

Edgar Filing: SHOPNET COM INC - Form 10KSB

SHOPNET COM INC
Form 10KSB
November 26, 2003

U.S. SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-KSB
(Mark One)

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

For the fiscal year ended June 30, 2003

OR

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

Commission File Number O-28690

SHOPNET.COM, INC.

(Name of Small Business Issuer in Its Charter)

Delaware

13-3871821

(State or Other Jurisdiction of
Incorporation or Organization)

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

112 West 34th Street, New York, New York 10120
(Address of Principal Executive Offices)

(212) 967-8303
(Issuer's Telephone Number, Including Area Code)

Securities registered pursuant to Section 12(b)
of the Exchange Act:

Title of Each Class and Name of Each Exchange on Which Registered
NONE

Securities registered pursuant to Section 12(g)
of the Exchange Act:
Common Stock, \$.001 par value
(Title of Class)

Check whether the Issuer (1) has filed all reports required to be filed by
Section 13 or 15(d) of the Securities Exchange Act of 1934 during the past 12
months (or for such shorter period that registrant was required to file such
reports), and (2) has been subject to such filing requirements for the past 90
days. Yes ☒ No ☐

Check if no disclosure of delinquent filers in response to Item 405 of
Regulation S-B is contained in this form, and no disclosure will be contained,
to the best of registrant's knowledge, in definitive proxy or information
statements incorporated by reference in Part III of this Form 10-KSB or any
amendment to this Form 10-KSB ☐.

The Registrant's consolidated revenues for the year ended June 30, 2003 were
\$7,599,223.

Edgar Filing: SHOPNET COM INC - Form 10KSB

The aggregate market value of the voting stock on November 19, 2003 (consisting of Common Stock, par value \$0.001 per share) held by non-affiliates was approximately \$72,202.13 based upon the closing price for such Common Stock on said date \$.01. On such date, there were 8,067,462 of Registrant's Common Stock outstanding.

PART I

ITEM 1. DESCRIPTION OF BUSINESS

The statements which are not historical facts contained in this Report are forward looking statements that involve risks and uncertainties, including, but not limited to instability of revenues, future losses and unpredictable operating results. The Company's actual results may differ materially from the results discussed in any forward looking statement. Unless otherwise indicated, all references to the number of our shares of common stock give effect to the 1 for 3 reverse stock split effected in February 1998, 100% Common Stock dividend effected in February 1999, 10% Common Stock dividend effected in February 2000 and the 20% Common Stock dividend effected in June 2000.

History

ShopNet.com, Inc. (the "Company" or "Shopnet") was formed in December 1995 in the State of Delaware, as Hollywood Productions, Inc. ("HPI"). Its purpose was to acquire screenplays and produce motion pictures. The Company changed its name from "Hollywood Productions, Inc." to "Shopnet.Com, Inc." in May 1999.

In September 1996, the Company acquired Breaking Waves, Inc. ("Breaking Waves"), a New York corporation, which remains a wholly owned subsidiary of the Company. This acquisition was contingent upon and was consummated simultaneously with the Company's initial public offering ("IPO") and marked the Company's entrance into the business of designing, manufacturing, and distributing (throughout the United States) young girls' swimwear and coordinating beach cover-ups and accessories.

In May 1999, Shopnet incorporated a new subsidiary, Hollywood Productions, Inc. ("Hollywood"), to which Shopnet assigned its motion picture business. As a result, Shopnet is now a holding company, owning 100% of Hollywood and Breaking Waves. Except where otherwise indicated, Shopnet and its subsidiaries are collectively referred to herein as the "Company."

Motion Picture Business

General

Since its inception in December 1995, the Company has co-produced three motion pictures: "Dirty Laundry," "Machiavelli Rises" and "The Girl." Each such film had limited theatrical runs shortly after release. The Company's primary focus for the foreseeable future will be to work directly, or through distribution arrangements with third parties, to establish distribution for these completed films through public or cable television - via pay-per-view, premium and standard channels - the sale of video rights and/or foreign distribution. To a lesser extent, the Company will continue to seek to acquire screenplays and produce motion pictures, either directly or through collaborative arrangements, to be distributed primarily through public or cable television and the sale of video rights.

"Dirty Laundry"

In March 1995, the Company entered into a property acquisition agreement (the "Purchase Agreement") and a co-production agreement (the "Production Agreement")

Edgar Filing: SHOPNET COM INC - Form 10KSB

with Rogue Features, Inc. ("Rogue"), an unaffiliated entity, to acquire the rights to and co-produce a motion picture of the screenplay entitled "Dirty Laundry." In addition, the Company and Rogue entered into a right of first refusal agreement with respect to the next two products of Rogue and/or its principals.

In April 1996, the Company formed D.L. Productions, Inc. ("D.L. Productions"), a New York corporation, as a wholly owned subsidiary, for the purpose of holding title to and producing the Dirty Laundry film and receiving revenues from the distribution thereof. The Purchase Agreement conveyed all rights to the screenplay and the film itself to the Company. In return, Rogue directed "Dirty Laundry" and has the right to 25% of its profits as described in the Production Agreement. Rogue also retained the right to produce a live comedy or musical upon the earlier of five years after Dirty Laundry's release or the Company's approval. In addition, Michael Normand, a principal of Rogue, retained the right to adapt the screenplay of Dirty Laundry into a novel on the Company's approval of the compensation it is to receive therefrom. The Production Agreement provided for the principals of Rogue to direct and retain creative control of the production of the film while the Company retains final approval.

In November 1997, with production of the movie complete, the Company effected the dissolution of D.L. Productions. Its assets were transferred to the Company, and the Company took over the marketing of Dirty Laundry.

In June 1998, the Company entered into an agreement with Artistic License Films, Inc. ("ALF") whereupon ALF agreed to use its best efforts to distribute the film in at least three New York theaters and two Los Angeles theaters. In exchange for its efforts, ALF received a \$20,000 retainer fee which constitutes an advance against ALF's distributor's fee of 25% of the gross receipts from the theatrical distribution of the film. The film had a limited run during the fall of 1998 and received marginal reviews (two stars out of four). Currently, the Company is working to distribute the film through various channels, including public or cable television, the sale of video rights and foreign distribution.

2

"Dirty Laundry" is a romantic comedy shot in the New York tri-state area. It stars Jay Thomas as Joey (a dry cleaner going through a mid-life crisis), and Tess Harper as Beth (a sex advice columnist for a woman's magazine and Joey's wife of 15 years). Joey's dry cleaning business is doing poorly, and he is convinced that he is aging prematurely. Given their increasing lack of intimacy, Beth encourages Joey to seek counseling, which he does unbeknownst to Beth, who has become attracted to her chiropractor. Throughout the film, a variety of bizarre mishaps occur which result in the couple's rekindling of their lost romance with a surprise ending. Mr. Thomas has co-starred in the motion picture "Mr. Holland's Opus" and is known for his television work in "Love & War," "Cheers," "Murphy Brown," and "Mork & Mindy," and, until recently, was the host of WTJM "Jammin" 105.1 FM, a New York radio station. Ms. Harper earned a Golden Globe nomination for her performance in the film "Tender Mercies" and an Oscar nomination for her role in the film "Crimes of the Heart."

"Machiavelli Rises"

In April 1998, the Company entered into a co-production agreement with North Folk Films, Inc. ("North Folk") for the production of a film entitled "Machiavelli Rises." The Company and North Folk formed a limited liability company, Battle Studies Productions, LLC ("Battle Studies"), to finance, produce, and distribute the film which commenced production in April 1998. The film was completed in November 1998. The film was written, directed, and co-produced by Efraim Horowitz and can be characterized as a contemporary ghost story about power, greed, love, and Leonardo Da Vinci's lost notebook. Total production costs to date have aggregated approximately \$433,000, of which the

Edgar Filing: SHOPNET COM INC - Form 10KSB

Company has funded approximately \$217,500. In accordance with the terms of the co-production agreement, the proceeds of the film will be distributed as follows: first, both parties shall be entitled to recoup their initial investment in the film, at 135% thereof; then, after repayment to the respective parties of additional costs incurred by same, any remaining proceeds shall be distributed 50% to North Folk and 50% to the Company. The film was shown in January 1999 in both New York and at the Brussels Film Festival.

In February 2000, "Machiavelli Rises" was one of thirty-eight films showcased at the New York Independent Film Festival ("NYIFF") in New York City where it was honored with the award for Best Screenplay. In addition, it was chosen (along with only six other films) for presentment at the Los Angeles distribution of the NYIFF in April 2000.

In September 2000 and January 2001, Battle Studies entered into two-year agreements with each of Raven Pictures International and Koan, Inc. for the distribution of "Machiavelli Rises" internationally and domestically, respectively. See "Management's Discussion and Analysis or Plan of Operation - Investment in Joint Ventures - Battle Studies Productions, LLC." To date, the film has not generated any distribution revenues.

"The Girl"

In July 1999, the Company entered into an agreement with ALF with respect to the production of a film entitled "The Girl." Pursuant to such agreement, the Company and ALF formed a limited liability company, The Girl, LLC ("Girl LLC"), to finance, produce and distribute the film. As of June 30, 2001, the Company invested \$35,000 for a 22.533% interest in Girl LLC. "The Girl" was completed in the spring of 2001, has been exhibited at several film festivals and had a very limited theatrical distribution in New York City. The Girl LLC is in the process of attempting to secure video and foreign distribution arrangements. "The Girl," which was filmed in Paris, categorized as a faux film noir, chronicles a lesbian relationship.

Production

The Company intends to continue to review screenplays for acquisition and co-production, although to a lesser extent. Typically, once a screenplay is acquired (i) a budget is prepared, (ii) revisions to the screenplay are made, (iii) the talent, production crews, and all ancillary items required for the filming of the motion picture are hired and/or otherwise obtained, and (iv) a film schedule is established. Once filming is complete, the film is edited, sound and special effects are added, and a final print is produced. The Company then arranges private showings of the film and attempts to secure domestic and foreign distributors.

Production of a motion picture requires approximately five to eight weeks of filming followed by approximately fourteen weeks of editing and adding sound and special effects. An additional twelve to sixteen weeks generally is required in order to secure a distributor for the film. If the Company cannot find a distributor, it will attempt to distribute the film itself. Once this process is complete, the film will be ready for release to theaters or other distribution channels. See "--Distribution, Billing and Revenues."

Distribution, Billing and Revenues

Generally, distribution of a film may be undertaken either by a motion picture studio, an independent distributor or through an agent. The Company expects that any existing films or future films it may produce will be distributed by an independent distributor or itself through an agent. In a distribution

Edgar Filing: SHOPNET COM INC - Form 10KSB

arrangement, the production company and the distributor determine who will incur what portion of the costs of marketing a film, at which time a budget is prepared and the extent of the release of the film is determined. The release of films may be done in platforming stages. A screening is then held, and critics are invited to review the film. If the film receives a favorable response from either the critics and/or the audience, the film's distribution will expand gradually into additional markets and theaters.

The Company does not expect extensive theatrical distribution of its existing or future films. Rather, after limited theatrical distribution a film may be distributed through public or cable television - via pay-per-view, premium, and standard channels - and/or through the sale or rental of videotapes. The Company may enter into agreements with different distributors for different markets or sell all the rights to one distributor. Revenues generated are distributed to all parties involved including the distributor, the producers, the owners, and the talent pursuant to extensive formulas previously agreed upon.

Distribution rights to motion pictures are granted legal protection under the copyright laws of the United States and most foreign countries which provide substantial civil and criminal sanctions for unauthorized duplication and exhibition of motion pictures. The Company plans to take all appropriate and reasonable measures to secure, protect, and maintain or obtain agreements from licensees to secure, protect, and maintain copyright protection for all of the motion pictures it distributes under the laws of all applicable jurisdictions.

The Company estimates that between 12 and 18 months will elapse between the commencement of expenditures by the Company in the acquisition of a screenplay, the production of a motion picture, and its release. The Company does not expect to receive revenues, if any, from the exploitation of a film until approximately 24 to 36 weeks after its release. Notwithstanding there can be no assurance that any completed film will ever establish distribution at any level or generate any revenues to the Company. Billing in the industry typically occurs quarterly: theaters pay distributors on a quarterly basis, and the Company is paid the following quarter. In the event a distributor desires to distribute one of the Company's films, however, such distributor may either (i) offer an initial payment to the Company against, or in addition to, future royalties or (ii) purchase the film outright.

Regulations

The Code and Ratings Administration of the Motion Picture Association of America, an industry trade association, assigns ratings for age-group suitability for viewing of motion pictures. While the Company will follow the practice of submitting most of its motion pictures for such ratings, the Company may review this policy from time to time.

United States television stations and networks, as well as foreign governments, impose regulations on the content of motion pictures which may restrict, in whole or in part, exhibition on television or in a particular territory. There can be no assurance that current and future restrictions on motion pictures released by the Company will not limit or affect the Company's ability to exhibit such motion pictures.

Competition in the Film Industry

The film industry is immense with many well capitalized industry leaders producing commercial films capable of wide theatrical distribution. The Company competes, and will continue to compete, with these and other institutions which produce, distribute, exploit and finance films, many of which have substantial financial and human resources considerably more extensive than the Company's. These institutions include the major film studios - including Disney, Universal, MGM, and Sony - as well as smaller independent film companies and television and

Edgar Filing: SHOPNET COM INC - Form 10KSB

cable networks. Industry members compete substantially for the hire or purchase of a limited number of producers, directors, actors, and screenplays which are able to attract major distribution in all media and all markets throughout the world.

The motion picture business is highly competitive and has an extremely high profile in terms of name recognition, with relatively insignificant barriers to entry, and numerous entities compete for the same directors, producers, actors/actresses, distributors, theaters, etc. There is intense competition within the film industry for exhibition times at theaters, as well as for distribution in other media, and for the attention of the movie-going public and other viewing audiences. Competition for distribution in other media is as intense as the competition for theatrical distribution, and not all films are licensed in other media. Each year, numerous production companies are formed, and numerous motion pictures are produced, all of which motion pictures seek full distribution and exploitation. Despite the increase in the number of films, a small number of films, those which receive widespread consumer acceptance, account for a large percentage of total box office receipts.

4

Swimwear Business

General

Breaking Waves is a designer, manufacturer, and distributor of girl's swimwear which is sold throughout the United States. In addition to swimwear, Breaking Waves also manufactures beach cover-ups and accessories to coordinate with its swimwear. Swimwear is made in children's sizes from 2-16 and in pre-teen sizes.

Breaking Waves markets swimwear under private brand labels including "Breaking Waves," and "All Waves". In July 2000, Breaking Waves added a new line of girls' swimwear which is sold under the label, "Coral Cove." Breaking Waves also licenses rights to the name "Daffy Waterwear" and the "Gottex" trademark in connection with the manufacture and sale of girls' swim and related beach wear.

Products, Design, Supplies and Inventory

Breaking Waves designs, manufactures, and sells both private label and name brand girl's swimwear and accessories. It has an office in Homestead, Florida where its designer designs all styles for its swimwear lines and accessory items. Each season, roughly 20-25 prints and fabrics are developed for the "Breaking Waves" line, with generally between 10 to 20 prints and fabrics developed for each of its other lines. For the year ended June 30, 2003, the "Coral Cove" line accounted for approximately 32% of Breaking Waves' total sales volume, with the other four lines accounting for, in equal parts, the remainder of Breaking Waves' volume for such period.

In designing its children's swimwear, Breaking Waves adapts certain of the prints and styles it is provided by Beach Patrol Inc., the licensor of "Daffy Waterwear" and Gottex Models Ltd., which management feels are appropriate for children's wear. Of each fabric or print chosen, the Company usually manufactures two swimsuits: a one-piece model and a two-piece model.

Once Breaking Waves has chosen the prints and colors it desires to use for its children's swimwear, it sends the artwork for the fabric to its agent in Korea who disseminates them to one or more clothing manufacturers for prototyping and the knitting or weaving and printing of fabrics. The manufacturer returns the fabrics to Breaking Waves, and upon Breaking Waves' approval, the fabrics are sent, with the desired design, to any one or more of several Indonesian or Korean companies where the fabric is cut and sewn into a completed product. Finished goods are shipped from the manufacturer to a public warehouse in the

Edgar Filing: SHOPNET COM INC - Form 10KSB

City of Industry, California. Breaking Waves has found that this process is the most cost-effective means of operating its business. It expects to continue its operations in this manner in the future, though it may use other manufacturers and suppliers in different countries.

Breaking Waves' swimwear typically is produced in two blended fabrics: one is a blend of nylon and lycra spandex, and the other is a blend of cotton, polyester, and lycra spandex. Each product line uses different designs and emphasizes different fabric blends.

For the year ended June 30, 2003, 74% of Breaking Waves' finished products were purchased from two Indonesian manufacturers and 26% of Breaking Waves' finished products were purchased from a South Korean manufacturer. For the year ended June 30, 2002, 74% of Breaking Waves' finished products were purchased from two Indonesian manufacturers and 26% of Breaking Waves' finished products were purchased from a South Korean manufacturer. Although the Company believes that the fabrics and non-fabric sub-materials it uses are readily available and that there are numerous manufacturers for such piece goods who offer similar terms and prices, there can be no assurance that management is correct in such belief. The unavailability of fabrics or the absence of clothiers, or the availability of either at unreasonable cost, could adversely affect the operations of Breaking Waves and the Company.

Since Breaking Waves purchases finished garments from overseas contractors, it does not buy or maintain an inventory of sub-materials. It has not experienced difficulty in satisfying finished garment requirements and considers its sources of supply adequate. Breaking Waves' inventory of garments varies depending upon its backlog of purchase orders and its financial position.

Marketing and Sales

The "Breaking Waves," "Coral Cove" and "Gottex" lines are distributed and sold through department and specialty stores. The "All Waves" label is sold to mass merchants and also as promotional goods in department stores. Private label programs are supplied to several major chains and department store groups.

Breaking Waves sells its swimwear and accessory items through its showroom sales staff and through independent sales representatives. Over the past several years, certain of its customers have included the Dillard and Federated department store groups as well as Kids R Us, Sears, Wal-Mart, T.J. Maxx and Marshalls. For the year ended June 30, 2003, Breaking Waves had three customers representing in the aggregate 44% of net sales as compared to two customers representing in the aggregate 36% of net sales for the year ended June 30, 2002.

5

Breaking Waves' merchandise is shipped pursuant to purchase orders sent by its customers and is sent f.o.b. shipping point (freight on board) meaning Breaking Waves is neither responsible for the goods during shipment nor for the delivery charge. Payment is due 30 days after shipment. No goods are shipped on consignment; therefore, except for non-conforming or damaged goods, all goods shipped are considered sold.

In addition to its in-house sales and showroom personnel, approximately twenty independent sales representatives throughout the United States sell Breaking Waves merchandise on a non-exclusive basis. These representatives service department stores and smaller specialty retailers. In some cases, separate independent representatives sell the "Daffy Waterwear" line. None of these representatives is under contract with Breaking Waves; nor does any receive a salary. Rather, each is paid a commission based upon his sales. In addition to showroom sales and sales representatives calling on customers, Breaking Waves exhibits its products at major trade shows. End of season and discontinued

Edgar Filing: SHOPNET COM INC - Form 10KSB

merchandise is sold to off-price stores.

Suspended Internet Activities

In March 1999, Breaking Waves launched an online wholesale children's swimwear website at www.breakingwaves.com. The website was designed to complement the company's wholesale distribution efforts by providing retailers instant access to more than 200 styles of Breaking Waves swimwear. The Company has determined, however, not to pursue this method of distribution, and its website is now dormant.

Work in Progress

Breaking Waves manufactures its swimwear lines from June to December based on its knowledge of the market and past sales. Customer orders generally start arriving in June and July. Goods are reordered by customers on a continual basis through the following June. The quantity of open purchase orders at any date may be affected by, among other things, the timing and recording of orders. Breaking Waves does not sell on consignment and accepts return of only such products as are imperfect or shipped in error.

The major design work takes place from January to May. Goods are manufactured, printed, and sewn overseas from June to December. Finished garments are shipped from the factory to a public warehouse in Los Angeles for shipments to retailers. The majority of shipments to retailers are made from November to May, with January through March being the peak shipping time.

Trademarks

Breaking Waves relies on common law and registered trademarks for usage of its private label swimwear lines under the names "Breaking Waves," "All Waves" and "Coral Cove." Breaking Waves has licensed rights to the "Little Me" and "Gottex" names for girls swim and beach wear. See "Management's Discussion and Analysis or Plan of Operations of - License Agreements" for a description of each of such license arrangements.

There can be no assurance that such trademarks owned or licensed by the Company adequately will be protected against infringement. In addition, there can be no assurance that Breaking Waves will not be found to be infringing on another company's trademark. In the event Breaking Waves finds another party to be infringing upon one of its trademarks, if registered, or is found by another company to be infringing upon such company's trademark, there can be no assurance that Breaking Waves will be successful in any resultant litigation it may ultimately become involved in.

Competition

There is intense competition in the swimwear apparel industry. Breaking Waves competes with many other manufacturers in these markets, many of which are larger and have greater resources than it does. Major competitors in the swimwear industry include "Ocean Pacific," "Ralph Lauren," and "Speedo." In addition, department stores and retailers have their own private label programs which are the major competition in the mass merchant business.

Breaking Waves' business is highly competitive with relatively insignificant barriers to entry and with numerous firms competing for the same customers. Breaking Waves is in direct competition with local, regional, and national clothing manufacturers, many of which have greater resources and more extensive distribution and marketing capabilities than it does. In addition, many large retailers have recently commenced sales of "store brand" garments which compete with those sold by Breaking Waves. Management believes that Breaking Waves' market share is not significant in its product lines.

Edgar Filing: SHOPNET COM INC - Form 10KSB

Many of the national clothing manufacturers have extensive advertising campaigns which develop and reinforce brand recognition. In addition, many of such manufacturers have agreements with department stores and national retail clothing chains to jointly advertise and market their products. Since Breaking Waves does limited advertising and marketing and has no agreement with any department store or national retail chain to advertise any of its products, it competes with companies that have brand names that are well known to the public. All other factors being equal, it can be expected that a retail shopper will buy a "brand name" garment before he buys an "unknown" brand, depending on price.

6

Seasonality

Breaking Waves' business is seasonal. A large portion of its revenues and profits are derived between November and March. Each year from April through October, Breaking Waves designs and manufactures the following season's swimwear lines. There can be no assurance that revenues received from December to June will support Breaking Waves' operations for the rest of the year.

Employees

Mr. Harold Rashbaum, the Company's Chairman of the Board, President, Chief Executive Officer and Chief Financial Officer oversees the Company's consolidated operations. The Company has one other executive officer, a designer, controller and 3 office personnel to oversee Breaking Wave's operations on a full-time basis, and employs a Vice-President of Design, Merchandising and Production on a part-time basis. Breaking Waves has approximately twenty independent sales persons representing the Breaking Wave's lines on a non-exclusive basis. Hollywood's operations are governed by Mr. Rashbaum. Most screenwriters, performers, directors, and technical personnel involved in the Company's films are members of guilds or unions which bargain collectively with producers on an industry-wide basis from time to time. Any work stoppages or other labor difficulties could delay the production of the films resulting in increased production costs and delayed return of investments.

Business Risks

Film Production

The likelihood of the success of any film and the Company's ability to stay on budget and on schedule for each film must be considered in light of the problems, expenses, difficulties, complications, and delays frequently encountered in connection with the production of a motion picture. Due to unforeseen problems and delays including illness, weather, technical difficulty, and human error, by completion, most films are considerably over budget. In addition, the lack of experience of management in this industry, the limited operating history and capital of the Company, and the competitive environment in which the Company operates may cause increased expenses due to mistakes and delays in the production of the films.

The success of a film in theatrical distribution, television, home video, and other ancillary markets is dependent upon public taste which is unpredictable and susceptible to change. The number and popularity of other films being distributed may also significantly affect the theatrical success of a film. Accordingly, it is impossible for anyone to predict accurately the success of any film at the time it enters production. The production of a motion picture requires the expenditure of funds based largely on a pre-production evaluation of the commercial potential of the proposed project.

Swimwear

Edgar Filing: SHOPNET COM INC - Form 10KSB

The apparel industry is a cyclical industry, with consumer purchases of swimwear, accessory items, and related goods tending to decline during recessionary periods when disposable income is low. Accordingly, a prolonged recession would in all likelihood have an adverse effect on the operations of Breaking Waves and the Company. Breaking Waves operates in only one segment of the apparel industry, specifically swimwear, and is therefore dependent on the demand for such goods. Decreases in the demand for swimwear products would have a material adverse effect on the Company's business as a whole.

Breaking Waves believes that its success in the swimwear industry depends in substantial part on its ability to anticipate, gauge, and respond to changing consumer demands and fashion trends in a timely manner. Breaking Waves attempts to anticipate consumer preferences. There can be no assurance, however, that it will be successful in this regard, and if it misjudges the market for any of its products, it may be faced with unsold finished goods, inventory, and work in process, which could have an adverse effect on the Company's operations as a whole.

ITEM 2. DESCRIPTION OF PROPERTY

The Company maintains its executive office at Breaking Waves' facilities. Breaking Waves maintains its executive offices and showroom at 112 West 34th Street, New York, New York 10120. Until January 1998, this space was approximately 1,000 square feet and comprised only office space. In January 1998, Breaking Waves amended its lease and rented an additional 1,000 square feet. The lease is for a term of seven years, expiring December 2004, at an annual rental of \$71,600. In July 2001, Breaking Waves terminated this lease, effective August 31, 2001. A new 6-year lease for an aggregate of 2,200 square feet expiring September 30, 2007 was signed, which became effective on December 1, 2001. Annual rent under the new lease is \$84,915 through December 31, 2004 and \$95,760 for the remainder of the lease. Breaking Waves also maintains a Florida office, comprising approximately 780 square feet, with annual payments of approximately \$11,000.

7

ITEM 3. LEGAL PROCEEDINGS

On or about June of 2000, an action was brought in the Queens County Supreme Court against the Company and several others claiming, among other things, that the Company allegedly breached a contract and engaged in fraudulent statements (including supposedly promising the plaintiff options and then not allowing the plaintiff to exercise these options). The plaintiff seeks, among other things, compensatory damages in the amount of \$497,500, punitive damages in the amount of \$995,000, together with costs and attorney's fees. The Company has responded to the complaint and denied the allegations. The Company intends to contest this action vigorously and believes that such claims against it are baseless and without merit.

The Company is not a party to any other material litigation and is not aware of any threatened litigation that would have a material adverse effect on its business. Neither the Company's officers, directors, affiliates, nor owners of record or beneficially of more than five percent of any class of the Company's Common Stock is a party to any material proceeding adverse to the Company or has a material interest in any such proceeding adverse to the Company.

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

None.

8

Edgar Filing: SHOPNET COM INC - Form 10KSB

PART II

ITEM 5. MARKET FOR COMMON EQUITY AND RELATED SHAREHOLDER MATTERS

Market Information

The Company's common stock is currently traded on the Over The Counter Bulletin Board (the "OTCBB"), under the symbol "SPNT". The Company's warrants are currently traded on the OTCBB under the symbol "SPNTW".

The following table sets forth the high and low sales prices for the common stock and warrants for the fiscal periods indicated as reported by in the over-the-counter market. The quotations shown represent inter-dealer prices without adjustment for retail mark-ups, mark-downs or commissions, and may not necessarily reflect actual transactions

Calendar Period	Common Stock		Warrants
	Low	High	Low
2001			
01/01/01 - 03/31/01	.19	.89	.09
04/01/01 - 06/30/01	1.00	2.18	.14
07/01/01 - 09/30/01	.42	1.56	.02
10/01/01 - 12/31/01	.36	1.25	.01
2002			
01/01/02 - 03/31/02	.02	.85	.01
04/01/02 - 06/30/02	.02	.30	.01
07/01/02 - 09/30/02	.03	.15	.01
10/01/02 - 12/31/02	.03	.09	.01
2003			
01/01/03 - 03/31/03	.01	.05	.01
04/01/03 - 06/30/03	.01	.03	.01
07/01/03 - 09/30/03	.02	.12	.01
10/01/03 - 11/18/03	.01	.04	.01

As of September 20, 2003, there were 49 holders of record of the Company's Common Stock, although the Company believes that there are approximately 431 additional beneficial owners of shares of Common Stock held in street name. As of November 20, 2002, the number of outstanding shares of the Company's Common Stock was 8,067,462. This number includes an aggregate of 2,420 shares of Common Stock being held by the Company on behalf of certain shareholders pending their submission for exchange of stock certificates outstanding on the date of the Company's one-for-three reverse stock split, as adjusted for the reverse stock split and subsequent stock dividends. The table reflects the price for post-dividend shares and post-adjustment Warrants since February 5, 1999.

Initially, each Warrant issued in the IPO entitled the holders thereof to purchase one share of the Company's Common Stock at an exercise price of \$6.50 per share, until September 9, 2001. On June 23, 1997, the Board of Directors approved a reduction in the exercise price of the Warrants from \$6.50 to \$3.00. On February 5, 1998, the Company effected a one for three reverse split of the Company's Common Stock. Accordingly, the Company adjusted the terms of the

Edgar Filing: SHOPNET COM INC - Form 10KSB

Warrants to reflect the reverse split such that exercise of three Warrants would entitle the holder to purchase one share of Common Stock at an exercise price of \$9.00. Giving effect to the February 1999 100% Common Stock dividend, February 2000 10% Common Stock dividend and June 2000 20% Common Stock dividend, the Warrants have been cumulatively adjusted such that the exercise of each Warrant at an exercise price of \$3.41 purchases .88 of a share of Common Stock or, each Warrant, exercisable at an exercise price of \$3.87 purchases 1 share of Common Stock.

In August 2001, the Company extended the term of the Warrants for an 18 month period. The current expiration date of the Warrants is March 10, 2003. There is no current Registration Statement on file with the Securities and Exchange Commission ("SEC") covering the shares of Common Stock issuable upon exercise of the Warrants. Accordingly, the Warrants cannot currently be exercised. The Company plans to file a Registration Statement with the SEC in the future.

On April 15, 1998, the Company's Board of Directors authorized the distribution of Distribution Warrants to all holders of shares of the Company's Common Stock as of the

9

May 8, 1998 Warrant Record Date. Pursuant to the distribution, each share held on the Warrant Record Date shall generate the issuance of one Distribution Warrant to purchase one share of Common Stock at an exercise price of \$4.00 per share. The Distribution Warrants, which are exercisable for a period of three years commencing one year after issuance, shall be issued and distributed once the Company has filed a registration statement for same and same has been declared effective by the SEC. The Company to date has not filed the registration statement.

Common Stock Dividends

20% Common Stock Dividend

On May 8, 2000, the Company's Board of Directors authorized the issuance of a 20% stock dividend to all holders of shares of the Company's Common Stock, par value \$0.001 per share (the "Common Stock") as of May 19, 2000 payable on June 19, 2000.

10% Common Stock Dividend

On January 7, 2000, the Company's Board of Directors authorized the issuance of a 10% stock dividend to all holders of Common Stock as of January 20, 1999, payable February 1, 2000.

100% Common Stock Dividend

On January 14, 1999, the Company's Board of Directors authorized the issuance of a stock dividend to all holders of shares of the Company's Common Stock as of January 29, 1999, payable on February 5, 1999.

The Company has paid no cash dividends and has no present plan to pay any cash dividends. Payment of future dividends will be determined from time to time by its board of directors, based upon its future earnings, if any, financial condition, capital requirements, and other factors. The Company is not presently subject to any contractual or similar restriction on its present or future ability to pay such dividends.

ITEM 6. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATIONS CAUTIONARY STATEMENTS ON FORWARD-LOOKING STATEMENTS

Edgar Filing: SHOPNET COM INC - Form 10KSB

CAUTIONARY STATEMENTS ON FORWARD-LOOKING STATEMENTS

Statements contained in this report which are not historical facts and may be considered forward looking information with respect to plans, projections, or future performance of the Company as defined under the Private Securities Litigation Reform Act of 1995. These forward-looking statements are subject to risks and uncertainties, which could cause actual results to differ materially from those projected. The words "anticipate", "believe", "estimate", "expect", "objective", and "think" or similar expressions used herein are intended to identify forward-looking statements. The forward-looking statements are based on the Company's current views and assumptions and involve risks and uncertainties that include, among other things, the effects of the Company's business, actions of competitors, changes in laws and regulations, including accounting standards, employee relations, customer demand, prices of purchased raw material and parts, domestic economic conditions, including housing starts and changes in consumer disposable income, and foreign economic conditions, including currency rate fluctuations. Some or all of the facts are beyond the Company's control.

General

Shopnet.com, Inc. was incorporated in the State of Delaware on December 1, 1995 as Hollywood Productions, Inc. On May 10, 1999, Shopnet filed an amendment to its Articles of Incorporation effecting a change in its name to its current one. On May 12, 1999, it incorporated a new wholly-owned subsidiary, Hollywood Productions, Inc. ("Hollywood"), to which it assigned its motion picture business thereby rendering Shopnet a holding company for Hollywood and another wholly-owned subsidiary, Breaking Waves. Shopnet was formed initially for the purpose of acquiring screenplays and producing motion pictures. In September 1996, in connection with the completion of its IPO, it acquired all of the capital stock of Breaking Waves which designs, manufactures, and distributes private and brand name label children's swimwear. As of June 30, 2001, the Company changed its year-end from December 31st to June 30th.

The consolidated financial statements at June 30, 2003, June 30, 2002 included the accounts of Shopnet and its wholly owned subsidiaries, Breaking Waves and Hollywood (collectively referred to as the "Company") except where otherwise indicated after elimination of all significant intercompany transactions and accounts.

10

The following discussion and analysis should be read in conjunction with the consolidated financial statements and related footnotes, which provide additional information concerning the Company's financial activities and condition. Since Shopnet and its subsidiaries operate in different industries, the discussion and analysis is presented by entity (Shopnet, Hollywood and Breaking Waves) in order to be more meaningful.

Critical Accounting Policies

a) Principles of consolidation

The accompanying consolidated financial statements include the accounts of Shopnet and its wholly owned subsidiaries, Breaking Waves and Hollywood (the "Company"), after elimination of all significant intercompany transactions and accounts. Affiliated companies, which are 20 to 50 percent owned, are accounted for under the equity method.

b) Inventory

Inventory consists of finished goods and is valued at the lower of cost (using the first-in, first-out method) or market. All inventory is pledged as

Edgar Filing: SHOPNET COM INC - Form 10KSB

collateral for factored receivables pursuant to a factoring agreement with a financial institution.

c) Film production and distribution costs

The Company follows industry standards in capitalizing film production and distribution costs. Film production and distribution costs include all costs associated with the writing, producing, and distribution of the film. Film costs include the costs of production, prints, pre-release, and other advertising expected to benefit future periods. These costs, as well as participation and talent residuals, are charged against earnings on an individual film basis in the ratio that the current year's gross film revenues bear to management's estimate of total remaining ultimate gross film revenues from all sources.

Film costs are stated at the lower of cost or estimated net realizable value on an individual film basis. Revenue and cost forecasts are continually reviewed by management and revised when warranted by changing conditions. Estimates of total gross revenue can change significantly due to the level of amortization, as adjusted. Such adjustments could have a material effect on the results of operations in future periods. When estimates of total revenue and costs indicate that a feature film will result in an ultimate loss, additional amortization is recognized to the extent required to produce a zero gross margin over the remaining life of the film.

c) Equity Method of Accounting

Investments in significantly (20 to 50 percent) owned affiliates are accounted for by the equity method of accounting, whereby the investment is carried at cost of acquisition, plus the Company's equity percentage in undistributed earnings or losses since acquisition. Reserves are provided where management determines that the investment or equity in earnings is not realizable.

d) Income taxes

The Company accounts for income taxes in accordance with the "liability method" of accounting for income taxes. Accordingly, deferred tax liabilities and assets are determined based on the difference between the financial statement and tax basis of assets and liabilities, using enacted tax rates in effect for the year in which the differences are expected to reverse. Current income taxes are based on the respective periods' taxable income for federal, state and city income tax reporting purposes.

e) Revenue and cost recognition

The terms of Breaking Waves' sales are FOB shipping point thereby revenue is recognized upon shipment from the warehouse. Sales returns are recorded upon acceptance of the goods by the warehouse. Duty costs, which are a component of cost of sales, are recorded upon the clearance of such goods through customs.

11

Revenues from the theatrical distribution of motion pictures are recognized when motion pictures are exhibited. Revenues from video sales are recognized, together with related costs, on the date that video units are made widely available for sale by retailers.

Revenues from the theatrical distribution of motion pictures are recognized when motion pictures are exhibited. Revenues from video sales are recognized, together with related costs, on the date that video units are made widely available for sale by retailers. Revenues from the licensing of feature films, together with related costs are recorded when the material is available for telecasting by the licensee and when certain other conditions are met. Film

Edgar Filing: SHOPNET COM INC - Form 10KSB

production and distribution costs are stated at the lower of unamortized cost or estimated net realizable value.

In accordance with Accounting Standard, Statement of Position ("SOP 00-2"), "Accounting by Producers and Distributors of Films,". SOP 00-2 establishes new accounting standards for, among other things, marketing and development costs. The Company uses the individual film forecast method to amortize film costs.

g) Earnings per share

Earnings per common share is computed pursuant to SFAS No. 128 "Earnings Per Share." Basic earnings per share are computed as net income (loss) available to common shareholders divided by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflect the potential dilution that could occur from common shares issuable through stock options, warrants and convertible preferred stock.

h) Use of estimates

In preparing financial statements in conformity with generally accepted accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions which affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and revenues and expenses during the reporting period. The most significant estimate with regard to these financial statements is the estimate of projected income of motion pictures which, is the basis used in amortizing film production and distribution costs. Actual results could differ from those estimates.

i) Fair value disclosure at June 30, 2003 and June 30, 2002:

The carrying value of cash, accounts receivable, inventory, accounts payable, accrued expenses, and capital lease obligations are a reasonable estimate of their fair value.

MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

Results of Operations

Year ended June 30, 2003 as compared to the year ended June 30, 2002

For the year ended June 30, 2003 and 2002, the Company reported a consolidated net loss of \$886,918 and \$436,562. Comprehensive loss for the year ended June 30, 2003 was \$886,918 as compared to a comprehensive loss of \$442,912 for the year ended June 30, 2002.

Breaking Waves

For the year ended June 30, 2003 and 2002, Breaking Waves generated net sales of \$7,599,223 and \$7,702,798, respectively, with related cost of sales amounting to \$5,257,972 and \$5,065,879, respectively. The decrease in net sales amounting to \$103,572, or approximately 2%, from 2002 to 2003 was primarily attributable to an increase in product charge backs.

The gross profit for the year ended June 30, 2003 amounted to \$2,341,251 or 31% of sales as compared to the year ended June 30, 2002 during which it amounted to \$2,636,919 or 35% of sales. The decrease in the gross profit percentage can be attributable to an increase in low margin sales during the last fiscal quarter.

Selling, general, and administrative expenses during the year ended June 30, 2003 and 2002 amounted to \$2,471,263 and \$2,238,211, respectively. The increase,

Edgar Filing: SHOPNET COM INC - Form 10KSB

amounting to \$233,052 or 11%, was primarily attributable to an increase in royalty fees, advertising and postage and delivery and computer expenses.

The major components of the Breaking Waves selling, general, and administrative expenses are as follows for the year ended June 30:

Officers, office staff, designer and sales, salaries and related benefits	
Commission expense	
Warehousing costs	
Royalty fees	
Rent expense	
Factor commissions	
Miscellaneous general corporate overhead expenses	

Interest expense in connection with its factoring agreement amounted to \$205,591 and \$248,303 for the year ended June 30, 2003 and 2002, respectively. The decrease is due to a reduction in the stated prime interest rate.

Breaking Waves generated a net loss of \$563,837 for the year ended June 30, 2003 and a net loss of \$82,366 for the year ended June 30, 2002.

The major components of the Breaking Waves selling, general, and administrative expenses as a percentage of sales are as follows for the year ended June 30:

	2003
Officers, office staff, designer and sales, salaries and related benefits	8%
Commission expense	3%
Warehousing costs	6%
Royalty fees	2%
Rent expense	1%
Factor commissions	1%
Miscellaneous general corporate overhead expense	11%

Hollywood

For the year ended June 30, 2003 and 2002, Hollywood generated no sales from its motion picture "Dirty Laundry". Although sales prior to and including the year ended June 30, 2003 were minimal, the Company is expending efforts to effect increased sales during the fiscal year ending June 30, 2004 and thereafter as a result of the implementation of a new marketing strategy which among other things, emphasizes the development of new marketing and distribution arrangements for "Dirty Laundry". Upon a review of the net realizable value of the movie cost, management has determined that a \$0 and \$208,564 write down was necessary as of June 30, 2003 and 2002, respectively. Accordingly, Hollywood generated a loss of \$663 and \$214,064 for the year ended June 30, 2003 and 2002, respectively. The loss of \$16,258 includes an equity loss of \$14,241 from Hollywood's investments in The Girl. LLC, a joint venture.

Subsequent to "Dirty Laundry", Hollywood also has invested in other movie

Edgar Filing: SHOPNET COM INC - Form 10KSB

ventures, some of which have generated revenue to date. See "Investment in Joint Ventures."

Shopnet.com

For the year ended June 30, 2003 and 2002, Shopnet generated no income.

Shopnet's selling, general, and administrative expense amounted to \$306,553 and \$367,902 for the year ended June 30, 2003 and 2002. This represents a decrease of \$61,349 or approximately 17%.

13

The major components of the Company's expenses are as follows for the year ended December 31:

Salaries (officer and office staff) and stock compensation and related benefits

Rent

Legal and professional fees

Consulting fees

Other general corporate and administrative expense

Shopnet generated a net loss of \$306,553 and \$352,501 for the year ended June 30, 2003 and 2002, respectively.

Liquidity and Capital Resources

At June 30, 2003, the Company's consolidated working capital deficit amounted to \$914,146.

At June 30, 2003, current assets consisted primarily of accounts receivables of \$158,963, and prepaid expenses of \$237,708 and restricted cash of \$250,000.

On or about September 12, 2000, Breaking Waves entered into a factoring and revolving inventory loan and security agreement ("factoring agreement") with Century Business Credit Corporation ("Century") to sell its interest in all present and future receivables without recourse. Breaking Waves submits all sales offers to Century for credit approval prior to shipment, and pays a factoring commission of .75% of receivables sold.

Century retains from the amount payable to Breaking Waves a reserve for possible obligations such as customer disputes and possible credit losses on unapproved receivables. Breaking Waves may take advances of up to 85% of eligible receivables and up to 50% of the value of finished goods in inventory, with interest payable monthly at the rate of 1 3/4% over prime.

Pursuant to the terms of a Reimbursement and Compensation Agreement, a trust ("Trust"), the beneficiary of which is a relative of the Company's President and Chief Executive Officer ("CEO"), pledged assets as collateral for securing a \$250,000 letter of credit to replace a portion of a letter of credit previously pledged by the Company.

Accordingly, on December 20, 2000 the original agreement with the factor was amended to allow such replacement of collateral. Breaking Waves' Loan and Security Agreement with Century dated December 20, 2000 requires the provision of one or more letters of credit in the aggregate amount of \$1,150,000 to

Edgar Filing: SHOPNET COM INC - Form 10KSB

partially secure the line of credit. On September 15, 2001, Century required the Company to increase the amount of collateralized standby letters of credit by \$300,000 raising such amount to \$1,450,000.

On May 3, 2001, the Agreement with the Trust was amended so that the letter of credit secured by the Trust was increased to \$400,000. As a condition of the amendment, the Company entered into a guarantee agreement with Gal Capital Corp., whose President is a relative of the Company's President and CEO to act as guarantor of the obligation to the Trust up to \$400,000 in exchange for a fee of \$42,500 which the Company paid on May 3, 2001. The amended letter of credit expired on September 1, 2001 and was subsequently amended on September 15, 2001.

On September 15, 2001, the Amended and Restated Reimbursement and Compensation Agreement was entered into and further amended the agreement with the Trust, so that the letter of credit secured by the Trust was increased to \$750,000. The amended letter of credit expired on September 1, 2002 but can be extended year to year at the Company's option for a period of ten years. On September 1, 2002, the letter of credit was extended. Breaking Waves agreed to reimburse the Trust for any and all losses, fees, charges and expenses to the Trust in the event the letter of credit is called by Century and/or the issuing bank demands reimbursement from the Trust. Breaking Waves' obligations are guaranteed by the Company in addition to being secured by a first

14

security interest in all of the assets of the Company and a subordinate security interest in all of the assets of Breaking Waves.

On September 15, 2001, the Company entered into a Reimbursement Agreement with relatives of a principal stockholder who is related to the President and CEO of the Company ("RAYA") who pledged assets as collateral for securing a \$300,000 letter of credit as additional collateral to secure Breaking Waves' Loan and Security Agreement with Century. Absent any default, the letter of credit will remain in effect for ten years.

Shopnet under a separate Security Agreement dated September 15, 2001 guarantees the agreement. In exchange for the letters of credit, the Trust and RAYA will proportionately, based on the total outstanding letters of credit, receive a fee of one and one quarter percent (1-1/4%) of net sales of Breaking Waves through June 30, 2002 and thereafter one and three quarters percent (1-3/4%) of net sales through September 30, 2011. In October 2001, the Trust and RAYA received advance payments to be applied towards future fees of \$24,500 and \$12,250, respectively. All future payments are payable forty five days after the close of each fiscal quarter. The fees are effective October 1, 2001. In September 2003, the letter of credit secured by RAYA was drawn on by Century, reducing Breaking Waves' liability to Century.

In September 2001, the Company and Breaking Waves retained Arc Financial Corp. ("ARC"), a British Virgin Island company, for a ten-year term to provide financial consulting services.

Pursuant to the terms of a consulting agreement ("ARC Consulting Agreement"), ARC was retained to assist the Company in the acquisition of financing to acquire inventory and for other corporate purposes ("Financing"), as well as consult with the Company with regard to its ongoing operations, promote sales of Breaking Waves' products and improving production.

Pursuant to the terms of the ARC Consulting Agreement, the Company and Breaking Waves agreed to compensate ARC (i) an annual fee of \$20,000 ("Base Fee") and (ii) a percentage of annual net sales in the amount of 1-1/4% through June 30, 2002 and 1-3/4% of net sales for each year of the term thereafter through September 30, 2011 ("ARC Percentage Fee"), payable 45 days after the closing of

Edgar Filing: SHOPNET COM INC - Form 10KSB

each fiscal quarter.

In October 2001, ARC received (i) a lump sum payment of \$209,000 reflecting full advance payment of the Base Fee and (ii) \$36,750 reflecting advance payment of the Arc Percentage Fee. The agreement with Arc expires September 30, 2011. The Company and Breaking Waves are entitled to terminate the ARC Consulting Agreement any time after September 30, 2006, in which event all prepaid fees are forfeited.

In December 2002, Breaking Waves entered into a Reimbursement and Compensation Agreement with TERE, S.A., a Swiss entity. As a consequence of Century being unwilling to grant credit to Breaking Waves unless it received one or more letters of credit satisfactory to it as well as cash collateral to partially secure the line of credit in such amounts as it deems appropriate, the Trust reduced the letter of Credit secured by it to \$500,000. TERE, S.A. agreed to loan Breaking Waves the sum of \$250,000 represented by a promissory note.

In September 2003, the letter of credit secured by the Trust was drawn upon by Century, reducing Breaking Waves' liability to Century.

The funds were deposited as cash collateral with Century to replace the reduced portion of the letter of credit secured by the Trust.

All obligations under this agreement are guaranteed by the Company as well as by ARC Financial and are secured by a security interest in all of the Company's assets, which are second in priority to Century.

As compensation, Breaking Waves paid to TERE all interest received from or credited to it by Century on the sums deposited pursuant to the Cash Collateral Agreement when received.

The term of the loan is for ten years.

15

ARC has agreed to pay to TERE, interest at the rate of 8% per annum on a quarterly basis.

The following table summarizes the percentage due each party, as noted above, as a percentage of net sales for the year ended June 30, 2003:

	% of Net Sales	Amount
	-----	-----
RAYA	0.58	\$ 44,076
ZAT	.24	17,934
ARC	1.75	132,988
	-----	-----
	2.57	\$ 194,998
	=====	=====

Interest expense related to the factor agreement totaled \$205,591 and \$248,303 for the year ended June 30, 2003 and 2002, respectively. Century has a secured interest in Breaking Waves' inventory as collateral for the advances. As of June 30, 2003, the net advances to Breaking Waves from Century amounted to \$1,054,187.

On November 8, 2002, the Company borrowed the sum of \$50,000 in the form of a promissory note from Amigal Salit, Ltd., an unrelated party. The note, which is non-interest bearing, is due on or before August 15, 2003.

Edgar Filing: SHOPNET COM INC - Form 10KSB

On the same date, the Company entered into an agreement with ARC Financial Corporation, whereby the Company using the proceeds received from Amigal Salit, Ltd., agreed to pay \$50,000 as an advance against fees to be owned by Breaking Waves to ARC Financial Corporation in connection with Breaking Waves obligation to pay certain fees to ARC as part of a consulting agreement as described in Note 9 herein.

The Company and Breaking Waves have experienced a significant cash shortfall in the months following June 30, 2003. In September, the Company obtained a loan in the amount of \$44,000 from U.S. Biomedical Corporation, a company whose former chief operating officer is the son-in-law of the Company's president. The term of the loan is for one year and it matures on September 9, 2004. The loan may be repaid, at U.S. Biomedical's option, either in cash or non-registered stock of the Company. Additionally, in September, the Company's president loaned the sum of \$5,000 to the Company on an interest free basis. On October 21, 2003, Breaking Waves was notified by Century that it was in default of its factoring agreement due to non payment of its obligations and that Century, under its factoring agreement with Breaking Waves, now has the option to foreclose on Breaking Waves' trademark and other collateral at anytime subsequent to October 21, 2003. As of November 18, 2003, no such action has been taken by Century.

The Company has incurred losses since its inception and has not yet been successful in establishing profitable operations. Further, the Company has current liabilities in excess of current assets. These factors raise substantial doubt about the ability of the Company to continue as a going concern. In this regard, management is proposing to raise any necessary additional funds not provided by operations through loans or through additional sales of its common stock or through a possible business combination with another company. There is no assurance that the Company will be successful in (a) raising this additional capital on acceptable terms or at all or (b) achieving profitable operations.

Investments in Joint Ventures

Battle Studies

Pursuant to a co-production agreement dated April 17, 1998 with North Folk Films, Inc., the Company invested through June 30, 2002, \$212,385 for a 50% interest in a new entity, Battle Studies Productions, LLC ("Battle Studies") a limited liability company. Battle Studies will be treated as joint venture in order to co-produce motion pictures and to finance the costs of production and distribution of such motion pictures. The joint venture retains all rights to the motion pictures, the screenplays, and all ancillary rights attached thereto.

16

The Company accounts for the investment in Battle Studies on the equity method. For the year ended June 30, 2003, and the year ended June 30, 2002 the Company recorded \$793 and \$2,355, respectively, of equity losses for its proportionate share of Battle Studies. No revenues have been derived from this film as of June 30, 2003 and June 30, 2002.

On October 12, 2000, Battle Studies entered into a distribution agreement with Raven Pictures International ("Raven Pictures") to distribute Battle Studies' motion picture ("Macheavelli Rises") to foreign countries. Battle Studies has granted rights under the agreement for the theatrical, video, non-theatrical and television markets. The term of the agreement is for twenty-four months for all portions of territory outside of the United States and English speaking Canada. Battle Studies expects to realize 75% (which is net of a 25% fee to Raven Pictures) of the expected estimated gross revenues derived from foreign countries less \$20,000 for marketing and advertising expense.

Edgar Filing: SHOPNET COM INC - Form 10KSB

On January 17, 2001, Battle Studies entered into a distribution agreement with KOAN to distribute and promote Battle Studies' motion picture ("Machiavelli Rises") in the United States and Canada. Battle Studies has granted rights under the agreement for free TV, pay TV, cable, satellite, video and DVD markets.

The terms of the agreement is for twenty-four months and it will be automatically renewed unless KOAN receives a letter of cancellation at least thirty days prior to the date of termination or if sales have not exceeded \$250,000 over the twenty-four month period. Battle studies expects to realize 70% (which is net of a 30% fee to KOAN) of the expected estimated gross revenues derived from the United States and Canada less \$5,000 per year for promotional costs.

The Girl

Pursuant to an agreement dated July 1, 1999 with Artistic License Films Inc., Hollywood invested, through June 30, 2003, \$35,000 for a 22.533% interest in a new entity, The Girl, LLC ("The Girl") a limited liability company. In return for its participation in The Girl, Hollywood is entitled to receive a non-contested, non-dilutable 22.533% ownership interest in The Girl, a recoupment of its investment on no less favorable terms than any other investor and 22.533% of any contingent compensation which shall be actually received by The Girl. The Girl retains all rights to the motion pictures, the screenplays, and all ancillary rights attached thereto.

Hollywood accounts for the investments in The Girl under the equity method. For the year ended June 30, 2003, and the year ended June 30, 2002, the Company recorded \$14,241 and \$0, respectively, in net equity losses.

Lease Commitments

Shopnet and Breaking Waves have entered into lease agreements for their administrative offices. Shopnet leases its administrative offices. Shopnet leased its administrative office pursuant to a 5-year lease that expired on November 30, 2001 at annual rent amounting to approximately \$70,000, before annual escalations.

Breaking Waves terminated its lease effective November 30, 2001. A new 6-year lease expiring September 30, 2007 was signed in July 2001 and is effective beginning December 1, 2001. Annual rent under the new lease is \$84,915 through December 31, 2004 and \$95,760 for the remainder of the lease. Lastly, Breaking Waves leases an offsite office for one of its designers on a month-to-month basis with annual payments approximating \$11,000.

The Company and Breaking Waves' approximate future minimum rentals under non-cancelable operating leases in effect on June 30, 2003 are as follows:

For the fiscal year ended June 30:

2004	\$84,915
2005	90,338
2006	95,760
2007	95,760
Thereafter	23,940

	\$ 390,713
	=====

Rent expense for the year ended June 30, 2003 amounted to \$81,646 and for the year ended June 30, 2002 amounted to \$94,508.

License Agreements

During June 2000, Breaking Waves entered into a license agreement with an effective date of November 1, 2000 with Gottex Models Ltd., as Israeli corporation and Gottex Models (USA) Corp., a New York corporation for the use of the trademark "Gottex" in the United States of America for children's swimwear. The agreement calls for a royalty fee of 7% of net sales with guaranteed minimum annual royalties of \$70,000 to \$140,000 over the life of the agreement. Breaking Waves recorded royalties under the agreement totaling \$163,019 and \$73,408 for the year ended June 30, 2003 and for the year ended June 30, 2002.

On July 29, 2002, Breaking Waves entered into a licensing agreement with LMH, Inc. whereby Breaking Waves was granted exclusive use of certain trademarks, namely "Little Me" and "Muffings" in the United States, Canada and Mexico, and the use of "Tapioca" and "Juniper" solely in the United States.

The licensing agreement has a term of three years ending on July 31, 2005, unless terminated earlier and agreed to by both parties.

In consideration of both the license granted and the design services to be performed by LMH, Breaking Waves has agreed to pay a sales royalty equal to 5% of net sales of the Licensor's products.

Under the terms of the agreement, Breaking Waves agreed to guarantee a minimum royalty payment of \$10,000 for the period August 1, 2002 to July 31, 2003.

For the second and third years of the agreement, Breaking Waves agreed to pay a minimum royalty of \$20,000 payable in four quarterly installments.

ITEM 7. FINANCIAL STATEMENTS

The financial statements for the year ended June 30, 2003 are attached to this filing after the signature page.

ITEM 8. CHANGES AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

On approval of its Audit Committee, on January 23, 2002 the Registrant dismissed Massella Rubenstein LLP (formerly Massella, Tomaro & Co. L.L.P., hereinafter "Massella"). The dismissal was not due to any discrepancies or disagreements between same and the Company on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure. Massella's report on the Registrant's financial statements for the six month transition period ended June 30, 2001 ("Transition Period") and fiscal years ended December 30, 2000 and December 30, 1999 did not contain any adverse opinions or disclaimers of opinion. Nor were such modified as to uncertainty, audit scope, or accounting principles. During the Transition Period and the two most recent fiscal years and any subsequent interim period through the date of the dismissal, the Company and Massella had no disagreements or "reportable events."

The Registrant dismissed Massella as part of a recently initiated cost savings program. The Registrant's Audit Committee approved, as of January 23, 2002, the engagement of Jerome Rosenberg CPA, P.C. as its principal accountant to audit its and its subsidiary's financial statements.

Item 8A. Controls and Procedures

Evaluation of disclosure controls and procedures

As of June 30, 2003, we carried out an evaluation of the effectiveness of

Edgar Filing: SHOPNET COM INC - Form 10KSB

the design and operation of its disclosure controls and procedures pursuant to Securities Exchange Act Rule 13a-14. This evaluation was done under the supervision and with the participation of our Principal Executive Officer and Principal Financial Officer. Based upon that evaluation, they concluded that our disclosure controls and procedures are effective in gathering, analyzing and disclosing information needed to satisfy our disclosure obligations under the Securities Exchange Act.

Changes in internal controls

There were no significant changes in our internal controls or in other factors that could significantly affect those controls since the most recent evaluation of such controls.

18

PART III

ITEM 9. DIRECTORS, EXECUTIVE OFFICERS, PROMOTERS AND CONTROL PERSONS; COMPLIANCE WITH SECTION 16(a) OF THE EXCHANGE ACT

Officers and Directors

The following table sets forth the names, ages, and titles of all directors and officers of the Company:

Name	Age	Position
Harold Rashbaum	75	President, CEO, CFO and Director

The Directors of the Company are elected annually by the stockholders, and the Officers of the Company are appointed annually by the Board of Directors. Vacancies on the Board of Directors may be filled by the remaining Directors. Each current Director and Officer will hold office until the next annual meeting of stockholders or until his successor is elected and qualified. The outside Directors do not receive a Director's fee for their participation as Directors. The outside Directors are Alain Le Guillou, M.D. (Until recently Harold Rashbaum was the father-in-law of Alain Le Guillou, M.D.), James B. Frakes and Debra Riggs. The Corporation does not have key man insurance on the lives of any of its Officers or Directors.

As permitted under the Delaware General Corporation Law, the Company's Certificate of Incorporation eliminates the personal liability of the directors to the Company or any of its shareholders for damages caused by breaches of said directors' fiduciary duties. As a result of such provision, shareholders may be unable to recover damages against directors for actions which constitute negligence or gross negligence or are in violation of their fiduciary duties. This provision in the Company's Certificate of Incorporation may reduce the likelihood of derivative and other types of shareholder litigation against directors.

Harold Rashbaum, age 75, has been the President, Chief Executive Officer, Chief Financial Officer and a Director of the Company since January 1997. Since September 1996, he has also been the President, Secretary, and sole Director of Breaking Waves, Inc. ("Breaking Waves"), a New York company which is a wholly-owned subsidiary of the Company. From May 1996 to January 1997, Mr. Rashbaum served as Secretary and Treasurer of the Company. Since September 1996, Mr. Rashbaum has been the Chairman of the Board of Directors of Play Co. Toys & Entertainment Corp. ("Play Co."), a public entity whose Common Stock, Series E Stock and Series E Warrants are quoted on the over-the-counter market on the OTC Bulletin Board. Mr. Rashbaum was a management consultant to Play Co. from July

Edgar Filing: SHOPNET COM INC - Form 10KSB

1995 to September 10, 1996. In May 1998, he was elected as a Director of Toys International, Inc. ("Toys"), a majority-owned subsidiary of Play Co. whose Common stock is traded on the SMAX segment of the Frankfurt Stock Exchange. On March 28, 2001, Play Co., Toys and Play Co. Toys Canyon Country, Inc. ("Play Co. Toys Canyon") each filed for protection under Chapter 11 of the United States Code with the United States Bankruptcy Court for the Southern District of New York. In August 2001, the case was converted to a Chapter 7 filing. Since February 1996, Mr. Rashbaum has also been the President and a Director of H.B.R. Consultant Sales Corp. ("HBR"), of which his wife is the sole shareholder.

Compliance with Section 16(A) of the Exchange Act

Section 16(a) of the Securities Exchange Act of 1934, as amended, requires the Company's officers, directors, and persons who beneficially own more than ten percent of a registered class of the Company's equity securities to file reports of securities ownership and changes in such ownership with the SEC. Officers, directors, and greater than ten percent beneficial owners also are required by rules promulgated by the Securities and Exchange Commission ("SEC") to furnish the Company with copies of all Section 16(a) forms they file.

No person ("a Reporting Person") who during the year ended June 30, 2003 was a director, officer, or beneficial owner of more than ten percent of the Company's Common Stock which is the only class of equity securities of the Company registered under Section 12 of the Securities Exchange Act of 1934, as amended, failed to file on a timely basis reports required by Section 16 of the Act. The foregoing is based solely upon a review by the Company of (i) Forms 3 and 4 during the most recent fiscal year as furnished to the Company under Rule 16a-3(e) under the Act, (ii) Forms 5 and amendments thereto furnished to the Company with respect to its most recent fiscal year, and (iii) any representation received by the Company from any reporting person that no Form 5 is required, except as described herein.

ITEM 10. EXECUTIVE COMPENSATION

Summary of Cash And Certain Other Compensation

The following table provides certain information concerning all Plan and Non-Plan (as defined in Item 402 (a)(ii) of Regulation S-B) compensation awarded to, earned by, or paid to the named executive officer during the years ended June 30, 2003, June 30, 2002 and the six month period ended June 30, 2001.

19

SUMMARY COMPENSATION TABLE

Name and Principal Position		Annual Compensation			Awards	Long-Term C
		Salary	Bonus	Other Annual Compen- sation	Restricted Stock Award(s)	Securities Underlying Options/ SARs
Year		(\$)	(\$)	(\$)	(\$)	(#)
Harold Rashbaum President, CEO, CFO And Director	2003	116,645	--	--	--	--
	2002	115,929	--	--	--	--
	2001	70,000 (1)	--	--	--	--
=====	=====	=====	=====	=====	=====	=====

Edgar Filing: SHOPNET COM INC - Form 10KSB

(1) Mr. Rashbaum received \$70,000 of salary during the six month period ended June 30, 2001.

(2) Represents an aggregate of 44,000 shares of Common Stock underlying options exercisable at \$1.38 per share, granted in April 1999.

Stock Options

The following table contains information regarding options to purchase Common Stock held at June 30, 2003 and June 31, 2002 by the Company's executive officer named in the Executive Compensation Table above.

=====					
AGGREGATED OPTION EXERCISES IN LAST FISCAL YEAR AND					
FISCAL YEAR END OPTION VALUES					

			Number of Securities Underlying		Value
			Unexercised Options at Fiscal		O
			Year End		
Name	Shares Acquired on Exercise	Value Realized	Exercisable	Unexercisable	Exerc

Harold Rashbaum	(1)	(1)	132,000 (2)	--	
=====					

(1) No options were exercised in the years ended June 30, 2003 and June 30, 2002.

(2) Represents an aggregate of 88,000 shares of Common Stock underlying options granted in March 1997 under the Company's Senior Management Incentive Plan, currently exercisable at \$1.46 per share, and an aggregate of 44,000 shares of Common Stock underlying options granted in April 1999, currently exercisable at \$1.38 per share.

(3) The options had no value at either June 30, 2003 or June 30, 2002, since as of such dates the aggregate exercise price of the options exceeded the aggregate market value of the underlying shares (based on the closing sales prices of the Company's Common Stock.)

Employment and Consulting Agreements

ShopNet.com, Inc.

Before he became an officer and director of the Company, Harold Rashbaum provided consulting services to the Company through HBR, a company of which he is an officer and director and of which his wife is the sole shareholder. HBR entered into an oral consulting agreement with the Company whereby it will receive 5% of the net profits received by the Company from the distribution of "Dirty Laundry." To date, HBR has not received any fees as a result of the distribution of "Dirty Laundry" not generating any net profits. See "Certain Relationships and Related Transactions."

Breaking Waves, Inc.

20

In November 1996, Breaking Waves entered into employment agreements with each of Malcolm Becker and Michael Friedland; these agreements expired in November 1999. The agreements initially provided that Messrs. Becker and Friedland each would

Edgar Filing: SHOPNET COM INC - Form 10KSB

be compensated at a salary of \$110,000 per annum during the term of his agreement and that each would be issued restricted shares of Common Stock, subject to a vesting schedule, annually during the term of his agreement.

In November 1996, 3,667 shares of the Company's Common Stock were issued to each of Messrs. Becker and Friedland, subject to the vesting schedule. In November 1997, 15,888 shares of the Company's Common Stock were issued to each of Messrs. Becker and Friedland, subject to the aforesaid vesting schedule.

In January 1998, Mr. Friedland's employment agreement was amended to provide for an increase in salary to \$130,000 per annum, and Mr. Becker's employment agreement was amended to reflect a reduction in the amount of time Mr. Becker would be required to devote to the business of Breaking Waves, a concomitant reduction in salary to \$60,000 per annum, and a reduction in the number of shares of Common Stock to be issued. In January 1999, Mr. Becker's employment agreement was further amended to reflect an increase in the amount of time Mr. Becker would be required to devote to the business of Breaking Waves and a concomitant increase in salary to \$70,000 per annum.

In each of May and November 2000, pursuant to their respective employment agreements, Messrs. Becker and Friedland received their final share issuances. Mr. Becker received an aggregate of 91,289 shares of Common Stock, 45,644 in May 2000 and 45,645 in November 2000. Mr. Friedland received an aggregate of 167,365 shares of Common Stock, 83,683 in May 2000 and 83,683 in November 2000. Messrs. Becker and Friedland each granted an option to BBC Capital Corp. ("BBC"), of which Ilan Arbel is President, to purchase an aggregate of 76,074 shares of common stock in the case of Mr. Becker and 139,471 shares in the case of Mr. Friedland, at an exercise price of \$4.50 per share. Such options expired to the extent of 1/2 of the underlying shares on May 27, 2001. The balance of the options scheduled to expire in November 2001 were terminated by BBC in August 2001.

Breaking Waves entered into a one-year consulting agreement in August 2000 with Larry Nash, Inc. ("Consultant") a New York corporation, whereby Mr. Nash, the Consultant's sole stockholder provides sales and consulting services in connection with Breaking Waves' Gottex line. Mr. Nash has provided similar services for the past twelve years with another company for which he represented the Gottex children's swimwear line. The agreement is automatically extended from year to year thereafter unless cancelled by either party on thirty (30) days' prior written notice. Pursuant to such agreement, the Consultant is compensated a percentage of net sales (as such term is defined) on all orders exclusively procured by him, ranging from 2.5 to 5%. He is entitled to additional compensation ranging from 1.5% to 3% of net sales for the Coral Cove, Gottex and Breaking Waves lines, generated by Company sales personnel he introduces to the Company.

See "Management's Discussion and Analysis or Plan of Operations-Factoring Agreements-Century Business Credit Corporation" for a description of the Arc Consulting Agreement.

Senior Management Incentive Plan

General

In May 1996, the Board of Directors adopted the Senior Management Incentive Plan (the "Management Plan") which was adopted by shareholder consent. The Management Plan provides for the issuance of an aggregate of 750,000 shares of Common Stock in connection with the issuance of stock options and other stock purchase rights to executive officers, key employees, and consultants.

The Management Plan was adopted to provide the Board of Directors with sufficient flexibility regarding the forms of incentive compensation which the

Edgar Filing: SHOPNET COM INC - Form 10KSB

Company will have at its disposal for rewarding executive officers, employees, and consultants (of either the Company or a subsidiary of same) who render significant services to the Company or its subsidiary with equity in the Company through the grant of stock options and other rights. The Management Plan was adopted to enable the Company to attract and retain qualified personnel without unnecessarily depleting the Company's cash reserves (by offering those persons who provide significant services a personal interest in the Company's growth and success) and to augment the Company's existing compensation programs.

The Management Plan is intended also to help the Company attract and retain key executive management personnel whose performance is expected to have a substantial impact on the Company's long-term profit and growth potential by encouraging and assisting those persons to acquire equity in the Company. It is contemplated that only persons who perform services of special importance to the Company will be eligible to participate under the Management Plan. A total of shares of Common Stock have been reserved for issuance under the Management Plan. It is anticipated that awards made under the Management Plan will be subject to three-year vesting periods, although the vesting periods are subject to the discretion of the Administrator (as defined below).

21

The Management Plan is to be administered by the Board of Directors or a committee of the Board if one is appointed for this purpose (the Board or such committee, as the case may be, will be referred to in the following description as the "Administrator"). Members of the Board of Directors who are eligible for awards or have been granted awards may not vote on any matters affecting the administration of the Management Plan or the grant of any award thereunder.

Subject to the specific provisions of the Management Plan, the Administrator will have the discretion to determine the recipients of the awards, the nature of the awards to be granted, the dates such awards will be granted, the terms and conditions of awards, and the interpretation of the Management Plan, except that any award granted to any employee of the Company who is also a director of the Company will also be subject - in the event the Administrator of such plan at the time such award is proposed to be granted does not satisfy the requirements regarding the participation of "disinterested persons" set forth in Rule 16b-3 ("Rule 16b-3") promulgated under the Securities Exchange Act of 1934, as amended (the "Exchange Act") - to the approval of an auxiliary committee consisting of not less than three individuals (all of whom qualify as "disinterested persons" as defined under Rule 16b-3. In the event the Board of Directors deems the formation of an auxiliary committee impractical, the Board is authorized to approve any award under the Management Plan.

As of the date hereof, the Company has not yet determined who will serve on such auxiliary committee, if one is required. The Management Plan generally provides that unless the Administrator determines otherwise, each option or right granted under the plan will become exercisable in full upon certain "change of control" events as described therein.

If any change is made in respect of the Common Stock subject to the Management Plan or subject to any right or option granted under the Management Plan (through merger, consolidation, reorganization, recapitalization, stock dividend, or dividend in property other than cash, stock split, liquidating dividend, combination of shares, exchange of shares, change in corporate structure, or otherwise), the Administrator will make appropriate adjustments to the Management Plan and the number of shares and price per share of Common Stock subject to outstanding rights or options. Generally, the Management Plan may be amended by action of the Board of Directors except that any amendment which would change the class of securities subject to the plan, increase the total number of shares subject to such plan, extend the duration of such plan, materially increase the benefits accruing to participants under such plan, or

Edgar Filing: SHOPNET COM INC - Form 10KSB

change the category of persons who can be eligible for awards under such plan must be approved by the affirmative vote of the owners of a majority of the Common Stock entitled to vote. The Management Plan permits awards to be made thereunder until November 2004.

Directors who are not otherwise employed by the Company will not be eligible for participation in the Management Plan. The Management Plan provides for four types of awards: stock options, incentive stock rights, stock appreciation rights (including limited stock appreciation rights), and restricted shares.

22

Incentive Stock Options ("ISOs" and "non-ISOs")

The Management Plan may be either incentive stock options which qualify as such under the Internal Revenue Code ("ISOs") or options which do not qualify under the Internal Revenue Code as ISOs ("non-ISOs"). ISOs may be granted at an option price of not less than 100% of the fair market value of the Common Stock on the date of grant except that an ISO granted to any person who owns Common Stock representing more than 10% of the total combined voting power of all classes of Common Stock of the Company ("10% Shareholder") must be granted at an exercise price of at least 110% of the fair market value of the Common Stock on the date of the grant. The exercise price of non-ISOs may not be less than 85% of the fair market value of the Common Stock on the date of grant. The Administrator will determine the exercise period of the options granted which shall be no less than one year from the date of grant. Non-ISOs may be exercisable for a period of up to 13 years from the date of grant. ISOs granted to persons other than 10% Shareholders may be exercisable for a period of up to 10 years from the date of grant; ISOs granted to 10% Shareholders may be exercisable for a period of up to five years from the date of grant. The aggregate fair market value (determined at the time an ISO is granted) of shares of Common Stock that are subject to ISOs held by a plan participant that may be exercisable for the first time during each calendar year may not exceed \$100,000.

Payment for shares of Common Stock purchased pursuant to exercise of stock options may be remitted in cash or by certified check or at the discretion of the Administrator (i) by promissory note, (ii) promissory note combined with cash, (iii) by shares of Common Stock having a fair market value equal to the total exercise price, or (iv) by a combination of items (i)-(iii) above. The provision that permits the delivery of already owned shares of stock as payment for the exercise of an option may permit "pyramiding." In general, pyramiding enables a holder to use shares of Common Stock owned in order to pay for the exercise of the stock option. This is done by transferring such shares to the Company as payment of the exercise price for the shares purchased pursuant to the exercise of the Option. The value of such shares shall be determined by the market value of the shares at the time of transfer. Thereafter, the shares received upon the exercise of the option could then be used to do the same. Thereby, the holder may start with as little as one share of Common Stock and use the shares of Common Stock acquired in successive, simultaneous exercises of the option to exercise the entire option, regardless of the number of shares covered thereby, with no additional cash or investment other than the original share of Common Stock used to exercise the option.

Upon termination of employment, an optionee will be entitled to exercise the vested portion of an option for a period of up to three months after the date of termination except that if the reason for termination was a discharge for cause, the option shall expire immediately, and if the reason for termination was death or permanent disability of the optionee, the vested portion of the option shall remain exercisable for a period of 12 months thereafter.

In March 1997, the Company granted to Mr. Rashbaum an option to purchase 88,000 shares of Common Stock at an exercise price of \$1.46 per share, pursuant to the

Management Plan.

Incentive Stock Rights

Incentive stock rights consist of incentive stock units each of which is equivalent to one share of Common Stock and may be awarded in consideration for services performed for the Company or any subsidiary. Each incentive stock unit shall entitle the holder thereof to receive, without payment of cash or property to the Company, one share of Common Stock in consideration for services performed for the Company or any subsidiary by the employee, subject to the lapse of the incentive periods, at which time the Company will issue one share of Common Stock

for each unit awarded upon the completion of each specified period. If the employment with the Company of the holder of the incentive stock units terminates prior to the end of the incentive period relating to the units awarded, the rights will thereupon be null and void, except that if termination is caused by death or permanent disability, the holder or his heirs, as the case may be, will be entitled to receive a pro rata portion of the shares represented by the units, based upon that portion of the incentive period which has elapsed prior to the death or disability.

23

Stock Appreciation Rights (SARs)

SARs may be granted to recipients of stock options under the Management Plan. In the discretion of the Board of Directors, SARs may be granted simultaneously with, or subsequent to, the grant of a related stock option and may be exercised to the extent that the related option is exercisable, except that no general SAR (as hereinafter defined) may be exercised within a period of six months of the date of grant of such SAR, and no SAR granted with respect to an ISO may be exercised unless the fair market value of the Common Stock on the date of exercise exceeds the exercise price of the ISO. An option holder may be granted general SARs ("general SARs"), limited SARs ("limited SARs"), or both. General SARs permit the holder thereof to receive - without payment of cash or property to the Company - cash, shares of Common Stock, or a combination of both in an amount determined by dividing (i) that portion, elected by the option holder, of the total number of shares which the holder is eligible to purchase multiplied by the amount, if any, by which the fair market value of a share of Common Stock (on the exercise date) exceeds the option exercise price of the related option by (ii) the fair market value of a share of Common Stock on the exercise date. Limited SARs are similar to general SARs except that, unless the Administrator determines otherwise, limited SARs may be exercised only during a prescribed period following the occurrence of one or more of the following "change of control" transactions: (i) the approval of the Board of Directors and shareholders of the Company of a consolidation or merger in which the Company is not the surviving corporation, the sale of all or substantially all of the assets of the Company, or the liquidation or dissolution of the Company, (ii) the commencement of a tender or exchange offer for the Company's Common Stock (or securities convertible into Common Stock) without the prior consent of the Board, (iii) the acquisition of beneficial ownership by any person or other entity (other than the Company or any employee benefit plan sponsored by the Company) of securities of the Company representing 25% or more of the voting power of the Company's outstanding securities, or (iv) in the event, during any period of two consecutive years or less, individuals who at the beginning of such period constitute the entire Board cease to constitute a majority of the Board, unless the election, or the nomination for election, of each new director is approved by at least a majority of the directors then still in office.

An SAR holder may exercise his SAR rights by giving written notice of such exercise to the Company, which specifies the number of shares of Common Stock involved. The exercise of any portion of either the related stock option or the

Edgar Filing: SHOPNET COM INC - Form 10KSB

tandem SARs will cause a corresponding reduction in the number of shares remaining subject to the option or the tandem SARs, thus maintaining a balance between outstanding options and SARs. SARs have the same termination provisions as the underlying stock options (as described above) in the event an SAR holder ceases to be an employee of the Company.

Restricted Stock Purchase Agreements

Restricted share agreements provide for the issuance of restricted shares of Common Stock to eligible participants under the Management Plan. The Board of Directors may determine the price to be paid by the participant for the shares or that the shares may be issued for no monetary consideration. The shares issued shall be subject to restrictions for a stated restricted period during which the participant must remain in the Company's employ in order to retain the shares. Payment may be made in cash, by promissory note, or via a combination of both.

Restricted shares awarded under the Management Plan will be subject to a period of time, designated by the Administrator as the "restricted period," during which the holder has limited rights with respect to such shares. The Administrator may also impose other restrictions, terms, and conditions that must be fulfilled before the restricted shares may vest. Upon the grant of restricted shares, stock certificates registered in the name of the recipient will be issued, and such shares will constitute issued and outstanding shares of Common Stock for all corporate purposes. The holder will have the right to vote the restricted shares and to receive all regular cash dividends (and such other distributions as the Administrator may designate, other than distributions made solely with respect to the restricted shares ("retained distributions"), if any, which are paid or distributed on the restricted shares and, generally, to exercise all other rights as a holder of Common Stock except that until the end of the restricted period: (i) the holder will not be entitled to take possession of the stock certificates representing the restricted shares or receive retained distributions, and (ii) the holder will not be entitled to sell, transfer, or otherwise dispose of the restricted shares. A breach of any restrictions, terms, or conditions established by the Administrator with respect to any restricted shares will cause a forfeiture of such restricted shares.

24

Upon expiration of the applicable restricted period(s) and the satisfaction of any other applicable conditions, the restricted shares and any dividends or other distributions not distributed to the holder (the "retained distributions") thereon will become vested. Any restricted shares and any retained distributions thereon which do not so vest will be forfeited to the Company. If prior to the expiration of the restricted period a holder's employ is terminated without cause or because of a total disability (in each case as defined in the Management Plan) or the holder dies, unless otherwise provided in the restricted share agreement providing for the award of restricted shares, the restricted period applicable to each award of restricted shares will thereupon be deemed to have expired. Unless the Administrator determines otherwise, if a holder's employment terminates prior to the expiration of the applicable restricted period for any reason other than as set forth above, all restricted shares and any retained distributions thereon will be forfeited. Upon forfeiture of any restricted shares, the Company will repay to the holder thereof any amount the holder originally paid for such shares.

Acceleration of all awards under the Management Plan shall occur, pursuant to the provisions of Section 13 the Management Plan, on the first day following the occurrence of any of the following: (a) the approval by the shareholders of the Company of an "Approved Transaction,"

(b) a "Control Purchase," or (c) a "Board Change."

Edgar Filing: SHOPNET COM INC - Form 10KSB

An "Approved Transaction" is defined as (i) any consolidation or merger of the Company in which the Company is not the continuing or surviving corporation or pursuant to which shares of Common Stock would be converted into cash, securities, or other property other than a merger of the Company in which the holders of Common Stock immediately prior to the merger have the same proportionate ownership of Common Stock of the surviving corporation immediately after the merger, (ii) any sale, lease, exchange, or other transfer (in one transaction or a series of related transactions) of all, or substantially all, of the assets of the Company, or (iii) the adoption of any plan or proposal for the liquidation or dissolution of the Company.

A "Control Purchase" is defined as circumstances in which any person (as such term is defined in Sections 13(d)(3) and 14(d)(2) of the Exchange Act), corporation, or other entity (other than the Company or any employee benefit plan sponsored by the Company) (i) shall purchase any Common Stock of the Company (or securities convertible into the Company's Common Stock) for cash, securities, or any other consideration pursuant to a tender offer or exchange offer, without the prior consent of the Board of Directors or (ii) shall become the "beneficial owner" (as such term is defined in Rule 13d-3 under the Exchange Act), directly or indirectly, of securities of the Company representing twenty-five percent (25%) or more of the combined voting power of the then outstanding securities of the Company ordinarily (and apart from rights accruing under special circumstances) having the right to vote in the election of directors (calculated as provided in paragraph (d) of such Rule 13d-3 in the case of rights to acquire the Company's securities).

A "Board Change" is defined as circumstances in which, during any period of two consecutive years or less, individuals who at the beginning of such period constitute the entire Board shall cease for any reason to constitute a majority thereof unless the election, or the nomination for election by the Company's shareholders, of each new director was approved by a vote of at least a majority of the directors then still in office.

25

ITEM 11. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table sets forth information as of November 20, 2003 with respect to the beneficial ownership of shares of Common Stock by (i) each person known by the Company to be the owner of more than 5% of the outstanding shares of Common Stock, (ii) each director or director nominee of the Company (iii) each executive officer of the Company for whom information is given in the Summary Compensation Table in this proxy statement and (iv) all officers and directors as a group. Except to the extent indicated in the footnotes to the following table or otherwise as specified in this Proxy Statement, each of the individuals/entities listed below possesses sole voting power with respect to the shares of Common Stock listed opposite his/its name.

Name and Address of Beneficial Owner (1) -----	Number of Shares Beneficially Owned (1) -----	Percent of Common S Owned -----
Fiduciara Biaggini Via Vanoni # 6 Lugano, Switzerland CH 6901 (3)	5,075,120	62.9
American Telecom Corp. C/o MW Todtman McNamara Chamber		

Edgar Filing: SHOPNET COM INC - Form 10KSB

P.O. Box 47 Road Town Tortola, BVI	53,100 (4)	.65
Harold Rashbaum	252,000 (5)	3.12
All Officers and Directors as a Group (one person)	252,000	3.12

* Less than 1% of the outstanding common stock.

(1) Unless otherwise indicated, the address for each listed director or officer is c/o Shopnet.Com, Inc., 112 West 34th Street, New York, New York 10120. As used in this table, "beneficial ownership" means the sole or shared power to vote or direct the voting or to dispose or direct the disposition of any security. For the purposes of this table, a person is deemed to be the beneficial owner of securities that can be acquired within 60 days from September 20, 2003 through the exercise of any option or warrant. Shares of Common Stock subject to options or warrants that are currently exercisable or exercisable within 60 days are deemed outstanding for computing the ownership percentage of the person holding such options or warrants, but are not deemed outstanding for computing the ownership percentage of any other person. The amounts and percentages are based upon 8,067,462 shares of common stock outstanding as of September 20, 2003.

(2) Does not give effect to the issuance of (i) 3,379,200 shares of Common Stock issuable upon exercise of the 3,840,000 outstanding Warrants (the exercise of each warrant at an exercise price of \$3.41 purchases .88 of a share of Common Stock) or (ii) 128,333 shares of Common Stock reserved for issuance under the Company's Senior Management Incentive Plan.

(3) Fiduciara Biaggini is a fiduciary company with an address at via Vanoni #6, Lugano, Switzerland CH 6901. Fiduciara Biaggini owns of record 5,075,120 shares of common stock. The Company believes that these shares are held trust for the benefit of other parties. The Company has contacted Fiduciara Biaggini in order to determine the ownership of the shares of common stock held of record by Fiduciara Biaggini. As of the date hereof, Fiduciara Biaggini has not responded to the Company's attempt to contact it.

(4) American Telecom Corp. ("ATC") is a corporation organized under the laws of the British Virgin Islands which is wholly-owned by Europe American Capital Foundation ("EACF"), a Liechtenstein Trust with an address at Pradafont Street #7, Vaduz Liechtenstein, c/o Dr. Wohlwerd. Mr. Arbel controlled EACF through October 2000 and has been President of ATC since July 2000. By virtue of his position with ATC, Mr. Arbel has voting and dispositive control over shares of the Company beneficially owned by ATC and therefore may be deemed to beneficially own such shares.

(5) Includes an aggregate of 132,000 shares of Common Stock underlying options granted to Mr. Rashbaum, the Chairman of the Board, President, Chief Financial Officer and Chief Executive Officer of the Company. See "Executive Compensation."

By virtue of Mr. Arbel's voting and dispositive control of shares of the Company owned by each of ATC (see footnote 4 above), Mr. Ilan Arbel may be deemed to beneficially own 0.71% of the Company's outstanding Common Stock.

ITEM 12. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

For the year ended June 30, 2003 and 2002 financial consulting fees were paid to

Edgar Filing: SHOPNET COM INC - Form 10KSB

a corporation and an individual who are related to the Company's President and CEO amounting to \$37,000 and \$22,900, respectively.

Breaking Waves' Loan and Security Agreement with Century Business Credit Corporation ("Century") dated December 20, 2000 requires the provision of one or more letters of credit in the aggregate amount of \$1,150,000 to partially secure the line of credit. Pursuant to the terms of a Reimbursement and Compensation Agreement ("Reimbursement and Compensation Agreement"), a trust ("Trust"), the beneficiary of which is the granddaughter of Harold Rashbaum, the Company's Chairman of the Board, President, Chief Financial Officer and Chief Executive Officer, and the daughter of Mr. Arbel, a former principal stockholder, provided the security underlying a letter of credit in the amount of \$250,000 issued by a bank to replace a portion of a letter of credit previously provided by the Company. Breaking Waves agreed to reimburse the Trust for any and all losses, fees, charges and expenses to the Trust in the event the letter of credit is called by Century and the issuing bank makes payment and then demands reimbursement from the Trust. Breaking Waves' obligations are guaranteed by the Company in addition to being secured by a first security interest in all of the assets of the Company and a subordinate security interest in all of the assets of Breaking Waves. Breaking Waves paid a fee of \$42,500 to the Trust and reimbursed the Trust for all related professional and other fees incurred by the Trust in connection with such transaction.

On May 3, 2001, the Company, Breaking Waves and the Trust entered into a First Amendment to Reimbursement and Compensation Agreement ("Amendment") pursuant to which the Trust increased the amount of security an additional \$150,000 for a total of \$400,000, including the original \$250,000. The Trust conditioned the additional \$150,000 of security upon the receipt of an additional Guaranty from a party satisfactory to it. Gal Capital Corp. ("Gal") provided a Guaranty agreeing to pay all obligations of Breaking Waves as contained in the original Reimbursement and Compensation Agreement and all related expenses in enforcing same. Gal received a fee of \$42,500 for the issuance of such guaranty. Mr. Arbel is President of Gal.

In September 2001, Century increased the required security in the form of letters of credit from \$1,150,000 to 1,450,000. The Company also sought to raise additional funds to secure the letter of credit in order to have available to it additional working capital.

Pursuant to an Amended and Restated Reimbursement and Compensation Agreement dated as of September 15, 2001, between the Trust and Breaking Waves, which superceded the original Reimbursement and Compensation Agreement, the Trust agreed to provide additional security to a bank in return for the issuance of a letter of credit from such bank to Century in the amount of \$350,000 (in addition to the original \$400,000) to replace a portion of a letter of credit previously provided by Shopnet in a similar amount. The Trust agreed to continue such letter of credit for a period of ten years, absent any default. The terms include the same reimbursement, guarantee and security provisions as in the original Reimbursement and Compensation Agreement. As compensation, the Trust is entitled to .83 percent of net sales of Breaking Waves through June 30, 2001, and 1.16% of net sales of Breaking Waves for each year thereafter ("Trust L/C Fees"). Such amounts are payable 45 days after the close of each fiscal quarter. On the closing date, Breaking Waves paid \$24,500 to the Trust as an advance of future Trust L/C Fees and reimbursed the Trust for all related professional fees.

In addition, Breaking Waves entered into a Reimbursement Agreement dated as of September 15, 2001 with Rivka and Yair Arbel ("RAYA") (Mr. Arbel's brother and sister-in-law), pursuant to which RAYA agreed to provide security to a bank in return for a letter of credit from such bank to Century in the amount of \$300,000 reflecting the increase of security required by Century. RAYA agreed to continue such letter of credit for a period of ten years, absent any default.

Edgar Filing: SHOPNET COM INC - Form 10KSB

The Reimbursement Agreement includes reimbursement provisions in favor of the Trust in the event the letter of credit is called by Century and is paid by the bank. All of Breaking Waves obligations are guaranteed by Shopnet and secured by Shopnet's assets. As compensation, the Trust and RAYA are entitled, proportionally based on the total outstanding letters of credit, to a fee equal to one and one quarter percent (1 1/4%) of net sales of Breaking Waves through June 30, 2002 and thereafter one and three quarters percent (1 3/4%) of net sales of Breaking Waves through September 30, 2011 ("RAYA L/C Fees"). Such amounts are payable forty-five days after the close of each fiscal quarter. In October 2001, the Trust and RAYA received advance payments to be applied towards future fees of \$24,500 and \$12,250, respectively.

27

The following table summarizes the percentage due to each party, as noted above, as a percentage of net sales for the year ended June 30, 2003:

	% of Net Sales	Amount
	-----	-----
RAYA	0.58	\$44,076
ZAT	0.24	17,934
ARC	1.75	132,988
	-----	-----
Total	2.57	\$194,998
	=====	=====

In August 2000, Breaking Waves received an \$80,000 advance from Play Co. against future orders of merchandise. No orders were received against this advance and in December 2000 Breaking Waves repaid the full \$80,000 to Play Co.

In October 1996, pursuant to a promissory note, the Company loaned Harold Rashbaum its President, Chief Financial Officer and Chief Executive Officer a total of \$50,000 bearing interest at 6 1/2% payable over three years. As of June 30, 2003, the unpaid portion, which is due on demand, amounted to \$37,000, which has been classified as current. As of June 30, 2003, the Company's President was also advanced additional funds totaling \$3,000 which are non-interest bearing and due on demand and are classified as current.

Before he became an Officer and Director of the Company, Mr. Rashbaum provided consulting services to the Company through HBR, a company of which he is an officer and director and of which his wife is the sole shareholder. In 1996, HBR entered into an oral consulting agreement with the Company providing for the payment to HBR of 5% of the net profits received by the Company from the distribution of "Dirty Laundry." To date, HBR has not received any fees as a result of the distribution of "Dirty Laundry" not generating any net profits.

Alain Le Guillou, a director of the Company, has been a consultant to the Company since 1996. Prior to July, 2001, he received \$12,000 per annum for such services which was subsequently reduced to \$6,000 per annum. Until recently, Dr. Le Guillou was the son-in-law of Harold Rashbaum.

During the years ended June 30, 2003 and June 30, 2002, the Company paid \$24,000 and \$24,000, respectively, in financial consulting fees to DRA Consulting, Inc., a company whose president is the daughter of the Company's Chairman of the Board, President, Chief Executive Officer.

28

ITEM 13. EXHIBITS AND REPORTS ON FORM 8-K

(a) The following financial statements of the Company are included as Part II,

Edgar Filing: SHOPNET COM INC - Form 10KSB

Item 8:

Index to Financial Statements	F
Independent Auditor's Report	F-1
Independent Accountants' Report	F-2
Balance Sheets	F-3
Statements of Operations	F-4 to F-5
Statement of Stockholders' Equity	F-6 to F-7
Statements of Cash Flows	F-8 to F-11
Notes to Financial Statements	F-12 to F-35

(b) Form 8-K

None.

(c) The following exhibits which are designated by an asterisk (*) are to be filed by amendment. Exhibits not so designated previously were filed with the Securities and Exchange Commission with either (i) the Registration Statement on Form SB-2, file no. 333-5098-NY, (ii) the Registration Statement on Form SB-2, file no. 333-5098-NY, Post- Effective Amendment No. 1, (iii) the Registration Statement on Form SB-2, file no. 333-5098-NY, Post-Effective Amendment No. 2, or (iv) such other documents as the Company has filed with the Securities and Exchange Commission. Pursuant to 17 C.F.R. 230.411, each exhibit filed by the Company is incorporated by reference herein.

3.1	Certificate of Incorporation of the Company
3.2	Amendment to Certificate of Incorporation of the Company, filed in June
3.4	By-Laws of the Company
3.6	Certificate of Incorporation of Breaking Waves, Inc.
3.7	By-Laws of Breaking Waves, Inc.
3.8	Certificate of Amendment to Certificate of Incorporation
4.1	Specimen Common Stock Certificate
4.2	Specimen Warrant Certificate
4.4	Form of Warrant Agreement between the Company, the Underwriter and Transfer & Trust Company
4.5	Form of Restricted Stock Agreement
10.2	The Company's Senior Management Incentive Plan
10.4	Consulting Agreement between Breaking Waves, Inc. and Dan Stone
10.5	Lease for premises at 112 West 34th Street, New York, New York
10.6	Lease for premises at 8410 N.W. 53rd Terrace, Miami, Florida
10.6(a)	Amendment to lease at 8410 N.W. 53rd Terrace, Miami, Florida
10.7	Stock Purchase Agreement between the Company, European Ventures Corp Inc., and the shareholders of Breaking Waves, Inc., dated May, 1996
10.9	Property Acquisition Agreement between the Company and Rogue Features, 1996
10.10	Co-production agreement between the Company and Rogue Features, Inc., and all amendments thereto
10.11	Right of First Refusal Agreement with principals of Rogue Features, Inc.
10.13	Shippers Agency Agreement between Hollywood Productions, Inc., Enterprises, Inc.
10.14	License Agreement between Breaking Waves, Inc. and Beach Patrol, Inc.
10.16	Employment Agreement with Michael Friedland (incorporated by reference exhibit in the Company's 10-KSB for the year ended December 31, 1996)
10.17	Employment Agreement with Malcolm Becker (incorporated by reference exhibit in the Company's 10-KSB for the year ended December 31, 1996)
10.18	Termination of Employment Agreement with Robert Melillo (incorporated by reference to the indicated exhibit in the Company's 10-KSB for the year ended December 31, 1996)

Edgar Filing: SHOPNET COM INC - Form 10KSB

10.19	Trident Releasing, Inc. License Agreement (incorporated by reference to the indicated exhibit in the Post-Effective Amendment No. 1)
	29
10.20	Cyclone Option Agreement (incorporated by reference to the indicated exhibit in the Post-Effective Amendment No. 1)
10.21	Cyclone Co-Writer Agreement (incorporated by reference to the indicated exhibit in the Post-Effective Amendment No.)
10.22	Heller Financial Agreement (incorporated by reference to the indicated exhibit in the Post-Effective Amendment No. 2)
10.23	Non-Executive Director Stock Option Plan (incorporated by reference to the indicated exhibit in the Company's June 1997 Annual Meeting)
10.24	Kawasaki Motors Corp., USA "Jet Ski" License Agreement (incorporated by reference to the indicated exhibit in the Company's 10-KSB for the year ended December 31, 1997)
10.25	Amendment to lease at 112 West 34th Street, New York, New York (incorporated by reference to the indicated exhibit in the Company's 10-KSB for the year ended December 31, 1997)
10.26	Form of Subscription Agreement used in connection with the Company's February 1998 Private Placement (incorporated by reference to the indicated exhibit in the Company's 10-KSB for the year ended December 31, 1997)
10.27	Form of Subscription Agreement used in connection with the Company's February 1998 Private Placement (incorporated by reference to the indicated exhibit in the Company's 10-KSB for the year ended December 31, 1998)
10.28	Amendment to Employment Agreement with Michael Friedland dated August 1, 1998 (incorporated by reference to the indicated exhibit in the Company's 10-KSB for the year ended December 31, 1998)
10.29	Amendment to Employment Agreement with Malcolm Becker dated January 1, 1999 (incorporated by reference to the indicated exhibit in the Company's 10-KSB for the year ended December 31, 1998)
10.30	Second Amendment to Employment Agreement with Malcolm Becker dated August 1, 1999 (incorporated by reference to the indicated exhibit in the Company's 10-KSB for the year ended December 31, 1998)
10.31	Lease for premises at 14 East 60th Street, Room 402, New York, New York (incorporated by reference to the indicated exhibit in the Company's 10-QSB for the quarter ended September 30, 1999)
10.32	Option Agreement - Robb Peck McCooley Clearing Corporation (incorporated by reference to the indicated exhibit in the Company's 10-QSB for the quarter ended September 30, 1999)
10.33	License Agreement with Gottex Models Ltd, dated November 1, 2000
10.34	Factoring Agreement with Century Business Credit Corp. dated September 1, 2000
10.35	Supplement to factoring or Security Agreement with Century Business Credit Corp. dated August 14, 2000
10.36	Corporate Guaranty unlimited between Century Business Credit Corp. and Shopnet.com, Inc. dated August 14, 2000
10.37	Trademark Collateral Security Agreement between Century Business Credit Corp. and Shopnet.com, Inc. dated August 14, 2000.
10.38	Consulting Agreement with Larry Nash, Inc., dated August 5, 2000
10.39	Lease between 112 West 34th Street Company, as landlord, and Breakin' Bad, LLC, as tenant, dated August 8, 2001.
16.1	Letter from Scarano & Tomaro, P.C. regarding dismissal of Scarano & Tomaro as auditors (incorporated by reference to the indicated exhibit in the Company's Form 8-K/A filed on November 24, 1998)
16.2	Letter from Massella Rubenstein LLP regarding dismissal of Massella Rubenstein LLP as auditors (incorporated by reference to the indicated exhibit in the Company's Form 8-K/A filed on November 24, 1998)

Edgar Filing: SHOPNET COM INC - Form 10KSB

Form 8-K filed on January 29, 2002)
21.1 Subsidiaries of the Registrant
31.1 Certification of the Chief Executive Officer and Chief Financial Officer
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.(filed herewith)
32.1 Certification of the Chief Executive Officer and Chief Financial Officer
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. (filed herewith)

30

Item 14. Principal Accountant Fees and Services.

Audit Fees. The aggregate fees billed by our auditors, for professional services rendered for the audit of the Company's annual financial statements for the years ended June 30, 2003 and 2002, and for the reviews of the financial statements included in the Company's Quarterly Reports on Form 10-QSB during the fiscal years were \$21,500 and \$15,000, respectively.

Audit Related Fees. For the years ended June 30, 2003 and 2002, the Company incurred fees to auditors of \$1,500 and \$1,500 for audit related fees, respectively.

All Other Fees. The aggregate fees billed by auditors for services rendered to the Company, other than the services covered in "Audit Fees" and for the fiscal years ended June 30, 2003 and 2002 were \$11,740 and \$-0-, which fees primarily related to the Company's tax returns.

The Audit Committee has considered whether the provision of non-audit services is compatible with maintaining the principal accountant's independence.

31

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 hereunto duly authorized on the 25th day of November, 2003.

ShopNet.Com, Inc.

By: /s/ Harold Rashbaum

Harold Rashbaum
Chairman of the Board, Chief Executive
Officer, Chief Financial Officer and President

Pursuant to the requirements of the Securities Act of 1933 as amended, this Registration Statement has been signed below by the following persons in the capacities and on the dates indicated.

Date 11/25/03

/s/ Harold Rashbaum
Harold Rashbaum
Chairman of the Board,
Chief Executive Officer,

Edgar Filing: SHOPNET COM INC - Form 10KSB

Chief Financial Officer
President, and Director

32

SHOPNET.COM, INC. AND SUBSIDIARIES

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

Independent auditors' report for the year ended June 30, 2003

Consolidated balance sheets as of June 30, 2003 and June 30, 2002

Consolidated statements of operations for the years ended June 30, 2003 and June 30, 2002

Consolidated statements of stockholders' equity for the years ended June 30, 2003 and June 30, 2002

Consolidated statements of cash flows for the years ended June 30, 2003 and June 30, 2002

Notes to consolidated financial statements

INDEPENDENT AUDITORS' REPORT

To the Board of Directors and Stockholders of Shopnet.com, Inc.

We have audited the accompanying consolidated balance sheet, statements of operations, stockholders' equity and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Shopnet.com, Inc. and subsidiaries as of June 30, 2003 and the consolidated results of its operations, changes in stockholders' equity and cash flows for the year ended in conformity with accounting principles generally accepted in the United States.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 16 to the financial statements, the Company has suffered recurring losses from operations and has a net capital deficiency that raises substantial doubt about its ability

Edgar Filing: SHOPNET COM INC - Form 10KSB

to continue as a going concern. Management's plans in regard to these matters are also described in Note 16. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

JEROME ROSENBERG, CPA, P.C.
August 21, 2003

F-1

SHOPNET.COM, INC. AND SUBSIDIARIES Consolidated Balance Sheet As of June 30, 2003 and June 30, 2002

ASSETS	June 30 2003
Current assets:	
Cash	\$ 2
Restricted cash (Note 9)	25
Accounts receivable, net (Note 3)	15
Inventory	7
Prepaid expenses (Note 5)	23
Advances to officer	4
Total current assets	78
Property and equipment, net (Note 4)	8
Film production and distribution costs, net	1,20
Costs in excess of net assets of business acquired (Note 6)	72
Investments in movie ventures (Note 7)	23
Deferred tax asset-non-current	22
Other assets	1
Total assets	\$ 3,27
	=====
LIABILITIES AND STOCKHOLDERS' EQUITY	
Current liabilities:	
Note payable (Note 17)	\$ 5
Due to factor (Note 9)	1,05
Accounts payable	53
Accrued expenses (Note 8)	4
Capital lease obligations	1
Other taxes payable	
Deferred tax liability	
Total current liabilities	1,70

Long Term Liabilities:	
Note Payable (Note 9)	25
Total liabilities	1,95

Edgar Filing: SHOPNET COM INC - Form 10KSB

Commitments and contingencies

Stockholders' equity

Common stock- \$.001 par value, 20,000,000 shares authorized, 8,067,462
shares issued and outstanding at June 30, 2003 and 7,472,224 shares
issued and

outstanding at June 30, 2002

Capital in excess of par value

Accumulated deficit

6,65

(5,34

Total stockholders' equity

1,32

Total liabilities and stockholders' equity

\$ 3,27

The accompanying notes should be read in conjunction with
the consolidated financial statements

F-2

SHOPNET.COM, INC. AND SUBSIDIARIES

Consolidated Statement of Operations

For the Years ended June 30, 2003 and June 30, 2002

	June 30, 2003	
Net sales	\$ 7,599,223	\$
Cost of sales	5,257,972	
Gross profit	2,341,251	
Expenses:		
Selling, general, and administrative	2,806,222	
Total expenses	2,806,222	
Loss before other income (expenses) and income tax benefit	(464,971)	
Other income (expenses):		
Equity in earnings (loss) of affiliate	(14,241)	
Rental income	-	
Interest and finance expense	(409,419)	
Interest income	1,713	
Total other income (expense)	(421,947)	
Loss before income tax benefit	(886,918)	
Income tax benefit	-	
Net loss	(886,918)	

Edgar Filing: SHOPNET COM INC - Form 10KSB

Other items of comprehensive loss	-	
Comprehensive loss	\$ (886,918)	\$
Basic and diluted loss per share:	\$ (.11)	\$
Weighted average number of common shares outstanding	7,869,049	

The accompanying notes should be read in conjunction with
the consolidated financial statements

F-3

SHOPNET.COM, INC. AND SUBSIDIARIES Consolidated Statement of Stockholders' Equity For The Years Ended June 30, 2003 and June 30, 2002

	Common Stock Shares	Amount	Additional Paid-in Capital	Accumulated Deficit	Conv Debe
Balances at June 30, 2001 (Balance forward)	7,472,244	\$ 7,472	\$ 6,638,852	\$ (4,017,179)	\$
Unrealized loss on marketable securities	-	-	-	-	
Loss for the year ended June 30, 2002	-	-	-	(436,562)	
Balances at June 30, 2002	7,472,224	7,472	6,638,852	(4,453,741)	
August 28, 2002, issuance of 5% Convertible debentures	-	-	-	-	
Nov. 6, 2002-Conversion of debentures into 595,238 shares	595,238	595	14,405	-	(
Net loss for the year ended June 30, 2003	-	-	-	(886,918)	
Balances at June 30, 2003	8,067,462	\$ 8,067	\$ 6,653,257	\$ (5,340,659)	\$

The accompanying notes should be read in conjunction with
the consolidated financial statements

F-4

SHOPNET.COM, INC. AND SUBSIDIARIES Consolidated Statement of Cash Flows

Edgar Filing: SHOPNET COM INC - Form 10KSB

For the Years Ended June 30, 2003 and June 30, 2002

	June 30, 2003
Cash flows from operating activities:	
Net loss	\$ (886,91
Adjustments to reconcile net income to net cash used in operating activities:	
Equity in loss of affiliate	14,24
Amortization and depreciation	27,87
Decrease (increase) in:	
Cash-restricted	(250,00
Accounts receivable	5,84
Other receivables	(57,58
Inventory	151,79
Prepaid expenses	61,26
Deferred tax asset	(1,58
Other assets	14,58
Increase (decrease) in:	
Accounts payable	253,49
Accrued expenses	37,80
Deferred tax liability	(1,56
Other taxes payable	10
Net adjustment	256,26
Net cash (used for) provided by operating activities	(630,65
Cash flows from investing activities:	
Acquisition of property and equipment	(40,17
Investment in movie ventures	
Net cash used in investing activities	\$ (40,17

The accompanying notes should be read in conjunction with
the consolidated financial statements

F-5

SHOPNET.COM, INC. AND SUBSIDIARIES
Consolidated Statement of Cash Flows
For the Years Ended June 30, 2003 and June 30, 2002
(Continued)

	June 30, 2003
Cash flows from financing activities:	

Edgar Filing: SHOPNET COM INC - Form 10KSB

Principal payments on capital lease obligations	\$ (7,49
Net proceeds from factoring agreement	363,59
Proceeds from sale of common stock	15,00
Issuance of note payable	50,00
Issuance of long-term note payable	250,00
Increase in capital leases	17,66

Net cash provided by (used in) financing activities	688,76

Net decrease in cash	17,93
Cash, beginning of period	3,30

Cash, end of period	\$ 21,24
	=====
Supplemental disclosure of cash flow information:	
cash paid for:	
Interest	\$ 314,57
	=====
Income taxes	\$
	=====

The accompanying notes should be read in conjunction with
the consolidated financial statements

F-6

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1- ORGANIZATION

Shopnet.com, Inc. ("Shopnet") was incorporated in the State of Delaware on December 1, 1995 under the name of Hollywood Productions, Inc. It was formed for the purpose of acquiring screenplays and producing motion pictures. On May 10, 1999, the Company filed an amendment to its Articles of Incorporation to change its name to Shopnet.com, Inc. On May 12, 1999, Shopnet incorporated a new wholly owned subsidiary, Hollywood Productions, Inc. ("Hollywood"), to which the Company assigned all of its film rights. Accordingly, Shopnet is considered a holding company. During September 1996, simultaneously with the completion of its Initial Public Offering ("IPO"), Shopnet acquired all of the capital stock of Breaking Waves, Inc. ("Breaking Waves"). Breaking Waves designs, manufactures, and distributes private and brand name labels of children's swimwear nationally. As of June 30, 2001, Shopnet and all of its subsidiaries changed their financial year-end from December 31st to June 30th.

NOTE 2- SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a) Principles of consolidation

The accompanying consolidated financial statements include the accounts of Shopnet and its wholly owned subsidiaries, Breaking Waves and Hollywood (collectively referred to as the "Company"), after

Edgar Filing: SHOPNET COM INC - Form 10KSB

elimination of all significant intercompany transactions and accounts. Affiliated companies, which are 20 to 50 percent owned, are accounted for under the equity method.

b) Cash and cash equivalents

The Company considers highly liquid investments with maturities of three months or less at the time of purchase to be cash equivalents. As of June 30, 2003 the Company did not maintain balances in accounts, which were in excess of Federal Deposit Insurance Corporation limits.

c) Accounts Receivable:

The Company utilizes the allowance method for recognizing the collectibility of its accounts receivables. The allowance method recognizes bad debt expense based on review of the individual accounts outstanding based on the surrounding facts. As of June 30, 2003 management provided an allowance of \$20,000. The accounts receivable balance on the balance sheet as of June 30, 2003 is shown net of this allowance.

d) Marketable securities

All the Company's marketable securities are classified as available for sale and recorded at current market value. Net unrealized gains and losses on marketable securities available for sale are credited or charged to other comprehensive income. Marketable securities were classified as non-current as a result of being pledged pursuant to certain factoring agreements.

F-7

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 2- SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

e) Inventory:

Inventory consists of finished goods and is valued at the lower of cost (using the first-in, first-out method) or market. All inventory is pledged as collateral for factored receivables pursuant to an agreement with a financial institution.

f) Property and Equipment:

Property and equipment are recorded at cost less accumulated depreciation and amortization. The Company provides for depreciation and amortization using the Straight-Line and the Modified Accelerated Cost Recovery System (MACRS) method over the estimated useful lives of the assets which range between three and seven years. Expenditures for maintenance and repairs are charged to operations as operating expenses, when incurred.

g) Film production and distribution costs:

The Company follows industry standards in capitalizing film production and distribution costs. Film production and distribution costs include all costs associated with the writing, producing, and distribution of the film. Film costs include the costs of production, prints,

Edgar Filing: SHOPNET COM INC - Form 10KSB

pre-release, and other advertising expected to benefit future periods. These costs as well as participation and talent residuals, are charged against earnings on an individual film basis in the ratio that the current year's gross film revenues bear to management's estimate of total remaining ultimate gross film revenues from all sources.

Film costs are stated at the lower of cost or estimated net realizable value on an individual film basis. Revenue and cost forecasts are continually reviewed by management and revised when warranted by changing conditions. Estimates of total gross revenues can change significantly due to the level of market acceptance of film products. Accordingly, revenue estimates are reviewed periodically and amortization is adjusted. Such adjustments could have a material effect on the results of operations in future periods. When estimates of total revenue and costs indicate that a feature film will result in an ultimate loss, additional amortization is recognized to the extent required to produce a zero gross margin over the remaining life of the film.

For the year ended June 30, 2003, the Company determined that the estimated net realizable value had not changed from what was reported at June 30, 2002 and accordingly made no adjustment to the estimated net realizable value.

F-8

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 2- SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

h) Intangible assets:

Effective for the year ended June 30, 2002, the Company adopted FAS 142 (Goodwill and Other Intangible assets). Under FAS 142, goodwill and indefinite lived intangible assets are no longer amortized but are reviewed annually for impairment. Goodwill is tested for impairment at the reporting unit level. Under FAS 142, the fair value of a reporting unit is compared to its carrying amount, including its goodwill. If the book value (carrying amount) is below the fair value assessment, there will be no impairment or loss. If the fair value is below the book value (carrying amount), then the Company needs to perform a second test to determine the gap between the impaired fair value of goodwill and its carrying amount.

The Company has determined that no impairment exists as of June 30, 2003. Accordingly, the book value has not been written down.

i) Equity Method of Accounting:

Investments in significantly (20 to 50 percent) owned affiliates are accounted for by the equity method of accounting, whereby the investment is carried at cost of acquisition, plus the Company's equity percentage in undistributed earnings or losses since acquisition. Reserves are provided where management determines that the investment or equity in earnings is not realizable.

j) Income taxes:

The Company accounts for income taxes in accordance with Statement of Financial Accounting Standards ("SFAS") No. 109, "Accounting for

Edgar Filing: SHOPNET COM INC - Form 10KSB

Income Taxes" which requires the use of the "liability method" of accounting for income taxes. Accordingly, deferred tax liabilities and assets are determined based on the difference between the financial statement and tax basis of assets and liabilities, using enacted tax rates in effect for the year in which the differences are expected to reverse. Current income taxes are based on the respective periods' taxable income for federal, state and city income tax reporting purposes.

k) Revenue and cost recognition:

The terms of Breaking Waves' sales are FOB shipping point thereby revenue is recognized upon shipment from the Company's warehouse. Sales returns are recorded upon acceptance of the goods by the warehouse. Duty costs, which are a component of cost of sales, are recorded upon the clearance of such goods through customs.

Revenues from the theatrical distribution of motion pictures are recognized when motion pictures are exhibited. Revenues from video sales are recognized, together with related costs, on the date that video units are made widely available for sale by retailers. Revenues from the licensing of feature films, together with related costs are recorded when the material is available for telecasting by the licensee and when certain other conditions are met. Film production and distribution costs are stated at the lower of unamortized cost or estimated net realizable value.

F-9

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 2- SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

k) Revenue and cost recognition: (continued)

The company recognizes revenue in accordance with the provisions of statement of financial Accounting Standard No. 139 and American Institute of Certified Public Accountants, Statement of Position 00-2 ("SOP 00-2"), "Accounting by Producers and Distributors of Films,". SOP 00-2 establishes new accounting standards for, among other things, marketing and development costs. The Company uses the individual film forecast method to amortize film costs.

l) Earnings per share:

Earnings per common share are computed pursuant to SFAS no. 128 "Earnings Per Share." Basic earnings per share are computed as net income (loss) available to common shareholders divided by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflect the potential dilution that could occur from common shares issuable through stock options, warrants and convertible preferred stock. Both basic earnings per share and diluted earnings per share are the same since the Company's outstanding stock options and warrants have not been included in the calculation because their effect would have been anti-dilutive.

m) Use of estimates:

Edgar Filing: SHOPNET COM INC - Form 10KSB

In preparing financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions which affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and revenues and expenses during the reporting period. The most significant estimate with regard to these financial statements is the estimate of projected income of motion pictures, which is the basis used in amortizing film production and distribution costs. Actual results could differ from those estimates.

n) Fair value disclosure at June 30, 2003:

The carrying value of cash, accounts receivable, inventory, marketable securities, accounts payable, accrued expenses, and capital lease obligations are a reasonable estimate of their fair value.

o) Reclassifications:

Certain prior period accounts have been reclassified to conform to the current year presentation.

p) Cost in excess of net assets of business acquired:

Cost in excess of net assets of business acquired in connection with the acquisition of Breaking Waves were amortized through June 30, 2002 on a straight line basis over the estimated useful life of the related assets acquired for a period of fifteen years. No amortization was recorded for the years ended June 30, 2003 and June 30, 2002. (See Note 6)

F-10

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 2- SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

q) Accounting for stock-based compensation:

The Company elected to continue to measure compensation cost using Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees," as is permitted by SFAS No. 123, "Accounting for Stock-Based Compensation." Accordingly, no compensation cost has been recognized for the options issued under the Incentive Plan, as the exercise price and market value at the date of grant were the same.

For companies that choose to continue applying APB No. 25, SFAS No. 123 requires certain pro forma disclosures as if the fair value method had been utilized. Had compensation cost for the Company's stock-based compensation plan been determined based on the fair value at the grant dates for awards under the plan consistent with the method of SFAS No. 123, the Company's net income (loss) and earnings per share would have been reduced to the pro forma amounts indicated below utilizing the Black-Sholes option pricing model:

Edgar Filing: SHOPNET COM INC - Form 10KSB

	June 30, 2003	June 30, 2002
Net income (loss)-		
as reported	\$ (886,918)	\$ (436,562)
	=====	=====
pro forma	\$ (886,918)	\$ (436,562)
	=====	=====
Basic and Diluted EPS-		
as reported	\$ (.11)	\$ (.06)
	=====	=====
pro forma	\$ (.11)	\$ (.06)

The fair market value of each option grant is estimated at the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions:

Dividend yield	0.00%
Expected volatility	30%
Risk-free interest rate	6%
Expected life	1-5 years

r) Effect of new accounting standards:

The Company does not believe that any recently issued accounting standards, not yet adopted by the Company, will have a material impact on its financial position and results of operations when adopted.

F-11

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 3 - ACCOUNTS RECEIVABLE

Accounts receivable is comprised of the following:

	June 30, 2003	June 30, 2002
	-----	-----
Accounts receivable	\$ 33,261	\$ 41,207
Charge back receivables	145,702	132,000
	-----	-----
Total receivables	178,963	17,199
	-----	-----
Less: allowance for doubtful accounts	(20,000)	(20,000)
	-----	-----
Net accounts receivables	\$ 158,233	\$ 107,227
	=====	=====

Charge back receivables represent various amounts that are temporarily withheld for payment by various customers until certain conditions are fulfilled. These amounts are considered fully collectible by Breaking

Edgar Filing: SHOPNET COM INC - Form 10KSB

Waves and are categorized as a current asset.

NOTE 4 - PROPERTY AND EQUIPMENT

Property and equipment is comprised of the following:

	June 30, 2003	June 30, 2002
	-----	-----
Furniture & fixtures	\$ 43,869	\$ 41,207
Computer equipment and software	170,134	132,000
Leasehold improvements	16,574	17,199
	-----	-----
	230,577	190,406
Less: accumulated depreciation and amortization	148,233	120,362
	-----	-----
	\$ 82,344	\$ 70,044
	=====	=====

Computer equipment and software amounting to \$79,169 is pledged in connection with capital lease obligations.

Depreciation and amortization expense for the year ended June 30, 2003 and for the year ended June 30, 2002 amounted to \$27,871, and \$36,286, respectively.

F-12

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 5- PREPAID EXPENSES

Prepaid expenses are comprised of the following:

	June 30, 2003	June 30, 2002
	-----	-----
Prepaid insurance	\$ 4,454	\$ 23,167
Prepaid taxes	6,120	22,641
Prepaid consulting fee (See Note 9)	177,650	198,550
Prepaid salaries	-	3,422
Other prepaid expenses	49,484	51,188
	-----	-----
Total prepaid expenses	\$ 237,708	\$298,968
	=====	=====

NOTE 6- ACQUISITION OF BREAKING WAVES, INC.

Pursuant to a stock purchase agreement dated May 31, 1996 (the "Agreement"), on September 24, 1996, the Company issued 110,000 shares

Edgar Filing: SHOPNET COM INC - Form 10KSB

of common stock in exchange for all of the issued and outstanding capital stock of Breaking Waves. The transaction was accounted for using the purchase method of accounting. As a result of the transaction, excess of cost over net assets acquired totaling \$1,064,283 was recorded and was being amortized over the useful lives of the related assets which was fifteen years.

Effective for the year ended June 30, 2002, the Company adopted FAS 142 (Goodwill and Other Intangible assets). Under FAS 142, goodwill and indefinite lived intangible assets are no longer amortized but are reviewed annually for impairment. Goodwill is tested for impairment at the reporting unit level. Under FAS 142, the fair value of a reporting unit is compared to its carrying amount, including its goodwill. If the book value (carrying amount) is below the fair value assessment, there will be no impairment or loss. If the fair value is below the book value (carrying amount), then the Company needs to perform a second test to determine the gap between the impaired fair value of goodwill and its carrying amount.

The Company has determined that no impairment exists as of June 30, 2003. Accordingly, the book value has not been written down.

F-13

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 7- INVESTMENTS IN MOVIE VENTURES

a) Battle Studies

Pursuant to a co-production agreement dated April 17, 1998 with North Folk Films, Inc., the Company invested through June 30, 2003, \$212,385 for a 50% interest in a new entity, Battle Studies Productions, LLC ("Battle Studies") a limited liability company. Battle Studies is accounted for as joint venture in order to co-produce motion pictures and to finance the costs of production and distribution of such motion pictures. The joint venture retains all rights to the motion pictures, screenplays, and all ancillary rights attached thereto.

The Company accounts for the investment in Battle Studies on the equity method. For the years ended June 30, 2003 and June 30, 2002 the Company, recorded equity losses of \$793 and \$2,355, respectively, for its proportionate share of Battle Studies losses. No revenues have been derived from this film as of June 30, 2003.

On October 12, 2000, Battle Studies entered into a distribution agreement with Raven Pictures International ("Raven Pictures") to distribute Battle Studies' motion picture ("Macheavelli Rises") to foreign countries. Battle Studies has granted rights under the agreement for the theatrical, video, non-theatrical and television markets. The term of the agreement is for twenty-four months for all portions of territory outside of the United States and English speaking Canada. Battle Studies expects to realize 75% (which is net of a 25% fee to Raven Pictures) of the expected estimated gross revenues derived from foreign countries less \$20,000 for marketing and advertising expense.

On January 17, 2001, Battle Studies entered into a distribution agreement with KOAN, Inc. ("KOAN") to distribute and promote Battle Studies' motion picture ("Machiavelli Rises") in the United States and Canada. Battle Studies has granted rights under the agreement for free TV, pay TV, cable,

Edgar Filing: SHOPNET COM INC - Form 10KSB

satellite, video and DVD markets. The terms of the agreement is for twenty-four months and it will be automatically renewed unless KOAN receives a letter of cancellation at least thirty days prior to the date of termination or if sales have not exceeded \$250,000 over the twenty-four month period.

Battle studies expects to realize 70% (which is net of a 30% fee to KOAN) of the expected estimated gross revenues derived from the United States and Canada less \$5,000 per year for promotional costs.

b) The Girl

Pursuant to an agreement dated July 1, 1999 with Artistic License Films Inc., Hollywood invested through June 30, 2003 \$35,000 for a 22.533% interest in a new entity, The Girl, LLC ("The Girl") a limited liability company. In return for its participation in The Girl, Hollywood is entitled to receive a non-contested, non-dilutable 22.533% ownership interest in The Girl, a recoupment of its investment on no less favorable terms than any other investor and 22.533% of 100% of any contingent compensation, which shall be actually received by The Girl. The Girl retains all rights to the motion pictures, the screenplays, and all ancillary rights attached thereto.

Hollywood accounts for the investments in The Girl under the equity method. For the year ended June 30, 2003 and the year ended June 30, 2002, the Company recorded \$14,241 and \$0, respectively, in net equity losses.

F-14

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 8- ACCRUED EXPENSES

Accrued expenses are comprised of the following:

	June 30, 2003	June 30, 2002
	-----	-----
Professional fees	\$ 6,729	\$ 4,718
Other corporate overhead	35,858	64
	-----	-----
	\$ 42,587	\$ 4,782
	=====	=====

NOTE 9- DUE TO FACTOR

Century Business Credit Corporation

On or about September 12, 2000, Breaking Waves entered into a factoring and revolving inventory loan and security agreement ("factoring agreement") with Century Business Credit Corporation ("Century") to sell its interest in all present and future receivables without recourse. Breaking Waves submits all sales offers to Century for credit approval prior to shipment, and pays a factoring commission of .75% of receivables sold.

Century retains from the amount payable to Breaking Waves a reserve for possible obligations such as customer disputes and possible credit losses on unapproved receivables. Breaking Waves may take advances of

Edgar Filing: SHOPNET COM INC - Form 10KSB

up to 85% of eligible receivables and up to 50% of the value of finished goods in inventory, with interest payable monthly at the rate of 1 3/4% over prime.

Pursuant to the terms of a Reimbursement and Compensation Agreement, a trust ("Trust"), the beneficiary of which is a relative of the Company's President and Chief Executive Officer ("CEO"), pledged assets as collateral for securing a \$250,000 letter of credit to replace a portion of a letter of credit previously pledged by the Company.

Accordingly, on December 20, 2000 the original agreement with the factor was amended to allow such replacement of collateral. Breaking Waves' Loan and Security Agreement with Century dated December 20, 2000 requires the provision of one or more letters of credit in the aggregate amount of \$1,150,000 to partially secure the line of credit. On September 15, 2001, Century required the Company to increase the amount of collateralized standby letters of credit by \$300,000 raising such amount to \$1,450,000.

On May 3, 2001, the Agreement with the Trust was amended so that the letter of credit secured by the Trust was increased to \$400,000. As a condition of the amendment, the Company entered into a guarantee agreement with Gal Capital Corp., whose President is a relative of the Company's President and CEO to act as guarantor of the obligation to the Trust up to \$400,000 in exchange for a fee of \$42,500 which the Company paid on May 3, 2001. The amended letter of credit expired on September 1, 2001 and was subsequently amended on September 15, 2001.

F-15

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 9- DUE TO FACTOR (Continued)

Century Business Credit Corporation (continued)

On September 15, 2001, the Amended and Restated Reimbursement and Compensation Agreement was entered into and further amended the agreement with the Trust, so that the letter of credit secured by the Trust was increased to \$750,000. The amended letter of credit expired on September 1, 2002 but can be extended year to year at the Company's option for a period of ten years. On September 1, 2002, the letter of credit was extended. Breaking Waves agreed to reimburse the Trust for any and all losses, fees, charges and expenses to the Trust in the event the letter of credit is called by Century and / or the issuing bank demands reimbursement from the Trust. Breaking Waves' obligations are guaranteed by the Company in addition to being secured by a first security interest in all of the assets of the Company and a subordinate security interest in all of the assets of Breaking Waves.

On September 15, 2001, the Company entered into a Reimbursement Agreement with relatives of an individual who is related to the President and CEO of the Company ("RAYA") who pledged assets as collateral for securing a \$300,000 letter of credit as additional collateral to secure Breaking Waves' Loan and Security Agreement with Century. Absent any default, the letter of credit will remain in effect for ten years. Shopnet under a separate Security Agreement dated September 15, 2001 guarantees the agreement. In September 2003, the letter of credit secured by RAYA was drawn upon by Century

Edgar Filing: SHOPNET COM INC - Form 10KSB

reducing Breaking Waves' liability to Century.

In exchange for the letters of credit, the Trust and RAYA will proportionately, based on the total outstanding letters of credit, receive a fee of one and one quarter percent (1-1/4%) of net sales of Breaking Waves through June 30, 2002 and thereafter one and three quarters percent (1-3/4%) of net sales through September 30, 2011. In October 2001, the Trust and RAYA received advance payments to be applied towards future fees of \$24,500 and \$12,250, respectively. All future payments are payable forty-five days after the close of each fiscal quarter. The fees are effective October 1, 2001.

In September 2001, the Company and Breaking Waves retained Arc Financial Corp. ("ARC"), a British Virgin Island company, for a ten-year term to provide financial consulting services.

Pursuant to the terms of a consulting services. Pursuant to the terms of a consulting agreement ("ARC Consulting Agreement"), ARC was retained to assist the Company in the acquisition of financing to acquire inventory and for other corporate purposes ("Financing"), as well as consult with the Company with regard to its ongoing operations, promote sales of Breaking Waves' products and improving production.

Pursuant to the terms of the ARC Consulting Agreement, the Company and Breaking Waves agreed to compensate ARC (i) an annual fee of \$20,000 ("Base Fee") and (ii) a percentage of annual net sales in the amount of 1-1/4% through June 30, 2002 and 1-3/4% of net sales for each year of the term thereafter through September 30, 2011 ("ARC Percentage Fee"), payable 45 days after the closing of each fiscal quarter.

In October 2001, ARC received (I) a lump sum payment of \$209,000 reflecting full advance payment of the Base Fee and (ii) \$36,750 reflecting advance payment of the Arc Percentage Fee. The agreement with Arc expires September 30, 2011. The Company and Breaking Waves are entitled to terminate the ARC Consulting Agreement any time after September 30, 2006, in which event all prepaid fees are forfeited.

F-16

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS

NOTE 9- DUE TO FACTOR (Continued)

Century Business Credit Corporation (Continued)

The following table summarizes the percentage due each party, as noted above, as a percentage of net sales for the year ended June 30, 2003:

	% of Net Sales	Amount
RAYA	0.58	\$ 44,076
ZAT	0.24	17,934
ARC	1.75	132,988
	2.57	\$194,998
	=====	=====

In December 2002, Breaking Waves entered into a Reimbursement and

Edgar Filing: SHOPNET COM INC - Form 10KSB

Compensation Agreement with TERE, S.A., a Swiss entity. As a consequence of Century being unwilling to grant credit to Breaking Waves unless it received one or more letters of credit satisfactory to it as well as cash collateral to partially secure the line of credit in such amounts, as it deems appropriate, the Trust reduced the letter of Credit secured by it to \$500,000. TERE, S.A. agreed to loan Breaking Waves the sum of \$250,000 represented by a promissory note. The funds were deposited as cash collateral with Century to replace the reduced portion of the letter of credit secured by the Trust.

In September 2003, the letter of credit secured by the Trust was drawn upon by Century, reducing Breaking Waves' liability to Century. The sum of \$250,000 in cash on deposit with Century has been classified on the accompanying balance sheet as restricted cash.

All obligations under this agreement are guaranteed by the Company and are secured by a security interest in all of the Company's assets.

As compensation, Breaking Waves paid to TERE all interest received from or credited to it by Century on the sums deposited pursuant to the Cash Collateral Agreement when received.

The term of the loan is for ten years.

ARC has agreed to pay to TERE, interest at the rate of 8% per annum on a quarterly basis.

Interest expense related to the factor agreement totaled \$205,591 and \$248,303 for the year ended June 30, 2003 and 2002, respectively. Century has a secured interest in Breaking Waves' inventory as collateral for the advances. As of June 30, 2003, the net advances to Breaking Waves from Century amounted to \$1,054,187.

Additionally, see Note 18 (Subsequent Events).

F-17

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS

NOTE 10- (BENEFIT OF) PROVISION FOR INCOME TAXES

(Benefit of) provision for income taxes is comprised of the following:

	Year ended June 30, 2003
Current:	
Federal	\$ -
State and local	980
	980
Deferred:	
Federal	-
State and local	(1,582)

Edgar Filing: SHOPNET COM INC - Form 10KSB

	(1,582)

Total (benefit of) provision for income taxes	\$ (602)
	=====

A reconciliation of the provision for income taxes on income per the federal statutory rate to the reported income tax expense is as follows:

	Year ended June 30, 2003

Federal statutory rate applied to pretax loss	\$ -
State and local income taxes, net of federal income tax benefit, applied to pretax loss	-
Permanent differences	-
Increase in valuation allowance	-
Current provision for state and local taxes	980
(Increase) in deferred tax assets	(1,582)

Increase (decrease) in deferred tax liability	\$ (602)
	=====

Income taxes are provided for the tax effects of transactions reported in the financial statements and consist of taxes currently due plus deferred taxes related to difference between the financial statement and income tax bases of assets and liabilities for financial statements and income tax reporting purposes.

Deferred tax assets and liabilities represent the future tax return consequences of these temporary differences, which will either be taxable or deductible in the year when the assets or liabilities are recovered or settled.

Accordingly, measurement of the deferred tax assets and liabilities attributable to the book-tax basis differential are computed at a rate of 34% federal and 11% state and local pursuant to SFAS No. 109.

F-18

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 10- (BENEFIT OF) PROVISION FOR INCOME TAXES (Continued)

The tax effect of significant items comprising the Company's net non-current deferred tax assets and liability are as follows:

	June 30, 2003

Net operating loss carryforwards	\$ 1,477,334
Inventory capitalization	51,736
Write down of film costs	-
Valuation allowance	(1,303,248)

Deferred non-current tax asset	225,822

Edgar Filing: SHOPNET COM INC - Form 10KSB

Equity earnings (loss) of affiliate	(14,241)
Depreciable assets	17,861
Deferred non-current tax liability	3,620
Net non-current deferred tax asset	\$ 222,202

Shopnet and its subsidiaries have a tax year-end of December 31st and file a consolidated tax return for federal tax purposes. For state and local purposes, Shopnet and its subsidiaries file separate tax returns. As such, each entity computes its state and local tax based on its own taxable income or loss.

At June 30, 2003 and June 30, 2002, the Company had a net operating loss carry-forward (NOL) of approximately \$3,576,000 for federal tax purposes and \$3,676,000 for state tax purposes, all of which expire between 2012 and 2022, Management believes it is more likely than not that the results of future operations will generate sufficient taxable income to realize the deferred tax assets.

NOTE 11- COMMITMENTS AND CONTINGENCIES

a) Lease commitments

Shopnet and Breaking Waves jointly share their administrative offices under a lease agreement signed July 2001 by Breaking Waves. Shopnet is provided office space by Breaking Waves on a rent-free basis. The lease agreement expires on September 30, 2007. Annual rent under this lease is \$84,915 through December 31, 2004 and \$97,560 for the remainder of the lease period. Additionally, Breaking Waves leases an offsite office for one of its designers on a month-to-month basis with annual payments approximating \$13,200.

F-19

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 11- COMMITMENTS AND CONTINGENCIES (Continued)

Lease commitments (continued)

The approximate annual future minimum rentals under non-cancelable operating lease signed by Breaking Waves are as follows:

For the fiscal year ended June 30:	
2004	\$ 84,915
2005	90,338
2006	95,760
2007	95,760
Thereafter	23,940

	\$ 390,713
	=====

Rent expense for the year ended June 30, 2003 and 2002 amounted to \$108,869 and \$94,508, respectively.

Edgar Filing: SHOPNET COM INC - Form 10KSB

b) Significant vendors and customers

Breaking Waves purchases 100% of its inventory from three vendors, two in Indonesia (74%) and the other in The Republic of Korea (26%). Breaking Waves believes other sources and vendors are available and that it is not dependent exclusively on these vendors. For the year ended June 30, 2003, the year ended June 30, 2002 Breaking Waves had three customers, which comprised 44% and 36% of net sales, respectively.

c) Seasonality

Breaking Waves' business is considered seasonal with a large portion of its revenues and profits being derived between November and March. Each year from April through October, Breaking Waves engages in the process of designing and manufacturing the following season's swimwear lines, during which time it incurs the majority of its production costs with limited revenues and also engages in the sale of product at negative gross margin to remove slow moving items and decrease its carrying cost.

d) License agreements

During June 2000, Breaking Waves entered into a license agreement with an effective date of November 1, 2000 with Gottex Models Ltd., an Israeli corporation and Gottex Models (USA) Corp., a New York corporation for the use of the trademark "Gottex" in the United States of America for children's swimwear. The agreement calls for a royalty fee of 7% of net sales with guaranteed minimum annual royalties of \$70,000 to \$140,000 over the life of the agreement. Breaking Waves recorded royalties under the agreement totaling \$163,019 and \$73,408 for the year ended June 30, 2003 and for the year ended June 30, 2002.

On July 29, 2002 Breaking Waves entered into a licensing agreement with LMH, Inc. whereby Breaking Waves was granted exclusive use of certain trademarks, namely "Little Me" and

F-20

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 11- COMMITMENTS AND CONTINGENCIES (Continued)

License agreements (continued)

"Muffings" in the United States, Canada and Mexico, and the use of "Tapioca" and "Juniper" solely in the United States.

The licensing agreement has a term of three years ending on July 31, 200, unless terminated earlier and agreed to by both parties.

In consideration of both the license granted and the design services to be performed by LMH, Breaking Waves has agreed to pay a sales royalty equal to 5% of net sales of the Licensor's products.

Under the terms of the agreement, Breaking Waves agreed to guarantee a minimum royalty payment of \$10,000 for the period August 1, 2002 to July 31, 2003.

Edgar Filing: SHOPNET COM INC - Form 10KSB

For the second and third years of the agreement, Breaking Waves agreed to pay a guaranteed minimum royalty of \$20,000 payable in four quarterly installments.

e) Co-production and property purchase agreements

Pursuant to co-production and property purchase agreements dated March 15, 1996, as amended, the Company acquired the rights to co-produce a motion picture and to finance the costs of production and distribution of such motion picture with the co-production. The Company retains all rights to the motion picture with the co-producer agreeing to finance \$100,000 of the cost of production. The Company retains all rights to the motion picture, the screenplay, and all ancillary rights attached thereto.

The motion picture was completed during the latter part of 1996 and, accordingly, the Company commenced the marketing and distribution process.

As of June 30, 2003 and June 30, 2002, the Company had invested \$1,971,956 for the co-production and distribution of such motion pictures whereas the co-producers have invested \$100,000. For the year ended June 30, 2003 and for the year ended June 30, 2002, the Company derived no revenues from the motion picture and had not amortized film costs.

For the years ended June 30, 2003 and June 30, 2002, the Company has not written down its film production and distribution costs as the carrying value of the asset equals its estimated net realizable value.

f) Litigation

On or about June of 2000, an action was brought in the Queens County Supreme Court against the Company and several others claiming, among other things, that the Company allegedly breached a contract and engaged in fraudulent statements (including supposedly promising the plaintiff options and then not allowing the plaintiff to exercise such options).

F-21

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 11- COMMITMENTS AND CONTINGENCIES (Continued)

Litigation (continued)

The plaintiff seeks, among other things, compensatory damages in the amount of \$497,500, punitive damages in the amount of \$995,000, together with costs and attorney's fees. The Company intends to contest the action vigorously and believes that such claims against it are baseless and without merit.

NOTE 12- STOCKHOLDERS' EQUITY

a) 1996 Senior Management Incentive Plan

The shareholders approved the 1996 Senior Management Incentive Plan ("Incentive Plan") in May 1996. Officers, key employees and

Edgar Filing: SHOPNET COM INC - Form 10KSB

non-employees, who in the judgment of the Company render significant service to the Company, are eligible to participate.

The Incentive Plan provided for the award of a broad variety of stock-based compensation alternatives such as non-qualified stock options, incentive stock options, restricted stock, performance awards and stock appreciation rights. The Incentive Plan provided 750,000 shares of common stock to be offered from either authorized and unissued shares or issued shares, which have been reacquired by the Company.

On March 14, 1997, the Company granted 132,000 options to purchase shares of common stock pursuant to the Company's Incentive Plan consisting of 88,000 options to the Company's President and 44,000 options to another officer. The exercise price of each option was fixed at \$1.46 (as revised) per share and the options expired in March 2002. No options were exercised.

During April 1999, the Company granted its President 44,000 stock options. The exercise price of each option is a \$1.38 per share and the options expire April 16, 2004.

F-22

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 12- STOCKHOLDERS' EQUITY (continued)

1996 Senior Management Incentive Plan (continued)

A summary of the status of the Company's stock options outstanding as of June 30, 2003 is as follows:

	Number Option

Outstanding at December 31, 1999	1
Granted	
Exercised	
Cancelled	

Outstanding at December 31, 2000	1
Granted	
Exercised	
Cancelled	

Outstanding at June 30, 2001	1
Granted	
Exercised	
Cancelled	1

Outstanding at June 30, 2002	
Granted	
Exercised	
Cancelled	

Outstanding at June 30, 2003	=====

Edgar Filing: SHOPNET COM INC - Form 10KSB

b) Warrants

- i) Initially, each Warrant issued in the initial public offering of September 24, 1996 entitled the holders thereof to purchase one share of the Company's common stock at an exercise price of \$6.50 per share, until September 9, 2002. On August 31, 2002, the Company extended the term of its warrants by 18 months. On June 23, 1997, the Board of Directors approved a reduction in the exercise price of the Warrants from \$6.50 to \$3.00. On February 5, 1998, the Company affected a one for three reverse split of the Company's common stock.
- ii) Accordingly, the Company adjusted the terms of the Warrants to reflect the reverse split such that exercise of three Warrants would entitle the holder to purchase one share of common stock at an exercise price of \$9.00. Giving effect to the January 1999 100% common stock dividend, the January 2001 10% common stock dividend and the May 2001 20% common stock dividend, the warrants have been cumulatively adjusted such that the exercise of each warrant at an exercise price of \$3.41 purchases .88 of a share of common stock. The warrants expired on March 10, 2003.

F-23

SHOPNET.COM, INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 12- STOCKHOLDERS' EQUITY (continued)

Warrants (continued)

- iii) On April 15, 1998, the Company's Board of Directors authorized the distribution of warrants to all shareholders of the Company's common stock as of May 8, 1998. Pursuant to the distribution, each shareholder of record will receive one warrant to purchase one share of common stock at an exercise price of \$4.00 per share. The warrants, which are exercisable for a period of three years, commencing one year after issuance and receipt by shareholder, shall be issued and distributed once the Company has file a registration statement for same and same has been declared effective by the Securities and Exchange Commission. The Company to date has not filed the registration statement.

NOTE 13- RELATED PARTIES TRANSACTIONS

- a) For the year ended June 30, 2003 and 2002 financial consulting fees were paid to a corporation and an individual who are related to the Company's President and CEO amounting to \$37,000 and \$22,900, respectively.
- b) During October 1996, pursuant to two promissory notes, the Company loaned two of its officers a total of \$87,000 bearing interest at six and one-half percent (6 1/2) payable over three years. As of June 30, 2003, the unpaid portion amounted to \$37,000, which has been classified as current. As of June 30, 2003, the Company's President was also advanced additional funds totaling \$3,000, which are non-interest bearing and due on demand and are classified as current.

Edgar Filing: SHOPNET COM INC - Form 10KSB

F-24

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 14- INDUSTRY SEGMENTS

The Company's operations have been classified into two segments: swimwear sales and film productions. Information about the two segments is as follows:

	Year Ended	
	June 30,	
	2003	
	Segment	Consolidated
Sales:		
Swimwear sales	\$ 7,599,223	
Film production	-	
Total sales		\$7,599,223
Operating income (loss):		
Swimwear sales		(156,081)
Film production		(2,287)
Total operating income (loss)		(158,368)
Corporate:		
General and administrative expense		(306,553)
(Loss) equity in earnings of affiliate		(14,291)
Amortization expense		-
Interest income		-
Interest and finance expense		(409,419)
Other		1,713
Loss from operating before (benefit)		(886,918)
(Benefit) provision for income tax		-
Net (loss) income		\$ (886,918)
Identifiable assets:		
Swimwear sales		\$ 652,432
Film productions		1,436,887
Corporate		1,181,661

Edgar Filing: SHOPNET COM INC - Form 10KSB

Total assets

\$3,270,980

=====

Operating profit is total revenue less cost of sales and operating expenses and excludes general corporate expenses, interest expenses and income taxes. Identifiable assets are those used by each segment of the Company's operations. Corporate assets are primarily cash and investments.

F-25

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 15- PRIVATE PLACEMENT

On June 17, 2002, the Company appointed Alliance Long Term Capital Corp. as its placement agent in connection with the proposed private placement on a best "efforts basis" of up to \$1,500,000 of 5% Convertible Debentures and up to \$1,500,000 of 10% Non-Convertible Debentures. The term of this Agreement commenced on June 17, 2002 and was terminated on December 19, 2002.

Both of the Convertible Debentures and the Debt will pay interest semi-annually and shall have a maturity date of four years from the date of issuance. The Convertible Debentures will be secured by the assets of the Company and will be subordinated to the factor's first security interest in all the assets of the Company.

On August 28, 2002, the Company received the sum of \$15,000 representing payment for a subscription of \$15,000 of the 5% Convertible Debentures as referenced in above. As of August 28, 2002 the Company did not issue these Debentures. No additional 5% Convertible Debentures nor any 10% Non-Convertible Debentures have been issued.

On November 6, 2002, the subscription was converted into 595,238 shares of common stock.

NOTE 16- GOING CONCERN

The accompanying financial statements have been prepared in conformity with generally accepted accounting principles, which contemplate continuation of the Company as a going concern. However, the Company has incurred losses since its inception and has not yet been successful in establishing profitable operations. Further, the Company has current liabilities in excess of current assets. These factors raise substantial doubt about the ability of the Company to continue as a going concern. In this regard, management is proposing to raise any necessary additional funds not provided by operations through loans or through additional sales of its common stock or through a possible business combination with another company. There is no assurance that the Company will be successful in (a) raising this additional capital on acceptable terms or at all or (b) achieving profitable operations. The financial statements do not include any adjustments that might result from the outcome of these uncertainties. Additionally, see Note 18 (Subsequent Events).

NOTE 17- NOTE PAYABLE

Edgar Filing: SHOPNET COM INC - Form 10KSB

On November 8, 2002, the Company borrowed the sum of \$50,000 in the form of a promissory note from Amigal Salit, Ltd., an unrelated party. The note, which is non-interest bearing, was due on or before August 15, 2003. The Company is in default not having remitted payment when due. Amigal Salit, Ltd. has not contacted the Company regarding payment of the note. This note payable is shown on the accompanying balance sheet as a current liability.

F-26

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 17- NOTE PAYABLE (Continued)

In connection with this Note, the Company issued to Amigal Salit, Ltd., 100,000 warrants to purchase shares of the Company's common stock, par value, \$.001 per share at \$.05 per share (the "Warrant"). Holder shall purchase the Warrant for its own account and not with a view toward public resale or distribution. Upon exercise, the shares underlying the Warrant shall be "restricted securities" as that term is defined in Rule 144. The shares of common stock underlying the Warrant shall be appropriately legended to prevent the resale of said securities without registration or an exemption from registration.

On the same date, the Company entered into an agreement with ARC Financial Corporation, whereby the Company using the proceeds received from Amigal Salit, Ltd., agreed to pay \$50,000 as an advance against fees to be owed by Breaking Waves to ARC Financial Corporation in connection with Breaking Waves obligation to pay certain fees to ARC as part of a consulting agreement as described in Note 9 herein.

NOTE 18- SUBSEQUENT EVENTS

The Company and Breaking Waves have experienced a significant cash shortfall in the months following June 30th.

In September, The Company obtained a loan in the amount of \$44,000 from U.S. biomedical Corporation, a company whose former chief operating officer is the son-in-law of the company's president. The term of the loan is for one year and it matures on September 9, 2004. The loan may be repaid, at U.S. Biomedical's option, either in cash or non-registered stock of the Company.

Additionally, in September, the Company's president loaned the sum of \$5,000 to the Company on an interest free basis.

On October 21st, Breaking Waves was notified by Century Business Credit Corporation, that it was in default of its factoring agreement due to non payment of its obligations and that Century, under its factoring agreement with Breaking Waves, now has the option to foreclose on Breaking Waves' trademark and other collateral at anytime subsequent to October 21st.

As of November 18, 2003, no such action has been taken by Century.

F-27