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LIVEWORLD INC
Form 10-Q
November 14, 2001

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

Form 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2001

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission file number 000-26657

LIVEWORLD, INC.

(Exact name of Registrant as specified in its charter)

Delaware

77-0426524

(State or other jurisdiction
of incorporation or organization)

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

307 Orchard City Drive, Suite 110
Campbell, California

95008

(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, including area code: (408) 871-5200

Former name, former address and former fiscal year,
if changed since last report:

1919 S. Bascom Ave.
Campbell, CA 95008.

Indicate by check mark whether the Registrant (1) has filed all reports
required to be filed by Section 13 or 15(d) of the Securities Exchange Act of
1934 during the preceding 12 months (or for such shorter period that the
Registrant was required to file such reports), and (2) has been subject to such
filing requirements for the past 90 days.

Yes No

-

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The number of shares of the Registrant's Common Stock, \$0.001 par value, outstanding at November 14, 2001 was 25,310,872.

LIVEWORLD, INC.

FORM 10-Q

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Part I. FINANCIAL INFORMATION
Item 1. Financial Statements

LIVEWORLD, INC.
UNAUDITED CONDENSED BALANCE SHEETS
(in thousands)

| | September 30, 2001 |
|----------------------------------------------|--------------------------------------|
| | ----- |
| | Assets |
| Current assets: | |
| Cash and cash equivalents | \$ 3,141 |
| Short term investments | - |
| Accounts receivable, net | 1,707 |
| Prepaid expenses and other current assets | 736 |
| | ----- |
| Total current assets | 5,584 |
| Property and equipment, net | 1,639 |
| Other assets | 2,952 |
| Goodwill, net | 232 |
| | ----- |
| Total assets | \$ 10,407 |
| | ===== |
| | Liabilities and Stockholders' Equity |
| Current liabilities: | |
| Notes payable, current portion | \$ 48 |
| Accounts payable | 96 |
| Accrued liabilities | 1,752 |
| Deferred revenue | 781 |
| | ----- |
| Total current liabilities | 2,677 |
| Notes payable, less current portion | - |
| | ----- |
| Total liabilities | 2,677 |
| Stockholders' equity: | |
| Common stock | 25 |
| Additional paid-in-capital | 134,944 |
| Deferred stock based compensation | (66) |
| Notes receivable from stockholders | (174) |
| Accumulated deficit | (126,977) |
| Treasury Stock, 54,687 common shares at cost | (22) |
| | ----- |
| Total stockholders' equity | 7,730 |
| | ----- |
| Total liabilities and stockholders' equity | \$ 10,407 |
| | ===== |

See accompanying notes to the condensed financial statements.

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LIVEWORLD, INC.
 UNAUDITED CONDENSED STATEMENTS OF OPERATIONS
 (In thousands, except per share amounts)

| | Three Months Ended | |
|-----------------------------------------------------------------|-----------------------|-----------------------|
| | September 30, 2001 | September 30, 2000 |
| Revenues: | | |
| Community solutions services | \$ 703 | \$ 925 |
| Event services | 156 | 931 |
| Market research services | 217 | 448 |
| Network services | - | 1,445 |
| | ----- | ----- |
| Total revenue | 1,076 | 3,749 |
| Cost of revenue | 1,109 | 3,973 |
| | ----- | ----- |
| Gross margin | (33) | (224) |
| Operating expenses: | | |
| Product development | 708 | 2,205 |
| Sales and marketing | 379 | 2,760 |
| General and administrative | 904 | 2,981 |
| Restructuring charges | 347 | - |
| Noncash advertising and promotional charges | - | 213 |
| Loss on Sale of Assets | - | - |
| Impairment of Fixed Assets | 2,302 | - |
| Amortization of goodwill | 18 | 171 |
| | ----- | ----- |
| Total operating expenses | 4,658 | 8,330 |
| | ----- | ----- |
| Loss from operations | (4,691) | (8,554) |
| Interest income, net | 65 | 455 |
| | ----- | ----- |
| Net loss | \$ (4,626) | \$ (8,099) |
| | ===== | ===== |
| Basic and diluted net loss per common share | \$ (0.18) | \$ (0.33) |
| | ===== | ===== |
| Weighted average basic and diluted common shares outstanding | 25,282 | 24,892 |
| | ===== | ===== |

See accompanying notes to the condensed financial statements.

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LIVEWORLD, INC.
 UNAUDITED CONDENSED STATEMENTS OF CASH FLOWS

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(In thousands)

| | Ni ----- September 30, 2001 ----- |
|-------------------------------------------------------------------------------|-----------------------------------------------|
| Cash flows from operating activities: | |
| Net loss | \$ (21,875) |
| Adjustments to reconcile net loss to net cash used in operating activities: | |
| Depreciation and amortization | 4,580 |
| Loss on sale of property and equipment | 2,051 |
| Impairment of Fixed Assets | 2,302 |
| Stock compensation expense | (147) |
| Noncash advertising and promotional charges | 2,171 |
| Provision for accounts receivable allowance | (869) |
| Changes in operating assets and liabilities: | |
| Accounts receivable | 1,743 |
| Prepaid expenses and other current assets | 358 |
| Accounts payable | (989) |
| Accrued liabilities | (1,386) |
| Deferred revenue | 35 |
| | ----- |
| Net cash used in operating activities | (12,026) |
| | ----- |
| Cash flows from investing activities: | |
| Purchases of property and equipment | (324) |
| Proceeds from sale of property and equipment | 510 |
| Cash paid for acquisition of Research Connections, Inc., net of cash acquired | - |
| Purchases of short-term investments | - |
| Proceeds from sale of short-term investments | 6,980 |
| Other assets | 1,046 |
| | ----- |
| Net cash provided by investing activities | 8,212 |
| | ----- |
| Cash flows from financing activities: | |
| Proceeds from sale of redeemable preferred stock, net of issuance costs | 25 |
| Proceeds from stock option and warrant exercises | - |
| Proceeds from repayment of stockholders' notes receivable | - |
| Repayment of notes payable | (59) |
| | ----- |
| Net cash (used in)/provided by financing activities | (34) |
| | ----- |
| Net (decrease) in cash and cash equivalents | (3,848) |
| Cash and cash equivalents at beginning of period | 6,989 |
| | ===== |
| Cash and cash equivalents at end of period | \$ 3,141 |
| | ===== |
| Cash paid during the period for interest | \$ 3 |
| | ===== |
| Supplemental disclosure of noncash financing activities: | |
| Common stock issuance for acquisition of Research Connections, Inc. | \$ - |
| | ===== |

See accompanying notes to the condensed financial statements.

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LIVEWORLD, INC. NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION

The condensed financial statements have been prepared by LiveWorld, Inc. pursuant to the rules and regulations of the Securities and Exchange Commission and include the accounts of LiveWorld, Inc. ("LiveWorld" or the "Company"). Certain information and note disclosures, normally included in financial statements prepared in accordance with generally accepted accounting principles, have been condensed or omitted pursuant to such rules and regulations. In the opinion of Management, the unaudited financial statements reflect all adjustments, consisting only of normal recurring adjustments except as described in the footnotes, necessary for a fair presentation of the financial position at September 30, 2001 and the results of operations for the three and nine months ended September 30, 2001 and 2000. The condensed balance sheet at December 31, 2000 has been derived from audited financial statements as of that date. Certain reclassifications have been made to the prior period's financial statements to conform to the September 30, 2001 presentation. These financial statements and notes should be read in conjunction with the Company's audited consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission on April 2, 2001.

The results of operations for the three and nine months ended September 30, 2001 are not necessarily indicative of the results that may be expected for future quarters or the year ending December 31, 2001.

As a result of our restructuring and other expense measurement actions, we have significantly reduced our cash spending and are aggressively managing our expenses relative to our cash on hand. We may need to reduce costs, further increase revenue and/or raise additional funds in order to meet our operating needs, to fund expansion, to develop new or enhance existing services or products, to respond to competitive pressures, or to acquire or invest in complementary businesses, technologies, services or products. In addition, in order to meet our long term liquidity needs, we may need to raise additional funds, establish a credit facility or seek other financing arrangements. Additional funding may not be available on favorable terms or at all.

The Company's financial statements have been prepared assuming that the Company will continue as a going concern. Recovery of the carrying amounts of certain assets, including property, equipment and goodwill, is dependent on continuing as a going concern.

2. NATURE OF OPERATIONS

LiveWorld was incorporated in the state of California in March 1996 and reincorporated in the state of Delaware in July 1999. LiveWorld is a provider of online marketing services for businesses. The Company offers businesses a wide range of services to help them develop and expand online relationships with customers, suppliers and employees. These services include producing online interactive events, conducting online market research, providing outsourced discussion boards, clubs, chat and event feeds and designing fully integrated customized communities. These communities offer services such as moderated chat, home pages, special event production, message boards and online event guides. The Company generates revenues by selling its online marketing services to corporations of various sizes within several industries. LiveWorld has incurred operating losses since inception through September 30, 2001. The Company had an accumulated deficit of \$127.0 million at September 30, 2001. On May 8, 2001, the Company formally changed its name from Talk City, Inc. to LiveWorld, Inc.

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3. ACCRUED LIABILITIES

| Accrued liabilities consist of: | September 30, 2001 | December 31, 2000 |
|---------------------------------------------|-----------------------|----------------------|
| | ----- | ----- |
| | (In thousands) | |
| Accrued compensation and benefits | \$529 | \$ 1,375 |
| Accrued general and administrative expenses | 552 | 562 |
| Accrued sales and marketing expenses | 40 | 321 |
| Accrued rent | 94 | 350 |
| Accrued moderator expenses | 20 | 300 |
| Other accrued liabilities | 517 | 230 |
| | ----- | ----- |
| | \$1,752 | \$ 3,138 |
| | ===== | ===== |

4. SEGMENT REPORTING

The Company has one operating segment because it is not organized by multiple segments for purposes of making operating decisions or assessing performance. This operating segment is currently comprised of three main areas of online business, including (i) community solutions, (ii) live event services, and (iii) market research services. The chief operating decision maker evaluates performance, makes operating decisions and allocates resources based on financial data consistent with the presentation in the accompanying financial statements.

The Company's operations and assets are based in the United States, and substantially all of its revenues have been earned from customers in North America. For the three months ended September 30, 2001, one of the Company's clients was responsible for more than 10% of its revenue. For the three months ended September 30, 2000, one of the Company's clients was responsible for more than 10% of its revenue. No single client was responsible for more than 10% of revenue for the nine months ended September 30, 2001 and 2000. Total receivables from this client were \$300,000 on September 30, 2001. Total receivables from another customer totaled \$208,000 on September 30, 2001.

5. COMPREHENSIVE INCOME (LOSS)

Comprehensive loss for the three and nine months ended September 30, 2001 and 2000 equaled the net loss.

6. NET LOSS PER COMMON SHARE

Diluted net loss per common share does not include the effects of the following potentially dilutive securities as of September 30, 2001 and 2000:

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| | September 30, 2001 | September 30, 2000 |
|---------------------------------------------|-----------------------|-----------------------|
| | ----- | ----- |
| | (In thousands) | |
| Common Stock Options | 6,226 | 4,852 |
| Common Stock Warrants | 991 | 991 |
| Unvested Common Stock Subject to Repurchase | 1 | 86 |
| | ----- | ----- |
| | 7,018 | 5,929 |
| | ===== | ===== |

The average exercise price of the Common Stock Options was \$0.17 and \$9.97 as of September 30, 2001 and September 30, 2000, respectively. The average exercise price of the Common Stock Warrants was \$5.83 as of September 30, 2001 and 2000.

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7. RECENTLY ISSUED ACCOUNTING STANDARDS

In July 2001, the FASB issued Statement of Financial Accounting Standards No. 141 ("SFAS 141"), "Business Combinations" and Statement of Financial Accounting Standards No. 142 ("SFAS 142"), "Goodwill and Intangible Assets."

SFAS 141 addresses the accounting for and reporting of business combinations. SFAS 141 requires that all business combinations be accounted for using the purchase method of accounting for acquisitions and eliminates the use of the pooling-of-interests method. SFAS 141 is effective for all business combinations initiated after June 30, 2001.

SFAS 142 addresses the accounting and reporting for acquired goodwill and other intangible assets. SFAS 142 changes the accounting for goodwill from an amortization method to an impairment-only method. The amortization of goodwill, including goodwill recorded in past business combinations, will cease upon adoption of SFAS 142. For goodwill acquired by June 30, 2001, SFAS 142 is effective for all fiscal years beginning after December 2001. Goodwill and intangible assets acquired after June 30, 2001 will be subject to immediate adoption of SFAS 142. The Company believes the adoption of SFAS 142 will not have a material effect on its financial statements.

8. RESTRUCTURING CHARGES

On July 27, 2001, the Company underwent a restructuring of operations to further reduce expenses. As a result of the restructuring, the Company reduced its total headcount by approximately 25 employees, or approximately 40% of its workforce. The Unaudited Condensed Statement of Operations for the three months ended September 30, 2001 includes a charge of approximately \$347,000 related to the restructuring, consisting entirely of employee severance. Substantially all liabilities related to the restructuring were paid as of September 30, 2001.

9. IMPAIRMENT OF FIXED ASSETS

In light of the restructurings that the Company has recently undertaken,

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the Company recorded an impairment charge of approximately \$2.3 million to reduce the carrying amount of certain fixed assets to their estimated fair value.

10. SUBSEQUENT EVENT

On October 17, 2001, the Company entered into a definitive agreement to terminate the lease on its former headquarters in Campbell, California. As a result of this agreement, LiveWorld reduced the future minimum lease payments by approximately \$13.2 million and its overall expected future obligations associated with the lease by approximately \$18 million. As part of this agreement, the Company agreed to surrender approximately \$1.5 million of its \$1.8 million letter of credit and its \$122,000 deposit, which are currently reported in Other Assets. The Company estimates that it will incur approximately \$960,000 in other charges, which include leasehold improvement write-offs, utility charges, repairs and broker fees associated with the termination of the lease.

On November 2, 2001, the Company announced a further restructuring, reducing its total headcount by two employees. In addition salary reductions were implemented for most employees, including all senior executives. The Company expects to take a charge of approximately \$53,000 for the three month period ended December 31, 2001 related to this restructuring, consisting entirely of employee severance.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

This section contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These forward-looking statements represent our expectations or beliefs concerning future events and include statements regarding our expectations or beliefs that we will not derive revenues from advertising and sponsorships; we will incur additional operating losses for the foreseeable future; product development expenses will decrease as the impact of our restructurings is realized; sales and marketing expenses will decrease; general and administrative costs will decrease; we will continue to evaluate possible acquisitions and investments; and our available cash and cash equivalents will be sufficient to meet our anticipated needs for working capital and capital expenditures for at least the next three to six months. Actual results could differ materially from those projected in the forward-looking statements as a result of known and unknown risk factors and uncertainties, and you should not rely on these forward-looking statements. Such factors may include, but are not necessarily limited to: whether we will continue to incur significant losses; our ability to generate increased revenues; the success of our recent restructurings; the feasibility of incurring more dilution by selling equity; our ability to increase the number of online marketing services clients, expand our online marketing services offerings and effectively implement these services; and attracting and retaining key personnel. In addition to the foregoing, please see the section in this report entitled "Risk Factors That May Affect Results of Operations and Financial Condition" for a description of other factors that might cause actual results to differ from those projected in the forward-looking statements herein. LiveWorld does not undertake any obligation to publicly update any forward-looking statement to reflect events or circumstances after the date on which any such statement is made or to reflect the occurrence of unanticipated events.

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Overview

We provide online community-based relationship marketing and support services for businesses to market to and support their customers and employees. From inception through September 2001, our operating activities have primarily been focused on:

- o developing the quality environment of our services;
- o building sales momentum and developing programs and content;
- o developing a comprehensive computer software and hardware infrastructure;
- o recruiting personnel; and
- o raising capital.

From inception through early 2001, we also owned and operated a consumer destination site, www.talkcity.com. During that period we also focused on developing the Talk City brand, expanding the site's audience and usage of services, establishing operating relationships with our network participants and generating advertising revenue on the Talk City site.

Substantially all of our revenues are fee based and derived from the sale of our online marketing services. Our online marketing services include consulting on the use and implementation of online communities, designing, operating and moderating customized communities, producing online events, conducting online market research and facilitating online meetings. These services help businesses develop and expand online relationships with customers, suppliers and employees. Revenues derived from online marketing services are recognized ratably over the term of the contract period, which coincides with when the services are performed, provided that the collection of the receivable is probable.

Cost of revenues includes payroll and related expenses associated with content and production personnel who conduct online market research, implement customized communities, and produce online

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events. Also included are moderator costs, Internet communication charges and server-related costs to support our Web site.

Operating expenses consist primarily of product development, sales and marketing, general and administrative and interest expenses. Product development expenses consist primarily of salaries, payroll taxes and benefits and expenditures related to software development, quality engineering and product marketing. Sales and marketing expenses consist primarily of advertising and promotion costs, salaries, commissions and other related costs of sales and marketing personnel and program expenses, public relations costs and other marketing expenses. General and administrative expenses consist of salaries, payroll taxes and benefits and related costs for general corporate functions, including executive management, finance, human resources, facilities, legal and fees for other professional services.

Sales and marketing expenses exclude noncash advertising and promotional charges related to our advertising on the NBC television network and in magazines owned by Hearst along with promotional services attributable to the operating agreements with NBC. These advertising activities are paid for through

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noncash in-kind investments. This in-kind program includes \$7.2 million of television commercials and print ads valued at rates discounted from the rate card to be incurred from 1998 through 2001. These amounts were determined based on the fair value of our common stock and warrants exchanged for the services received. At September 30, 2001, all of the Company's non-cash in-kind investments were fully amortized.

We incurred losses of \$1.3 million in 1996, \$6.4 million in 1997, \$15.7 million in 1998, \$40.1 million in 1999, \$41.6 million in 2000, and \$21.9 million through the first nine months of 2001. These losses include noncash advertising and promotional charges of \$19.6 million through September 30, 2001. At September 30, 2001, we had an accumulated deficit of \$127.0 million. We anticipate that we will incur additional operating losses for the foreseeable future.

On July 27, 2001, the Company underwent a restructuring of operations to further reduce expenses. As a result of the restructuring, the Company reduced its total headcount by 25 employees, or approximately 40% of its workforce. In addition the Company implemented an across-the-board salary reduction program. The Unaudited Condensed Statement of Operations for the three months ended September 30, 2001 includes a charge of approximately \$347,000 for the quarter ended September 30, 2001 related to the restructuring, consisting entirely of employee severance.

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Results of Operations

The following table sets forth, for the periods indicated, the percentage of net revenue represented by certain items reflected in LiveWorld's Condensed Financial Statements:

| | Three Months Ended September 30, | | Nine Mon Septem |
|----------------------------------------------|-------------------------------------|-------|--------------------|
| | 2001 | 2000 | 2001 |
| | ----- | ----- | ----- |
| Net revenue | 100 % | 100 % | 100 % |
| Cost of revenue | 103 | 106 | 155 |
| | ----- | --- | ----- |
| Gross margin | (3) | (6) | (55) |
| Operating expenses: | | | |
| Product development | 66 | 59 | 85 |
| Sales and marketing | 35 | 74 | 55 |
| General and administrative | 84 | 80 | 126 |
| Restructuring charges | 32 | -- | 22 |
| Non-cash advertising and promotional charges | -- | 6 | 55 |
| Loss on Sale of Assets | -- | -- | 46 |
| Impairment of Fixed Assets | 214 | -- | 58 |
| Amortization of goodwill | 2 | 5 | 64 |
| | ----- | ----- | ----- |
| Total operating expenses | 433 | 222 | 511 |
| | ----- | ----- | ----- |
| Operating loss | (436) | (228) | (566) |

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| | | | |
|----------------------|--------|--------|--------|
| | 6 | 12 | 10 |
| Interest income, net | ----- | ----- | ----- |
| Net loss | (430)% | (216)% | (556)% |
| | ==== | ==== | ==== |

Net Revenue. Net revenue decreased 71% to approximately \$1.1 million for the three months ended September 30, 2001, from \$3.7 million for the three months ended September 30, 2000, a decrease of approximately \$2.6 million. This decrease was primarily the result of decreased advertising sales as the Company sold off the advertising business in May 2001. In addition, revenue for the fee based services, particularly live events and market research, was also lower as a result of the more difficult economic conditions. Revenue for certain fee-based services such as consulting, moderation and discussion boards increased. For the nine months ended September 30, 2001, net revenue decreased 67%, to \$3.9 million, from \$11.8 million for the nine months ended September 30, 2000. This decrease is primarily the result of lower advertising revenue as well as lower fee-based services as a result of a slowdown in marketing spending by clients in response to the changing economic conditions. This decrease was partially offset by revenue of \$338,000 from the one-year operating agreement executed in connection with the sale of the consumer unit and associated web site, www.talkcity.com. Substantially all of LiveWorld's revenue is derived within North America.

Cost of Revenue. Cost of revenue was \$1.1 million, or 103% of total revenue, for the three months ended September 30, 2001, compared to \$4.0 million, or 106% of total revenue, for the three months ended September 30, 2000. Cost of revenue decreased in absolute dollars by \$2.9 million compared to the same period in the prior year, which was primarily due to lower personnel-related costs resulting from the reductions in headcount stemming from the recent restructurings. Cost of revenue was \$6.1 million, or 155% of total revenue, for the nine months ended September 30, 2001, compared to \$11.7 million, or 99% of total revenue, for the nine months ended September 30, 2000. Cost of revenue decreased in absolute dollars by \$5.6 million compared to the same period in the prior year, primarily due to lower personnel-related costs resulting from the headcount reductions that were part of the recent restructurings.

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Product Development. Product development expenses for the three months ended September 30, 2001 and 2000 were approximately \$708,000, or 66% of total revenue, and \$2.2 million, or 59% of total revenue, respectively. Product development expenses for the nine months ended September 30, 2001 and 2000 were approximately \$3.4 million, or 85% of total revenue, and \$5.9 million, or 50% of total revenue, respectively. The decrease in absolute dollars was primarily attributable to lower personnel-related costs as a result of the Company's restructurings. LiveWorld expects that product development expenses will decrease slightly for the foreseeable future as the impact of the July 2001 restructuring is more fully realized.

Sales and Marketing. Sales and marketing expenses for the three months ended September 30, 2001 and 2000 were approximately \$379,000, or 35% of total revenue, and approximately \$2.8 million, or 74% of total revenue, respectively. Sales and marketing expenses for the nine months ended September 30, 2001 and 2000 were approximately \$2.2 million, or 55% of revenue, and \$12.3 million, or 105% of revenue, respectively. The decrease in absolute dollars in sales and marketing expenses for the quarter and for the first nine months of 2001 was primarily attributable to a decrease in online advertising expenses and by a

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decrease in sales personnel and associated expenses. LiveWorld expects that sales and marketing expenses will remain constant or decrease slightly in absolute dollars in the foreseeable future.

General and Administrative. General and administrative expenses for the three months ended September 30, 2001 and 2000 were approximately \$904,000, or 84% of total revenue, and \$3.0 million, or 80% of total revenue, respectively. General and administrative expenses for the nine months ended September 30, 2001 and 2000 were approximately \$5.0 million, or 126% of total revenue, and \$8.8 million, or 75% of total revenue, respectively. The expenses for the nine months ended September 30, 2001 include the result of a realized gain of \$250,000 from the sale of the Company's minority investment in Matchnet, which had previously been written down to \$0. The decrease in general and administrative costs was also attributable to a reduction in headcount. LiveWorld expects that general and administrative costs will decrease in the future, as the Company realizes the benefits of the July 2001 restructuring and the lower costs resulting from the smaller office space for our headquarters.

Non-cash Advertising and Promotional Charges. Noncash advertising and promotional charges for the three months ended September 30, 2001 and 2000 were \$0, and \$213,000, or 6% of total revenue, respectively. For the nine months ended September 30, 2001 and 2000, noncash advertising and promotional charges were \$2.2 million, or 55% of total revenue, and \$1.4 million, or 12% of total revenue, respectively. The increase in noncash and promotional charges for the nine-month period ended 9/30/01 was primarily due to increased amortization of advertising provided under the Hearst advertising agreement. All noncash in-kind investments were fully amortized as of June 30, 2001.

Restructuring. Pursuant to the July 2001 restructuring, and the associated reduction in workforce of 25 employees, or approximately 40% of the total workforce, the Unaudited Condensed Statement of Operations for the three months ended September 30, 2001 includes a charge of approximately \$347,000. This charge is comprised of costs for employee severance. Substantially all liabilities related to the restructuring were paid as of September 30, 2001. Such restructuring charges represent 32% of revenue for the three months ended September 30, 2001. There was no similar charge in the same period in 2000. We cannot be certain that additional expenditures or charges will not be required in the future. In addition, LiveWorld cannot be certain that its restructuring will be successfully accepted or adopted by the market, including its current investors or securities analysts, the Company's current or potential business or consumer clients, the Company's current or potential network participants, or its current or potential advertisers. If the restructuring is not accepted or adopted, our business could suffer.

Amortization of Goodwill. For the three months ended September 30, 2001, the Company recorded a charge of \$18,000 for the amortization of goodwill. This compares to a charge of \$171,000 for the three months ended September 30, 2000. For the nine months ended September 30, 2001, and September 30, 2000, including an impairment charge of approximately \$2.3 million in the quarter ended June 30, 2001, amortization of goodwill was \$2.5 million and \$513,000, respectively.

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Loss on Sale of Assets. For the nine months ended September 30, 2001, the Company recorded a charge of \$1.8 million in connection with the sale of its consumer unit, its web site, www.talkcity.com, and the associated server infrastructure. There was no similar charge for the nine months ended September 30, 2000.

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Impairment of Fixed Assets. In light of the restructurings that the Company has recently undertaken the Company recorded an impairment charge of approximately \$2.3 million, to reduce the carrying amount of certain fixed assets to their estimated fair values. There was no similar charge for the nine months ended September 30, 2000.

Interest Income, Net. Interest income, net, includes income from LiveWorld's cash and investments and expenses related to its equipment financing obligations. Interest income, net for the three months ended September 30, 2001 and 2000 was approximately \$65,000 and \$455,000, respectively. Interest income, net for the nine months ended September 30, 2001 and 2000 was approximately \$409,000 and \$1.8 million, respectively. The reduction in interest income, net, resulted from declining interest income on lower cash, cash equivalent and short-term investment balances, as well as lower interest rates earned on balances.

Income Taxes. FASB Statement No. 109 provides for the recognition of deferred tax assets if realization of such assets is more likely than not. Based upon historical operating performance and the reported cumulative net losses in all prior years, LiveWorld has provided a full valuation allowance against its net deferred tax assets. The Company evaluates the realizability of the deferred tax assets on a quarterly basis.

Liquidity and Capital Resources

Since our inception in March 1996, we have financed our operations primarily through the private placement of our preferred stock, our initial public offering in July 1999 and, to a lesser extent, through equipment financing. As of September 30, 2001, we had approximately \$3.1 million in cash and cash equivalents.

Our capital requirements depend on numerous factors, including market acceptance of our services, the resources we allocate to our product development, system infrastructure, marketing and selling our services and other factors. Additionally, we will continue to evaluate possible acquisitions of and investments in complementary businesses, technologies, services or products and to expand our sales and marketing programs. As a result of our restructuring and other expense measurement actions we have significantly reduced our cash spending and are aggressively managing our expenses relative to our cash on hand. We may need to raise additional funds in order to meet our operating needs, to fund expansion, to develop new or enhance existing services or products, to respond to competitive pressures, or to acquire or invest in complementary businesses, technologies, services or products. In addition, in order to meet our long term liquidity needs, we may need to raise additional funds, establish a credit facility or seek other financing arrangements. Additional funding may not be available on favorable terms or at all.

Net cash used in operating activities was approximately \$12.0 million and \$25.4 million for the nine months ended September 30, 2001 and 2000, respectively. Cash used in operating activities in each of these periods was primarily the result of net operating losses excluding the effects of non-cash advertising expenses and depreciation and amortization.

Net cash provided by investing activities was approximately \$8.2 million and \$20.2 million for the nine months ended September 30, 2001 and 2000, respectively. Cash provided by investing activities for the nine months ended September 30, 2001 was the primarily the result of sales of short-term investments and the proceeds from the sale of assets, partially offset by purchases of equipment. Cash provided by investing

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activities for the nine months ended September 30, 2000 consisted of approximately \$33.4 million in sales of short-term investments partially offset by approximately \$6.4 million in purchases of equipment, approximately \$4.9 million in purchases of short-term investments and \$1.5 million placed into an escrow fund for an employment agreement with the former sole shareholder of RCI.

Net cash used in financing activities was approximately \$34,000 for the nine months ended September 30, 2001. Net cash provided by financing activities was \$1.1 million for the nine months ended September 30, 2000. Net cash used in financing activities for the nine months ended September 30, 2001 consisted of principal payments on notes payable. Net cash provided by financing activities for the nine months ended September 30, 2000 consisted primarily of net proceeds of approximately \$1.2 million from stock option and warrant exercises partially offset by principal payments on notes payable.

As of September 30, 2001, the Company's principal commitments consisted of obligations outstanding under operating leases. In October 1999, the Company signed a nine-year, three and one-half month lease for a new 56,000 square foot corporate headquarters in Campbell, California, which commenced on December 15, 1999 and which has since been terminated (as further discussed in Note 9 to the financial statements and as discussed below). As security for the lease, the Company provided a \$2,100,000 letter of credit, which was to have been reduced by \$300,000 per year after every twelve months through December 14, 2005, provided no default has occurred. As of September 30, 2001, a \$1,800,000 certificate of deposit with a one-year maturity was held as collateral by a bank for guarantee of the letter of credit. The certificate of deposit is included in Other Assets. Future minimum lease payments under all non-cancelable operating leases totaled approximately \$13.9 million as of September 30, 2001. As described in the Note 9 to the financial statements, on October 8, 2001, LiveWorld entered into a definitive agreement to terminate the lease. As a result of this agreement, LiveWorld reduced the future minimum lease payments by approximately \$13.2 million, and the overall anticipated obligation associated with the lease by approximately \$18 million.

Risk Factors That May Affect Results of Operations and Financial Condition

LiveWorld may need substantial additional capital to fund continued business operations in 2002 and cannot be sure that additional financing will be available

LiveWorld may require additional capital to fund its business operations. The rate at which LiveWorld utilizes its capital is affected by the operational and developmental costs incurred and the extent to which LiveWorld becomes profitable on a cash-flow basis. To date, LiveWorld has not been profitable on a cash-flow basis and substantial capital has been used to fund the operating losses. LiveWorld incurred losses of \$1.3 million in 1996, \$6.4 million in 1997, \$15.7 million in 1998, \$40.1 million in 1999, \$41.6 million in 2000, and \$21.9 million through the first nine months of 2001. LiveWorld cannot assure you that it will operate at or near levels that are necessary to become profitable on a cash-flow basis. Since inception, LiveWorld has experienced negative cash flow from operations and expects to experience significant negative cash flow from operations for the near future.

LiveWorld continues to evaluate alternative means of financing to meet its needs. We may need to raise additional funds in order to meet our operating needs, to fund expansion, to develop new or enhance existing services or products, to respond to competitive pressures, or to acquire or invest in complementary businesses, technologies, services or products. In addition, in

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order to meet our long term liquidity needs, we may need to raise additional funds, establish a credit facility or seek other financing arrangements. Additional funding may not be available on favorable terms or at all.

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If LiveWorld is not able to obtain such capital, it may take actions to conserve its cash balances, including significantly reducing its operating expenses, downsizing its corporate headquarters staff and closing existing facilities, all of which could have a material adverse effect on its business, financial condition and LiveWorld's ability to reduce losses or generate profits. For example, in September 2000, December 2000, March 2001, May 2001 and July 2001, LiveWorld underwent separate restructurings.

In the past, LiveWorld has funded its operating losses and capital expenditures through proceeds from equity offerings and, to a lesser extent, proceeds from debt financing and equipment leases. Changes in equity markets in the past year have adversely affected LiveWorld's ability to raise equity financing and have adversely affected the markets for debt financing and equipment leasing for companies with a history of losses such as LiveWorld. If LiveWorld raises additional funds through the issuance of equity, equity-linked or debt securities, those securities may have rights, preferences or privileges senior to those of the rights of its common stock and, in light of LiveWorld's current market capitalization, LiveWorld's stockholders may experience substantial dilution.

LiveWorld's common stock was delisted from Nasdaq, which could result in a decrease in liquidity of our stock

LiveWorld common stock was delisted from trading on the Nasdaq National Market due to a failure to comply with the required \$1.00 minimum bid price, and it now trades on the over-the-counter bulletin board market under the symbol LVWD.OB. This delisting could result in significantly decreased liquidity for LiveWorld stock, making it much more difficult to purchase or sell LiveWorld stock or obtain accurate quotations as to the price of the Company's securities.

LiveWorld's stock price has traded far below the initial offering price and could remain at this low price, which could affect its ability to acquire other companies, leave it vulnerable to take over attempts and result in securities class action litigation

Since LiveWorld's initial public offering in July 1999, the market price of its common stock has traded at or significantly below the initial offering price of \$12.00 per share, and has traded below \$1.00 continuously since October 2000. If the price per share does not increase, the Company's investors may incur a substantial loss on their investment. In addition, the sustained depression of the market price of its common stock may hamper the Company's ability to conduct business, and in particular, could make it more difficult to pursue acquisitions of potential complementary businesses, leaving it vulnerable to a hostile takeover and result in securities class action litigation.

LiveWorld's stock price may continue to be depressed due to broad economic, market and industry factors beyond its control

LiveWorld's stock price may continue to be depressed due to a variety of factors, including factors beyond its control. These broad market and industry factors could continue to harm the market price of its Common Stock, regardless of the Company's performance. These factors include:

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- o announcements of or new programming by the Company or its competitors, including the Company's announcement of its restructurings;
- o conditions or trends in the Internet services industry;
- o changes in the market valuations of Internet companies;
- o additions or departures of key personnel; and
- o sales of substantial amounts of its Common Stock or other securities in the open market.

General political and economic conditions, such as recession or interest rate or currency rate fluctuations, also could harm the market price of the Company's Common Stock.

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If the recent restructurings of LiveWorld, designed to increase awareness of and refocus the Company's business on online marketing services, are not accepted, the Company's results of operations may decrease and the business may be adversely affected

In June 2000, the Company underwent a restructuring of operations to more clearly focus LiveWorld as an online marketing services provider, pursuant to which it reorganized its business into four main areas of operations, which include online live events services, market research services, community solutions, and network and syndication services. As a result of the June restructuring, the Company reduced its total headcount by 35 employees, or approximately 15% of its total workforce. In December 2000, the Company underwent a separate restructuring to further align the Company to sell and implement fee-based services. As a result of the December restructuring, the Company reduced its total headcount by 55 employees, or 30% of the total workforce. On March 16, 2001, the Company announced a further restructuring to recognize changes in the economic environment and complete its transition to a 100% fee-based marketing services model, including a reduction of its total headcount by 30%. On May 18, 2001 the Company announced a further restructuring and reduced its headcount by 21 employees, or 25% of the workforce. On July 27, 2001, LiveWorld further reduced headcount by 25 employees, or 40% of the workforce. If the restructurings do not increase awareness or generate sales of the Company's online marketing services at the level it anticipates, or at all, the Company's management and other resources will have been expended with no increase in revenues, which could decrease its results of operations, and otherwise adversely affect the business.

The reductions in workforce related to the restructurings could result in market uncertainty and decreased employee morale

The reductions in LiveWorld's workforce as a result of the restructurings could result in market concerns about the operations of the Company. Workforce reductions sometimes result in operational concerns about a company in the market and, while the Company's reductions were in connection with the restructurings, the Company may not be able to respond adequately to reports of securities analysts or the market. In addition, the Company must take the appropriate steps to sustain and prevent any decrease in employee morale due to the reductions in workforce.

Fluctuations in quarterly operating results may cause the stock price to decline

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The Company's operating results in one or more future quarters may be below the expectations of its investors, and as a result the price of its Common Stock could decline. LiveWorld expects that its quarterly operating results will continue to fluctuate significantly and be affected by many factors, the more important of which include:

- o general economic conditions;
- o its dependence on increased online marketing services revenues;
- o the length of its sales cycle;
- o its ability to increase its audience of loyal, engaged clients and consumers;
- o management of growth; and
- o potential technical difficulties or system down time affecting the Internet generally or the Company specifically.

These factors are described in more detail in the risk factors described below. Many of these factors are beyond the Company's control.

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LiveWorld's growth will depend on its ability to increase its online marketing services revenues

LiveWorld has derived, and will continue to derive, a substantial portion of its revenues from the sale of online marketing services. If the Company does not continue to develop online marketing services revenues, its revenues may not meet its expectations or may decline and LiveWorld will need to revise its revenue model to reflect this. The Company's growth and future success will depend on its ability to increase the number of its online marketing services clients, expand its online marketing services offerings, effectively implement these services and increase the average revenue per project and per client. LiveWorld's ability to generate significant online marketing services revenues will also depend, in part, on its ability to create new online marketing services offerings without diluting the value of its existing programs.

Current and potential competitors could decrease LiveWorld's market share and harm its business

Increases in the number of companies competing for the attention and spending of businesses, could result in price reductions, reduced margins or loss of market share, any of which could decrease LiveWorld's revenues and contribute to the Company not achieving profitability and failing. The barriers to entry in the Internet marketing services market are low and the Company expects the number of its competitors to increase. LiveWorld competes for business clients with numerous companies, including Prospero Technologies Corporation, Yahoo Broadcast, PeopleLink and Participate.com.

Year to year revenue growth in past periods may not be indicative of future growth

The Company achieved significant revenue growth in 2000 as compared to 1999, although the Company has experienced sequential declines in quarterly revenue from the second quarter of 2000 through the third quarter of 2001. Accurate predictions of future growth are difficult because of its limited operating history as well as of the rapid changes in its markets as a result of increased competition, evolving technology and clients' business requirements. Accordingly, current and potential investors should not rely on past revenue growth as a prediction of future growth.

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LiveWorld's variable sales cycle may cause the Company to incur substantial expenses and expend management time without generating the corresponding revenues, which would slow its cash flow

LiveWorld's sales cycle varies in length of time. During the sales cycle, the Company may expend substantial funds and management resources without generating corresponding revenues. The time between the date of its initial contact with a potential client and the execution of a contract with that client typically ranges from a few weeks for smaller agreements to several months for larger agreements. Its sales cycle is also subject to delays as a result of factors over which the Company has little or no control, including the following:

- o budgetary constraints;
- o internal acceptance reviews;
- o the success and continued internal support of online marketing services clients; and
- o the possibility of cancellation or delay of projects by online marketing services clients.

The length and uncertainty of its sales cycle also may harm its billing and collection efforts. The length of the sales cycle might prevent the Company from rendering its services on a more accelerated basis, which slows its cash flow and reduces its ability to fund the expenditures the Company incurs during the sales cycle.

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LiveWorld's growth will depend upon the acceptance of the Internet as an attractive medium for its online marketing services clients

LiveWorld's current and potential business clients must accept the Internet as an attractive and sustainable substitute medium for the traditional methods to which they are accustomed. The market for online marketing services may not continue to develop and may not be sustainable. The Internet, as an online marketing services solution, has not been available for a sufficient period of time for the Company to gauge its effectiveness as compared with traditional methods, such as trade shows, phone and mail surveys and video conferencing.

LiveWorld's paid moderators could be viewed as employees rather than independent contractors, which could subject the Company to adverse tax and employee benefit consequences

LiveWorld treats its paid moderators, consisting of approximately 229 individuals as of September 30, 2001, as independent contractors. The Company's paid moderators sign independent contractor agreements and are paid a flat monthly fee or per hour. Laws governing the distinction between independent contractors and employees are not entirely clear, and some jurisdictions may rule that the Company's paid moderators are employees rather than independent contractors. If this happens, the Company could be subject to substantial tax and employee benefit liabilities as well as other penalties.

LiveWorld's volunteer community leaders could be viewed as employees, which would substantially increase its operating expenses

If the Company's active volunteer community leaders, consisting of approximately 620 individuals as of September 30, 2001, were viewed as employees, LiveWorld could be subject to payment of back wages and other

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penalties, and its operating expenses could substantially increase. From time to time, former volunteers of other companies have filed complaints with the Labor Department and class action lawsuits claiming they were treated like employees and should have been paid.

LiveWorld's chief executive officer and chief community officer are critical to its business, and they may not remain with the Company in the future

LiveWorld's future success will depend, to a significant extent, on the continued services of Peter Friedman, its Chairman of the Board and Chief Executive Officer, and Jenna Woodul, its Chief Community Officer. The loss of the services of Mr. Friedman or Ms. Woodul could cause the Company to incur increased operating expenses and divert other senior management time in searching for their replacements. The loss of their services could also harm its reputation, as its business clients and advertisers and network participants could become concerned about its future operations. The Company does not have long-term employment agreements with Mr. Friedman or Ms. Woodul, and the Company does not maintain any key person life insurance policies.

LiveWorld must continually attract and retain its sales, engineering and other key personnel or the Company will be unable to execute its business strategy

LiveWorld's future success also will depend on its ability to attract, retain and motivate highly skilled sales, engineering and other key personnel. Competition for such personnel is intense, and the Company may be unable to successfully attract, integrate or retain sufficiently qualified personnel.

LiveWorld may be unable to consummate potential acquisitions or investments or successfully integrate them with its business, which could slow its growth strategy

As part of its strategy to expand its online marketing services if resources permit, the Company may acquire or make investments in complementary businesses, technologies, services or products if appropriate

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opportunities arise. LiveWorld may be unable to identify suitable acquisition or investment candidates at reasonable prices or on reasonable terms. Additionally, regardless of whether suitable candidates are available, the Company may be unable to consummate future acquisitions or investments, in part due to the low market price if its stock and the limited availability of cash, which could harm the Company's growth strategy. If LiveWorld does acquire a company or make other types of acquisitions, the Company could have difficulty integrating the acquired services, personnel or technologies. These difficulties could disrupt its ongoing business, distract its management and employees, and increase its expenses.

System failures or slow downs would harm the Company's reputation and thus reduce its attractiveness to its current and future business clients, users, network participants and advertisers

System failures would harm the Company's reputation and reduce its attractiveness to businesses, network participants and advertisers. LiveWorld's ability to attract potential business clients, network participants and advertisers to promote its brand will depend significantly on the performance of its network infrastructure. In addition, a key element of its strategy is to

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effectively perform its online marketing services for its business clients in order to increase the usage of its online marketing services by business clients. Increased usage of the Company's online marketing services could strain the capacity of its infrastructure, resulting in a slowing or outage of its services and reduced traffic to its Web sites. LiveWorld may be unable to improve its technical infrastructure in relation to increased usage of its services. In addition, the Company's users depend on Internet service providers, online service providers and other Web site operators for access to its Web sites. Many of these providers and operators have also experienced significant outages in the past, and they could experience outages, delays and other difficulties due to system failures unrelated to the Company's systems.

LiveWorld's communications and other computer hardware operations are subject to disruptions which are out of its control and for which the Company may not have adequate insurance

A disaster could severely damage the Company's ability to deliver its products and services to its customers. LiveWorld depends on its ability to maintain and protect its facilities, which include communications hardware and other computer hardware operations. These operations, which are separate from its principal offices, are located at facilities in San Jose, California. San Jose may exist on or near a known earthquake fault zone. In addition, earlier this year, California experienced power outages due to a shortage in the supply of power within the state. If they resume, power outages could interrupt our operations and also the operations of our vendors and subcontractors within the state of California. Although the facilities in which we host our computer systems are designed to be fault tolerant, the systems are susceptible to damage from fire, floods, earthquakes, power loss, telecommunications failures, and similar events, such as computer viruses or electronic break-ins, any of which could disrupt its Web sites. Although we maintain general business insurance against fires, floods and some general business interruptions, there can be no assurance that the amount of coverage will be adequate in any particular case.

LiveWorld must keep pace with rapid technological change and the intense competition of the Internet industry in order to succeed

LiveWorld's market is characterized by rapidly changing technologies, frequent new product and service introductions and evolving industry standards. The growth of the Internet and intense competition in the industry exacerbate these market characteristics. In addition, in recent months many Internet-related companies, similar to LiveWorld, have consolidated or restructured in order to remain competitive within the Internet industry. To succeed, LiveWorld will need to effectively implement its restructurings, integrate the various software programs and tools required to enhance and improve its service offerings and manage its business. Any enhancements or new services or features must meet the requirements of its current and prospective clients and must achieve significant market acceptance. The Company's success also will depend on its ability to adapt to rapidly changing technologies by continually improving the performance features and reliability of its services. The Company may experience difficulties that could delay or prevent the successful

development, introduction or marketing of new services. LiveWorld could also incur substantial costs if it needs to modify its services or infrastructure to adapt to these changes.

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Changes in government regulation could limit LiveWorld's Internet activities or result in additional costs of doing business on the Internet

Although few laws or regulations exist that specifically regulate communications on the Internet, LiveWorld expects more stringent laws and regulations to be enacted due to the popularity and use of the Internet. Any new legislation or regulations or the application of existing laws and regulations to the Internet could limit user volume and increase operating expenses. In addition, the application of existing laws to the Internet is uncertain and may take years to resolve and could expose the Company to substantial liability for which LiveWorld might not be indemnified by the content providers or other third parties. Existing laws and regulations currently, and new laws and regulations are likely to address a variety of issues, including the following:

- o user privacy and expression;
- o the rights and safety of children;
- o information security;
- o the convergence of traditional channels with Internet commerce; and
- o taxation and pricing.

If Internet Service Providers become regulated in a manner similar to long distance telephone carriers, Internet growth may slow, which would cause the Company's revenues to decrease

If Internet growth slows due to proposals to regulate Internet Service Providers in a way similar to long distance telephone carriers, LiveWorld's volume and the demand for its online marketing services would decline, causing its revenues to decrease. The use of the Internet has burdened the existing telecommunications infrastructure and led to interruptions in phone service in areas with high Internet use. Several telecommunications companies and local telephone carriers have petitioned the Federal Communications Commission to regulate Internet Service Providers and online service providers in a manner similar to long distance telephone carriers and to impose access fees. If this were to occur, the costs of communicating on the Internet could increase substantially, potentially slowing the growth in use of the Internet.

LiveWorld may be subject to liability for publishing or distributing content over the Internet

LiveWorld may be subject to claims relating to content that is published on or downloaded from its Web sites. The Company also could be subject to liability for content that is accessible from its Web sites through links to other Web sites. Although LiveWorld carries general liability and multimedia liability insurance, the Company's insurance may not cover potential claims of this type or may not be adequate to cover all costs incurred in defense of potential claims or to indemnify the Company for all liability that may be imposed. In addition, any claims like this, with or without merit, would result in the diversion of its financial resources and management personnel.

LiveWorld may be liable for misappropriation by others of its users' personal information

If third parties were able to penetrate the Company's network security or otherwise misappropriate its users' personal information, LiveWorld could be subject to liability. These could include claims for impersonation or other similar fraud claims.

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LiveWorld may be liable for its use or sale of its users' personal information

LiveWorld currently uses its users' personal information internally to determine how to improve its services, applications and features, and to target its advertisements and communications. The Company also uses this information externally to provide its advertisers with the demographics of its user base. LiveWorld may, in the future, sell its user information on an aggregate, not individual, basis. LiveWorld could be subject to liability claims by its users for misuses of personal information, such as for unauthorized marketing purposes. In addition, the Federal Trade Commission has previously investigated various Internet companies regarding their use of personal information. The Company could incur additional expenses if new regulations regarding the use of personal information are introduced or if its privacy practices are investigated.

Possible infringement of LiveWorld's intellectual property rights by third parties could substantially increase its operating expenses and harm its ability to conduct business

Other parties may assert claims of infringement of intellectual property or other proprietary rights against LiveWorld, and in fact, the Company has been subject to such claims in the past. These claims, even if without merit, could require the Company to expend significant financial and managerial resources. Furthermore, if claims like this were successful, LiveWorld might be required to change its trademarks, alter its content or pay financial damages, any of which could substantially increase its operating expenses. The Company also may be required to obtain licenses from others to refine, develop, market and deliver new services. LiveWorld may be unable to obtain any needed license on commercially reasonable terms or at all, and rights granted under any licenses may not be valid and enforceable. LiveWorld has been subject to claims and expects to be subject to legal proceedings and claims from time to time in the ordinary course of its business, including claims of alleged infringement of trademarks and other intellectual property rights of third parties by the Company and its licensees.

If LiveWorld raises additional capital through the issuance of new securities, existing stockholders will incur additional dilution

In order to meet its liquidity needs, the Company may need to raise additional capital. However, if the Company raises additional capital through the issuance of new securities, its stockholders will be subject to additional dilution. In addition, any new securities issued may have rights, preferences or privileges senior to those securities held by the Company's current stockholders.

LiveWorld's undesignated Preferred Stock may inhibit potential acquisition bids for the Company, cause the market price for its Common Stock to fall and diminish the voting rights of the holders of its Common Stock

If the Company's Board of Directors issues Preferred Stock, potential acquirers may not make acquisition bids for the Company, the Company's stock price may fall and the voting rights of existing stockholders may diminish as a result. The Board has the authority to issue up to 5,000,000 shares of Preferred Stock in one or more series. The Board can fix the price, rights, preferences, privileges and restrictions of the Preferred Stock without any further vote or action by the stockholders.

LiveWorld has anti-takeover defenses that could delay or prevent an acquisition of the Company

Provisions of LiveWorld's Certificate of Incorporation, Bylaws and Delaware

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law could make it more difficult for a third party to acquire the Company, even if doing so would be beneficial to the stockholders

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Item 3. Quantitative and Qualitative Disclosures about Market Risk

LiveWorld's exposure to market risk for changes in interest rates relates primarily to its investment portfolio. The Company does not use derivative financial instruments in its investment portfolio. LiveWorld places its investments with high quality issuers and, by policy, limits the amount of credit risk exposure to any one issuer. The Company is averse to principal loss and ensures the safety and preservation of its invested funds by limiting default, market and reinvestment risk. LiveWorld classifies its cash equivalents and short-term investments as "fixed rate" if the rate of return on such instruments remains fixed over their term. These "fixed rate" instruments include fixed rate commercial paper, corporate notes, and market auction preferred securities. We classify our cash equivalents and short-term investments as "variable rate" if the rate of return on such investments varies based on the change in a predetermined index or set of indices during their term. These "variable rate" investments primarily include money market accounts held at various securities brokers and banks. The table below presents the amounts and related weighted average interest rates of the Company's investment portfolio at September 30, 2001:

| | Average Interest Rate | Book Value | Fair Value |
|----------------------------|--------------------------|----------------|---------------|
| | ----- | ----- | ----- |
| | | (In thousands) | |
| Cash and Cash equivalents: | | | |
| Fixed rate | 2.85% | \$1,138 | \$1,138 |
| Variable rate | 3.06% | 2,003 | 2,003 |

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

During Q3, 2001 the Company filed a lawsuit in San Jose, CA against MatchNet PLC and SocialNet, Inc., to collect money the Company believes is owed in the form of past due invoices and under a 1999 operating agreement between the Company and SocialNet, obligations which LiveWorld contends MatchNet expressly agreed to perform. The total amount of money the Company is seeking is approximately \$1.1 Million. The Company, although confident in the merits of its claim, by definition cannot be assured of prevailing in this legal action and as such is not recording this money as revenue or cash in its financial statements at this time.

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

2.1(1) Agreement and Plan of Reorganization between the Company and Research Connections, Inc., dated January 3, 2000.

2.2(2) Purchase Agreement, dated as of May 16, 2001, by and between myESP

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Acquisition Corporation, a Delaware corporation, and LiveWorld, Inc., a Delaware corporation.

- 2.3(2) Web Site Services and Maintenance Agreement, dated as of May 16, 2001, by and between LiveWorld, Inc., a Delaware corporation and myESP Acquisition Corporation, a Delaware corporation.
- 3.2(3) Second Amended and Restated Certificate of Incorporation of the Company.
- 3.3(3) Bylaws of the Company.
- 4.1(3) Form of the Company's Common Stock certificate.
- 4.2(3) Third Amended and Restated Shareholders Rights Agreement, dated April 23, 1999, between the Company and the parties named therein, as amended on May 26, 1999.

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- (1) Incorporated by reference from the Company's Annual Report on Form 10-K for the period ended December 31, 1999.
 - (2) Incorporated by reference from the Company's Report on Form 8-K, filed on May 31, 2001.
 - (3) Incorporated by reference from the Company's 424(b) Prospectus, dated July 19, 1999, as declared effective by the Securities and Exchange Commission on July 19, 1999

(b) Reports on Form 8-K

No reports on Form 8-K were filed during the three months ended September 30, 2001.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

LIVEWORLD, INC.
(Registrant)

Date: November 14, 2001

By: /s/ Peter H. Friedman

Peter H. Friedman
President and Chief Executive Officer
(principal financial or chief financial
officer and duly authorized signatory)

