IENTERTAINMENT NETWORK INC
Form 10QSB
August 14, 2001

U.S. Securities and Exchange Commission
WASHINGTON, D.C. 20549

FORM 10-QSB

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF
THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2001

Commission file number 0-29750

IENTERTAINMENT NETWORK, INC.
(Exact name of small business issuer as specified in its charter)

North Carolina	56-2092059
(State of incorporation)	(I.R.S. Employer Identification Number)

124-126 Quade Drive
Cary, North Carolina 27513
(Address of principal executive office)

(919) 678-8301
(Issuer's telephone number)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes [X]   No [_]

As of August 136, 2001, (the most recent practicable date), there were 15,914,311 shares of the issuer's Common Stock, $.10 par value per share, outstanding.

Transitional Small Business Disclosure Format (check one)

Yes [_]   No [X]

1

IENTERTAINMENT NETWORK, Inc.

Form 10-QSB Quarterly Report

INDEX

		PAGE
PART I	FINANCIAL INFORMATION	
Item 1	Financial Statements	3

Item 2	Management's Discussion and Analysis of Financial Condition and Results of Operations	14
PART II	OTHER INFORMATION	18
Item 1	Legal Proceedings	18
Item 2	Changes in Securities and Use of Proceeds	18
Item 3	Defaults Upon Senior Securities	18
Item 4	Submission of Matters to a Vote of Security Holders	18
Item 5	Other Information	19
Item 6	Exhibits and Reports on Form 8-K	20
SIGNATURES		21

2

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

iEntertainment Network, Inc.
Consolidated Balance Sheets
(In thousands, except share data)

	June 30 2001 UNAUDITED	December 2000 AUDITED
Assets		
Current assets:		
Cash and cash equivalents	$ 352	$ 4
Trade receivables, net of allowances of $110 and $80 at June 30, 2001 and December 31, 2000, respectively	172	8
Prepaid expenses and other	164	1
Total current assets	688	1,4
Property and equipment, net	787	9
Software development costs, net	744	6
Other noncurrent assets	17	
Total assets	$ 2,236	$ 3,0
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable and accrued expenses	$ 959	$ 1,1
Current portion of capital lease obligations	30	

Total current liabilities	989	1,2
Capital lease obligations, less current portion	31	
Total liabilities	1,020	1,2
Stockholders' equity:		
Series D Convertible Preferred Stock $.10 par value; liquidation and stated value of $1,000 per share, plus accumulated accretion, 4,911 shares authorized, issued and outstanding	5,392	5,2
Common stock, $.10 par value; 50,000,000 shares authorized; 15,914,311 and 15,914,311 shares issued and outstanding	1,591	1,5
Additional paid-in capital	38,157	38,1
Accumulated deficit	(43,872)	(43,1
Accumulated other comprehensive loss	(52)	(
Total stockholders' equity	1,216	1,7
Total liabilities and stockholders' equity	$ 2,236	$ 3,0

See accompanying notes.

3

iEntertainment Network, Inc.

Consolidated Statements of Operations
(In thousands, except share and per share data)

	Three months ended June 30 2001	Three months ended June 30 2000	Six mo June 30 2001
Net revenues:			
CD-ROM product sales	$ -	$ -	$ -
Online sales	280	393	537
Advertising and other	144	1,557	458
Royalties and licenses	18	55	21
Total net revenues	442	2,005	1,016
Cost of revenues:			
Cost of products and services	59	30	96
Royalties and amortized software costs	69	71	82
Total cost of revenues	128	101	178
Gross profit	314	1,904	838
Operating expenses:			
Sales and marketing	191	1,167	729
Product development	397	370	660
General and administrative	233	416	505
Goodwill amortization	-	401	-

Reversal of accrued liabilities for prize points	6	-	(447
Total operating expenses	827	2,354	1,447
Operating loss	(513)	(450)	(609
Other (income) expense:			
Interest (income)/expense	-	2	-
Other	(52)	(11)	(71
Total other income	(52)	(9)	(71
Loss before income taxes	(461)	(441)	(538
Income tax expense	-	9	-
Net loss	(461)	(450)	(538
Accretion of Series D Convertible Preferred Stock	(73)	(73)	(147
Net loss available to common stockholders	$ (534)	$ (523)	$ (685
Basic and diluted loss per share:			
Net loss per share	$ (0.03)	$ (0.03)	$ (0.04
Weighted average shares used in computing basic and diluted loss per share	15,914,311	15,079,317	15,914,311

4

iEntertainment Network, Inc.

Consolidated Statements of Cash Flows
(In Thousands)

	Six months ended June	
	2001	2
Operating activities		
Net loss	$ (538)	$(1,
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	270	
Amortization of capitalized software development costs	81	
Noncash compensation expense	-	
Issuance of common stock for services	-	
Write-off of accrued liability for prize points	(447)	
Changes in operating assets and liabilities:		
Trade receivables	642	(1,
Prepaid expenses net and other assets	5	
Accounts payable and accrued expenses	225	(
Royalties and commissions payable	-	
Net cash provided by (used in) operating activities	238	(2,
Investing activities		
Purchase of property and equipment	(142)	(

Capitalized software development costs	(167)	(
Net cash used in investing activities	(309)	(
Financing activities		
Proceeds from issuance of common and preferred stock	-	
Stock registration costs	-	
Payments on capital lease obligations	(18)	
Net cash (used in) provided by financing activities	(18)	
Effect of currency exchange rate changes on cash and cash equivalents	4	
Net decrease in cash and cash equivalents	(85)	(1,
Cash and cash equivalents at beginning of period	437	3,
Cash and cash equivalents at end of period	$ 352	$ 1,

iEntertainment Network, Inc.

Consolidated Statements of Cash Flows (continued)
(In Thousands)

	Six months ended June 3	
	2001	2000
Noncash investing and financing activities		
Issuance of common stock in connection with development agreement	$ -	$ 4
Issuance of common stock in connection with employee severance	$	$ 12
Issuance of common stock in settlement of liabilities	$ -	$ 30
Fixed assets acquired under capital lease	$ -	$ 4

See accompanying notes.

iEntertainment Network, Inc.

Notes to Consolidated Financial Statements
(INFORMATION AS OF June 30, 2001 AND FOR THE SIX AND THREE MONTHS ENDED
June 30, 2001 AND 2000 IS UNAUDITED)

1. Description of Business and Significant Accounting Policies

Basis of Presentation

The accompanying unaudited financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and article 10 of Regulation S-X. Accordingly they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting solely of normal recurring accruals) considered necessary for a fair presentation of the statements have been included. The interim operating results are not necessarily indicative of the results that may be expected for a full fiscal year. The balance sheet at December 31, 2000 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. For further information, refer to the financial statements and accompanying footnotes thereto included in the Company's Annual Report on Form 10-KSB for the year ended December 31, 2000.

Description of Business

iEntertainment Network, Inc. (the "Company") is a developer and publisher of Internet games and an operator of online game services. The Company develops and publishes proprietary online multi-player games and has built an Internet distribution infrastructure which offers online gamers a variety of free, subscription and pay-per-play games and services, including simulation, parlor, strategy, role playing and action games.

Disposition of CD-ROM Assets

In connection with the Company's June 1999 disposition of its CD-ROM assets, management decided to terminate certain CD-ROM distribution agreements and began negotiations to mutually release each partner from any obligation under the terms of these agreements. In the second quarter of 1999, the Company estimated a liability of $850,000 for potential settlements upon termination of these agreements. The balance of this liability at March 31, 2001 and December 31, 2000 was $195,000 and is reflected as accounts payable and accrued expenses in the consolidated balance sheets. In the first quarter of 2000, the Company settled with its two largest distributors by paying $250,000 in cash and issuing common stock valued at $300,000.

Consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, iMagicOnline Corporation, Interactive Magic Ltd. and Interactive Magic GmbH. All significant intercompany accounts and transactions have been eliminated in consolidation.

Cash and Cash Equivalents

Cash and cash equivalents include amounts in demand deposit accounts and investments with an original maturity date of three months or less when purchased.

iEntertainment Network, Inc.

Notes to Consolidated Financial Statements (continued)

1. Description of Business and Significant Accounting Policies (continued)

Software Development Costs

The Company capitalizes costs incurred in the development of it's gaming software. Capitalization of such costs is discontinued when a product is available for general release to customers. Capitalized software development costs are capitalized at the lower of cost or net realizable value and amortized using the greater of the revenue curve method or the straight-line method over the estimated economic life of the related product. Amortization begins when a product is ready for general release to customers.

Information related to net capitalized software development costs is as follows: (in thousands):

	June 30 2001	December 31 2000
Balance at beginning of year	$ 658	$ 92
Capitalized	167	658
Amortized	(81)	(92)
Balance at end of year	$ 744	$ 658

Revenue Recognition

Revenue from online sales is recognized at the time the game is played and is based either upon actual usage by the customer on an hourly basis or on an unlimited use subscription basis. The Company records advertising revenues in the period the advertising impressions are delivered to customers. The Company records advertising revenues net of related administrative fees as reported by its outside advertising vendor. The Company's advertising contracts do not guarantee a minimum number of impressions to be delivered.

In December 1999, the Securities and Exchange Commission released Staff Accounting Bulletin ("SAB") No. 101, "Revenue Recognition in Financial Statements", which provides guidance on the recognition, presentation, and disclosure of revenue in financial statements. SAB No. 101 provides guidance on a variety of revenue recognition issues, including gross versus net income statement presentation. Based on the criteria of SAB No. 101, the Company presents its advertising revenues net of these administrative fees.

iEntertainment Network, Inc.

Notes to Consolidated Financial Statements (continued)

Description of Business and Significant Accounting Policies (continued)

Revenue Recognition (continued)

Revenue from CD-ROM product sales was recognized at the time of product shipment. Revenue from royalties and licenses is recognized when earned under the terms of the relevant agreements with original equipment manufacturers ("OEMs"), international distributors and other third parties. With respect to license agreements that provide customers the right to multiple copies in exchange for guaranteed amounts, net revenue is recognized upon delivery of the product master or the first copy provided collectibility is probable. Per copy royalties on sales that exceed the guarantee are recognized as earned. The Company accepts product returns and provides price protection on certain unsold merchandise. Revenue is recorded net of an allowance for estimated future returns, markdowns, price protection and warranty costs. Such reserves are based upon management's evaluation of historical experience, current industry trends and estimated costs.

In October 1997, the Accounting Standards Executive Committee "(AcSEC)" issued Statement of Position "(SOP)" 97-2, "Software Revenue Recognition" as amended in March 1998 by SOP 98-4 and October 1998 by SOP 98-9. These SOPs provide guidance on applying generally accepted accounting principles in recognizing revenue on software transactions. The Company adopted SOP 97-2 for software transactions entered into beginning January 1, 1998. Based on the current requirements of the SOPs, application of these statements did not have a material impact on the Company's revenue recognition policies. However, AcSEC is currently reviewing further modifications to the SOP with the objective of providing more definitive, detailed implementation guidelines. This guidance could lead to unanticipated changes in the Company's operations and revenue recognition practices.

Revenue from certain software development contracts with fixed price components is recognized on the percentage of completion basis in accordance with the American Institute of Certified Public Accountants' SOP 81-1, "Accounting for Performance of Construction-Type and Certain Production-Type Contracts." In accordance with SOP 81-1, the Company recognizes percentage of completion revenue based upon the ratio of accumulated incurred costs to the total estimated costs to complete each contract.

The accounts receivable allowance at June 30, 2001, and December 31, 2000, includes a reserve for doubtful accounts, which management records based on historical experience and current evaluation of potential collectibility issues. The Company does not require collateral for unpaid balances. Credit losses have historically been within management's expectations.

Reclassifications

The Company reclassified Software development costs in the balance sheet as of December 31, 2000 from a current asset to a non-current asset to conform with the presentation in the June 30, 2001 balance sheet. The reclassification did not affect stockholders' equity or net loss as previously reported.

iEntertainment Network, Inc.

Notes to Consolidated Financial Statements (continued)

Description of Business and Significant Accounting Policies (continued)

Comprehensive Loss

The following chart details the Company's comprehensive loss for the periods presented:

	Three months ended June 30		Six months ended June 30	
	2001	2000	2001	200
Net Loss	$(461)	$(450)	$(538)	$(1,46
Other comprehensive income - foreign				

currency translation adjustment	1	6	4	4
Comprehensive loss	$(460)	$(444)	$(534)	$(1,41

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 disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates include provisions for doubtful accounts, sales returns and allowances, warranty provisions, and estimates regarding the recoverability of capitalized software development costs. Actual results could differ from those estimates.

Basic Net Loss Per Share

Basic net loss per share has been calculated in accordance with SFAS No. 128, "Earnings Per Share". Basic net loss per share is calculated by dividing net loss available to common stockholders by the weighted average shares of common stock outstanding during the period.

Had the Company been in a net income position, diluted earnings per share would have been presented and would have included potential common shares related to outstanding options and warrants. The diluted earnings per share computation is not included, as all potential common shares are antidilutive.

Impact of Recently Issued Accounting Pronouncements

In June 1998, the Financial Accounting Standards Board issued SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities". SFAS No. 133, as amended, is required to be adopted in years beginning after June 15, 2000. The Company's January 1, 2000 adoption of the new statement did not have a significant affect on earnings or the consolidated financial position of the Company.

iEntertainment Network, Inc.

Notes to Consolidated Financial Statements (continued)

2. Stockholders' Equity

Series D Redeemable Convertible Preferred Stock

The following is a summary of the terms of the Series D Redeemable Convertible Preferred Stock ("Series D Preferred"):

Dividends

There are no dividends automatically payable on the Series D Preferred. No dividends may be paid to the common stockholders while any Series D Preferred shares are outstanding.

Liquidation Preferences

Upon any liquidation, dissolution or winding up of the Company, before anything can be paid to the holders of common stock, the holders of the Series D

Preferred will be entitled to receive $1,000 per share, plus an amount equal to a 6% annual return on that amount since the November 1999 issuance date and any penalty amounts due thereunder, if any.

Redemption

The Series D Preferred must be redeemed by the Company if it is requested to do so by the holders of a majority of the outstanding Series D Preferred shares upon: (1) failure by the Company to comply with certain terms of the Articles of Incorporation, the Securities Purchase and Exchange Agreement or the related Registration Rights Agreement with respect to the Series D Preferred; (2) bankruptcy of the Company; or (3) certain changes in control of the Company.

In any such event, the redemption price per share would be equal to the greater of (1) $1,200 per share, plus an amount equal to a 6% annual return since November 1999 on the $1,000 paid for each share and any penalty amounts due under the terms of the Series D Preferred (including, but not limited to, as a result of the failure to convert or deliver shares on a timely basis), and (2) the "Parity Value" of the shares, which equals the product of (a) the number of shares of the Company's common stock into which the Series D Preferred could have been converted multiplied by (b) the highest reported closing price per share of the common stock between the event triggering the right to request redemption and the payment of the redemption price.

A registration statement was filed and became effective in March 2000, which removed the redemption feature that was outside the control of the Company. Accordingly, the Company classified the Series D preferred stock as permanent equity during the first quarter of 2000.

The Series D preferred stockholders are entitled to a 6% annual return on the stated value of the preferred stock, upon liquidation, conversion, and redemption within control of the Company. Accordingly, the Company has recorded this return as accretion to the stated value of the preferred stock and a charge to accumulated deficit. For the three and six months ended June 30, 2001 and 2000, the recorded accretion was $734,000 and $147,000 respectively. Accumulated accretion at June 30, 2001, and December 31, 2000 was $482,000 and $335,000, respectively.

2. Stockholders' Equity (continued)

Conversion

Following shareholder approval of the Series D Preferred Stock financing in December 1999, the Series D Preferred shares were convertible at $1 per share of common stock. At any time, a holder of Series D Preferred Stock may convert all of those shares into common stock. Each share of Series D Preferred was initially convertible into 1,000 shares of common stock. The number of shares of common stock issuable upon conversion of a share of Series D Preferred increases over time to provide the holder additional common stock equal to a 6% annual return since November 1999 and any penalty amounts otherwise due thereunder. Subject to certain conditions, the Series D Preferred Stock will automatically convert into common stock in November 2002.

Voting

The Series D Preferred has no voting rights other than as provided by law and except that the approval of the holders of a majority of the outstanding Series D Preferred is required for: (1) any adverse change to the rights of the Series D Preferred; (2) the creation of securities having senior or equal rights; (3) an increase in the authorized number of shares of Series D Preferred; (4) an increase in the par value of the common stock; or (5) any action that would result in certain taxes being imposed on the Series D Preferred.

3. Stock Options and Warrants

The following summarizes the Company's stock option and warrant activity:

	Shares Available for Grant - 1995 Plans	Shares Available for Grant - 1998 Plans	Options Outstanding	We A Exerc Pe
Balances at December 31, 2000	331,985	309,815	3,410,142	
Options granted	(90,000)	-	90,000	
Options canceled	162,863	30,000	(192,863)	
Balances at June 30, 2001	404,848	339,815	3,307,279	

At June 30, 2001, the Company had 2,502,852 options exercisable at exercise prices ranging from $0.25 - $6.00 per share.

The Company had 1,131,905 and 1,210,903 warrants outstanding at March June 30, 2001 and December 31, 2000, respectively, all of which were exercisable at prices ranging from $1.00 to $9.60 per share.

iEntertainment Network, Inc.

Notes to Consolidated Financial Statements (continued)

4. Accrued Liability for Prize Points

The Company has operated a prize point system for the users of its online games. In 2000, prize points were redeemable for cash and other prizes. The Company had recorded an accrued liability of $343,000 in accounts payable and accrued expenses on its December 31, 2000 balance sheet based on management's best estimate of prize points that have not been redeemed. At December 31, 2000, the Company also recorded a liability in accounts payable for redeemed but unpaid prize points of $112,000. In 2001, the Company revised its prize point redemption policy such that prize points are no longer directly redeemable for cash or merchandise. Prize points have been converted to chance points and may now be used by customers to enter prize drawings. Due to the change in its prize point system, management has determined that the Company no longer has prize point obligations as previously recorded in the December 31, 2000 balance sheet. Accordingly, the accrued liability of $343,000 and the payable of $112,000 have been reversed and were netted against operating expenses in the Consolidated Statement of Operations for the quarter ending March 31, 2001.

Following the Company's restructuring of its prize point system in early 2001, three individuals filed complaints with the Consumer Protection Division of the

Office of the Attorney General for the State of North Carolina with respect to prize points that they wanted to redeem for cash prizes. The Attorney General's Office also has asserted that the Company's operation of the game of "Bingo," which the Company allows users to play for free, violates North Carolina's gambling statutes. Management, after consultation with counsel, does not believe that the Company has violated such statutes, which, as interpreted by North Carolina's Attorney General's Office, would cause free Bingo games operated by many companies to be in violation. In order to avoid costly litigation, however, the Company is attempting to negotiate reasonable settlements regarding these claims; however, there can be no assurance that reasonable settlements will be reached. Management cannot reasonably estimate the amount of a settlement at this time: therefore no reserve has been accrued on the balance sheet at June 30, 2001. In addition, such settlements would not bar individual consumer claims or claims of violations of other states' gaming regulations. Consequently, there can be no assurance that future claims will not be made against the Company.

The Company is in the process of changing its operations of its "Bingo" game in order to help resolve its dispute with the Office of the Attorney General of North Carolina. As a result of anticipated reductions in "Bingo's" prize point eligibility necessary to effect these changes, the Company may experience a substantial decrease in the amount of traffic on the Company's "Bingo" website. If the amount of traffic on the Company's "Bingo" website does substantially decrease, the Company's advertising revenues will also substantially decrease.

IENTERTAINMENT NETWORK, Inc.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

RESULTS OF OPERATIONS - THREE AND SIX MONTHS ENDED JUNE 30, 2001 COMPARED TO THREE AND SIX MONTHS ENDED JUNE 30, 2000

OVERVIEW

During the fourth quarter of fiscal 2000, the Company, reacting to an adverse pricing environment for online advertising, restructured its operations, thereby significantly reducing personnel and overhead costs.

NET REVENUES

Net revenues decreased by 76% to $.5 million for the three months ended June 30, 2001 from $2.0 million for the three months ended June 30, 2000. Net revenues decreased by 71% to $ 1.0 million for the six months ended June 30, 2001 from $3.6 million for the six months ended June 30, 2000.

The following table summarizes the changes in the components of revenue from 2000 to 2001:

	Three months ended June 30 ($000)	Six months ended June 30 ($000)
Revenue for the period in 2000	$ 2,005	$ 3,560
Increase / (Decrease) in Advertising and Other Revenue	(1,413)	(2,160)
Increase / (Decrease) in Pay for Play Revenue	(113)	(279)

Increase / (Decrease) in Royalty & Licensing	(37)	(95)
Increase / (Decrease) in CD-ROM revenue	-	(10)
Revenue for the period in 2001	$ 442	$ 1,016

Advertising revenues decreased 91% to $0.1 million for the three months ended June 30, 2001 from $1.6 million for the three months ended June 30, 2000. Advertising revenues decreased 82% to $0.5 million for the six months ended June 30, 2001 from $2.6 million for the six months ended June 30, 2000. All increases in advertising impressions served over the periods were more than offset by a precipitous drop in advertising pricing across the Internet.

Pay-for-Play revenue decreased 29% to $0.3 million for the three months ended June 30, 2001 from $0.4 million for the three months ended June 30, 2000 and decreased 34% to $0.5 million for the six months ended June 30, 2001 from $0.8 million for the six months ended June 30, 2000., primarily due to changes in the pricing model that management implemented in order to stimulate user growth and increase revenues. During the fourth quarter of fiscal 2000, the Company introduced a flat fee, unlimited play option into its pricing matrix. Previously, players paid for each hour played. The new plan drew a significant portion of existing players, but failed to attract a sufficient numbers of new players to offset the loss of revenues generated by high usage players.

IENTERTAINMENT NETWORK, Inc.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (CONTINUED)

COST OF REVENUES

Cost of revenues consists of costs of products sold (including cost of Internet access) and royalties and amortization of software development costs. Cost of revenues in the three month period ending June 30, 2001 increased 26% compared to the comparable period in 2000 due primarily to a duplication of internet access charges necessitated by a facilities move. Cost of revenues decreased 52% to $0.2 million in the six month period ending June 30, 2001 from $0.4 million in the six month period ended June 30, 2000. This decrease was due primarily to the elimination of royalties associated with operating third-party software.

OPERATING EXPENSES

Operating expenses decreased by 65% to $0.8 million for the three months ended June 30, 2001 from $2.4 million for the three months ended June 30, 2000. Operating expenses decreased by 69% to $1.4 million for the six months ended June 30, 2001 from $4.7 million for the six months ended June 30, 2000.

The following table summarizes the changes in the components of operating expenses from 2000 to 2001:

	Three months ended June 30 ($000)	Six months ended June 30 ($000)
Operating Expenses for the period in 2000	$2,354	$ 4,688
Increase/ (Decrease) in Sales and Marketing	(976)	(1,181)

Increase/ (Decrease) in Product Development	27	(285)
Increase/ (Decrease) in General and Administrative	(187)	(527)
Increase/ (Decrease) in Goodwill Amortization	(401)	(801)
Increase/ (Decrease) in Reversal of liabilities for prize points	6	(447)
Operating Expenses for the period in 2001	$ 827	$ 1,447

SALES AND MARKETING

Sales and marketing expenses decreased by 84% to $0.2 million for the three months ended June 30, 2001 from $1.2 million for the three months ended June 30, 2000., and decreased by 62% to $0.7 million for the six months ended June 30, 2001 from $1.9 million for the six months ended June 30, 2000. These decreases were due primarily to the reduction of costs associated with customer incentives and personnel cost savings arising from the Company's restructuring in late 2000. Beginning with Q1the first quarter of 2001, the Company revised its prize point redemption policy such that prize points are no longer directly redeemable for cash or merchandise. Prize points have been converted to chance points and are used to enter fixed-value prize drawings, resulting in a decreases of $0.4 million and $0.6 million for the three and six months ended June 30, 2001, respectively, compared to the corresponding periods in 2000. Accordingly, the associated accrued liability related to unredeemed prize points of $0.3 million and the payable of $0.1 million related to redeemed, but unpaid, prize points were reversed against operating expenses in the quarter ended March 31, 2001.

Following the Company's restructuring of its prize point system in early 2001, three individuals filed complaints with the Consumer Protection Division of the Office of the Attorney General for the State of North Carolina with respect to prize points that they wanted to redeem for cash prizes. The Attorney General's Office also has asserted that the Company's operation of the game of "Bingo,"

IENTERTAINMENT NETWORK, Inc.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (CONTINUED)

SALES AND MARKETING (CONTINUED)

gambling statutes. Management, after consultation with counsel, does not believe that the Company has violated such statutes, which, as interpreted by North Carolina's Attorney General's Office, would cause free Bingo games operated by many companies to be in violation. In order to avoid costly litigation, however, the Company is attempting to negotiate reasonable settlements regarding these claims; however, there can be no assurance that reasonable settlements will be reached. Management cannot reasonably estimate the amount of a settlement at this time: therefore no reserve has been accrued on the balance sheet at June 30, 2001. In addition, such settlements would not bar individual consumer claims or claims of violations of other states' gaming regulations. Consequently, there can be no assurance that future claims will not be made against the Company.

The Company is in the process of changing its operations of its "Bingo" game in order to help resolve its dispute with the Office of the Attorney General of North Carolina. As a result of anticipated reductions in "Bingo's" prize point eligibility necessary to effect these changes, the Company may experience a substantial decrease in the amount of traffic on the Company's "Bingo" website. If the amount of traffic on the Company's "Bingo" website does substantially which the Company allows users to play for free, violates North Carolina's decrease, the Company's advertising revenues will also substantially decrease.

PRODUCT DEVELOPMENT

Product development expenses increased slightly in the three month period ended June 30, 2001 from the prior year's comparable period and decreased 30% to $0.7 million for the six months ended June 30, 2001 from $0.9 million for the six months ended June 30, 2000. The Company's restructuring in December 2000 resulted in decreases in staffing costs and overhead in each of the first two quarters of 2001.

GENERAL AND ADMINISTRATIVE

General and administrative expenses decreased by 44% to $0.2 million for the three months ended June 30, 2001 from $0.4 million for the three months ended June 30, 2000. General and administrative expenses decreased by 51% to $0.5 million for the six months ended June 30, 2001 from $1.0 million for the six months ended June 30, 2000, primarily due to savings associated with the closure of the Company's European operations and savings in staffing costs effected by the Company's restructuring in December 2000.

GOODWILL AMORTIZATION

Goodwill from the MPG-Net acquisition, acquired in mid -first quarter 1999, was previously being amortized to expense over 36 months. Goodwill from the Gamers Net acquisition, acquired in third quarter 1999, was previously being amortized to expense over 24 months. During the second -half of fiscal 2000, the Company experienced a significant revenue stream reduction as a result of a downturn in the online advertising market, which indicated potential impairment of its recorded goodwill values. The Company determined that unamortized goodwill relating to both MPG-Net and The Gamers Net had become fully and permanently impaired. And accordingly, the balance of unaudited goodwill at December 31, 2000 was written down to $0.

IENTERTAINMENT NETWORK, Inc.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (CONTINUED)

LIQUIDITY AND CAPITAL RESOURCES

As of June 30, 2001, the Company had cash and cash equivalents of $.4 million. The following table summarizes is a condensed table of cash and cash equivalents on hand and major cash flow items:

Cash and cash equivalents on hand, December 31, 2000	$ 437
Net loss	(538)
Add: non-cash charges and expenses	(96)
Changes in working capital	872
Net Cash Provided By Operations	238
Net investing and financing activities	(327)
Effect of exchange rates on cash and cash equivalents	4
Net change in cash and cash equivalents	(85)
Cash and cash equivalents on hand, June 30, 2001	$ 352

The Company used $2.4 million less net cash in operating activities during the first six months of 2001 compared with the same period in 2000. This decrease was primarily due to the contraction of the business as effected by the Company's restructuring during the fourth quarter of fiscal 2000, resulting in reduced cash operating requirements.

The Company's success is dependent upon its ability to generate sufficient cash flow to meet its obligations on a timely basis, to obtain additional financing or refinancing as may be required, and ultimately to attain profitability. Management expects to be able to attract additional capital, if needed, for its online operations. However, there can be no assurance that management's plans will be executed as anticipated.

As of the balance sheet date, the Company believes that it may not have sufficient cash resources to fund its operations through the next twelve months. There is no assurance that the Company will be able to close on any financing transaction. The Company does not have any current arrangements or commitments for any future financing. The Company may not be able to obtain sufficient additional financing to satisfy its cash requirements or the Company may be required to obtain financing on terms that are not favorable to it and its shareholders. The Company received a going concern opinion on its December 31, 2000 audited financial statements. The Company's auditors' opinion issued in conjunction with the Company's audited financial statements for the period ended December 31, 2000 raised substantial doubt about the Company's ability to continue as a going concern.

If the Company is unable to obtain additional financing when needed, it may be required to delay or scale back product development and marketing programs in order to meet its short-term cash requirements, which could have a material adverse effect on its business, financial condition and results of operations.

The Company's forecast for the period of time through which its financial resources will be adequate to support its operations is a forward-looking statement that involves risks and uncertainties, and actual results could vary. The factors described in the preceding paragraphs will impact the Company's future capital requirements and the adequacy of its available funds.

EURO CONVERSION

On January 1, 1999, the European Community began denominating significant financial transactions in a new monetary unit, the Euro. The Euro is intended to replace the traditional currencies of the individual EU member countries. During the fourth quarter of 1999, the Company decided to close its European operations and therefore is not converting internal financial systems to the Euro as a functional currency during this closure period.

IENTERTAINMENT NETWORK, Inc.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Following the Company's restructuring of its prize point system in early 2001, three individuals filed complaints with the Consumer Protection Division of the Office of the Attorney General for the State of North Carolina with respect to prize points that they wanted to redeem for cash prizes. The Attorney General's Office also has asserted that the Company's operation of the game of "Bingo," which the Company allows users to play for free, violates North Carolina's gambling statutes. Management, after consultation with counsel, does not believe that the Company has violated such statutes, which, as interpreted by North Carolina's Attorney General's Office, would cause free Bingo games operated by many companies to be in violation. In order to avoid costly litigation, however, the Company is attempting to negotiate reasonable settlements regarding these claims; however, there can be no assurance that reasonable settlements will be reached. In addition, such settlements would not bar individual consumer claims or claims of violations of other states' gaming regulations. Consequently, there can be no assurance that future claims will not be made against the Company.

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

From January 1, 2001 through June 30, 2001, the Company (1) granted options to purchase 12,500 shares of common stock to two contractors for services priced at market value on the date of issuance; (2) granted options to purchase 77,500 shares of common stock to 10 employees priced at market value on the date of grant.

Items (1) and (2) were exempt from registration under Section 5 of the Securities Act of 1933, as amended, by reason of Section 4(2) of the Act and Regulation D of the Securities and Exchange Commission.

IENTERTAINMENT NETWORK, Inc.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

At an annual shareholders meeting held on June 5, 2001, the following matters were approved:

- approval and ratification of an amendment to the Company's Articles of Incorporation reducing the minimum number of directors from five to three.
- election of three directors;
- approval and ratification of an amendment to the Company's 1998 Stock Option Plan to increase the number of shares of common stock reserved for issuance under the plan from 1,800,000 to 2,300,000 shares;
- approval and ratification of the appointment of Ernst & Young LLP.

IENTERTAINMENT NETWORK, Inc.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS (CONTINUED)

The respective vote tabulations are detailed below:

Proposal 1	For	Against	Abstain
Amendment to the Articles of Incorporation	12,164,985	83,465	17,205

Proposal 2	For	Withhold
Jacob Agam	8,719,558	3,546,097
Marc S. Goldfarb	8,719,558	3,546,097

Michael Pearce	8,719,558	3,546,097	

Proposal 3	For	Against	Abstain
Amendment to the 1998 Stock Option Plan	12,053,904	189,046	22,705

Proposal 4	For	Against	Abstain
Appointment of Ernst & Young, LLC	12,241,851	11,459	12,345

ITEM 5. OTHER INFORMATION

Forward Looking Statements

In connection with the "Safe Harbor" provisions of the Private Securities Litigation Reform Act of 1995, readers of this document are advised that this document contains both statements of historical facts and forward-looking statements. Our forward-looking statements include statements related to capital needs, ability to raise capital, and the market for our common stock. Words such as "anticipates," "expects," "intends," "plans," "believes," "seeks," "estimates" and similar expressions are intended to identify forward-looking statements. Our forward-looking statements are subject to certain risks and uncertainties that could cause actual results to differ materially from those indicated by the forward-looking statements.

Our forward-looking statements are based on current expectations, estimates and projections about our industry, management's beliefs, and certain assumptions made by management. These statements are not guarantees of future performance and actual actions or results may differ materially. These statements are subject to certain risks, uncertainties and assumptions that are difficult to predict. We undertake no obligation to update publicly any forward-looking statements as a result of new information, future events or otherwise, unless required by law.

You should carefully consider the risks described in the Company's Form 10-KSB, together with all of the other information included in this Form 10-QSB, before making an investment decision. The risks and uncertainties described are not the only ones we face. If any of the these risks actually occur, it is likely that our business, financial condition or operating results would be harmed. In such case, the trading price of our common stock could decline, and you could lose all or part of your investment.

IENTERTAINMENT NETWORK, Inc.

ITEM 5. OTHER INFORMATION (continued)

Delisting of our Common Stock from Nasdaq's SmallCap Market(TM)

As of the close of business on March 23, 2001, the bid price of the Company's of the Company's common stock as quoted on Nasdaq's SmallCap MarketTM was $0.1875 per share. Because the Company had failed to comply with the $1.00 minimum bid requirement for continued listing of its common stock on the SmallCap Market(TM) as set forth in Marketplace Rule 4310(c)(8)(B), . As of the close of business on March 23, 2001, our minimum bid price was $0.1875 per share. The Company's common stock was delisted from the SmallCap Market(TM) at the opening of business on April 5, 2001. The Company decided not to appeal this determination. Following this delisting, trading in the Company's common stock has been conducted in the over-the-counter markets such as the OTC Bulletin Board(R). The OTCBB is a regulated quotation service that displays real-time quotes and volume information in over-the-counter equity securities. The OTCBB does not impose listing standards or requirements other than regular filings with the SEC. It also does not provide automatic trade executions and does not maintain relationships with quoted issuers. Stocks traded on the OTCBB may face a loss of market makers and a lack of readily available bid and ask prices. These stocks may also experience a greater spread between the bid and ask price and a general loss of liquidity. Certain investors have policies against purchasing or holding OTCBB securities. The delisting and subsequent trading on the OTCBB, have had, and will continue to have, a material adverse effect on both trading volume and market value of our stock. Since delisting, our stock price has traded from a low of $0.05 to a high of $0.28 per share, and the closing price of our stock on August 310, 2001 was $0.065.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(A) EXHIBITS

None

(B) REPORTS ON FORM 8-K

None

IENTERTAINMENT NETWORK, Inc.

SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

IENTERTAINMENT NETWORK, INC.

By: /s/ Michael C. Pearce

Michael C. Pearce
Chief Executive Officer

By: /s/ Allan Kalbarczyk

Allan Kalbarczyk
Chief Accounting Officer