SHOPNET COM INC
Form 10QSB
February 19, 2003

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

FORM 10-QSB
(Mark One)

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

For the quarterly period ended December 31, 2002

OR

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

For the transition period from __________ to __________

Commission File Number 0-28690
SHOPNET.COM, INC.
(Exact Name of Small Business Issuer as Specified in its Charter)

Delaware	13-3871821
(State or Other Jurisdiction of Incorporation or Organization)	(IRS Employer Identification No.)

112 West 34th Street, Suite 902, New York, New York 10120
(Address of Principal Executive Offices)

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

14 East 60th Street, Suite 402, New York, NY 10022
(Former Name, Former Address, and Former Fiscal Year, if Changed Since Last Report)

Check whether the Issuer (1) 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 [X] No [ ]

APPLICABLE ONLY TO CORPORATE ISSUERS

State the number of shares of each of the issuer's classes of common equity outstanding as of the latest practicable date: Common Stock, par value $.001 par value: 8,067,462 shares outstanding as of February 13, 2003.

SHOPNET.COM, INC. AND SUBSIDIARIES

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SHOPNET.COM, INC. AND SUBSIDIARIES
Consolidated Balance Sheets
As of December 31, 2002 and June 30, 2002

ASSETS

Current assets:

Cash	
Accounts receivable, net	
Other receivables	
Inventory	
Prepaid expenses	
Advances to officer	
Total current assets	
Property and equipment, net	
Film production and distribution costs, net	
Costs in excess of net assets of business acquired	
Investments in movie ventures	
Deferred tax asset-non-current	
Other assets	
Total assets	

LIABILITIES AND STOCKHOLDERS' EQUITY

Current liabilities:

Due to factor ....
Loan payable ....
Accounts payable ....
Accrued expenses ....
Capital lease obligations ....
Other taxes payable ....
Deferred tax liability ....

Total current liabilities ....

Total liabilities ....

Commitments and contingencies

Stockholders' equity
Common stock- $.001 par value, 20,000,000 shares authorized, 8,067,462 shares issued and outstanding at December 31, 2002 and 7,472,224 shares issued and outstanding at June 30, 2002 ....
Capital in excess of par value ....
Accumulated deficit ....

Total stockholders' equity ....

Total liabilities and stockholders' equity ....

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

SHOPNET.COM, INC. AND SUBSIDIARIES
Consolidated Statement of Operations and Comprehensive Income (Loss)
(Unaudited)

	Six Months Ended		Three Mo
	Dec. 31, 2002	Dec. 31, 2001	Dec. 31, 2002
Net sales	$ 750,678	$ 1,700,705	$ 730,871
Cost of sales	247,239	1,098,622	145,792
Gross profit	503,439	602,083	585,079
Expenses:			
Selling, general, and administrative	981,746	979,147	515,479
Amortization of costs in excess of net assets of business acquired	--	35,476	--

Total expenses	981,746	1,014,623	515,479
Income (loss) before other income (expenses) and provision for income taxes	(478,307)	(412,540)	69,600
Other income (expenses):			
Equity in earnings (loss) of affiliate	--	(63)	--
Rental income	--	9,050	--
Interest and financial expense	(90,185)	(155,919)	(66,998)
Interest income	936	10,933	936
Total other income (expense)	(89,249)	(135,999)	(66,062)
Income (loss) before provision for income taxes	(567,556)	(548,539)	3,538
Provision (benefit) for income taxes	--	--	--
Net income (loss)	(567,556)	(548,539)	3,538
Other items of comprehensive (loss) income	--	(6,350)	--
Comprehensive loss	$ (567,556)	$ (554,889)	$ 3,538
Basic:			
Net loss per share	$ (.074)	$ (.07)	$ .0004
Weighted average number of common shares outstanding	7,670,637	7,472,224	7,869,049

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

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SHOPNET.COM, INC. AND SUBSIDIARIES
Consolidated Statement of Stockholders' Equity
For The Six Months Ended December 31, 2002
(Unaudited)

	Common Stock		Additional Paid-in	Accumula
	Shares	Amount	Capital	Deficit

Balances at June 30, 2002 (Audited)	7,472,224	$ 7,472	$ 6,638,852	$(4,453,7
August 28, 2002, issuance of 5% Convertible debentures	--	--	--	--
Nov. 6, 2002-Conversion of debentures into 595,238 shares	595,238	595	14,405	(567,5
Net loss (Unaudited)				
Balances at December 31, 2002	$ 8,067,462	$ 8,067	$ 6,653,257	$(5,021,2

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

SHOPNET.COM, INC. AND SUBSIDIARIES
Consolidated Statement of Cash Flows
For The Six Months Ended December 31, 2002 And 2001
(Unaudited)

	Dec. 31, 2002
Cash flows from operating activities:	
Net loss	$ (567,556
Adjustments to reconcile net income to net cash used in operating activities:	
Equity in loss of affiliate	--
Amortization and depreciation	13,326
Decrease (increase) in:	
Accounts receivable	(66,819
Other receivables	88,118
Inventory	(3,724,067
Prepaid expenses	(49,995
Advances to officer	(1,971
Other assets	1,743
Increase (decrease) in:	
Due to factor	2,707,527
Accounts payable	1,555,960
Accrued expenses	1,134
Deferred liability	750
Other taxes payable	(491
Net cash used in operating activities	(42,341
Cash flows from investing activities:	
Acquisition of property and equipment	(26,950
Net cash used in investing activities	(26,950

Cash flows from financing activities:	
Principal payments on capital leases	(5,057
Issuance of new capital leases	17,663
Issuance of convertible debentures	15,000
Loans Payable	50,000
Net cash used in financing activities	77,606
Net decrease in cash and restricted cash	8,315
Cash and restricted cash, beginning of period	3,309
Cash and restricted cash, end of period	$ 11,624
Supplemental disclosure of cash flow information: cash paid during the period for :	
Interest	$ 90,185
Income taxes	$ --

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

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS

NOTE 1- ORGANIZATION

Shopnet.com, Inc. ("Shopnet" or the "Company") 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, 2002, Shopnet and all of its subsidiaries changed their financial year end from December 31 to June 30.

NOTE 2- INTERIM RESULTS AND BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements as of December 31, 2002 and for the six month periods ended December 31, 2002 and December 31, 2001 and for the three month periods ended December 31, 2002 and December 31,2001 have been

prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-QSB and Items 303 and 310 of Regulation S-B. In the opinion of management, the unaudited financial statements have been prepared on the same basis as the annual financial statements and reflect all adjustments, which include only normal recurring adjustments, necessary to present fairly the financial position as of December 31, 2002 and the results of operations and cash flows for the six month periods ended December 31, 2002 and December 31, 2001 are not necessarily indicative of the results to be expected for any subsequent quarter or the entire fiscal year. The balance sheet at June 30, 2002 has been derived from the audited financial statements at that date.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to the Securities and Exchange Commission's rules and regulations. The Company believes, however, that the disclosures in this report are adequate to make the information presented not misleading in any material respect. The accompanying consolidated financial statements should be read in conjunction with the audited financial statements of Shopnet.com, Inc. and Subsidiaries as of June 30, 2002 and for the year then ended and notes thereto included in the Company's report on Form 10-KSB filed on October 15, 2002.

The Company in the quarter ended December 31, 2002 has implemented a number of initiatives which it believes will reduce its costs of operations and alleviate in the following six months its working capital deficiency. In particular, the Company believes that the repayment of its indebtedness to Century (See Note 7) and the recent reductions in interest rates will reduce interest expense.

NOTE 2- INTERIM RESULTS AND BASIS OF PRESENTATION (continued)

In December 2001, the Company consolidated all of its operation's in the New York metropolitan region into one new facility (See Note 9(a)), creating a savings through synergies in office expense and decrease in rent and salaries. The Company has, also, recently refocused its sales efforts, to the extent possible, to eliminate unprofitable or low margin sales and has had improved sales and orders for the current fiscal year.

NOTE 3- SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a) Recently adopted accounting principles - Film accounting

Pursuant to SFAS no. 139, the Company adopted Statement of Position ("SOP") 00-2, "Accounting by Producers or Distributors of Films" during the six months ended December 31, 2002. SOP 00-2

established new film accounting standards, including changes in revenue recognition and accounting for advertising, development and overhead costs. Specifically, SOP 00-2 requires advertising costs for theatrical and television products to be expensed as incurred. This compares to the Company's previous policy of first capitalizing these costs and then expensing them over the related revenue streams. In addition, SOP 00-2 requires development costs for abandoned projects and certain indirect overhead costs to be charged to film costs, which was required under the previous accounting rules, SOP 00-2 also in other areas, such as revenue recognition, generally are consistent with the Company's existing accounting policies. SOP 00-2 was adopted as of July 1, 2002, and had no effect on the Company's consolidated results of operations, financial position or cash flows.

b) Recently issued accounting pronouncements

The Company does not believe that any recently issued but not yet effective accounting standards, have a material effect on the Company's consolidated financial position, results of operations or cash flows except for the effect of adoptions of SFAS No. 142, " Goodwill and Other Intangible assets". It addresses how intangible assets that are acquired individually or with a group of other assets (but not those acquired in a business combination) should be accounted for in financial statements upon their acquisition. SFAS 142 also addresses how goodwill and other intangible assets should be accounted for after they have been initially recognized in the financial statements. The Company adopted the provisions of this new standard beginning with the first quarter of 2002.

c) Earnings per share:

Basic earnings (loss) per share is computed by dividing net income (loss) income attributable to common shares, by the weighted average number of common shares outstanding during each period. Diluted earnings (loss) per share is similar to basic earnings (loss) share, except that the weighted average number of common shares is outstanding is increased to reflect the dilutive effect of potential common shares, such as the conversion of the 5% convertible debentures, as if they had been issued.

NOTE 4- 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 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 level. Under FAS 142, the fair value of a reporting unit is compared to its carrying amount, including 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), 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 had determine that no impairment existed as of December 31, 2002. Accordingly, the book value was not further written down.

NOTE 5- 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 December 31, 2002, $217,500 for a 50% interest in a new entity, Battle Studies Productions, LLC ("Battle Studies") a limited liability company. Battle Studies is accounted for as a 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.

b) The Girl

Pursuant to an agreement dated July 1, 1999 with Artistic License Films Inc., Hollywood invested through December 31, 2002 $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.

The Company accounts for the investments in Battle Studies and The Girl under the equity method. For the six months ended December 31, 2002 and 2001, the Company recorded no equity losses from these investments.

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SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS

NOTE 6- MARKETABLE SECURITIES- AFFILIATE

Breaking Waves owned 1,270,000 unregistered common shares of

Play Co. Toys & Entertainment Corp. ("Play Co."), a toy retailer and a publicly traded company whose Chairman of the Board was also the President of Shopnet and Breaking Waves.

Breaking Waves' ownership percentage was approximately 1.5% of Play Co. The investment in Play Co. was accounted for under the requirements of SFAS No. 115, "Accounting for Certain investments in Debt and Equity Securities." Under SFAS 115, the securities were considered available for sale and therefore the carrying value was based on the fair market value of the securities at December 31, 2002 and 2001 which amounted to $0 as of both dates.

The change in the fair market value of the securities during the periods are recorded as an unrealized gain or loss as a component of comprehensive income. The Company pledged such shares as collateral for a standby letter of credit in connection with Breaking Waves entering into a new factoring agreement with Century Business Credit Corporation ("Century") and were therefore considered non-current (See Note 7).

On March 28, 2001 Play Co. filed for protection under Chapter Eleven of the United States Code with the United States Bankruptcy Court for the Southern District of New York. The filing was converted into a Chapter Seven filing on August 28, 2001.

NOTE 7- 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 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") and a relative of a principal stockholder, 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.

SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS

NOTE 7- DUE TO FACTOR

Century Business Credit Corporation

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

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. 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 and are secured by a security interest in all of the Company's assets.

As compensation, Breaking Waves paid 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 quarterly basis.

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. The Agreement is guaranteed by Shopnet under a separate Security Agreement dated September 15, 2001.

NOTE 7- DUE TO FACTOR

Century Business Credit Corporation (continued)

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.

The following table summarizes the percentage due each party, as noted above, as a percentage of net sales for the three months ended December 31, 2002:

	% of Net Sales	Amount
RAYA	0.58	$ 4,353
ZAT	1.16	8,708
ARC	1.75	13,137
	3.49	$ 26,198

Interest expense related to the factor agreement totaled $63,702 and $102,883 for the six months ended December 31, 2002 and 2001, respectively. Century has a secured interest in Breaking Waves' inventory as collateral for the advances. As of December 31, 2002, the net advances to Breaking Waves from Century amounted to $3,398,122.

NOTE 8- NOTE PAYABLE

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.

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 7 (b) herein. The consulting fees being paid in advance under this agreement are those fees which would become due and payable for the periods ending December 31, 2002 and March 31, 2003.

NOTE 9- 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 $11,000.

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:	
2003	$ 63,686
2004	84,915
2005	90,338
2006	95,760
2007	95,760
Thereafter	23,940
	$454,399

Rent expense for the six months ended December 31, 2002 and 2001 amounted to $53,188 and $68,127, respectively.

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 three months ended December 31, 2002 Breaking Waves had three customers, which comprised approximately 40%, of net sales. For the six months ended December 31, 2001, Breaking Waves had 2 customers which compromised 85% of net sales.

NOTE 9- COMMITMENTS AND CONTINGENCIES

c) Seasonality

Breaking Waves' business is considered seasonal with a large portion of its revenues and profits being derived between December and April. 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 margins 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, 2001 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 $86,680 and $42,611 for the six

months ended December 31, 2002 and 2001, respectively.

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 December 31, 2002, the Company invested $1,971,956 for the co-production and distribution of such motion pictures whereas the co-producers have invested $100,000. For the six months ended December 31, 2002 and 2001, the Company derived no revenue from the motion picture and amortized no film costs.

For the six months ended December 31, 2002 and 2001 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 these options).

NOTE 9- COMMITMENTS AND CONTINGENCIES (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 10- STOCKHOLDERS' EQUITY

a) 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, the Warrants will now expire on March 10, 2003. 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.

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.

ii) 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.

b) 5% Convertible Debentures

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 shall terminate on the earlier of the completion of the Placement or can be terminated at any time after six months from June 17, 2002. The agreement was terminated on December 19, 2002.

NOTE 10- STOCKHOLDERS' EQUITY (continued)

b) 5% Convertible Debentures (continued)

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 above. On August 31st, $15,000 of these convertible debentures were issued by the Company. No additional 5 % convertible Debentures nor any 10% Non-Convertible Debentures have been issued.

At any time prior to or at the time of repayment of this Note by the Company, the Holder may elect to convert some or all of the principal and interest owing on this Note into shares of the Company's common stock, subject to the restrictions contained herein. The conversion rate shall equal the amount to be converted, divided by 30% of the average closing bid price of the common stock of the 90 trading days prior to the date of conversion. Such election to convert shall be evidenced by completion of the conversion notice and delivery of such notice to the Company. The Holder's right to convert the obligations due under this Note to common stock shall supercede the Company's right to repay such obligations in cash, subject to the restrictions contained herein.

The 5% convertible debentures were issued to Amigal Salit, Ltd., an Israeli Company controlled by the sister-in-law of a relative of the Company's President and CEO.

On November 6, 2002, the holder of the $15,000 Convertible Debentures ("Amigal Salit, Ltd.") elected to convert these notes into 595,238 shares of the Company's $.001 par value common stock. On that date, the Company issued 595,238 common shares to Amigal.

Upon this conversion, Amigal owns approximately 7.4% of the Company's outstanding common shares.

NOTE - 11 RELATED PARTIES TRANSACTIONS

a) For the six months ended December 31, 2002 and 2001 financial consulting fees were paid to a corporation and an individual who are related to the Company's President and CEO amounting to $18,725 and $17,445, 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 December 31, 2002, the unpaid portion amounted to $37,000, which has been classified as current. As of December 31, 2002, 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.

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SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS

NOTE - 12 SEGMENT INFORMATION

The Company's operations have been classified into two

segments: swimwear sales and film productions. These operating segments were based on the nature of the projects and services offered. Operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and assess performance. The Company's CEO has been identified as the chief decision maker. The Company's chief operating decision maker directs the allocation of resources to operating segments based on the profitability and cash flow of the respective segments.

	Six Months Ended December 2002		
	Segment	Consolidated	
Sales:			
Swimwear sales	$ 750,678		$ 1,
Film production	-		
Total sales		$ 750,678	
Operating income (loss):			
Swimwear sales		$ 504,039	
Film production		(600)	
Total operating income (loss)		$ 504,039	
Corporate:			
General and administrative expense		$ (981,746)	
(Loss) equity in earnings of affiliate		-	
Amortization expense		-	
Interest income		936	
Interest and finance expense		(90,185)	
Other		-	
Loss from operating before (benefit)		(567,556)	
Provision for income tax		-	
Net (loss) income		$ (567,556)	
Identifiable assets:			
Swimwear sales		$ 4,302,913	
Film productions		1,450,504	
Corporate		1,200,816	
Total assets		$ 6,954,233	

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SHOPNET.COM, INC. AND SUBSIDIARIES

NOTES TO FINANCIAL STATEMENTS

NOTE - 12 SEGMENT INFORMATION (continued)

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.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

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. ("Shopnet" or the "Company") 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, 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, 2002, the company changed its year end from December 31 to June 30.

The consolidated financial statements at December 31, 2002 and 2001 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.

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 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

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

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

Critical Accounting Policies (continued)

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.

d) 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.

e) 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.

f) 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.

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. In accordance with Financial Accounting Standards Board's Statement of Financial Accounting Standards ("SFAS") No. 53, "Financial Reporting by Producers and Distributors of Motion Pictures Films," the individual film forecast method is used to amortize film costs.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

Critical Accounting Policies (continued)

g) Earnings per share

Earnings per common share is computed pursuant to SFAS No. 128 "Earnings Per Share." Basic earnings per share is computed as net income (loss) available to common share holders divided by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflects 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 assumption 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 December 31, 2002 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.

Three months ended December 31, 2002 as compared to the three months ended December 31, 2001

For the three months ended December 31, 2002, the Company reported consolidated net income of $3,538 as compared to a consolidated income of $23,225 for the three months ended December 31, 2001.

Breaking Waves

For the three months ended December 31, 2002 and 2001, Breaking Waves generated net sales of $730,871 and $1,335,592, respectively, with related cost of sales amounting to $145,792 and $693,300 respectively. The decrease in sales amounting to $604,721, or approximately 46%, from 2001 to 2002 was primarily attributable to the subsequent deferment on new orders into the next period.

The gross profit for the three months ended December 31, 2002 amounted to $585,079, or 80% of sales as compared to the three months ended December 31, 2001 during which it amounted to $642,292, or 48% of sales.

Selling, general, and administrative expenses during the three months ended December 31, 2002 and 2001 amounted to $515,479 and $404,277, respectively. The

increase amounting to $111,202 or approximately 28%, is primarily attributable to an increase in selling expenses as a result of increased sales efforts.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

Breaking Waves (continued)

The major components of the Breaking Waves selling, general, and administrative expenses are as follows for the three months ended December 31:

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 $66,998 and $51,461 for the three months ended December 31, 2002 and 2001, respectively. The increase is due primarily to an increase in sales orders which resulted in additional borrowings by Breaking Waves.

Breaking Waves generated net income of $97,543 and a loss of $238,056 for the three months ended December 31, 2002 and 2001 respectively.

Hollywood

On May 12, 1999, Shopnet incorporated a wholly-owned subsidiary, Hollywood, to which it assigned its film production business. All film related operations prior to May 12, 1999 were conducted by Shopnet under its former name.

For the three months ended December 31, 2002 and 2001, Hollywood generated no sales form its motion picture "Dirty Laundry". Although sales prior to and including the six months ended June 30, 2002 were minimal, the company expects to effect increased sales during the fiscal year ending June 30, 2002 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 no write down was necessary as of December 31, 2002 and 2001, respectively, Accordingly, Hollywood generated a loss of $600 each for the three months ended December 31, 2002 and 2001, respectively.

Subsequent to "Dirty Laundry", Hollywood also has invested in other movie ventures, some of which have generated revenue to date. See "Investment in Joint Ventures."

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

Shopnet.com

For the three months ended December 31, 2002, Shopnet generated no income. For the corresponding three month period ends December 31, 2001, it generated only minimal income comprised of interest from its money market and other ancillary revenue from its corporate office.

Shopnet's selling, general, and administrative expense amounted to $71,271 and $104,082 for the three months ended December 31, 2002 and 2001. This represents a decrease of $32,811, or approximately 32%.

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

	200
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 $71,271 and $103,784 for the three months ended December 31, 2002 and 2001, respectively. These net losses include, on a consolidated basis, amortization of goodwill of $17,738 for the period ended December 31, 2001.

Six months ended December 31, 2002 as compared to the six months ended December 31, 2001

For the six months ended December 31, 2002 and 2001, the Company reported a consolidated net loss of $567,556 and $548,539 after an income tax expense of $0 and a tax benefit of $16,974 and a comprehensive net loss of $567,556 and $554,889, respectively.

Breaking Waves

For the six months ended December 31, 2002 and 2001, Breaking Waves generated net sales of $750,678 and $1,700,715, respectively, with related cost of sales amounting to $247,239 and $1,098,622, respectively. The decrease in sales amounting to $950,027, or approximately 56%, from 2001 to 2002 was primarily attributable to the subsequent deferment of new orders into the next period.

The gross profit for the six months ended December 31, 2002 amounted to $503,439, or 67% of sales as compared to the six months ended December 31, 2001 during which it amounted to $602,083, or 35% of sales. The increase in the gross profit percentage can be attributable to an increase in inventory of $582,375 at December 31, 2002 as compared to inventory on hand at December 31, 2001.

Selling, general, and administrative expenses during the six months ended

December 31, 2002 and December 31, 2001 amounted to $834,424 and $789,343, respectively. The increase amounted to $2,599 or less than 1%.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

Breaking Waves (continued)

The major components of the Breaking Waves selling, general, and administrative expenses are as follows for the six months ended December 31:

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 $63,702 and $102,833 for the six months ended December 31, 2002 and 2001, respectively. The decrease is due to a decrease in sales, as well as a reduction in the stated prime interest rate.

Breaking Waves owns 1,270,000 unregistered common shares ("Play Co. Shares") of Play Co. Toys & Entertainment Corp. ("Play Co, " a toy retailer and a publicly traded company whose Chairman of the Board is also the President of Shopnet and Breaking Waves).

Breaking Waves' ownership percentage is approximately 1.5% of Play Co.'s outstanding Common Stock. The investment in Play Co. is accounted for under the requirements of SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities. " Under SFAS 115, the securities are considered available for sale and therefore the carrying value is based on the fair market value of the securities at December 31, 2002 and 2001 which amounted to $0 and $337,000, respectively. The change in the fair market value of the securities during the periods is recorded as an unrealized gain or loss as a component of comprehensive income. The company has pledged such shares as collateral for a standby letter of credit in connection with Breaking Waves' factoring agreement with Century Business Credit Corporation ("Century") and the are therefore considered non-current.

On March 28, 2001, Play Co. filed for protection under Chapter Eleven of the United States Code with the United States Bankruptcy Court for the Southern District of New York. The filing was converted into a Chapter Seven filing on August 28, 2001.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

Breaking Waves (continued

Breaking Waves recorded an unrealized (loss) of $(6,350) for the six months ended December 31, 2001, which has been recorded as a component of comprehensive income (loss) in the statement of operations.

Breaking Waves generated a net loss of $433,301 for the six months ended December 31, 2002 and a net loss of $187,860 for the six months ended December 31, 2001.

Hollywood

For the six months ended December 31, 2002 and 2001, Hollywood generated no sales form its motion picture "Dirty Laundry". Although sales prior to and including the six months ended June 30, 2002 were minimal, the company expects to effect increased sales during the fiscal year ending June 30, 2002 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 no write down was necessary as of December 31, 2002 and 2001, respectively, Accordingly, Hollywood generated a loss of $1,200 and $1,241 for the six months ended December 31, 2002 and 2001, respectively.

Subsequent to "Dirty Laundry", Hollywood also has invested in other movie ventures, some of which have generated revenue to date. See "Investment in Joint Ventures."

Shopnet.com

For the six months ended December 31, 2002, Shopnet generated no income. For the six months ended December 31, 2001, it generated minimal income comprised of interest from its money market and other ancillary revenue from its corporate office.

Shopnet's selling, general, and administrative expense amounted to $133,056 and $189,204 for the six months ended December 31, 2002 and 2001. This represents a decrease of $56,148, or approximately 30%.

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

	2002
Salaries (officer and office staff) and stock compensation and related benefits	$ 59,6
Rent	-
Legal and professional fees	20,1
Consulting fees	18,7
Other general corporate and administrative expense	34,5

Shopnet generated a net loss of $133,056 and $209,532 for the six months

ended December 31, 2002 and 2001, respectively. These net losses include, on a consolidated basis, amortization of goodwill of $17,738 for the six months ended December 31, 2001.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

Liquidity and Capital Resources

At December 31, 2002, the Company's consolidated working capital deficit amounted to $873,575.

At December 31, 2002, current assets consisted primarily of inventory of $3,954,116 and prepaid expenses of $348,963.

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") and a relative of a principal stockholder, 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 and a principal stockholder of the Company 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 security interest in all of the assets of the Company and a subordinate security interest in all of the assets of Breaking Waves.

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.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

Liquidity and Capital Resources

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 and are secured by a security interest in all of the Company's assets.

As compensation, Breaking Waves paid 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 quarterly basis.

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. The Agreement is guaranteed by Shopnet under a separate Security Agreement dated September 15, 2001.

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.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

Liquidity and Capital Resources

The following table summarizes the percentage due each party, as noted above, as a percentage of net sales for the three months ended December 31, 2002:

	% of Net Sales	Amount
RAYA	0.58	$ 4,353
ZAT	1.16	8,708
ARC	1.75	13,137
	3.49	$ 26,198

Interest expense related to the factor agreement totaled $63,702 and $102,883 for the six months ended December 31, 2002 and 2001, respectively. Century has a secured interest in Breaking Waves' inventory as collateral for the advances. As of December 31, 2002, the net advances to Breaking Waves from Century amounted to $3,398,122.

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

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 7 (b) herein. The consulting fees being paid in advance under this agreement are those fees which would become due and payable for the periods ending December 31, 2002 and March 31, 2003.

Investments in Joint Ventures

Battle Studies Productions, LLC

In April 1998, the Company entered into a co-production agreement with North Fork Bank for "Machiavelli Rises." The Company and North Fork formed Battle Studies to finance, produce and distribute the film. Battle Studies will be treated as a joint venture in order to co-produce motion pictures and to finance the cost 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. Total production costs to date have aggregated approximately $425,000 of which the Company has funded approximately $218,500. 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 cost incurred by same, any remaining proceeds shall be distributed 50% to North Fork and 50% to the Company. The film was shown in January 1999 in both New York and the Brussels Film Festival.

The Company accounts for the investment in Battle Studies on the equity method. For the six months ended December 31, 2002 and 2001, the Company, recorded no equity losses for its proportionate share of Battle Studies. No revenues have been derived from this film as of December 31, 2002.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

On October 12, 2001, 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, 2002, 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, LLC

Pursuant to an agreement dated July 1, 1999 with ALF for the production of a film entitled "The Girl", Hollywood invested through December 31, 2002, $35,000 for a 22.533% interest in a new entity, The Girl, LLC a limited liability company ("Girl LLC"). In return for its participation in Girl LLC, Hollywood shall be entitled to receive a non-contested, non-dilutable 22.533% ownership interest in Girl LLC, 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 Girl LLC. Girl LLC retains all rights to the motion pictures, the screenplays, and all ancillary rights attached thereto. "The Girl" is completed and has been exhibited at several film festivals. Girl LLC is in the process of attempting to secure video and foreign

distribution arrangements for the film.

Hollywood accounts for the investment in Girl LLC under the equity method. Accordingly, as of December 31, 2002, the Company has recorded its investment at $33,702. This represents its initial investment of $35,000 less $1,298 of equity loss for its proportionate share of Girl LLC.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

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 $11,000.

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:	
2003	
2004	
2005	
2006	
2007	
Thereafter	

	$
	=======

Rent expense for the six months ended December 31, 2002 and 2001 amounted to $53,188 and $68,127, respectively.

License Agreement

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 $86,680 and $42,611 for the six months ended December 31, 2002 and December 31, 2001, respectively.

ITEM 3. CONTROLS AND PROCEDURES

As of December 31, 2002, an evaluation was performed under the supervision and with the participation of the Company's management, including the Chief Executive Officer and our Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based on that evaluation, The Company's management including the Chief Executive Officer and Chief Financial Officer, concluded that the Company's disclosure, our disclosure controls and procedures were effective as of December 31, 2002, there have been no significant changes in the Company's internal controls or in other factors that could significantly affect our internal controls subsequent to December 31, 2002.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

None

Item 2. Changes in Securities and Use of Proceeds

None

Item 3. Defaults Upon Senior Securities

None

Item 4. Submission of Matters to a Vote of Security Holders

None

Item 5. Other Information

None

Item 6. Exhibits and Reports on Form 8-K

a) Exhibit

99.1 Certification by Harold Rashbaum, Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

b) Reports

None

SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

SHOPNET.COM, INC.

By:/s/Harold Rashbaum
Harold Rashbaum, President,
Chief Executive Officer and
Chief Financial Officer

Dated: February 13, 2002

CERTIFICATION

I, Harold Rashbaum, certify that:

1. I have reviewed this quarterly report of Form 10-Q of Shopnet.com, Inc.;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4. I am responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

a) Designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiary, is made know to me by other within those entities, particularly during the period in which this quarterly report is being prepared;

b) Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

c) Presented in this quarterly report my conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function);

a) All significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: February 13, 2002

/s/Harold Rashbaum
Harold Rashbaum
President