred in the application development stage of a project be capitalized. We exercise judgment in determining which stage of development a software project is in at any point in time.

In accordance with EITF 00-2 "Accounting for Web Site Development Costs," we expense costs related to the planning and post implementation phases of our Web site development efforts. Direct costs incurred in the development phase are capitalized. Costs associated with minor enhancements and maintenance for the Web site are included in expenses in the accompanying consolidated statements of operations.

Capitalized Web site and software development costs are included in internal-use software in property and equipment, and amortized over the estimated useful life of the products, which is usually three years. In accordance with the above accounting literature, we estimate the amount of time spent by our engineers in developing our software and enhancements to our Web sites.

Valuation of Goodwill, Identified Intangibles and Other Long-lived Assets

We test goodwill and intangible assets for impairment in accordance with SFAS No. 142, "Goodwill and Other Intangible Assets", and test property, plant and equipment for impairment in accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." We assess the impairment of goodwill, identifiable intangible assets, and other long-lived assets whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Factors we consider important which could trigger an impairment review include the following:

- a significant decline in actual projected revenue;
- a significant decline in the market value of our shares;
- a significant decline in performance of certain acquired companies relative to their original projection;
- a significant difference between our net book value and our market value;
- a significant decline in our operating results relative to our operating forecasts;
- a significant change in the manner of our use of the acquired assets or the strategy for our overall business;
- a significant decrease in the market value of an asset;
- a shift in technology demands and development; and
- a significant turnover in key management or other personnel.

When we determine that the carrying value of goodwill, other intangible assets, and other long-lived assets may not be recoverable based upon the existence of one or more of the above indicators of impairment, we measure any impairment based on a projected discounted cash flow method using a discount rate determined by our management to be commensurate with the risk inherent in our current business model. In the case of the other intangible assets and other long-lived assets, this measurement is only performed if the projected undiscounted cash flows for the asset are less than its carrying value. No indicators of impairment in goodwill were present in 2003. We had impairment charges related to long-lived assets of \$1.5 million in 2003 in accordance with SFAS 144.

Accounting for Business Combinations

We have acquired the stock or specific assets of a number of companies from 1999 through 2004 some of which were considered to be business acquisitions. Under the purchase method of accounting, the cost, including transaction costs, are allocated to the underlying net assets, based on their respective estimated fair values. The excess of the purchase price over the estimated fair values of the net assets acquired is recorded as goodwill.

The judgments made in determining the estimated fair value and expected useful lives assigned to each class of assets and liabilities acquired can significantly impact net income. For example, different classes of assets will have useful lives that differ (e.g., the useful life of member database (three year amortization) may not be the same as the useful life of subscriber lists (three months) or domain names (indefinite lives)). Consequently, to the extent a longer-lived asset is ascribed greater value under the purchase method than a shorter-lived asset, there may be less amortization recorded in a given period or no amortization for indefinite lived intangibles.

Determining the fair value of certain assets and liabilities acquired is judgmental in nature, and often involves the use of significant estimates and assumptions.

The value of our intangible and other long-lived assets, including goodwill, is exposed to future adverse changes if we experience declines in operating results or experience significant negative industry or economic trends or if future performance is below historical trends. We periodically review intangible assets and goodwill for impairment using the guidance of applicable accounting literature. We continually review the events and circumstances related to our financial performance and economic environment for factors that would provide evidence of the impairment of goodwill, identifiable intangibles, and other long-lived assets.

Legal Contingencies

We are currently involved in certain legal proceedings, as discussed in the notes to the financial statements and under "Business — Legal Proceedings." To the extent that a loss related to a contingency is reasonably estimable and probable, we accrue an estimate of that loss. Because of the uncertainties related to both the amount and range of loss on certain pending litigation, we may be unable to make a reasonable estimate of the liability that could result from an unfavorable outcome of such litigation. As additional information becomes available, we will assess the potential liability related to our pending litigation, and make or, if necessary, revise our estimates. Such revisions in our estimates of the potential liability could materially impact our results of operations and financial position.

Accounting for Income Taxes

We account for income taxes using the asset and liability method, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and tax bases of the assets and liabilities. In accordance with the provisions of SFAS 109, "Accounting for Income Taxes," we record a valuation allowance to reduce deferred tax assets to the amount expected to more likely than not be realized in our future tax returns. As of June 30, 2004 and December 31, 2003, we had a valuation allowance that completely offset our deferred tax asset. Should we determine in the future that we will more likely than not be able to realize all or part of our net deferred tax assets, we will adjust the valuation allowance so that we will have a deferred tax asset for the amount we determine to be more likely than not to be realized in our future tax returns.

Restatement of Consolidated Financial Statements for the First Half of 2003

MatchNet has restated its consolidated financial statements for the first half of 2003 to correct certain errors as described below:

In previous periods the Company incorrectly recognized a full month of revenue in the month in which members paid in advance for their membership subscription fees (regardless of the effective date of the subscription) and deferred the balance of the fees for multi-month subscriptions. In July of 2003, the Company began to defer revenue on a daily basis (based on the effective date of the subscription and restated prior period's financial statements). The effect on the three and six months ended June 30, 2003 was to decrease revenues by approximately \$303,000 and \$628,000 respectively.

In previous periods we had capitalized bounty costs, which represented amounts paid to third parties for members acquired on an individual basis through third party Web sites or e-mail campaigns. These costs were being amortized over a three year period, on an accelerated basis. In 2003 we determined that these costs should be expensed as incurred, and that we should restate the prior periods' financial statements to conform to U.S. generally accepted accounting principles. The reason for the change was that bounty costs were meant to drive free memberships or registrations. A member was not required to become a paying subscriber. Therefore, those expenses should be recognized immediately, since a conversion from non-paying member to a paying subscriber is not guaranteed. Accordingly, we have restated the consolidated financial statements to expense these costs as incurred. The effect on the three months ended March 31, 2003 was to decrease operating expenses by \$591,000. There was no change related to bounty in the second quarter of 2003.

From 1998 through 2002 the Company acquired several businesses and assets. At that time, the fair values of the intangible assets acquired were not properly determined. In 2004, the Company hired a valuation expert to measure the fair value of such assets at the date of each acquisition. As a result of this process, the Company determined that certain allocations previously reported were inappropriate. The effect on the three and six months ended June 30, 2003 was to increase amortization expense by approximately \$76,000 and \$155,000 respectively.

We did not timely accrue for some services provided. The accompanying financial statements for the three and six months ended June 30, 2003 were restated to properly and timely accrue for these

liabilities. The effects on the three and six months ended June 30, 2003 was to increase operating expenses by approximately \$60,000 and decrease operating expenses by approximately \$101,000 respectively.

The Company identified certain errors in the prior years consolidation process. The effects on the net loss for the three and six months ended June 30, 2003 was a decrease of approximately \$314,000 and \$157,000 respectively.

Results of Operations

Business Metrics

Active members grew to approximately 9.8 million at June 30, 2004 from approximately 7.1 million at June 30, 2003, or 38%. This increase was primarily due to increased marketing efforts and the increased popularity of online personals services.

Subscribers at June 30, 2004 increased to approximately 235,000 from approximately 125,000 at June 30, 2003, or 88%. This increase corresponds with the increase in active members and improved conversion of active members to paying subscribers.

Average revenue per subscriber, which represents the inverse of subscriber churn as calculated below multiplied by the average monthly subscription price, decreased to approximately \$74.00 for both the three and six months ended June 30, 2004 from approximately \$84.00 and \$82.00 in the three and six months ended June 30, 2003, respectively. The decrease was primarily due to a higher subscriber churn in the three and six months ended June 30, 2004, and a change in the revenue mix among our key Web sites whereby a higher percentage of subscribers at June 30, 2004 subscribed to our lower priced AmericanSingles Web site as compared to June 30, 2003.

The subscriber churn was approximately 31% and 32% for the three and six months ended June 30, 2004 respectively as compared to 29% for both the three and six months ended June 30, 2003. Subscriber churn represents the ratio expressed as a percentage of (i) subscriber cancellations in the period divided by the average of the subscribers at the beginning and end of the period, and (ii) the number of months in the period. The increase in churn was primarily due to a change in the revenue mix among our key Web sites whereby a higher percentage of subscribers at June 30, 2004 subscribed to our AmericanSingles Web site as compared to June 30, 2003. AmericanSingles typically has a higher subscriber churn than our other key Web site, JDate.

The average subscriber acquisition cost, which represents marketing expense divided by the total number of subscribers added during the period, was approximately \$44.00 and \$40.00 for the three months ended June 30, 2004 and 2003 respectively. Average subscriber acquisition cost for both the six months ended June 30, 2004 and 2003 was \$37.00. In general, the costs of online advertising have recently increased, and these costs are expected to continue to increase as long as the demand for online advertising remains robust. Significant increases in the costs of online advertising may increase subscriber acquisition cost. Commencing in late 2004 or early 2005, we expect to expand to offline advertising, such as television, radio, and print, which may be more expensive and could increase our subscriber acquisition costs. As we initiate these additional marketing efforts to build offline brand recognition, we expect that marketing expenses will increase, and that there will initially be a significant lag between the time we incur the offline advertising expense and the receipt of revenues resulting from this advertising spend. As a result, we expect that our subscriber acquisition costs will be higher in the initial stages of our offline advertising efforts.

Three Months Ended June 30, 2004 Compared to Three Months Ended June 30, 2003.

Net Revenues

Substantially all of our net revenues are derived from subscription fees, and to a lesser extent from certain promotional events, which accounted for less than 2% of net revenues for the three and six months ended June 30, 2004 and 2003. Revenues are presented net of credits and credit card chargebacks. We expect net revenues from promotional events to comprise an even smaller percentage of net revenues in the future. We also expect to generate revenues from advertising on our Web sites in the future. Our subscriptions are offered in durations of one, three, six or twelve

months. Plans with durations of longer than one month are available at discounted rates. Some subscription programs renew automatically for subsequent periods until subscribers terminate them.

Net revenues increased 88% to \$15.8 million in the three months ended June 30, 2004 compared to \$8.4 million in the three months ended June 30 2003. The increase in net revenues is primarily due to an increase in subscriptions, as discussed above.

Operating Expenses

Operating expenses primarily consist of marketing, customer service, technical operations, product development, and administrative expenses. Operating expenses increased 116% to approximately \$19.9 million in the three months ended June 30, 2004 from approximately \$9.2 million in the three months ended June 30, 2003. Stated as a percentage of net revenues, operating expenses were 126% in the three months ended June 30, 2004 compared to 110% in three months ended June 30, 2003. The increase was primarily the result of a higher level of general and administrative expenses, and increased online marketing expense.

Marketing: Marketing expenses primarily consist of costs to obtain new subscribers and advertising costs. Marketing expenses increased 108% to approximately \$10.0 million for three months ended June 30, 2004 from approximately \$4.8 million in the three months ended June 30, 2003 largely as a result of expanded online advertising campaigns. We plan to increase our marketing expenditures in the remainder of 2004 with additional online and possible offline advertising. The costs of online marketing are rising and are expected to continue to increase as long as the demand for online advertising remains robust. Marketing costs are expected to increase as we pursue our rebranding effort and are expected to increase as a percentage of revenues in the initial stages of our offline advertising efforts due to the expected lag in the receipt of revenues generated from those off line marketing efforts as described above.

Customer Service: Customer service expenses primarily consist of costs associated with our member service center. Customer service expenses increased 80% to approximately \$900,000 in the three months ended June 30, 2004 from approximately \$460,000 in the three months ended June 30, 2003, largely as a result of increased number of employees necessary to support the larger number of members. We expect these costs to continue to increase as we seek to further support increased usage of our services by our members.

Technical Operations: Technical operations expenses primarily consist of the people and systems necessary to support our network, Internet connectivity, and other data and communication support. Technical operations expenses increased 100% to approximately \$2.0 million in the three months ended June 30, 2004 from approximately \$1.0 million in the three months ended June 30, 2003, largely as a result of the growth in the number of members and traffic (usage or people clicking on our URL domains to use our service) to our Web sites. We expect these costs to increase with any increase in traffic, unique users, registrants or subscribers.

Product Development: Product development expenses primarily consist of costs incurred in the development, creation, and enhancement of our Web sites and services. Product development expenses increased 86% to approximately \$427,000 in the three months ended June 30, 2004 from approximately \$229,000 in the three months ended June 30, largely as a result of costs associated with technical enhancements to our Web sites. We expense these costs as incurred, unless they are required to be capitalized. Capitalized costs were approximately \$87,000 and \$286,000 in the three months ended June 30, 2004 and 2003, respectively. The amortization of these costs is included in this line item. We expect these costs to increase as we develop additional features and functionality on our Web sites in order to enhance our members' experience and satisfaction, and increase the number and percentage of members that become paying subscribers.

General and Administrative Expenses: General and administrative expenses primarily consist of personnel-related costs, professional fees, occupancy and other overhead costs. General and administrative expenses increased 119% to approximately \$5.7 million in the three months ended

June 30, 2004 from approximately \$2.6 million in the three months ended June 30, 2003; largely as a result of an increase in hiring people to support growth. We expect these general and administrative expenses to increase as we continue to hire a number of key management personnel, including a Chief Financial Officer, Controller, and General Counsel, and pursue future growth opportunities and manage the increasing complexity associated with growth.

Stock-Based Compensation: Stock-based compensation is recognized over the vesting period of the subject securities, and is based on the excess on the date of grant of the deemed fair value of the underlying shares and the exercise price on the date of grant. Stock-based compensation was approximately \$689,000 in the three months ended June 30, 2004 compared to zero in the three months ended June 30, 2003.

Interest Income and Other Expenses, Net: Interest income and other expenses, net primarily consist of gains (losses) associated with temporary investments in interest bearing accounts and marketable securities. Interest income and other expenses, net decreased to expenses of approximately \$28,000 in the three months ended June 30, 2004 from income of approximately \$57,000 in the three months ended June 30, 2003.

Net Loss

Net loss increased to approximately \$4.1 million in the three months ended June 30, 2004 from approximately \$737,000 in the three months ended June 30, 2003 largely as a result of the increase in operating expenses to expand and grow during the period, and invest for future opportunities.

Six Months Ended June 30, 2004 Compared to Six Months Ended June 30, 2003.

Net Revenues

Substantially all of our net revenues are derived from subscription fees, and to a lesser extent from certain promotional events, which accounted for less than 2% of net revenues for the six months ended June 30, 2004 and 2003. Net revenues increased 99% to \$30.9 million in the first half of 2004, compared to \$15.5 million in the first half of 2003. The increase in net revenues is primarily due to an increase in subscriptions, as discussed above.

Operating Expenses

Operating expenses increased 124% to approximately \$37.9 million in the first six months of 2004 from approximately \$16.9 million in the first six months of 2003. Stated as a percentage of net revenues, operating expenses were 123% in the first six months of 2004 compared to 109% in the first six months of 2003. The increase was primarily the result of a higher level of general and administrative expenses and increased online marketing expense. The increase as a percentage of net revenues was primarily due to an employee severance charge of approximately \$2.4 million, and a non-cash stock-based compensation charge of approximately \$2.4 million.

Marketing: Marketing expenses primarily consist of costs to obtain new subscribers and advertising costs. Marketing expenses increased 106% to approximately \$17.1 million for the first six months of 2004 from approximately \$8.3 million in the first six months of 2003, largely as a result of expanded online advertising campaigns.

Customer Service: Customer service expenses increased 90% to approximately \$1.9 million in the first six months of 2004 from approximately \$1.0 million in the first six months of 2003, largely as a result of increased number of employees necessary to support the larger number of members.

Technical Operations: Technical operations expenses increased 83% to approximately \$3.3 million in the first six months of 2004 from approximately \$1.8 million in the first six months of 2003, largely as a result of the growth in the number of members, and traffic (usage or people clicking on our URL domains to use our service) to our Web sites.

Product Development: Product development expenses primarily consist of costs incurred in the development, creation, and enhancement of our Web sites and services. Product development expenses increased 78% to approximately \$706,000 in the first six months of 2004 from approximately \$397,000 in the first six months of 2003, largely as a result of costs associated with technical enhancements to our Web sites. Capitalized costs were approximately \$325,000 and \$448,000 in the first six months of 2004 and 2003, respectively.

General and Administrative Expenses: General and administrative expenses increased 137% to approximately \$12.1 million in the first six months of 2004 from approximately \$5.1 million in the first six months of 2003, largely as a result of an increase in hiring people to support growth and an employee severance charge of approximately \$2.4 million.

Stock-Based Compensation: Stock-based compensation was approximately \$2.4 million in the first six months of 2004 compared to zero in the first six months of 2003.

Interest Income and Other Expenses, Net: Interest income and other expenses, net primarily consist of gain (loss) associated with temporary investments in interest bearing accounts and marketable securities. Interest income and other expenses, net decreased to expense of approximately \$32,000 in the first six months of 2004 from income of approximately \$110,000 in the first six months of 2003.

Net Loss

Net loss increased to approximately \$7.1 million in the first six months of 2004 from approximately \$1.3 million in the first six months of 2003 largely as a result of the increase in operating expenses to expand and grow during the period and invest for future opportunities, as well as an employee severance payment of approximately \$2.4 million and stock-based compensation of \$2.4 million.

Liquidity and Capital Resources

At June 30, 2004, we had cash, cash equivalents and marketable securities of approximately \$9.5 million. We have historically financed our operations with internally generated funds and offerings of equity securities. We have no revolving or term credit facilities.

Net cash provided by (used in) operating activities was approximately (\$1.0) million and \$1.1 million for the six months ended June 30, 2004 and 2003 respectively.

Net cash used in investing activities was approximately \$7.4 million for the six months ended June 30, 2004. Cash related to investing activities was used primarily for acquisitions requiring approximately \$4.2 million and capital expenditures of approximately \$3.6 million. Net cash used in investing activities was approximately \$313,000 for the six months ended June 30, 2003.

Net cash provided by financing activities was approximately \$12.8 million for the six months ended June 30, 2004, which consisted primarily of net proceeds from the issuance of equity securities. Net cash provided by financing activities was approximately \$35,000 for the six months ended June 30, 2003.

For the six months ended June 30, 2004 we had capital expenditures of approximately \$3.6 million.

We currently anticipate that existing cash, cash equivalents and marketable securities and cash flow from operations will be sufficient to meet our anticipated needs for working capital, operating expenses and capital expenditures for at least the next 12 months. We may need to raise additional funds in the future to fund more aggressive brand promotions and rapid expansion, develop newer or enhanced services, respond to competitive pressures or acquire complementary businesses, technologies or services. Such additional financing may not be available on terms acceptable to us or at all. If additional funds are not available or not available on acceptable terms, we may not be able to fund our expansion, promote our brands, take advantage of acquisition opportunities, develop or enhance services or respond to competitive pressures.

Interest Rate Risk

Our exposure to market rate risk for changes in interest rates relates primarily to our cash, cash equivalents and marketable securities. We have not used derivative financial instruments to mitigate such risk. We invest our excess cash in debt instruments of the U.S. Government and its agencies.

Investments in both fixed-rate and floating-rate interest-earning instruments carry a degree of interest rate risk. Fixed-rate securities may have their fair market value adversely impacted due to a rise in interest rates, while floating-rate securities may produce less income than expected if interest rates fall. Due in part to these factors, our future investment income may fall short of expectations due to changes in interest rates or we may suffer losses in principal if forced to sell securities which have declined in market value due to changes in interest rates.

Foreign Currency Exchange Risk

As we increase our operations in international markets we may become exposed to potentially volatile movements in currency exchange rates. Foreign exchange gains and losses were not material to our earnings for the six months ended June 30, 2004 and 2003.

Change in Accountants

On March 23, 2004, upon the authorization of our board of directors, we dismissed Stonefield Josephson and engaged Ernst & Young LLP as our independent auditors.

During the years ended December 31, 2003 and 2002, and the subsequent period from January 1, 2004 to March 23, 2004, Stonefield Josephson did not have any disagreement with us on any matter of accounting principles or practices, financial statement disclosure or auditing scope or procedure, which disagreements, if not resolved to the satisfaction of Stonefield Josephson, would have caused them to make reference to the subject matter of the disagreement in connection with their reports on our financial statements for such years. The reports of Stonefield Josephson on financial statements for the years ended December 31, 2002 and 2001 did not contain an adverse opinion or disclaimer of opinion, and were not qualified or modified as to uncertainty, audit scope or accounting principles. We did not consult with Ernst & Young LLP on any financial or accounting reporting matters before its appointment.

Notwithstanding the foregoing, during the course of the preparation of our financial statements for the year ended December 31, 2003, we discovered accounting inaccuracies in previously reported financial statements, including those for the years ended December 31, 2002 and 2001 that were covered by reports issued by Stonefield Josephson. Difficulties arose from differing views between Ernst & Young LLP and Stonefield Josephson regarding the necessity and scope of a restatement of 2002 and 2001 financial statements. Up to that point, we had expected to include Stonefield Josephson's reports on those years. However, we were unable to timely obtain concurrence from Stonefield Josephson that restatements were required and the extent of such restatements. As a result, we directed Ernst & Young LLP to re-audit the years ended December 31, 2002 and 2001 and we have restated our financial statements for these years and for the first two quarters of 2003 to correct inappropriate accounting entries.

The restatements primarily related to the timing of recognition of deferred revenue and the capitalization of bounty costs, which are the amounts paid to online marketers to acquire members. The restatements, which are in accordance with United States generally accepted accounting principles, pertained primarily to timing matters and had no impact on cash flow from operations or our ongoing operations. The impact on net loss for 2002 and 2001 was an increase of \$1.0 million and \$1.5 million, respectively.

OTHER DETAILS

Management Changes During the First Six Months of 2004

In order to prepare for growth and scalability, the following officers were hired in the first six months of 2004:

- In June 2004, Jessica Pezzullo became the Chief Marketing Officer.
- In April 2004, Ken Ross became the Chief Communications Officer.

In February 2004, Todd Tappin became our President and Chief Executive Officer. In March 2004, Joe Y. Shapira resigned as Chief Executive Officer but continues to serve as Executive Co-Chairman of our Board of Directors. In March 2004, Alon Carmel resigned as President but continues to serve as Executive Co-Chairman of our Board of Directors.

In March 2004, Adam Kravitz resigned as our General Counsel. In connection with his resignation and further to the terms of his employment agreement, MatchNet paid Mr. Kravitz as severance an aggregate of approximately \$2.4 million. Mr. Kravitz continued to serve as our Secretary and as a member of our Board until the end of the second quarter when he resigned.

Changes in the Board of Directors During the First Six Months of 2004

Florian Homm and Franklin Urteaga resigned from the Board of Directors in March 2004. Todd Tappin and David Siminoff replaced them as directors in the same month.

There were no other changes to the Board of Directors during the first six months of 2004.

Subsidiaries Added During the First Half of 2004

In January 2004, MatchNet formed a Canadian subsidiary, Enterprise Canada MatchNet, Inc., to own its Canadian domain names.

Proposed Public Offering

On August 4, 2004 MatchNet, Inc., filed an S-1 registration statement with the Securities & Exchange Commission for a "firm commitment" public offering of its common stock. It is currently anticipated that the common stock will be offered by the United States corporation and certain selling shareholders. It is expected that the common stock will be quoted on the NASDAQ National Market. The proceeds of the offering are expected to be primarily used for working capital purposes.

RISK FACTORS

You should carefully consider the risks described below together with all of the other information included in this semi-annual report before making a decision as to whether to invest in our ordinary shares. The risks and uncertainties described below are not the only ones facing us. Additional risks and uncertainties that we are unaware of, or that we currently deem immaterial, also may become important factors that adversely affect us. If any of the following risks actually occurs, our business, financial condition or results of operations could be materially adversely affected.

Risks Related to Our Business

Our limited operating history and relatively new business model in an emerging and rapidly evolving market makes it difficult to evaluate our future prospects.

MatchNet, plc. commenced operations in September 1998 and we have only a short operating history with our subscription-based business model. As a result, we have very little operating history for you to assess our future prospects. Also, we derive nearly all of our net revenues from online subscription fees, which is an early-stage business model that has undergone rapid and dramatic changes. You must consider our business and prospects in light of the risks and difficulties we will encounter as an early-stage company in a new and rapidly evolving market. We may not be able to assess or address these risks and difficulties, which could materially harm our business and operating results.

We have significant operating losses.

We have historically generated significant operating losses. As of June 30, 2004, we had an accumulated deficit of approximately \$39.1 million. We had a net loss of approximately \$7.1 million for the six months ended June 30, 2004 and approximately \$10.9 million for the year ended December 31, 2003. We anticipate an operating loss for the year ending December 31, 2004, for at least the first two quarters of 2005 and possibly for the year ending December 31, 2005. We expect that our operating expenses will continue to materially increase during the next several years as a result of the rebranding of our company, the promotion of our services, the hiring of additional key personnel, the expansion of our operations, including the launch of new Web sites, and entering into strategic alliances and joint ventures. If our revenues do not grow at a substantially faster rate than these expected increases in our expenses or if our operating expenses are higher than we anticipate, we may not be profitable and we may incur additional losses, which could be significant.

Our ability to generate positive cash flow and operating profits as a relatively new company in a new and evolving business will depend upon a number of factors that are difficult to predict, including factors such as:

- continued acceptance of online personals services;
- our ability to create and increase brand awareness and attract and retain a large number of members and subscribers, including our ability to convert members into paying subscribers;
- level of usage of the Internet and traffic to our Web sites;
- our ability to maintain current, and develop new, relationships with portals, search engines, ISPs and other Web properties and entities capable of attracting individuals who might subscribe to our fee generating services;
- our ability to implement our expansion plans or integrate newly acquired companies, including controlling the costs associated with such expansion or acquisitions;
- our ability to control costs related to general infrastructure including the amount and timing of operating and capital expenditures;
- our ability to introduce new Web sites, features and functionality on a timely basis;
- our ability to scale technological and other infrastructure across our various Web sites;
- our ability to protect our data from loss or electronic or magnetic corruption;
- providing for failover and disaster recovery programs;
- our ability to upgrade our technologies and protect our sites from technology failures, which could cause revenue loss and allow affiliates to terminate their contracts with us;
- our ability to attract, retain and motivate qualified personnel;
- our ability to expand and compete internationally;
- introduction of new products or services by our competitors; and
- our ability to anticipate and adapt to the changing Internet business and any changes in government regulation.

Our business depends on strong brands and if we are not able to maintain and enhance our brands, or if we are not successful in our rebranding efforts, our business and operating results would be harmed.

We believe that establishing and maintaining our brands is critical to our efforts to attract and expand our membership and subscriber base. We believe that the importance of brand recognition will continue to increase, given the growing number of Internet sites and the low barriers to entry for companies offering online personals services. We intend to change our name and consolidate our online dating properties, with the exception of JDate, under the new company umbrella brand name. To attract and retain members and subscribers, and to promote and maintain our brands in response to competitive pressures, we intend to substantially increase our financial commitment to creating and maintaining distinct brand loyalty among these groups. We intend to institute a marketing program designed to heighten our brand recognition, including our rebranding efforts, and attract additional members and subscribers. The impact of the change of our name and rebranding efforts cannot be fully predicted. The lack of an established brand image for the new company name and the possibility that our strategy to create a recognizable and well known brand may not succeed may materially and adversely affect our business. If we do not generate a corresponding increase in revenues as a result of our rebranding and continuing branding efforts or otherwise fail to successfully promote our new and existing brands, or if we incur excessive expenses in our rebranding efforts and in our attempt to promote and maintain our new and existing brands, we will continue to incur losses, which may increase, and the value of our shares could decline. If visitors, members and subscribers to our Web sites, and affiliate and distribution partners do not perceive our existing services to be of high quality, or if we introduce new services or enter into new business ventures that are not favorably received by such parties, the value of our brands could be diluted, thereby decreasing the attractiveness of our Web sites to such parties.

As part of our rebranding efforts, we intend to spend substantial advertising dollars in offline media such as television, radio and print. Our company has no significant experience in offline advertising and we cannot assure you that these efforts will be successful. In addition, should these offline methods become more costly than currently anticipated, our profitability will be adversely affected.

If our efforts to attract a large number of members, convert members into paying subscribers and retain our paying subscribers are not successful, our revenues and operating results would suffer.

Our future growth depends on our ability to attract a large number of members, convert members into paying subscribers and retain our paying subscribers. This in turn depends on our ability to deliver a high-quality online personals experience to these members and subscribers. Our competitors are developing highly targeted content as well as innovations in technology, online advertising and providing information. As a result, we must continue to invest significant resources in order to enhance our existing products and services and introduce new high-quality products and services that people will use. If we are unable to predict user preferences or industry changes, or if we are unable to modify our products and services on a timely basis, we may lose existing subscribers and may fail to attract new subscribers. Our operating results would also suffer if our innovations are not responsive to the needs of our subscribers or are not brought to market in an effective or timely manner.

Our subscriber acquisition costs vary depending upon prevailing market conditions and may increase significantly in the future.

Our subscriber acquisition costs are dependent in part upon our ability to purchase advertising at a reasonable cost. Our advertising costs vary over time, depending upon a number of factors, some of which are beyond our control. Historically, we have used online advertising as the primary means of marketing our services. In general, the costs of online advertising have recently increased substantially and these costs are expected to continue to increase as long as the demand for online advertising remains robust. Commencing in late 2004 or early 2005, we expect to expand to offline advertising such as television, radio and print, which may be more expensive and which will initially increase our subscriber acquisition costs. As we initiate these additional marketing efforts to build

offline brand recognition, we expect there will be a significant lag between the time we incur the offline advertising expense and the receipt of revenues resulting from this advertising spend. As a result, we expect that our subscriber acquisition costs will be higher in the initial stages of our offline advertising efforts. If we are not able to reduce our other operating costs, increase our subscriber base or increase revenue per subscriber to offset these anticipated increases, our profitability will be adversely affected.

We must keep pace with rapid technological change to remain competitive; our services are not well-suited to many alternate Web access devices.

We operate in a market characterized by rapidly changing technology, evolving industry standards, frequent new product and service announcements, enhancements, and changing customer demands. Accordingly, our success will depend on our ability to adapt to rapidly changing technologies and industry standards, and our ability to continually improve the speed, performance, features, ease of use and reliability of services in response to both evolving demands of the marketplace and competitive service and product offerings. There have been occasions when we have not been as responsive as many of our competitors in adapting our services to changing industry standards and the needs of our members and subscribers. Introducing new technology into our systems involves numerous technical challenges, substantial amounts of capital and personnel resources and often takes many months to complete. We intend to continue to devote substantial efforts and funds towards the development of additional technologies and services. For example, in 2003 and 2004 we have introduced a number of new Web sites and features, and we anticipate the introduction of additional Web sites and features in 2004 and 2005. We may not be successful in integrating new technology into our Web sites on a timely basis, which may degrade the responsiveness and speed of our Web sites. Such technology, once integrated, may not function as expected.

In addition, the number of people who access the Internet through devices other than desktop and laptop computers, including mobile telephones and other handheld computing devices, has increased dramatically in the past few years, and we expect this growth to continue. The lower resolution, functionality and memory currently associated with such mobile devices makes the use of our services through such mobile devices more difficult, and generally impairs the member experience relative to access via desktop and laptop computers. If we are unable to attract and retain a substantial number of such mobile device users to our online personals services or if we are unable to develop services that are more compatible with such mobile communications devices, our growth could be adversely affected.

The online personals business is highly competitive. Competition presents an ongoing threat to the success of our business.

We expect competition in the online personals business to continue to increase because there are no substantial barriers to entry. We believe that our ability to compete depends upon many factors both within and beyond our control, including the following:

- the size and diversity of our member and subscriber bases;
- the timing and market acceptance of products and services, including the developments and enhancements to those products and services, offered by us or our competitors;
- customer service and support efforts;
- selling and marketing efforts;
- ease of use, performance, price and reliability of solutions developed either by us or our competitors; and
- our brand strength relative to our competitors.

We compete with traditional dating and personals services, as well as newspapers, magazines and other traditional media companies that provide dating and personals services. We also compete with large Internet information hubs, or portals, such as Yahoo!, as well as online personals companies such as Match.com, a wholly-owned subsidiary of InterActiveCorp. Many of our current and potential competitors have longer operating histories, significantly greater financial, technical, marketing and other resources and larger customer bases than we do. These factors may allow our competitors to respond more quickly than we can to new or emerging technologies and changes in customer

requirements. These competitors may engage in more extensive research and development efforts, undertake more far-reaching marketing campaigns and adopt more aggressive pricing policies which may allow them to build larger member and subscriber bases than we have. Our competitors may develop products or services that are equal or superior to our products and services or that achieve greater market acceptance than our products and services. This could attract subscribers away from our Web sites and reduce our market share.

In addition, current and potential competitors are making, and are expected to continue to make, strategic acquisitions or establish cooperative, and, in some cases, exclusive relationships with significant companies or competitors to expand their businesses or to offer more comprehensive products and services. To the extent these competitors or potential competitors establish exclusive relationships with major portals, search engines and ISPs, our ability to reach potential members through online advertising may be restricted. Any of these competitors could cause us difficulty in attracting and retaining members and converting members into subscribers and could jeopardize our existing affiliate program and relationships with portals, search engines, ISPs and other Web properties.

Expansion into international markets is important to our long-term success, and our limited experience in the operation of our business outside the United States increases the risk that our international expansion efforts and operations will not be successful.

One of our strategies is to expand our presence in international markets. Although we currently have offices in Germany, Israel and the U.K. and Web sites that serve the Australian, Canadian, German, Israeli and U.K. markets, we have only limited experience with operations outside the United States. Our primary current international operations are in Israel, which has political risks to our business associated with the continuing hostilities there. Expansion into international markets requires management and resources. In addition, we face the following additional risks associated with our expansion outside the United States:

- challenges caused by distance, language and cultural differences;
- local competitors with substantially greater brand recognition, more users and more traffic than we have;
- our need to create and increase our brand recognition and improve our marketing efforts internationally and build strong relationships with local affiliates;
- longer payment cycles in some countries;
- credit risk and higher levels of payment fraud;
- legal and regulatory restrictions;
- political, social and economic instability;
- foreign currency risk;
- potentially adverse tax consequences; and
- higher costs associated with doing business internationally.

These risks could harm our international expansion efforts, which would in turn harm our business and operating results.

If we are unable to attract, retain or motivate key personnel or hire qualified personnel, our business will be harmed.

Our performance and success is largely dependent on the talents and efforts of highly skilled individuals. Many of our executive officers and other key management talent were recently recruited to fill newly created positions in response to our expanding operations. For example, Todd Tappin, our President and Chief Executive Officer, joined us in February 2004. In addition, certain of our recently hired executives have limited or no experience in the online personals industry. We do not maintain any key-person life insurance policies and certain of our key employees, including Mr. Tappin, do not have employment contracts. We also do not have non-competition agreements with most employees, although these agreements are of limited enforceability in California. The loss of any of our management or key personnel could seriously harm our business.

In addition, we will need to identify, hire, and retain a number of key management personnel, including a Chief Financial Officer, Controller and General Counsel, as well as other highly skilled personnel for other areas of our organization. Competition in our industry for such personnel is intense, and we are aware that certain of our competitors have directly targeted our employees. Our continued ability to compete effectively depends on our ability to attract new employees and to retain and motivate our existing employees.

As we become a more mature company, we may find our recruiting efforts more challenging. The incentives to attract, retain and motivate employees provided by our option grants or by future arrangements, such as through cash bonuses, may not be as effective as in the past. If we do not succeed in attracting excellent personnel or retaining or motivating existing personnel, we may be unable to grow effectively.

Our executive management has worked as a team for only a limited period of time, which may harm their ability to manage effectively.

Todd Tappin, our President and Chief Executive Officer, joined our company in February 2004. Although Joe Y. Shapira and Alon Carmel resigned as our Chief Executive Officer and President, respectively, upon the hiring of Mr. Tappin, both of them have remained in an executive and day-to-day operating capacity and involved in corporate decision-making as Executive Co-Chairmen of the Board. Each of Messrs. Tappin, Shapira and Carmel have different and distinct management skills, backgrounds and styles and from time to time may work independently on new business or product development, which may be without the complete knowledge or understanding of the others' activities. Because Messrs. Tappin, Shapira and Carmel have only worked together as a team for a limited period of time, there are inherent risks in the management of our company with respect to decision-making, business direction, product development and strategic relationships. In addition, certain other key management roles, such as Chief Financial Officer, Controller and General Counsel, have not yet been filled, and others have only been filled recently. In the event our Chief Executive Officer, and Executive Co-Chairmen of the Board and other members of our management team are unable to work well together or agree on certain operating principles, business direction or business transactions or in providing cohesive leadership, our business would be harmed and may also result in one or more of these individuals discontinuing their service to our company.

We cannot assure you that we will effectively manage our growth.

We have experienced rapid growth and demand for our services since inception. The growth and expansion of our business and service offerings places a continuous significant strain on our management, operational and financial resources. We are required to manage multiple relations with various strategic partners, technology licensors, members and other third parties. In the event of further growth of our operations or in the number of our third party relationships, our computer systems, procedures or internal controls may not be adequate to support our operations and our management may not be able to manage any such growth effectively. To effectively manage our growth, we must continue to implement and improve our operational, financial and management information systems and to expand, train and manage our employee base.

We expect our growth rates to decline and our negative operating margins could deteriorate.

We believe our revenue growth rate will decline as our net revenues increase to higher levels. It is possible that our negative operating margin will deteriorate if revenue growth does not exceed planned increases in expenditures for all aspects of our business in an increasingly competitive environment, including sales and marketing, general and administrative and technical operations expenses.

Our business depends on our server and network hardware and software and our ability to obtain network capacity; our current failover may be inadequate to prevent an interruption of use of our services.

The performance of our server and networking hardware and software infrastructure is critical to our business and reputation and our ability to attract Web users, advertisers, members and e-commerce

partners to our Web sites and to convert members to subscribers. An unexpected and/or substantial increase in the use of our Web sites could strain the capacity of our systems, which could lead to a slower response time or system failures. Although we have not had any significant delays, any slowdowns or system failures could adversely affect the speed and responsiveness of our Web sites and would diminish the experience for our members and visitors. We face risks related to our ability to scale up to our expected customer levels while maintaining superior performance. If the usage of our Web sites substantially increases, we may need to purchase additional servers and networking equipment to maintain adequate data transmission speeds, the availability of which may be limited or the cost of which may be significant. Any system failure that causes an interruption in service or a decrease in the responsiveness of our Web sites could reduce traffic on our Web sites and, if sustained or repeated, could impair our reputation and the attractiveness of our brands as well as reduce revenue and negatively impact our operating results.

Furthermore, we rely on many different software applications, some of which have been developed internally. If these hardware and software systems fail, it would adversely affect our ability to provide our services. If we receive a significant unexpected increase in usage and are not able to rapidly expand our transaction-processing systems and network infrastructure without any systems interruptions, it could seriously harm our business and reputation. We have experienced occasional systems interruptions in the past as a result of unexpected increases in usage, and we cannot assure you we will not incur similar or more serious interruptions in the future.

In addition, we do not currently have adequate disaster recovery systems in place, which means in the event of any catastrophic failure involving our Web sites, we may be unable to serve our Web traffic for up to several days. Our servers operate from only a single site in Southern California and the absence of a backup site could exacerbate this disruption. Any system failure, including network, software or hardware failure, that causes such an interruption in the delivery of our Web sites and services or a decrease in responsiveness of our services would result in reduced visitor traffic, reduced revenue and would adversely affect our reputation and brands.

The failure to establish and maintain affiliate agreements and relationships could limit the growth of our business.

We have entered into, and expect to continue to enter into, arrangements with affiliates to increase our member base, bring traffic to our Web sites and enhance our brands. If any of the current agreements are terminated, we may not be able to replace the terminated agreement with an equally beneficial arrangement. We cannot assure you that we will be able to renew any of our current agreements when they expire or, if we are able to do so, that such renewals will be available on acceptable terms. We also do not know whether we will be successful in entering into additional agreements or that any relationships, if entered into, will be on terms favorable to us.

We rely on a number of third party providers, and their failure to perform or termination of our relationships with them could harm us.

We rely on third parties to provide important services and technologies to us, including third parties that manage and monitor our offsite data center located in Southern California, ISPs and credit card processors. In addition, we license technologies from third parties to facilitate our ability to provide our services. Any failure on our part to comply with the terms of these licenses could result in the loss of our rights to continue using the licensed technology, and we could experience difficulties obtaining licenses for alternative technologies. Furthermore, any failure of these third parties to provide these and other services, or errors, failures, interruptions or delays associated with licensed technologies, could significantly harm our business. Any financial or other difficulties our providers may face may have negative effects on our business, the nature and extent of which we cannot predict. We exercise little or no control over these third party providers, which increases our vulnerability to problems with the services and technologies they provide and license to us. In addition, if any fees charged by third party providers were to substantially increase, such as if ISPs began charging us for email sent by our subscribers to other subscribers; we may not be profitable and may incur additional losses.

If we fail to develop or maintain an effective system of internal controls, we may not be able to accurately report our financial results or prevent fraud. As a result, current and potential shareholders could lose confidence in our financial reporting; this would harm our business and the trading price of our shares.

Effective internal controls are necessary for us to provide reliable financial reports and effectively prevent fraud and to operate successfully as a public company. If we cannot provide reliable financial reports or prevent fraud, our reputation and operating results would be harmed. We have in the past discovered, and may in the future discover, areas of our internal controls that need improvement. For example, during our 2003 audit, our external auditors brought to our attention a need to restate 2001 and 2002 annual results as well as 2003 interim results.

Our external auditors also noted in a letter to management certain reportable conditions involving internal controls and operations. According to the letter, we currently do not have a sufficient amount or type of staff in the financial, accounting and external reporting areas, including a Controller and a Chief Financial Officer, nor do we have an adequate automated accounting system. We are currently seeking to hire appropriate staff as soon as practicable, and we intend to replace our accounting system within approximately 12 months, but each of these matters may take longer. Other reportable conditions involve the inadequacy of our procedures regarding: reconciliation of our accounts; proof of internal review and approval of accounting items; documentation of key accounting assumptions, estimates and/or conclusions; and documentation of accounting policies and procedures. We are currently taking steps to address these conditions, but we may be hampered in this regard by our current level of staffing and our current accounting system. We also have not yet developed or implemented a disaster recovery plan or business continuity plan for our accounting and related information technology systems. Any disaster could therefore materially impair our ability to maintain timely accounting and reporting. In addition, we need to hire a General Counsel.

We cannot be certain that our efforts to improve our internal controls will be successful or that we will be able to maintain adequate controls over our financial processes and reporting in the future. Any failure to develop or maintain effective controls, or difficulties encountered in their implementation or delay in the implementation of our new accounting system or other effective improvement of our internal controls could harm our operating results or cause us to fail to meet our reporting obligations. Ineffective internal controls could also cause investors to lose confidence in our reported financial information, which would likely have a negative effect on the trading price of our shares.

We face risks related to our recent accounting restatements.

Our global depository shares trade on the Frankfurt Stock Exchange in Germany. Pursuant to the laws governing this exchange, we publicly reported our quarterly and annual operating results. On April 28, 2004, we publicly announced that we had discovered accounting inaccuracies in previously reported financial statements. As a result, following consultation with our new auditors, we have restated our financial statements for the first two quarters of 2003 and for each of the years ended December 31, 2002 and 2001 to correct inappropriate accounting entries.

The restatements primarily related to the timing of recognition of deferred revenue and the capitalization of bounty costs, which are the amounts paid to online marketers to acquire members. The restatements are in accordance with United States generally accepted accounting principles and pertained primarily to timing matters and had no impact on cash flow from operations or our ongoing operations. The impact on net loss for 2002 and 2001 was an increase of \$1.0 million and \$1.5 million, respectively.

The restatement of these financial statements may lead to litigation claims and/or regulatory proceedings against us. The defense of any such claims or proceedings may cause the diversion of management's attention and resources, and we may be required to pay damages if any such claims or proceedings are not resolved in our favor. Any litigation or regulatory proceeding, even if resolved in our favor, could cause us to incur significant legal and other expenses. Moreover, we may be the subject of negative publicity focusing on the financial statement inaccuracies and resulting restatement. The occurrence of any of the foregoing could harm our business reputation and cause the price of our shares to decline.

We may not be successful in protecting our Internet domain names or proprietary rights upon which our business relies or avoiding claims that we infringe upon the proprietary rights of others.

We regard substantial elements of our Web sites and the underlying technology as proprietary, and attempt to protect them by relying on trademark, service mark, copyright, patent and trade secret laws, and restrictions on disclosure and transferring title and other methods. We also generally enter into confidentiality agreements with our employees and consultants, and generally seek to control access to and distribution of our technology, documentation and other proprietary information. Despite these precautions, it may be possible for a third party to copy or otherwise obtain and use our proprietary information without authorization or to develop similar or superior technology independently. Effective trademark, service mark, copyright, patent and trade secret protection may not be available in every country in which our services are distributed or made available through the Internet, and policing unauthorized use of our proprietary information is difficult. Any such misappropriation or development of similar or superior technology by third parties could adversely impact our future financial results.

We believe that our Web sites, services, trademarks, patent, and other proprietary technology do not infringe on the rights of third parties. However, there can be no assurance that our business activities will not infringe upon the proprietary rights of others, or that other parties will not assert infringement claims against us. From time to time, we have been, and expect to continue to be, subject to claims in the ordinary course of business including claims of alleged infringement of the trademarks, service marks and other intellectual property rights of third parties by us. Although such claims have not resulted in any significant litigation or had a material adverse effect on our business to date, any such claims and resultant litigation might subject us to temporary injunctive restrictions on the use of our products or services and could result in significant liability for damages for intellectual property infringement, require us to enter into royalty agreements, or restrict us from using infringing software or technologies in the future. Even if not meritorious, such litigation could be time-consuming and expensive and could result in the diversion of management's time and attention.

We currently hold various Web domain names relating to our brands and in the future may acquire new Web domain names. The regulation of domain names in the United States and in foreign countries is subject to change. Governing bodies may establish additional top-level domains, appoint additional domain name registrars or modify the requirements for holding domain names. As a result, we may be unable to acquire or maintain relevant domain names in all countries in which we conduct business. Furthermore, the relationship between regulations governing domain names and laws protecting trademarks and similar proprietary rights is unclear. We may be unable to prevent third parties from acquiring domain names that are similar to, infringe upon or otherwise decrease the value of our existing trademarks and other proprietary rights or those we may seek to acquire. Any such inability could harm our business.

We may face potential liability, loss of users and damage to our reputation for violation of our privacy policy.

Our privacy policy prohibits the sale or disclosure to any third party of any member's personal identifying information, except to the extent expressly set forth in the policy. Growing public concern about privacy and the collection, distribution and use of information about individuals may subject us to increased regulatory scrutiny and/or litigation. In the past, the Federal Trade Commission has investigated companies that have used personally identifiable information without permission or in violation of a stated privacy policy. If we are accused of violating the stated terms of our privacy policy, we may be forced to expend significant amounts and financial and managerial resources to defend against these accusations and we may face potential liability. Our membership database holds confidential information concerning our members, and we could be sued if any of that information is misappropriated or if a court determines that we have failed to protect that information.

We may be liable as a result of information retrieved from or transmitted over the Internet.

We may be sued for defamation, civil rights infringement, negligence, copyright or trademark infringement, invasion of privacy, personal injury, product liability or other legal claims relating to information that is published or made available on our Web sites and the other sites linked to it. These types of claims have been brought, sometimes successfully, against online services in the past. We also offer email services, which may subject us to potential risks, such as liabilities or claims resulting from unsolicited email or spamming, lost or misdirected messages, security breaches, illegal or fraudulent use of email or interruptions or delays in email service. Our insurance does not specifically provide for coverage of these types of claims and therefore may not adequately protect us against these types of claims. In addition, we could incur significant costs in investigating and defending such claims, even if we ultimately are not liable. If any of these events occur, our revenues could be materially adversely affected and the value of our shares may decline.

Our quarterly results may fluctuate because of many factors. Investors should not rely on quarterly operating results as indicative of future results because they are subject to fluctuations.

Fluctuations in operating results or the failure of operating results to meet the expectations of public market analysts and investors may negatively impact the value of our shares. Quarterly operating results may fluctuate in the future due to a variety of factors that could affect revenues or expenses in any particular quarter. Fluctuations in quarterly operating results could cause the value of our shares to decline. Investors should not rely on quarter-to-quarter comparisons of results of operations as an indication of future performance. Factors that may affect our quarterly results include:

- the demand for, and acceptance of, our online personals services and enhancements to these services;
- the timing and amount of our subscription revenues;
- the introduction, development, timing, competitive pricing and market acceptance of our Web sites;
- and services and those of our competitors;
- the magnitude and timing of marketing initiatives and capital expenditures relating to our rebranding;
- efforts and expansion of our operations;
- the cost and timing of online and offline advertising and other marketing efforts;
- the maintenance and development of relationships with portals, search engines, ISPs and other Web;
- properties and other entities capable of attracting potential subscribers to our Web sites;
- Technical difficulties, system failures, system security breaches, or downtime of the Internet in general or of our products and services specifically;
- costs related to any acquisitions or dispositions of technologies or businesses; and
- general economic conditions, as well as those specific to the Internet and related industries.

As a result of the factors listed above and because the online personals business is still immature, making it difficult to predict consumer demand, it is possible that in future periods results of operations may be below the expectations of public market analysts and investors. This could cause the market price of our shares to decline.

Acquisitions could result in operating difficulties, dilution and other harmful consequences.

We plan during the next few years to further extend and develop our presence both within the United States and internationally, partially through acquisitions of entities offering online personals services and related businesses. We have a limited amount of experience acquiring companies and the companies we have acquired have been small. We have evaluated, and expect to continue to evaluate, a wide array of potential strategic transactions. From time to time, we may engage in discussions regarding potential acquisitions. Any of these transactions could be material to our financial condition and results of operations. In addition, the process of integrating an acquired company, business or technology may create unforeseen operating difficulties and expenditures and

is risky. For example, we are currently engaged in litigation with respect to our acquisition of SocialNet, Inc. in 2001. In addition, our acquisition of a 20% interest in a Swedish online personals company is currently pending. The areas where we may face risks include:

- the need to implement or remediate controls, procedures and policies appropriate for a larger company at companies that prior to the acquisition lacked these controls, procedures and policies;
- diversion of management time and focus from operating our business to acquisition integration challenges;
- cultural challenges associated with integrating employees from the acquired company into our organization;
- dependence on co-investors or controlling shareholders for performance of any joint venture or similar arrangement that we make that is not subject to our control;
- retaining employees from the businesses we acquire; and
- the need to integrate each company's accounting, management information, human resource and other administrative systems to permit effective management.

The anticipated benefit of many of our acquisitions may not materialize. Future acquisitions or dispositions could result in potentially dilutive issuances of our equity securities, the incurrence of debt, contingent liabilities or amortization expenses, or write-offs of goodwill, any of which could harm our financial condition. Future acquisitions may require us to obtain additional equity or debt financing, which may not be available on favorable terms or at all.

We may need additional capital to finance our growth or to compete.

We currently anticipate that existing cash, cash equivalents, and marketable securities and cash flow from operations will be sufficient to meet our anticipated needs for working capital, operating expenses and capital expenditures for at least the next 12 months. We may need to raise additional capital in the future to fund more aggressive brand promotions and rapid expansion, develop newer or enhanced services, respond to competitive pressures or acquire complementary businesses, technologies or services. Such additional financing may not be available on terms acceptable to us or at all. If additional financing is not available or not available on acceptable terms, we may not be able to fund our expansion, promote our brands, take advantage of acquisition opportunities, develop or enhance services or respond to competitive pressures. Additionally, any issuance of additional capital shares could dilute your investment and announcements of additional share issuances often cause market prices to decline.

Our business could be significantly impacted by the occurrence of natural disasters and other catastrophic events.

Our operations depend upon our ability to maintain and protect our data center, which is located in Southern California and is managed by a third party. Our business is therefore susceptible to earthquakes and other catastrophic events, including acts of terrorism. We currently lack adequate redundant hardware and software systems supporting our services at an alternate site. We may not be able to prevent outages and downtime caused by natural disasters and other events out of our control, which could adversely affect our reputation, brands and business.

The initial option grants are fully vested to many of our senior management and key employees. Therefore, these employees may not have sufficient financial incentive to stay with us.

With the exceptions of Todd Tappin, our President and Chief Executive Officer, and other executive officers and key employees who have recently joined our company, many of our senior management personnel and other key employees have become, or will soon become, substantially vested in their initial share option grants. While we often grant additional share options to management personnel and other key employees after their hire dates to provide additional incentives to remain employed by us, their initial grants are usually much larger than follow-on grants. Employees may be more likely to leave us after their initial option grant fully vests, especially if the shares underlying the options have significantly appreciated in value relative to the option exercise price.

If we account for employee share options using the fair value method, it could significantly reduce our net income or increase our losses.

There has been ongoing public debate about whether share options granted to employees should be treated as a compensation expense and, if so, how to properly value such charges. On March 31, 2004, the Financial Accounting Standard Board (FASB) issued an Exposure Draft, Stock-Based Payment: an amendment of FASB statements No. 123 and 95, which would require a company to recognize, as an expense, the fair value of share options and other stock-based compensation to employees beginning in 2005 and subsequent reporting periods. If we elect or are required to record an expense for our stock-based compensation plans using the fair value method as described in the Exposure Draft, we could have significant and ongoing accounting charges.

We may face risks associated with currency fluctuations.

Our foreign operations may subject us to currency fluctuations and such fluctuations may adversely affect our financial position and results. However, sales and expenses to date have occurred primarily in the United States. For this reason, we have not engaged in foreign exchange hedging. In connection with our planned international expansion, currency risk positions could change correspondingly and the use of foreign exchange hedging instruments could become necessary. Effects of exchange rate fluctuations on our financial condition, operations, and profitability may depend on how successfully we manage our foreign currency risks. There can be no assurance that steps taken by management to address foreign currency fluctuations will eliminate all adverse effects and accordingly, we may suffer losses due to adverse foreign currency fluctuation.

It has been and may continue to be expensive to obtain and maintain insurance.

We contract for insurance to cover potential risks and liabilities. In the current environment, insurance companies are increasingly specific about what they will and will not insure. It is possible that we may not be able to get enough insurance to meet our needs, we may have to pay very high prices for the coverage we do get, or we may not be able to acquire any insurance for certain types of business risk or may have gaps in coverage for certain risks. This could leave us exposed to potential claims. If we were found liable for a significant claim in the future, our operating results could be negatively impacted.

Risks Related to Our Industry

The percentage of canceling subscribers in comparison to other subscription businesses requires that we must continually seek new subscribers to maintain or increase our current level of revenue.

Internet users in general, and users of online personals services specifically, freely navigate and switch among a large number of Web sites. Subscriber churn represents a ratio, expressed as a percentage, of (i) subscriber cancellations in a period divided by the average of the subscribers at the beginning and end of the period and (ii) the number of months in the period. For the six months ended June 30, 2004 and 2003, subscriber churn was 32% and 29%, respectively. We cannot assure you that we will be able to maintain our subscriber churn, and it may increase in the future. This makes it difficult for us to have a stable member base and requires that we constantly attract new subscribers at a faster rate than subscription terminations to maintain or increase our current level of revenue. If we are unable to attract new subscribers on a cost-effective basis, our business will not grow and our profitability will be adversely affected.

We face certain risks related to the physical and emotional safety of our members.

Given the nature of online personals services, we cannot control the actions of our members in their communication or physical actions and there is a possibility that one or more of our members could be physically or emotionally harmed following interaction with another member on one of our Web sites. We warn our members that we do not and cannot screen other members, and given our lack of physical presence, we do not take any action to ensure personal safety on a meeting arranged following contact initiated via our Web sites. If an unfortunate incident of this nature occurred in a

meeting of two people following contact initiated on one of our Web sites or a Web site of one of our competitors, any resulting negative publicity could materially and adversely affect the online personals industry in general. Any such incident involving one of our Web sites could damage our reputation and our brands. This, in turn, could adversely affect our revenues and could cause the value of our shares to decline. In addition, the affected members could initiate legal action against us, which could cause us to incur significant expense, whether or not successful, and further damage our reputation.

We are exposed to risks associated with credit card fraud and credit payment.

We depend on continuing availability of credit card usage to process subscriptions, and this availability in turn depends on acceptable levels of charge-backs and fraud performance. We have suffered losses and may continue to suffer losses as a result of subscription orders placed with fraudulent credit card data, even though the associated financial institution approved payment. Under current credit card practices, a merchant is liable for fraudulent credit card transactions when, as is the case with the transactions we process, that merchant does not obtain a cardholder's signature. A failure to adequately control fraudulent credit card transactions would result in significantly higher credit card-related costs.

Our network is vulnerable to security breaches and inappropriate use by Internet users, which could disrupt or deter future use of our services.

Concerns over the security of transactions conducted on the Internet and the privacy of users may inhibit the growth of the Internet and other online services generally, and online commerce in particular. Our failure to successfully prevent security breaches could significantly harm our business, reputation and results of operations and could expose us to lawsuits by state and federal consumer protection agencies, by governmental authorities in the foreign jurisdictions in which we operate, and by consumers. Anyone who is able to circumvent our security measures could misappropriate proprietary information, including customer credit card and personal data, cause interruptions in our operations or damage our brand and reputation. Such breach of our security measures could involve the disclosure of personally identifiable information and could expose us to a material risk of litigation, liability or a governmental enforcement proceeding. We cannot assure you that our financial systems and other technology resources are completely secure from security breaches or sabotage, and we have occasionally experienced security breaches and attempts at "hacking." We may be required to incur significant additional costs to protect against security breaches or to alleviate problems caused by breaches. Any well-publicized compromise of our security or the security of any other Internet provider could deter people from using our services or the Internet to conduct transactions that involve transmitting confidential information or downloading sensitive materials, which would adversely affect our business.

Computer viruses may cause our systems to incur delays or other service interruptions and could damage our reputation and affect our ability to provide our services and adversely affect our revenues. The inadvertent transmission of computer viruses could also expose us to a material risk of loss or litigation and possible liability. Moreover, if a computer virus affecting our system is highly publicized, our reputation could be significantly damaged resulting in the loss of current and future members and subscribers.

Our business depends in part on the growth and maintenance of the Internet infrastructure.

Our success will depend in part on the continued growth and maintenance of the Internet infrastructure. This includes maintenance of a reliable network backbone with the necessary speed, data capacity and security for providing reliable Internet services. Internet infrastructure may be unable to support the demands placed on it if the number of Internet users continues to increase, or if existing or future Internet users access the Internet more often or increase their bandwidth requirements. In addition, viruses, worms and similar programs may harm the performance of the Internet. We also have no control over the third party telecommunications, cable or other providers of access services to the Internet that our members rely upon. There have been instances where regional and national telecommunications outages have caused us to experience service interruptions during which our members could not access our subscription-based services. Any

additional interruptions, delays or capacity problems experienced with any points of access between the Internet and our members could adversely affect our ability to provide services reliably to our members. The temporary or permanent loss of all or a portion of our services on the Internet, the Internet infrastructure generally, or our members' ability to access the Internet could disrupt our business activities, harm our business reputation, and result in a loss of revenue. Additionally, the Internet, electronic communications and telecommunications industries are subject to federal, state and foreign governmental regulation. New laws and regulations governing such matters could be enacted or amendments may be made to existing regulations at any time that could adversely impact our services. Any such new laws, regulations or amendments to existing regulations could disrupt or adversely affect the profitability of our business.

We face risks associated with our dependence on computer and telecommunications infrastructure.

Our services are dependent upon the use of the Internet and telephone and broadband communications to provide high-capacity data transmission without system downtime. For example, there have been instances where regional and national telecommunications outages have caused us to experience systems interruptions. Any additional interruptions, delays or capacity problems experienced with the telephone connection could adversely affect our ability to provide services to our customers. The temporary or permanent loss of all or a portion of the telecommunications system, or significant delays, could cause disruption of our business activities and result in a loss of revenue. Additionally, the telecommunications industry is subject to regulatory control. Amendments to current regulations could disrupt or adversely affect the profitability of our business.

In addition, if any of our current agreements with telecommunications providers are terminated, we may not be able to replace the terminated agreement with an equally beneficial arrangement. There can be no assurance that we will be able to renew any of our current agreements when they expire or, if we are able to do so, that such renewals will be available on acceptable terms. We also do not know whether we will be successful in entering into additional agreements or that any relationships, if entered into, will be on terms favorable to us.

We may become subject to burdensome government regulations and legal uncertainties affecting the Internet that could adversely affect our business.

Legal uncertainties surrounding domestic and foreign government regulations could increase our costs of doing business, require us to revise our services, prevent us from delivering our services over the Internet or slow the growth of the Internet, any of which could increase our expenses, reduce our revenues or cause our revenues to grow at a slower rate than expected and materially adversely affect our business, financial condition and results of operations. Laws and regulations related to Internet communications, security, privacy, intellectual property rights, commerce, taxation, entertainment, recruiting and advertising are becoming more prevalent, and new laws and regulations are under consideration by the United States Congress, state legislatures and foreign governments. Any legislation enacted or restrictions arising from current or future government investigations or policy could dampen the growth in use of the Internet generally and decrease the acceptance of the Internet as a communications, commercial, entertainment, recruiting and advertising medium. In addition to new laws and regulations being adopted, existing laws may be applied to the Internet. Many areas of law affecting the Internet remain unsettled, even in areas where there has been some legislative action. It may take years to determine whether and how existing laws such as those governing consumer protection, intellectual property, libel and taxation apply to the Internet. In the normal course of our business, we handle personally identifiable information pertaining to our members and Web site visitors residing in the United States as well as foreign countries. In recent years, many of these countries have adopted privacy, security, and data protection laws and regulations intended to prevent improper uses and disclosures of personally identifiable information. In addition, some jurisdictions impose database registration requirements for which significant monetary and other penalties may be imposed for noncompliance. These laws may impose costly administrative requirements, limit our handling of information, and subject us to increased government oversight and financial liabilities. Privacy laws and regulations in the United States and foreign countries are subject to change and may be inconsistent, and additional requirements may be imposed at any time. These laws and regulations, the costs of complying with them, administrative fines for noncompliance and the possible need to adopt different compliance measures in different jurisdictions could increase our expenses and would cause the value of our shares to decline.

Our principal shareholders can exercise significant influence over MatchNet.

Joe Y. Shapira, Alon Carmel, and Tiger Technology Management, L.L.C. and their respective affiliates will beneficially own in the aggregate, approximately 60% of the outstanding shares of our shares. As a result, these shareholders possess significant influence over MatchNet, giving them the ability, among other things, to elect a majority of our Board of Directors and approve significant corporate transactions. Such share ownership and control may also have the effect of delaying or preventing a change in control of our company, impeding a merger, consolidation, takeover or other business combination involving our company or discourage a potential acquirer from making a tender offer or otherwise attempting to obtain control of our company which could adversely affect the market price of our shares.

DIVIDEND POLICY

We have never declared or paid any cash dividends on our shares. We currently anticipate that we will retain all of our future earnings for use in the expansion and operation of our business and do not anticipate paying any cash dividends in the foreseeable future. We also may incur indebtedness in the future that may prohibit or effectively restrict the payment of dividends on our shares. Any future determination related to our dividend policy will be made at the discretion of the board.

CERTAIN RELATIONSHIPS AND RELATED PARTY TRANSACTIONS

Since January 1, 2003, we have not been a party to, and we have no plans to be a party to, any transaction or series of similar transactions in which the amount involved exceeded or will exceed \$60,000 and in which any current director, executive officer, holder or more than 5% of our shares, or entities affiliated with them, had or will have a material interest, other than as described in the transactions described below.

Advances to Executives

Pursuant to then existing compensation arrangements, we made advances to executive employees of approximately \$1.4 million representing payments under guaranteed compensation arrangements as of December 31, 2002. During 2003, the Board of Directors declared the guarantees to have been earned during the year and the receivable was charged against operating results. The executive officers who received advances were Joe Y. Shapira, who was our Chief Executive Officer as of December 31, 2003 and is currently our Executive Co-Chairman of the Board, and Alon Carmel, who was our President as of December 31, 2003 and is currently our Executive Co-Chairman of the Board, who were advanced approximately \$700,000 each.

Remote Concepts LLC

In 2003, MatchNet entered into a verbal marketing arrangement with Remote Concepts LLC, an entity owned 32.5% by each of Joe Y. Shapira and Alon Carmel. Remote Concepts LLC has developed a table top wireless paging system for use by patrons at restaurants. Further to the verbal arrangement, we expensed approximately \$120,000 paid to Remote Concepts LLC for ad placement on these systems.

Other Relationships

Several relatives of each of Joe Y. Shapira and Alon Carmel hold non-executive positions with our company and MatchNet Israel.

LEGAL PROCEEDINGS

On July 13, 2001, Liveworld, Inc. filed a complaint in the Santa Clara County Superior Court in California against our company and SocialNet, Inc. In February 2001, we purchased the outstanding shares of SocialNet pursuant to a share exchange agreement. The plaintiff contends that we assumed the obligations of SocialNet pursuant to a letter agreement to purchase \$1.5 million of services from the plaintiff and that we failed to purchase the services and induced SocialNet to breach the letter agreement with the plaintiff. The complaint, as amended, alleges breach of contract, breach of implied covenant of good faith and fair dealing, quantum meruit, fraud, intentional interference with contract and fraudulent transfers. The plaintiff is seeking compensatory damages in the approximate amount of \$1.1 million plus interest and punitive damages. In July 2002, we filed a cross-complaint for declaratory relief and rescission and in November 2002 we filed a demurrer on the interference with contract claim, which was overruled. In September 2003, we moved for summary judgment, which was denied. The court has scheduled a settlement conference for October 20, 2004 and a trial date of October 25, 2004. We believe the plaintiff's complaints as to our company are without merit and will defend against them vigorously in this matter. No assurance can be given, however, that this matter will be resolved in our favor.

On August 10, 2001, Comdisco, Inc. filed a complaint in the Santa Clara County Superior Court in California against our company, SocialNet and certain officers and directors of our company and SocialNet. The plaintiff's complaint generally contends that we assumed the obligations of SocialNet as a result of our purchase of SocialNet, which had defaulted on its financing arrangements with the plaintiff. The plaintiff's complaint, as amended, alleges breach of written contract, anticipatory repudiation, intentional interference with contract, recovery of equipment with damages, fraudulent transfer, constructive trust, breach of fiduciary duty, aiding and abetting breach of fiduciary duty, conspiracy to fraudulently transfer assets and conspiracy to breach fiduciary duty. The plaintiff is seeking compensatory damages plus interest, attorney's fees in the amount of approximately \$4 million, punitive damages, avoidance of allegedly fraudulent transfers, possession of collateral, and other non-monetary damages. In December 2003, the court denied the plaintiff's application for a writ of attachment. All parties have filed motions for summary judgment. The court has scheduled a settlement conference for September 15, 2004 and a jury trial for September 20, 2004. We believe the plaintiff's complaints as to our company are without merit and will defend against them vigorously in this matter. No assurance can be given, however, that this matter will be resolved in our favor.

Three separate yet similar class action complaints have been filed against our company. On June 21, 2002, Tatyana Fertelmeyster filed an Illinois class action complaint against our company in the Circuit Court of Cook County, Illinois, based on an alleged violation of the Illinois Dating Referral Services Act. In *Jason Adelman v. MatchNet, plc., Los Angeles Superior Court Case No. BC 306167*, the plaintiff filed a nationwide class action complaint against our company based on an alleged violation of California Civil Code section 1694 et seq., which regulates businesses that provide dating services. On September 12, 2002, Lili Grossman filed a New York class action complaint against our company in the Supreme Court in the State of New York based on alleged violations of the New York Dating Services Act and the Consumer Fraud Act. In each of these cases, the complaint included allegations that as an alleged dating service, our company is required to provide language in our contracts that allows members to rescind their contracts within three days, that allows reimbursement of a portion of the contract price if the member dies during the term of the contract and/or that allows members to cancel their contracts in the event of disability or relocation. Causes of action include breach of applicable state and/or federal laws, fraudulent and deceptive business practices, breach of contract and unjust enrichment. The plaintiffs are seeking remedies including declaratory relief, restitution, actual damages although not quantified, treble damages and/or punitive damages, and attorney's fees and costs. *Huebner v. InterActiveCorp., L.A.S.C. Case No. BC 305875* involves a similar action brought against InterActiveCorp's Match.com that has been ruled related to *Adelman*, but the two cases have not been consolidated. We have filed a motion for summary judgment and the court has certified an Illinois class in the case brought by Ms. Fertelmeyster. The court has ordered Ms. Fertelmeyster to complete all depositions and discovery in connection with the motion for summary judgment on or before August 31, 2004. In December 2002, the Supreme Court of New York dismissed the case brought by Ms. Grossman, although the plaintiff is appealing the decision. A status conference with respect to the Adelman case was held on May 11, 2004, at which

time the Court ordered the parties to mediation. A post- mediation status conference was held on Friday, July 16, 2004. At that status conference, the court suggested that the parties agree to a bifurcation of the liability issue. Discovery and motions are stayed pending the mediation. Although we have a demurrer on file, that demurrer will not be heard until the stay is lifted. We believe that each of the plaintiff's purported class action lawsuits are without merit and will defend against each of them vigorously. No assurance can be given, however, that these matters will be resolved in our favor.

MATCHNET PLC AND SUBSIDIARIES

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MATCHNET PLC
CONSOLIDATED BALANCE SHEETS
(In thousands, except share data)

ASSETS	June 30, 2004 (unaudited)	December 31, 2003
CURRENT ASSETS:		
Cash and cash equivalents	\$ 6,343	\$ 2,035
Marketable securities	3,149	3,780
Accounts receivable	808	410
Advances to employees	233	450
Other receivables	293	50
Prepaid advertising expenses	23	232
Prepaid expenses and other	<u>1,167</u>	<u>620</u>
Total current assets	12,016	7,577
Property and equipment, net	6,480	4,273
Goodwill, net	7,725	2,024
Intangible assets, net	1,095	987
Deposits and other assets	<u>1,300</u>	<u>2,228</u>
Total Assets	<u>\$ 28,616</u>	<u>\$ 17,089</u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	\$ 2,618	\$ 3,385
Accrued liabilities	8,316	4,555
Deferred revenue	3,937	3,232
Current portion of obligations under capital leases	<u>333</u>	<u>316</u>
Total current liabilities	15,204	11,488
Obligations under capital leases, net of current portion	-	171
Commitments and contingencies (Note 4)		
SHAREHOLDERS' EQUITY:		
Authorized capital £400,000 divided into 40,000,000 ordinary shares of 1p each; issued and outstanding 23,070,442 as of June 30, 2004, 19,556,699 shares as of December 31, 2003 at a stated value of:	408	313
Additional paid-in-capital	55,123	39,737
Deferred stock-based compensation expense	(2,707)	(2,572)
Accumulated other comprehensive income (loss)	(290)	(40)
Accumulated deficit	<u>(39,122)</u>	<u>(32,008)</u>
Total shareholders' equity	<u>13,412</u>	<u>5,430</u>
Total liabilities and shareholders' equity	<u>\$ 28,616</u>	<u>\$ 17,089</u>

See accompanying notes to unaudited consolidated financial statements

MATCHNET PLC
UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	<u>2004</u>	<u>2003</u> (restated)	<u>2004</u>	<u>2003</u> (restated)
Net revenues	\$15,812	\$8,423	\$30,862	\$15,459
Operating expenses:				
Marketing	9,951	4,811	17,080	8,326
Customer service	903	458	1,878	1,021
Technical operations	1,974	994	3,318	1,813
Product development	427	229	706	397
General and administrative (excluding stock-based compensation)	5,695	2,628	12,078	5,111
Stock-based compensation	689	--	2,401	--
Amortization of intangible assets	238	58	482	189
Total operating expenses	<u>19,877</u>	<u>9,178</u>	<u>37,943</u>	<u>16,857</u>
Operating loss	(4,065)	(755)	(7,081)	(1,398)
Interest (income) and other expenses, net	28	(57)	32	(110)
Loss before income taxes	(4,093)	(698)	(7,113)	(1,288)
Provision for income taxes	--	39	1	40
Net loss	<u>\$(4,093)</u>	<u>\$(737)</u>	<u>\$(7,114)</u>	<u>\$(1,328)</u>
Net loss per ordinary share- basic and diluted	\$(0.18)	\$(0.04)	\$(0.33)	\$(0.07)
Weighted average ordinary shares outstanding-basic and diluted	22,264	18,736	21,521	18,722

See accompanying notes to unaudited consolidated financial statements

MATCHNET PLC

UNAUDITED CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY

(In thousands)

	Ordinary Shares		Additional Paid-in- capital	Deferred share Compensation	Comprehensive Income (loss)	Accumulated Deficit	Total Shareholders' Equity
	Shares	Amount					
BALANCE December 31, 2003	19,557	\$ 313	\$ 39,737	\$ (2,572)	\$ (40)	\$ (32,008)	\$ 5,430
Issuance of ordinary shares upon exercise of share options and warrants	2,913	84	9,204	--	--	--	9,288
Private Placement of Ordinary Shares	600	11	3,646	--	--	--	3,657
Unrealized loss on marketable securities	--	--	--	--	(250)	--	(250)
Share compensation	--	--	2,536	(135)	--	--	2,401
Net loss	--	--	--	--	--	(7,114)	(7,114)
BALANCE, June 30, 2004	<u>23,070</u>	<u>\$ 408</u>	<u>\$ 55,123</u>	<u>\$ (2,707)</u>	<u>\$ (290)</u>	<u>\$ (39,122)</u>	<u>\$ 13,412</u>

See accompanying notes to unaudited consolidated financial statements

MATCHNET PLC
UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Six Months Ended June 30,	Six Months Ended June 30,
	<u>2004</u>	<u>2003</u> (restated)
Cash flows from operating activities:		
Net loss	\$ (7,114)	\$ (1,328)
Adjustments to reconcile net loss to cash flows from operating activities:		
Depreciation and amortization	1,852	809
Fair value of compensatory share options and warrants	2,401	-
Changes in operating assets and liabilities:		
Accounts receivable	(398)	25
Advances to employee and executives and other receivables	(26)	(111)
Prepaid advertising expense	209	(279)
Prepaid expenses and other assets	(1,665)	(365)
Accounts payable and accrued liabilities	2,994	1,560
Deferred revenue	705	820
Net cash provided by (used in) operating activities	<u>(1,042)</u>	<u>1,131</u>
Cash flows from investing activities:		
Sales of marketable securities	3,381	1,067
Purchases of marketable securities	(3,000)	-
Purchase of property and equipment	(3,577)	(1,390)
Purchases of businesses and intangible assets	(4,245)	10
Net cash used in investing activities	<u>(7,441)</u>	<u>(313)</u>
Cash flows from financing activities:		
Proceeds from issuance of ordinary shares	12,945	35
Principal payments of capital lease obligations	(154)	-
Net cash provided by financing activities	<u>12,791</u>	<u>35</u>
Net increase (decrease) in cash	4,308	853
Cash at beginning of period	2,035	463
Cash at end of period	<u>\$ 6,343</u>	<u>\$ 1,316</u>
Supplemental disclosure of cash flow information:		
Cash received during the period for interest	\$ (11)	\$ (108)
Cash paid during the period for income taxes	\$ 1	\$ 40
Supplemental information of non-cash investing and financing activities:		
Equipment capital lease financing		\$ 438

See accompanying notes to unaudited consolidated financial statements

MATCHNET PLC
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. THE COMPANY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Company

MatchNet, plc. (the Company) is a public limited company organized under the laws of England. The Company and its consolidated subsidiaries provide Internet personals services, whereby single individuals are able to post information about themselves ("profiles") on the Company's Web sites and search and contact other individuals who have posted profiles. The Company conducts its business primarily in the United States, and has plans for international expansion.

Membership in the Company's online services, which includes the posting of a personal profile and photos, and access to its database of profiles is free. The Company charges a subscription fee for one, three, six and twelve-month subscriptions to members allowing them to initiate communication with other members and subscribers via the Company's confidential e-mail communications platform. Two-way communications through the Company's confidential e-mail platform can only take place between paying subscribers.

Reclassifications

The operating expense line items in the accompanying consolidated statements of operations have been revised in 2003 to provide a more detailed presentation of operating results which, in management's opinion, is more representative of the Company's business. The prior period's expense line items have been reclassified to conform to the 2004 presentation. These reclassifications have no effect on reported net revenues or on net loss.

Interim Financial Information

These unaudited interim consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States. Certain information and note disclosures normally included in the consolidated annual financial statements prepared in accordance with generally accepted accounting principles in the United States have been omitted from this interim report. In the opinion of the Company's management, the unaudited interim consolidated financial statements have been prepared on the same basis as the audited consolidated financial statements and include all adjustments (consisting of normal recurring accruals) necessary for the fair presentation of the Company's financial position, results of operations and cash flows as of and for the six months ended June 30, 2004. Results for the six months ended June 30, 2004 are not necessarily indicative of the results to be expected for the year ending December 31, 2004.

Revenue Recognition and Deferred Revenue

Substantially all of the Company's revenues are derived from subscription fees. The Company recognizes revenue in accordance with accounting principles generally accepted in the United States and with Securities and Exchange Commission Staff Accounting Bulletin No. 104, "Revenue Recognition". Recognition occurs ratably over the subscription period, beginning when there is persuasive evidence of an arrangement, delivery has occurred (access has been granted), the fees are fixed and determinable, and collection is reasonably assured. Subscribers pay in advance, primarily using a credit card, and all purchases are final and nonrefundable. Fees collected in advance for subscriptions are deferred and recognized as revenue using the straight line method over the term of the subscription.

The Company derives a small amount of revenues (less than 2% of revenue for the six months ended June 30, 2004 and 2003) from certain promotional events. Revenues and the related expenses associated with these events are recognized at the conclusion of each event.

Barter transactions are valued based on amounts realized in similar cash transactions occurring within six months prior to the date of the barter transaction. Revenue from barter arrangements totaled \$203,000 and \$7,000 for the six months ended June 30, 2004 and 2003, respectively.

Comprehensive Income

Comprehensive income (loss) is defined as the change in equity of a business enterprise during a period from transactions and other events and circumstances from non-owner sources. For the Company, comprehensive income (loss) consists of its reported net loss and the net unrealized gains or losses on marketable securities. Comprehensive loss for each of the periods presented is comprised as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	<u>2004</u>	<u>2003</u>	<u>2004</u>	<u>2003</u>
Net (loss)	\$(4,093)	\$(737)	\$(7,114)	\$(1,328)
Changes in unrealized gains/ (losses) in available for sale securities, net of tax effects	<u>(31)</u>	<u>(4)</u>	<u>(250)</u>	<u>(19)</u>
Total comprehensive (loss)	<u><u>\$(4,124)</u></u>	<u><u>\$(741)</u></u>	<u><u>\$(7,364)</u></u>	<u><u>\$(1,347)</u></u>

Advertising Costs

Advertising costs are expensed as incurred. For the six months ended June 30, 2004 and 2003, the Company incurred advertising costs amounting to approximately \$15.1million and \$8.2 million, respectively.

Share Compensation

The Company accounts for stock-based employee compensation arrangements in accordance with the provisions of Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees", and related interpretations. Under APB No. 25, compensation expense is recognized over the vesting period based on the excess, if any, on the date of grant of the deemed fair value of the underlying shares and the exercise price on the date of grant.

The Company follows the pro forma disclosure requirements of Statement of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock-Based Compensation", which require presentation of the pro forma effect of the fair value based method on net income (loss) and net income (loss) per share in the notes to consolidated financial statements.

If compensation expense was determined based on the fair value at the date of grant, the Company's net loss and net loss per share for the three and six months ended June 30, 2004 and 2003 would have been as follows (all amounts are in thousands, except per share data):

	Three Months Ended June 30,		Six Months Ended June 30,	
	<u>2004</u>	<u>2003</u>	<u>2004</u>	<u>2003</u>
Net loss, as reported	\$ (4,093)	\$ (737)	\$ (7,114)	\$ (1,328)
Add-back: Total employee share compensation recorded in the accompanying consolidated statements of operations	64	-	233	-
Less: Total compensation as if the fair value method was used, net of tax effect	<u>(1,383)</u>	<u>(1,094)</u>	<u>(2,817)</u>	<u>(2,222)</u>
Pro forma net loss	<u>\$ (5,412)</u>	<u>\$ (1,831)</u>	<u>\$ (9,698)</u>	<u>\$ (3,550)</u>
Net loss per common share:				
As reported	\$ (0.18)	\$ (0.04)	\$ (0.33)	\$ (0.07)
Pro forma	<u>\$ (0.24)</u>	<u>\$ (0.10)</u>	<u>\$ (0.45)</u>	<u>\$ (0.19)</u>

In accordance with SFAS No. 123, the fair value of each option grant was estimated as of the grant date using the Black-Scholes option-pricing model for the three and six months ended June 30, 2004 and 2003 assuming risk-free interest rates of approximately 3.5 percent and 2 percent respectively; volatility of approximately 70 percent and 75 percent; zero dividend yield; and expected lives of four years for all periods.

The Company accounts for shares issued to non-employees in accordance with the provisions of SFAS No. 123 and EITF 96-18, "Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods and Services".

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management 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 the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

2. ACQUISITIONS

Point Match

On January 16, 2004, the Company acquired the assets of Point Match Ltd., an Israeli corporation, in exchange for cash of \$6,290,000 of which \$2,046,000 was placed in escrow in 2003. This transaction was recorded under the purchase method of accounting with \$5,700,000 being allocated to goodwill, \$430,000 to member databases, \$130,000 to subscriber databases, and \$30,000 to domain name.

The following unaudited pro forma financial information presents the combined results of Matchnet, plc. and Point Match Ltd. as if the acquisition had occurred as of January 1, 2003, after applying certain adjustments (in thousands, except per share amounts):

	Year Ended December 31, <u>2003</u>	Six Months Ended June 30, <u>2004</u>
Net revenues	\$ 39,051	\$ 30,948
Net loss	\$ (12,176)	\$ (7,026)
Net loss per share basic and diluted	\$ (0.64)	\$ (0.33)

3. SHAREHOLDERS' EQUITY

MatchNet has adopted the disclosure-only provisions of Statement of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock-Based Compensation". Accordingly, no compensation cost has been recognized in the results of operations for nonqualified share options and warrants.

In 1999 and in connection with an offering of the Company's ordinary shares, warrants were issued for approximately 800,000 ordinary shares at an exercise price of \$1.05 per share. The Company may call the warrants, if for a period of twenty consecutive business days the shares have been traded at a price equal to not less than 125% of the exercise price. Warrants were exercised for 34,000 shares in 2003 and 608,848 shares in 2002, with net proceeds to the Company of approximately \$35,000 in 2003 and \$656,000 in 2002. As of June 30, 2004, warrants for 138,000 shares remain outstanding and exercisable through their expiration date of January 15, 2005.

In July 2003, warrants were issued to consultants for the purchase of up to 1,000,000 shares of the company's ordinary shares at an exercise price of \$2.50 per share. Of these warrants, 500,000 vested immediately were exercisable and non-forfeitable, and 500,000 vest based on certain performance criteria and upon certain circumstances. The Company has treated these warrants as variable and accordingly recognized compensation expense in the six months ended June 30, 2004 in the amount of \$1,568,000. This transaction also resulted in a deferred share compensation balance of \$1,485,000 as of June 30, 2004, based on the fair value of the warrants. On a quarterly basis, the Company is required to recognize an increase or decrease in compensation expense based on the then fair value of such warrants. The warrants expire in 2007.

Employee Share Option Plan

The Company has an Executive Share Option Scheme (the Plan), that provides for the granting of share options by the Board of Directors of the Company to employees, consultants, and employee directors. The exercise price of options granted under the Plan, are based on the estimated fair market value of the ordinary shares on the date of grant. Options granted under the Plan vest and terminate over various periods as defined by each option grant (in general, from 4 to 5 years from the grant date), and in accordance with the terms of the Plan. The Plan terminates in April 2010, and restricts shares to be issued to a maximum of 17,000,000 shares, with approximately 4,066,540 shares available for future grants as of June 30, 2004.

In July 2003, options were issued to consultants for the purchase of up to 225,000 shares of the company's ordinary shares at an exercise price of \$2.07 per share. The company has treated these options as variable and accordingly recorded expenses for the six months ended June 30, 2004 of \$602,000. This transaction also resulted in a deferred share compensation balance of \$856,000 at June 30, 2004. On a quarterly basis, the Company is required to recognize an increase or decrease in compensation expense based on the then fair value of such options. The options expire in 2007.

In July 2003 and April 2004, loans were made to employees for the exercise of 100,000 and 15,000 options respectively. These loans were deemed a "synthetic" re-pricing under EITF 00-23, "Issues Related to the Accounting for Stock Compensation under APB Opinion No. 25 and FASB Interpretation No. 44" and resulted in variable accounting. The company recorded expenses in the six months ended June 30, 2004 of \$231,000 resulting from these transactions. These transactions also resulted in a deferred share compensation balance of \$366,000 at June 30, 2004. On a quarterly basis, the Company is required to recognize an increase or decrease in compensation expense based on the fair value of such options.

Information relating to outstanding share options is as follows:

	Number of Shares (In Thousands)	Weighted Average Price Per Share
Outstanding at December 31, 2003	10,309	\$ 2.35
Granted	1,721	\$ 7.08
Exercised	(2,896)	\$ 3.20
Cancelled	(191)	\$ 4.26
Outstanding at June 30, 2004	<u>8,943</u>	<u>\$ 2.86</u>

The following summarizes information relating to share options outstanding and exercisable at June 30, 2004. On March 27, 2004 a change of control triggered the immediate vesting of certain options. (amounts in thousands, except per share data):

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Number Of Shares	Weighted Average Remaining Life	Weighted Average Exercise Price	Number Of Shares	Weighted Average Exercise Price
\$2.04 to \$10.19	2,921	3	\$ 5.08	536	\$ 3.38
\$2.02	4,085	2	\$ 2.02	4,085	\$ 2.02
\$0.89 to \$1.87	<u>1,937</u>	1	\$ 1.27	<u>1,897</u>	\$ 1.26
	<u>8,943</u>			<u>6,518</u>	

4. COMMITMENTS AND CONTINGENCIES

Litigation

On July 13, 2001, Liveworld, Inc. filed a complaint in the Santa Clara County Superior Court in California against our company and SocialNet, Inc. In February 2001, we purchased the outstanding shares of SocialNet pursuant to a share exchange agreement. The plaintiff contends that we assumed the obligations of SocialNet pursuant to a letter agreement to purchase \$1.5 million of services from the plaintiff and that we failed to purchase the services and induced SocialNet to breach the letter agreement with the plaintiff. The complaint, as amended, alleges breach of contract, breach of implied covenant of good faith and fair dealing, quantum meruit, fraud, intentional interference with contract and fraudulent transfers. The plaintiff is seeking compensatory damages in the approximate amount of \$1.1 million plus interest and punitive damages. In July 2002, we filed a cross-complaint for declaratory relief and rescission and in November 2002 we filed a demurrer on the interference with contract claim, which was overruled. In September 2003, we moved for summary judgment, which was denied. The court has scheduled a settlement conference for October 20, 2004 and a trial date of October 25, 2004. We believe the plaintiff's complaints as to our company are without merit and will defend against them vigorously in this matter. No assurance can be given, however, that this matter will be resolved in our favor.

On August 10, 2001, Comdisco, Inc. filed a complaint in the Santa Clara County Superior Court in California against our company, SocialNet and certain officers and directors of our company and SocialNet. The plaintiff's complaint generally contends that we assumed the obligations of SocialNet as a result of our purchase of SocialNet, which had defaulted on its financing arrangements with the plaintiff. The plaintiff's complaint, as amended, alleges breach of written contract, anticipatory repudiation, intentional interference with contract, recovery of equipment with damages, fraudulent transfer, constructive trust, breach of fiduciary duty, aiding and abetting breach of fiduciary duty, conspiracy to fraudulently transfer assets and conspiracy to breach fiduciary duty. The plaintiff is

seeking compensatory damages plus interest, attorney's fees in the amount of approximately \$4 million, punitive damages, avoidance of allegedly fraudulent transfers, possession of collateral, and other non-monetary damages. In December 2003, the court denied the plaintiff's application for a writ of attachment. All parties have filed motions for summary judgment. The court has scheduled a settlement conference for September 15, 2004 and a jury trial for September 20, 2004. We believe the plaintiff's complaints as to our company are without merit and will defend against them vigorously in this matter. No assurance can be given, however, that this matter will be resolved in our favor.

Three separate yet similar class action complaints have been filed against our company. On June 21, 2002, Tatyana Fertelmeyster filed an Illinois class action complaint against our company in the Circuit Court of Cook County, Illinois, based on an alleged violation of the Illinois Dating Referral Services Act. In *Jason Adelman v. MatchNet, plc., Los Angeles Superior Court Case No. BC 306167*, the plaintiff filed a nationwide class action complaint against our company based on an alleged violation of California Civil Code section 1694 et seq., which regulates businesses that provide dating services. On September 12, 2002, Lili Grossman filed a New York class action complaint against our company in the Supreme Court in the State of New York based on alleged violations of the New York Dating Services Act and the Consumer Fraud Act. In each of these cases, the complaint included allegations that as an alleged dating service, our company is required to provide language in our contracts that allows members to rescind their contracts within three days, that allows reimbursement of a portion of the contract price if the member dies during the term of the contract and/or that allows members to cancel their contracts in the event of disability or relocation. Causes of action include breach of applicable state and/or federal laws, fraudulent and deceptive business practices, breach of contract and unjust enrichment. The plaintiffs are seeking remedies including declaratory relief, restitution, actual damages although not quantified, treble damages and/or punitive damages, and attorney's fees and costs. *Huebner v. InterActiveCorp., L.A.S.C. Case No. BC 305875* involves a similar action brought against InterActiveCorp's Match.com that has been ruled related to *Adelman*, but the two cases have not been consolidated. We have filed a motion for summary judgment and the court has certified an Illinois class in the case brought by Ms. Fertelmeyster. The court has ordered Ms. Fertelmeyster to complete all depositions and discovery in connection with the motion for summary judgment on or before August 31, 2004. In December 2002, the Supreme Court of New York dismissed the case brought by Ms. Grossman, although the plaintiff is appealing the decision. A status conference with respect to the *Adelman* case was held on May 11, 2004, at which time the Court ordered the parties to mediation. A post-mediation status conference was held on Friday, July 16, 2004. At that status conference, the court suggested that the parties agree to a bifurcation of the liability issue. Discovery and motions are stayed pending the mediation. Although we have a demurrer on file, that demurrer will not be heard until the stay is lifted. We believe that each of the plaintiff's purported class action lawsuits are without merit and will defend against each of them vigorously. No assurance can be given, however, that these matters will be resolved in our favor.

5. RELATED PARTY TRANSACTIONS

Several relatives of each of Joe Y. Shapira and Alon Carmel, hold non-executive positions with MatchNet or MatchNet Israel.

6. RESTATEMENT OF CONSOLIDATED FINANCIAL STATEMENTS FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2003

The Company has restated its consolidated financial statements for the three and six months ended June 30, 2003 to correct certain errors as described below:

In previous periods the Company incorrectly recognized a full month of revenue in the month in which members paid in advance for their membership subscription fees (regardless of the effective date of the subscription) and deferred the balance of the fees for multi-month subscriptions. In July of 2003, the Company began to defer revenue on a daily basis (based on the effective date of the subscription and restated prior period's financial statements). The effect on the three and six months ended June 30, 2003 was to decrease revenues by approximately \$303,000 and \$628,000 respectively.

In previous periods we had capitalized bounty costs, which represented amounts paid to third parties for members acquired on an individual basis through third party Web sites or e-mail campaigns. These costs were being amortized over a three year period, on an accelerated basis. In 2003 we determined that these costs should be expensed as incurred, and that we should restate the prior periods' financial statements to conform to U.S. generally accepted accounting principles. The reason for the change was that bounty costs were meant to drive free memberships or registrations. A member was not required to become a paying subscriber. Therefore, those expenses should be recognized immediately, since a conversion from non-paying member to a paying subscriber is not guaranteed. Accordingly, we have restated the consolidated financial statements to expense these costs as incurred. The effect on the three months ended March 31, 2003 was to decrease operating expenses by \$591,000. There was no change related to bounty in the second quarter of 2003.

From 1998 through 2002 the Company acquired several businesses and assets. At that time, the fair values of the intangible assets acquired were not properly determined. In 2004, the Company hired a valuation expert to measure the fair value of such assets at the date of each acquisition. As a result of this process, the Company determined that certain allocations previously reported were inappropriate. The effect on the three and six months ended June 30, 2003 was to increase amortization expense by approximately \$76,000 and \$155,000 respectively.

We did not timely accrue for some services provided. The accompanying financial statements for the three and six months ended June 30, 2003 were restated to properly and timely accrue for these liabilities. The effects on the three and six months ended June 30, 2003 was to increase operating expenses by approximately \$60,000 and decrease operating expenses by approximately \$101,000 respectively.

The Company identified certain errors in the prior years consolidation process. The effects on the net loss for the three and six months ended June 30, 2003 was a decrease of approximately \$314,000 and \$157,000 respectively.

MATCHNET PLC
UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS
(Amounts in thousands, except per share data)

	Three Months Ended June 30, 2003		Six Months Ended June 30, 2003	
	Restated	As Previously Reported (a)	Restated	As Previously Reported (a)
Net revenues	\$ 8,423	\$ 8,726	\$ 15,459	\$ 16,087
Operating expenses	9,178	8,964	16,857	16,798
Operating loss	(755)	(238)	(1,398)	(711)
Interest (income) and other expenses, net	(57)	335	(110)	643
Loss before income taxes	(698)	(573)	(1,288)	(1,354)
Provision for Income taxes	39	39	40	40
Net loss	<u>\$ (737)</u>	<u>\$ (612)</u>	<u>\$ (1,328)</u>	<u>\$ (1,394)</u>
Net loss per ordinary share – Basic and diluted	<u>\$ (0.04)</u>	<u>\$ (0.03)</u>	<u>\$ (0.07)</u>	<u>\$ (0.07)</u>
Weighted average ordinary shares outstanding – Basic and diluted	<u>18,736</u>	<u>18,707</u>	<u>18,722</u>	<u>18,707</u>

Note: (a) Includes effect of reclassifications to conform to the current period presentation.