INFOSPACE INC
Form 10-Q
November 10, 2008
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended September 30, 2008

or

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from __________ to __________

Commission File Number: 000-25131

INFOSPACE, INC.

(Exact name of registrant as specified in its charter)

Delaware	**91-1718107**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
601 108th Avenue NE, Suite 1200 Bellevue, Washington	**98004**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: (425) 201-6100

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check One):

Large accelerated filer ¨ Accelerated filer x Non-accelerated filer ¨ Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act) ¨ Yes x No

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Class	Outstanding at October 31, 2008
Common Stock, Par Value $.0001	34,573,674

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INFOSPACE, INC.

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Item 1. Financial Statements

INFOSPACE, INC.

UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

(amounts in thousands, except share data)

	September 30, 2008	December 31, 2007 (restated, see Note 1)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 179,235	$ 498,326
Short-term investments, available-for-sale	12,961	39,019
Accounts receivable, net of allowance of $93 and $202	14,985	17,081
Notes and other receivables	761	7,104
Prepaid expenses and other current assets	2,047	1,902
Assets of discontinued operations		4,730
Total current assets	209,989	568,162
Property and equipment, net	20,118	10,945
Long-term investments, available-for-sale	18,227	37,472
Goodwill and other intangible assets, net	44,123	44,123
Other long-term assets	6,353	10,722
Total assets	$ 298,810	$ 671,424
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 6,393	$ 5,148
Accrued expenses and other current liabilities	21,337	78,543
Special dividend payable		299,296
Liabilities of discontinued operations	3,052	21,753
Total current liabilities	30,782	404,740
Other long-term liabilities	1,548	634
Total liabilities	32,330	405,374
Commitments and contingencies (Note 5)		
Stockholders equity:		
Common stock, par value $.0001 authorized, 900,000,000 shares; issued and outstanding, 34,563,583 and 34,321,954 shares	3	3
Additional paid-in capital	1,289,743	1,279,225
Accumulated deficit	(1,024,645)	(1,013,880)
Accumulated other comprehensive income	1,379	702
Total stockholders equity	266,480	266,050
Total liabilities and stockholders equity	$ 298,810	$ 671,424

See accompanying notes to unaudited Condensed Consolidated Financial Statements.

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INFOSPACE, INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

AND COMPREHENSIVE LOSS

(amounts in thousands, except per share data)

	Three months ended September 30,		Nine months ended September 30,	
	2008	**2007**	**2008**	**2007**
Revenues	$ 39,469	$ 33,852	$ 119,979	$ 101,479
Operating expenses:				
Content and distribution	18,265	15,274	58,119	42,819
Systems and network operations	3,238	2,295	8,454	6,980
Product development	2,757	2,086	7,895	6,849
Sales and marketing	6,882	5,518	16,712	17,008
General and administrative	5,940	12,694	18,622	51,893
Depreciation	2,160	1,443	5,378	4,099
Restructuring and other, net	(9)	623	(1,880)	(1,879)
Total operating expenses	39,233	39,933	113,300	127,769
Operating income (loss)	236	(6,081)	6,679	(26,290)
Gain (loss) on investments, net	(11,046)		(22,115)	65
Other income, net	1,458	2,804	6,355	12,489
Loss from continuing operations before income taxes	(9,352)	(3,277)	(9,081)	(13,736)
Income tax expense	(548)	(3,355)	(153)	(10,324)
Loss from continuing operations	(9,900)	(6,632)	(9,234)	(24,060)
Loss from discontinued operations, net of taxes	(12)	(5,625)	(1,323)	(16,867)
Loss on sale of discontinued operations, net of taxes	(13)		(208)	
Net loss	$ (9,925)	$ (12,257)	$ (10,765)	$ (40,927)
Loss per share Basic and diluted				
Loss from continuing operations	$ (0.29)	$ (0.20)	$ (0.27)	$ (0.74)
Loss from discontinued operations	(0.00)	(0.17)	(0.04)	(0.52)
Loss on sale of discontinued operations	(0.00)		(0.00)	
Net loss per share	$ (0.29)	$ (0.37)	$ (0.31)	$ (1.26)
Weighted average shares outstanding used in computing basic and diluted loss per share	34,479	33,158	34,371	32,421
Comprehensive loss				
Net loss	$ (9,925)	$ (12,257)	$ (10,765)	$ (40,927)
Foreign currency translation adjustment	(110)	87	4	106
Unrealized gain (loss) on investments, available-for-sale	(49)	75	(1,382)	47
Reclassification adjustment for other than temporary losses on investments, available-for-sale, included in net loss			2,055	
Comprehensive loss	$ (10,084)	$ (12,095)	$ (10,088)	$ (40,774)

See accompanying notes to unaudited Condensed Consolidated Financial Statements.

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INFOSPACE, INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(amounts in thousands)

	Nine months ended September 30,	
	2008	**2007**
Operating activities:		
Net loss	$ (10,765)	$ (40,927)
Adjustments to reconcile net loss to net cash used by operating activities:		
Loss from discontinued operations	1,323	16,867
Loss on sale of discontinued operations	208	
Loss on investments	22,115	(65)
Stock-based compensation	11,384	17,205
Depreciation	5,378	4,099
Deferred income taxes	(1,423)	618
Net gain on sale of non-core assets	(1,897)	(3,248)
Restructuring and other, net	17	1,369
Other	17	(113)
Cash provided (used) by changes in operating assets and liabilities:		
Accounts receivable	2,025	(2,208)
Notes and other receivables	5,927	1,231
Prepaid expenses and other current assets	(145)	996
Other long-term assets	3,278	367
Accounts payable	(464)	(3,825)
Accrued expenses and other current and long-term liabilities	(58,554)	(7,040)
Net cash used by operating activities	(21,576)	(14,674)
Investing activities:		
Purchases of property and equipment	(10,672)	(4,294)
Other long-term assets	(1,003)	
Loan to equity investee		(2,000)
Proceeds from the sale of assets	2,313	2,884
Proceeds from sales and maturities of investments	43,980	265,199
Purchases of investments	(17,984)	(127,834)
Net cash provided by investing activities	16,634	133,955
Financing activities:		
Special dividend paid	(299,146)	(208,203)
Proceeds from stock option and warrant exercises	16	12,833
Proceeds from issuance of stock through employee stock purchase plan	438	1,381
Repayment of capital lease obligation	(96)	
Net cash used by financing activities	(298,788)	(193,989)
Discontinued operations:		
Net cash provided (used) by operating activities attributable to discontinued operations	(15,361)	39,322
Net cash used by investing activities attributable to discontinued operations		(13,568)
Net cash provided (used) by discontinued operations	(15,361)	25,754
Net decrease in cash and cash equivalents	(319,091)	(48,954)
Cash and cash equivalents:		

Beginning of period	498,326	162,387
End of period	$ 179,235	$ 113,433
Non cash items:		
Purchases of property and equipment under capital lease	$ 1,601	$

See accompanying notes to unaudited Condensed Consolidated Financial Statements.

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INFOSPACE, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. The Company and Basis of Presentation

InfoSpace, Inc. (the Company or InfoSpace) develops search tools and technologies that assist consumers with finding content and information on the Internet. The Company offers online search services that enable Internet users to locate information, merchants, individuals, and products online. The Company offers search services through its Web sites as well as through the Web properties of distribution partners. Partner versions of Web offerings are generally private-labeled and delivered with each distribution partner s unique requirements.

In 2007, the Company sold its directory and mobile businesses. The operating results of the directory and mobile businesses have been presented as discontinued operations in the accompanying unaudited Condensed Consolidated Financial Statements for all periods presented.

The accompanying unaudited Condensed Consolidated Financial Statements include all adjustments, consisting of normal recurring adjustments that, in the opinion of management, are necessary to present fairly the financial information set forth herein. Certain information and note disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) have been condensed or omitted pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (SEC). Results of operations for the three and nine months ended September 30, 2008 are not necessarily indicative of future financial results. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual amounts may differ, perhaps materially, from these financial estimates.

The Company s chief executive officer, who is its chief operating decision maker, reviews financial information presented on a consolidated basis accompanied by revenue information disaggregated by geographic region and other measures for purposes of allocating resources and evaluating financial performance. The Company s operations are not organized into components below the consolidated unit level, and operating results are not reported to the chief executive officer for components below the consolidated unit level. Accordingly, the Company s management considers InfoSpace to be in a single reporting segment and a single operating unit structure.

Investors should read these interim unaudited Condensed Consolidated Financial Statements and related notes in conjunction with the audited financial statements and related notes included in the Company s Annual Report on Form 10-K for the year ended December 31, 2007.

Restatement

Subsequent to the issuance of the Company s consolidated financial statements for the year ended December 31, 2007, the Company identified certain errors affecting the Company s income tax provision for the year ended December 31, 2007 related to the determination of the amount of net operating loss carryforwards utilized in 2007 to offset taxable income for 2007. These errors resulted principally from the recognition of its utilization of alternative minimum tax credit carryforwards, as well as errors related to temporary differences in the tax bases of certain assets and liabilities. As a result of these errors, the Company overstated the portion of the utilization of net operating loss carryforwards that relate to tax deductions associated with the exercise of stock options, which are accounted for as additional paid-in capital, with a corresponding overstatement of its income tax expense from continuing operations in the amount of $6.3 million for the year ended December 31, 2007. The Company also overstated its tax expense related to discontinued operations by $892,000 for the year ended December 31, 2007. These errors also resulted in an overstatement of additional paid-in capital of $7.0 million and an overstatement of accrued expenses and other current liabilities of $160,000 as of December 31, 2007.

The Company believes the correction of these errors is not material to the 2007 consolidated financial statements, and therefore the Company plans to restate its 2007 consolidated financial statements when issuing its 2008 consolidated financial statements. The liabilities and stockholders equity sections of the accompanying unaudited Condensed Consolidated Balance Sheet as of December 31, 2007 have been restated from amounts previously reported.

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The effects of this restatement on the unaudited Condensed Consolidated Balance Sheet as of December 31, 2007 are as follows (in thousands):

	December 31, 2007		
	As previously reported	Adjustment	As restated
Accrued expenses and other current liabilities	$ 78,703	$ (160)	$ 78,543
Total current liabilities	$ 404,900	$ (160)	$ 404,740
Total liabilities	$ 405,534	$ (160)	$ 405,374
Additional paid-in capital	$ 1,286,219	$ (6,994)	$ 1,279,225
Accumulated deficit	$ (1,021,034)	$ 7,154	$ (1,013,880)
Total stockholders equity	$ 265,890	$ 160	$ 266,050

The effects of this restatement on the results of operations for the three months and year ended December 31, 2007 are as follows (in thousands, except per share data):

	Three months ended December 31, 2007			Year ended December 31, 2007		
	As previously reported	Adjustment	As restated	As previously reported	Adjustment	As restated
Income tax expense	$ (9,347)	$ 6,262	$ (3,085)	$ (19,671)	$ 6,262	$ (13,409)
Loss from continuing operations	(66,677)	6,262	(60,415)	(90,737)	6,262	(84,475)
Loss from discontinued operations, net of taxes	(8,439)	60	(8,379)	(25,306)	60	(25,246)
Gain on sale of discontinued operations, net of taxes	130,622	832	131,454	130,622	832	131,454
Net income	$ 55,506	$ 7,154	$ 62,660	$ 14,579	$ 7,154	$ 21,733
Net income per share Basic and diluted						
Loss from continuing operations	$ (2.00)	$ 0.18	$ (1.82)	$ (2.78)	$ 0.19	$ (2.59)
Loss from discontinued operations	(0.25)	0.00	(0.25)	(0.77)	0.00	(0.77)
Gain on sale of discontinued operations	3.92	0.03	3.95	4.00	0.03	4.03
Net income per share	$ 1.67	$ 0.21	$ 1.88	$ 0.45	$ 0.22	$ 0.67

The effects of this restatement on cash flows for the year ended December 31, 2007 are as follows (in thousands):

	Year ended December 31, 2007		
	As previously reported	Adjustment	As restated
Operating activities:			
Net income	$ 14,579	$ 7,154	$ 21,733
Loss from discontinued operations	$ 25,306	$ (60)	$ 25,246
Gain on sale of discontinued operations	$ (130,622)	$ (832)	$ (131,454)
Deferred income taxes	$ 19,810	$ (6,994)	$ 12,816
Excess tax benefits from stock-based award activity	$ (30,694)	$ 6,994	$ (23,700)
Accrued expenses and other current and long-term liabilities	$ 33,882	$ (160)	$ 33,722
Net cash used by operating activities	$ (33,378)	$ 6,102	$ (27,276)
Financing activities:			
Excess tax benefits from stock-based award activity	$ 30,694	$ (6,994)	$ 23,700
Net cash used by financing activities	$ (162,391)	$ (6,994)	$ (169,385)

Discontinued operations:			
Operating activities	$ 33,760	$ 60	$ 33,820
Investing activities	$ 341,767	$ 832	$ 342,599
Net cash provided by discontinued operations	$ 375,527	$ 892	$ 376,419
Net increase in cash and cash equivalents	$ 335,939	$	$ 335,939

The Company intends to include restated 2007 consolidated financial statements, giving effect to the adjustments noted above, in its 2008 Annual Report on Form 10-K.

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2. Fair Value Measurements

On January 1, 2008, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 157, *Fair Value Measurements*, issued by the Financial Accounting Standards Board (FASB). SFAS No. 157 defines fair value, establishes a framework for measuring fair value for the purposes of GAAP, and expands required disclosures about fair value measurements. SFAS No. 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value hierarchy of the Company s financial assets carried at fair value and measured on a recurring basis is as follows (in thousands):

		Fair value measurements at the reporting date using		
	September 30, 2008	Quoted prices in active markets using identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Cash and cash equivalents	$ 179,235	$ 179,235	$	$
Available-for-sale securities	31,188	12,961		18,227
Equity investment				
Warrants	94			94
	$ 210,517	$ 192,196	$	$ 18,321

The Company s available-for-sale securities include $18.2 million of auction rate securities (ARS), which are classified as long-term, in the Level 3 category within the input hierarchy, because there are significant unobservable inputs associated with those investments. The Company s ARS are floating rate securities with either long-term maturities or no maturity date, which are marketed by financial institutions with auction reset dates primarily at 28 day intervals to provide short-term liquidity. The ARS that the Company owns are comprised of two types. The first type of ARS is collateralized by investment-grade corporate debt and prime-rated mortgage-backed debt, has a long-term maturity date, and is insured in the event of default by monoline insurance companies. The second type of ARS has no maturity date and, in the event of default or liquidation of the collateral by the ARS issuer, the Company is entitled to receive non-convertible preferred shares in the ARS issuer; ARS of that type are also known as auction rate preferred securities (ARPS). Beginning in August 2007, auctions for the ARS that the Company held at September 30, 2008 began to fail due to insufficient bids from buyers which resulted in higher interest rates being earned on those securities. While the Company receives regular interest payments for those ARS, the Company does not expect to be able to receive the principal amounts until one or more of the following events occur: future auctions of those ARS are successful, the Company sells those securities in a secondary market which is currently not active, or the issuers redeem those ARS.

Changes in the fair values of financial assets measured on a recurring basis by using significant Level 3 inputs in the three and nine months ended September 30, 2008 are as follows (in thousands):

	Financial assets using significant Level 3 inputs for determining fair value Three and nine months ended September 30, 2008					
	ARS rated AA	ARPS rated from AA to B	Total ARS and ARPS	Equity investment	Warrants	Total
Balance at January 1, 2008	$ 20,905	$ 16,567	$ 37,472	$ 2,000	$ 188	$ 39,660
Other-than-temporary impairment	(2,331)	(8,738)	(11,069)			(11,069)
Temporary impairment	(1,279)		(1,279)			(1,279)
Temporary impairment reclassified to other-than-temporary	1,804	251	2,055			2,055
Balance at June 30, 2008	19,099	8,080	27,179	2,000	188	29,367
Other-than-temporary impairment	(5,955)	(2,997)	(8,952)	(2,000)	(94)	(11,046)
Balance at September 30, 2008	$ 13,144	$ 5,083	$ 18,227	$	$ 94	$ 18,321

In the three and nine months ended September 30, 2008, the Company recorded an other-than-temporary impairment of its available-for-sale investments in Gain (loss) on investments, net in the accompanying unaudited Condensed Consolidated Statement of Operations and Comprehensive Loss of $9.0 million and $20.0 million, respectively, which included zero ($0) and $2.1 million of impairments previously classified as temporary, respectively. The Company did not record any investment impairments in Gain (loss) on investments, net in the three and nine months ended September 30, 2007.

The Company reviews the impairments of its available-for-sale investments in accordance with the provisions of SFAS No. 115, *Accounting for Certain Investments in Debt and Equity Securities*, and related guidance issued by the FASB and the SEC. The Company classifies the impairment of any individual ARS as either temporary or other-than-temporary. The differentiating factors between temporary and other-than-temporary impairments are primarily the length of the time and the

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extent to which the fair value has been less than cost, the financial condition and near-term prospects of the issuer and the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

As of January 1, 2008, the Company held warrants to purchase shares it held in a privately-held company that had a carrying value of $188,000. In the three and nine months ended September 30, 2008, the Company recorded a charge of $94,000 related to those warrants in Gain (loss) on investments, net in the accompanying unaudited Condensed Consolidated Statement of Operations and Comprehensive Loss, reducing the carrying value of those warrants to $94,000. The warrants are classified in Other long-term assets, in Level 3, because there are significant unobservable inputs associated with them. The Company considers the warrants to be derivatives, and follows SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities,* as amended and interpreted, which requires that all derivatives be carried at fair value. The Company accounts for all derivatives by recognizing the changes in their fair values as gains or losses on investments in its unaudited Condensed Consolidated Statements of Operations and Comprehensive Loss.

The Company uses fair value measurements on a recurring basis in the assessment of its equity investment in a privately-held company classified as Other long-term assets, in Level 3, because there are significant unobservable inputs associated with them. In the three and nine months ended September 30, 2008, the Company recorded an other-than-temporary impairment charge of $2.0 million, reducing the carrying value of its investment in that privately-held company to zero ($0). The Company assesses its investment in that privately-held company for impairment in accordance with FASB Staff Position FAS 115-1/124-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments* and the SEC s Staff Accounting Bulletin Topic 5M, *Other Than Temporary Impairment of Certain Investments in Debt and Equity Securities*. The Company did not record any impairment charges for the investment in a privately-held company in the three and nine months ended September 30, 2007.

In the three and nine months ended September 30, 2008 and 2007, the Company did not measure the fair value of any of its assets or liabilities other than cash and cash equivalents, available-for-sale investments, warrants and investment in a privately-held company. The Company s management considers the carrying values of accounts receivable, notes and other receivables, prepaid expenses and other current assets, accounts payable, accrued expenses and other current liabilities and assets and liabilities of discontinued operations to approximate fair values primarily due to their short-term nature.

3. Stock-Based Compensation

The Company has included the following amounts for stock-based compensation expense, including the cost related to the Employee Stock Purchase Plan (ESPP), in the accompanying unaudited Condensed Consolidated Statements of Operations and Comprehensive Loss for the three and nine months ended September 30, 2008 and 2007 (in thousands):

	Three months ended September 30,		Nine months ended September 30,	
	2008	**2007**	**2008**	**2007**
Systems and network operations	$ 494	$ 377	$ 1,307	$ 842
Product development	1,080	706	2,720	1,891
Sales and marketing	1,074	1,926	2,965	4,628
General and administrative	1,535	4,710	4,392	9,844
Total	$ 4,183	$ 7,719	$ 11,384	$ 17,205

Excluded from the amounts for the three and nine months ended September 30, 2008 and 2007 are the following amounts of stock-based compensation included in Restructuring, resulting from equity awards held by terminated employees, capitalized as part of internal-use software, and reclassified as discontinued operations (amounts in thousands):

	Three months ended September 30,		Nine months ended September 30,	
	2008	**2007**	**2008**	**2007**
Restructuring	$	$ 170	$ 60	$ 102

Internal-use software	115	209	552	411
Discontinued operations directory business		303	52	1,246
Discontinued operations mobile business		5,264	89	10,932
Total	$ 115	$ 5,946	$ 753	$ 12,691

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To estimate the compensation expense that was recognized under SFAS No. 123(R) (SFAS No. 123(R)), *Share-Based Payment*, for the three and nine months ended September 30, 2008 and 2007, the Company used the fair value at date of grant for restricted stock units and the Black-Scholes-Merton option-pricing model with the following weighted-average inputs for its stock option grants:

	Employee stock option plans			
	Three months ended September 30,		Nine months ended September 30,	
	2008	2007	2008	2007
Risk-free interest rate			2.46%	4.87%
Expected dividend yield			0%	0%
Expected volatility			47%	50%
Expected life			2.8 years	2.5 years

No stock options were granted during the three months ended September 30, 2008 and 2007.

To estimate the compensation expense that was recognized under SFAS No. 123(R), for the three and nine months ended September 30, 2008 and 2007, the Company used the Black-Scholes-Merton option-pricing model with the following weighted-average inputs for its ESPP incentive plans:

	Employee stock purchase plans			
	Three months ended September 30,		Nine months ended September 30,	
	2008	2007	2008	2007
Risk-free interest rate	2.01%	5.07%	2.53%	5.10%
Expected dividend yield	0%	0%	0%	0%
Expected volatility	39%	52%	60%	46%
Expected life	6 months	6 months	6 months	6 months

4. Net Loss Per Share

Basic net loss per share is computed using the weighted average number of common shares outstanding during the period. Diluted loss per share is computed using the weighted average number of common shares outstanding plus the number of potentially dilutive shares outstanding during the period. Potentially dilutive shares consist of the incremental common shares issuable upon the exercise of outstanding stock options and warrants using the treasury stock method. Potentially dilutive shares are excluded from the computation of earnings per share if their effect is antidilutive. The treasury stock method calculates the dilutive effect for stock options and warrants with an exercise price less than the average stock price during the period presented.

	Three months ended September 30,		Nine months ended September 30,	
(in thousands)	**2008**	**2007**	**2008**	**2007**
Weighted average common shares outstanding, basic and diluted	34,479	33,158	34,371	32,421
Antidilutive stock option, restricted stock unit, and warrant equivalents excluded from dilutive share calculation	1,222	1,412	989	1,710
Outstanding stock options with an exercise price more than the average price during the quarter not included in dilutive share calculation	4,007	5,575	4,788	5,437

5. Commitments and Contingencies

The following are the Company s contractual commitments associated with its capital and operating lease obligations (in thousands):

	Remainder of 2008	2009	2010	2011	2012	2013	Total
Operating lease commitments	$ 416	$ 1,641	$ 1,640	$ 1,607	$ 1,659	$ 283	$ 7,246
Capital lease commitments (net of imputed interest and executory costs)	137	551	565	209			1,462
Total	$ 553	$ 2,192	$ 2,205	$ 1,816	$ 1,659	$ 283	$ 8,708

As of September 30, 2008, the Company has pledged $5.9 million as collateral for standby letters of credit and bank guaranties for certain of its property leases, which is primarily included in Other long-term assets.

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Contingencies

In the three and nine months ended September 30, 2008, the Company recorded expense from settlements and estimated liabilities from loss contingencies of $550,000 and $2.7 million, respectively in Loss from discontinued operations in the accompanying unaudited Condensed Consolidated Statement of Operations and Comprehensive Loss. Additionally, as of September 30, 2008, it is reasonably possible that additional losses from contingencies may be incurred, although the Company cannot reasonably estimate any additional possible losses.

Litigation

From time to time the Company is subject to various legal proceedings or claims that arise in the ordinary course of business. Although the Company cannot predict the outcome of these matters with certainty, the Company s management does not believe that the disposition of these ordinary course matters will have a material adverse effect on the Company s financial position, results of operations or cash flows.

Other

In the ordinary course of business, the Company may provide indemnifications of varying scope and terms to customers, vendors, partners and other parties. The Company has agreed to hold certain parties harmless against losses arising from a breach of representations or covenants, or other claims made against certain parties. It is not possible to determine the maximum potential amount for which the Company could be held liable under these indemnification agreements due to the conditional nature of the Company s obligations and the unique facts and circumstances involved in each particular agreement. Accordingly, the Company has not recorded a liability related to such indemnification provisions.

The Company periodically enters into agreements that require minimum performance commitments. The Company s management believes that the likelihood is remote that any such arrangements will have a significant adverse effect on its financial position or liquidity. Accordingly, the Company has not recorded a liability related to these contingencies.

6. Restructuring and Other, net

For the three months ended September 30, 2008 and 2007, the Company recorded the recapture of previously recorded Restructuring charges of $9,000 and recorded additional restructuring charges of $558,000, respectively. Restructuring charges were $17,000 and $1.4 million for the nine months ended September 30, 2008 and 2007, respectively.

In 2007, the Company sold its directory and mobile businesses and, as a result, committed to a plan to make operational changes to its business, which included a reduction in its workforce and, as part of the workforce reduction, consolidation of its facilities.

In 2006, as a result of being informed by one of its carrier partners that it intended to develop direct relationships for mobile ringtone content with the major record labels beginning in 2007, the Company committed to a plan to substantially reduce its mobile content offerings and make operational changes to its business, which included a reduction in its workforce and, as part of the workforce reduction, consolidation of its facilities. The Company recorded $71.9 million of expense related to the plans described above through September 30, 2008.

The Company does not expect to incur material additional restructuring charges in 2008 related to initiatives identified to date that have not yet been recognized in the unaudited Condensed Consolidated Statements of Operations and Comprehensive Loss.

Restructuring for the three and nine months ended September 30, 2008 and 2007 consists of the following (in thousands):

	Three months ended September 30,		Nine months ended September 30,	
	2008	2007	2008	2007
Employee separation	$ (2)	$ 240	$ 52	$ 601
Stock-based compensation		170	60	102
Contractual commitments		76	(88)	549
Estimated future lease losses	(7)		(7)	(84)
Other		72		201

$ (9)	$ 558	$ 17	$ 1,369

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At September 30, 2008, the liability associated with the restructuring related charges was $4,000 and consisted of the following (in thousands):

	Employee separation	Contractual commitments	Facility abandonment	Total
Liability at December 31, 2007	$ 7,289	$ 230	$ 109	$ 7,628
Provision for Restructuring	24			24
Adjustments	112	(86)	(94)	(68)
Payments in six months ended June 30, 2008	(7,365)	(144)		(7,509)
Liability at June 30, 2008	60		15	75
Adjustments	(2)		(7)	(9)
Payments in three months ended September 30, 2008	(54)		(8)	(62)
Liability at September 30, 2008	$ 4	$	$	$ 4

Other, net consists of costs and/or benefits that are not directly associated with other revenues or operating expense classifications. Other, net benefit of zero ($0) and $1.9 million for the three and nine months ended September 30, 2008, respectively, and cost of $65,000 and benefit $3.2 million for the three and nine months ended September 30, 2007, respectively, consisted of the net gain on sale of certain non-core assets.

7. Income Taxes

As discussed in Note 7 to the consolidated financial statements in the Company s Annual Report on Form 10-K for the year ended December 31, 2007, the Company has a valuation allowance against the full amount of its net deferred tax asset. The Company currently provides a valuation allowance against deferred tax assets when it is more likely than not that some portion, or all of its deferred tax assets, will not be realized.

The Company recorded an income tax expense of $548,000 and $153,000 for the three and nine months ended September 30, 2008, respectively. The Company recorded an income tax expense of $3.4 million and $10.3 million for the three and nine months ended September 30, 2007, respectively. Income tax expense for each period included U.S. federal tax, state and foreign taxes. Income tax expense for the three months ended September 30, 2008 differed from the tax expense at the statutory rates primarily due to non-deductible permanent differences and applying a valuation allowance against deferred tax assets arising during the period. Income tax expense for the nine months ended September 30, 2008 differed from the tax expense at the statutory rates primarily due to non-deductible permanent differences, applying a valuation allowance against deferred tax assets arising during the period, and certain one-time items primarily attributable to restructuring. Income tax expense for the three and nine months ended September 30, 2007 differed from the tax expense at the statutory rates due to non-deductible permanent differences and applying a valuation allowance against deferred tax assets.

During the three and nine months ended September 30, 2008, there were no material changes to the unrecognized tax benefits, the total amount of unrecognized tax benefits that would affect the effective tax rate if recognized, the amount of interest and penalties recognized in connection with the unrecognized tax benefits, and the tax years that remain subject to examination. The Company does not believe there will be any material changes in its unrecognized tax benefits over the next twelve months.

Subsequent to the issuance of the Company s consolidated financial statements for the year ended December 31, 2007, the Company identified certain errors affecting the Company s income tax provision for the year ended December 31, 2007. The liabilities and stockholders equity sections of the accompanying unaudited Condensed Consolidated Balance Sheet as of December 31, 2007 have been restated from amounts previously reported to reflect the correction of these errors. See Note 1 for further information regarding this restatement.

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8. Discontinued Operations

In 2007, the Company completed the sales of its directory and mobile businesses. The results of operations from the directory and mobile businesses are reflected in the unaudited Condensed Consolidated Financial Statements as discontinued operations for all periods presented. Revenue, income (loss) before taxes, income tax benefit (expense), income (loss) from discontinued operations, net of taxes and gain (loss) on sale of discontinued operations, net of taxes for the three and nine months ended September 30, 2008 and 2007 are presented below (in thousands):

	Three months ended September 30, 2008			Three months ended September 30, 2007		
	Directory	**Mobile**	**Total**	**Directory**	**Mobile**	**Total**
Revenue from discontinued operations	$	$ 45	$ 45	$ 8,740	$ 14,896	$ 23,636
Income (loss) from discontinued operations before taxes		(638)	(638)	2,070	(11,045)	(8,975)
Income tax benefit (expense)	(72)	698	626	(689)	4,039	3,350
Income (loss) from discontinued operations, net of taxes	$ (72)	$ 60	$ (12)	$ 1,381	$ (7,006)	$ (5,625)
Gain (loss) on sale of discontinued operations, net of taxes	$ (18)	$ 5	$ (13)	$	$	$

	Nine months ended September 30, 2008			Nine months ended September 30, 2007		
	Directory	**Mobile**	**Total**	**Directory**	**Mobile**	**Total**
Revenue from discontinued operations	$	$ 125	$ 125	$ 25,894	$ 87,288	$ 113,182
Income (loss) from discontinued operations before taxes	204	(2,063)	(1,859)	9,959	(36,344)	(26,385)
Income tax benefit (expense)	(76)	612	536	(3,775)	13,293	9,518
Income (loss) from discontinued operations, net of taxes	$ 128	$ (1,451)	$ (1,323)	$ 6,184	$ (23,051)	$ (16,867)
Gain (loss) on sale of discontinued operations, net of taxes	$ 48	$ (256)	$ (208)	$	$	$

Income (loss) from discontinued operations includes previously unallocated depreciation, amortization, stock-based compensation expense, income taxes, and other corporate expenses that were attributable to the directory and mobile businesses.

Assets and liabilities from discontinued operations at September 30, 2008 and December 31, 2007, which entirely related to the Company s mobile business, consist of the following (in thousands):

	September 30, 2008	December 31, 2007
Accounts receivable	$	$ 4,730
Accounts payable	$ 42	$ 3,214
Other current liabilities	3,010	18,539
Liabilities of discontinued operations	$ 3,052	$ 21,753

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9. Recent Accounting Pronouncements

In December 2007, the FASB issued SFAS No. 141 (revised 2007), *Business Combinations* (SFAS No. 141(R)). In SFAS No. 141(R), the FASB retained the fundamental requirements of SFAS No. 141 to account for all business combinations using the acquisition method and for an acquiring entity to be identified in all business combinations. However, the revised standard requires the acquiring entity in a business combination to recognize all the assets acquired and liabilities assumed in the transaction; establishes the acquisition-date fair value as the measurement objective for all assets acquired and liabilities assumed; and requires the acquirer to immediately expense costs related to the acquisition. SFAS No. 141(R) is effective for annual periods beginning on or after December 15, 2008. Accordingly, any business combinations the Company engages in will be recorded and disclosed according to the provisions of SFAS No. 141 until January 1, 2009. The impact that SFAS No. 141(R) will have on the Company s consolidated financial statements when effective will depend upon the nature, terms and size of the acquisitions completed after the effective date.

On January 1, 2008, the Company adopted the provisions of SFAS No. 157, *Fair Value Measurements*. SFAS No. 157 defines fair value, establishes a framework for measuring fair value and expands disclosure of fair value measurements. SFAS No. 157 applies under other accounting pronouncements that require or permit fair value measurements and accordingly, does not require any new fair value measurements. On February 12, 2008, the FASB issued Staff Position No. FAS 157-2, *Effective Date of FASB Statement No. 157*, which delayed the effective date of SFAS No. 157 for nonfinancial assets and nonfinancial liabilities to fiscal years beginning after November 15, 2008. The adoption of SFAS No. 157 for financial assets and liabilities did not have a material impact on the Company s financial position, cash flows, or results of operations. The Company is currently evaluating the remaining provisions of SFAS No. 157 to determine what effect its adoption on January 1, 2009 for nonfinancial assets and nonfinancial liabilities will have on its financial position, cash flows, and results of operations.

On October 10, 2008, the FASB issued Staff Position (FSP) No. 157-3, *Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active*. FSP No. 157-3 clarifies the application of SFAS 157 in a market that is not active and provides an example to illustrate key considerations in determining the fair value of a financial asset when the market for that financial asset is not active. FSP No. 157-3 became effective immediately, including prior periods for which financial statements have not been issued. Therefore, the Company adopted the provisions of FSP No. 157-3 in its consolidated financial statements for the three months ended September 30, 2008. The adoption did not have a material impact on the Company s financial position, cash flows or results of operations.

10. Subsequent Event

In October 2008, the Company committed to a plan to close its European facilities by the end of 2008. Cash charges of approximately $700,000 are expected and primarily relate to employee separation.

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

This report contains forward-looking statements that involve risks and uncertainties. You should not rely on forward-looking statements. The statements in this report that are not purely historical are forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended. We use words such as anticipate, believe, plan, expect, future, intend, may, will, should, estimate, predict, potential, continue, and similar expressions to identify such forward-looking statements. These forward-looking statements include, but are not limited to:

- *statements regarding new and future products and services;*
- *statements regarding our future business plans and growth strategy, including plans to reduce or expand specific operations;*
- *the expected demand for and benefits of our products and services for our customers and distribution partners;*
- *statements regarding the successful execution of our strategic initiatives;*
- *statements regarding seasonality of revenue and concentration of revenue sources;*
- *anticipated benefits from the business and technologies we have acquired, or invested in, or intend to acquire or invest in;*
- *anticipated development or acquisition of intellectual property and resulting benefits;*
- *anticipated results of potential or actual litigation;*
- *statements regarding our competitive environment;*
- *statements regarding the impact of governmental regulation;*
- *statements regarding employee hiring and retention, including anticipated reductions in force and headcount;*
- *statements regarding the future payment of dividends;*
- *anticipated revenue and expenses;*
- *statements regarding expected impacts of changes in accounting rules;*

- *statements regarding use of cash, cash needs and ability to raise capital;*
- *statements regarding the condition of our cash investments and any income derived therefrom;*
- *statements regarding the current or future state of financial or credit markets; and*
- *statements regarding potential liability from contractual relationships.*

Forward-looking statements are subject to known and unknown risks, uncertainties and other factors that may cause our results, levels of activity, performance, achievements and prospects, and those of the Internet industries generally, to be materially different from those expressed or implied by such forward-looking statements. These risks, uncertainties and other factors include, among others, those identified under Item 1A, Risk Factors and elsewhere in this report.

Overview

InfoSpace, Inc. (InfoSpace , our or we) is a developer of search tools and technologies that assist consumers with finding content and information on the Internet. We use our metasearch technology to power our own branded Web sites and provide online search services to distribution partners.

We offer search services that enable Internet users to locate information, merchants, individuals, and products online. We offer search services through our owned Web sites, Dogpile.com, WebCrawler.com, MetaCrawler.com, and WebFetch.com, as well as through the Web properties of distribution partners. Partner versions of our Web offerings are generally private-labeled and delivered with each distribution partner s unique requirements.

We were founded in 1996 and are incorporated in the state of Delaware. Our principal corporate office is located in Bellevue, Washington. We also have an office in Bangalore, India. Our common stock is listed on the NASDAQ Global Select Market under the symbol INSP.

From 2004 to 2007, InfoSpace was comprised of three businesses: online search, online directory, and mobile. The mobile business was comprised of a mobile content product offering and a mobile services offering. In 2006, as a result of being informed by one of our carrier partners that it intended to develop direct relationships for mobile ringtone content with the major record labels beginning in 2007, we restructured our operations accordingly, substantially reduced our mobile content offerings in 2007 and sold significant portions of our remaining mobile content assets. In addition, we undertook

further strategic restructuring initiatives in 2007 which resulted in the sales of our online directory business and mobile services business in the fourth quarter of 2007. In December 2007, as a result of the sales of those businesses, we committed to a plan to make operational changes to our business, which included a reduction in our workforce and, as part of the workforce reduction, consolidation of our facilities. Following the sale of our mobile and directory businesses, our revenues are derived exclusively from providing online search services.

We generate revenues from our Web search services when an end user of our services clicks on a paid search link displayed on our owned Web site or displayed on a distribution partner s Web property. We receive content for our search services from certain content providers, whom we refer to as our customers. Revenue from Google and Yahoo! jointly account for over 95% of our total revenue for the three and nine month periods ended September 30, 2008, and we expect this concentration to continue in the foreseeable future. As such, if either of these customers reduce or eliminate the content it provides to us or our distribution partners, or if either of these customers were unwilling to pay us amounts that they owe us, our financial results may materially suffer. Our principle agreements with these customers expire in 2011.

In addition to revenues from search services, we earn service revenue from certain distribution partners, such as a fixed monthly fee in exchange for portal infrastructure services.

Our ability to grow our online search services revenue on our owned Web sites relies on growth in the volume of paid clicks, the fees advertisers pay our customers for these paid clicks, and the percentage of these fees our customers share with us. In recent periods, on our owned Web sites, we have experienced an increase in paid clicks, primarily driven by our marketing initiatives, partially offset by lower average fees per paid click from our customers.

Similar to our owned Web sites, revenues from distribution partners are dependent upon growth in the volume of paid clicks, the fees advertisers pay our customers for these paid clicks, and the percentage of these fees our customers share with us. We have experienced steady growth in revenues from our search services offered through the Web properties of distribution partners, which has been primarily attributable to growth in paid click volumes from new distribution partners Web properties in the United States. This growth has been partially offset by reductions in the average fees that our customers share with us. In recent periods, our customers process of measuring the quality of paid clicks and adjusting the fees paid to us has adversely affected revenues from certain of our distribution partners. In an effort to drive quality traffic to our customers, we continue to invest in product development to expand our online search services offered to our distribution partners.

Engineering, operations and product management personnel remain paramount to our ability to deliver high quality online search services as well as enhance our current technology and grow our product offerings. As such, we expect to continue to invest in our workforce and increase our research and development operations in India. Additionally, we may utilize our cash and short-term and long-term available-for-sale investments to acquire businesses and other assets that will enhance our current technologies and extend our product offerings.

In October 2008, we committed to a plan to close our European facilities by the end of 2008, and expect to incur approximately $700,000 in charges primarily related to employee separation.

Company Internet Site and Availability of SEC Filings

Our corporate Internet site is located at www.infospaceinc.com. We make available on that site our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K, as well as any amendments to those filings, and other filings we make electronically with the U.S. Securities and Exchange Commission (the SEC). The filings can be found in the Investor Relations section of our site and are available free of charge. Information on our Internet site is not part of this Form 10-Q. In addition, the SEC maintains an Internet site at www.sec.gov that contains reports, proxy and information statements, and other information regarding us and other issuers that file electronically with the SEC.

Overview of Third Quarter 2008 Operating Results

The following is an overview of our operating results for the three months ended September 30, 2008. A more detailed discussion, comparing our operating results for the three and nine months ended September 30, 2008 and 2007, is included under the heading Historical Results of Operations in this Management s Discussion and Analysis of Financial Condition and Results of Operations.

Revenues from continuing operations for the three months ended September 30, 2008 increased to $39.5 million from $33.9 million in the three months ended September 30, 2007. This increase was due to an increase in revenue from search results delivered through certain of our distribution partners in the United States and an increase in paid click volume on our owned properties attributable primarily to our direct marketing initiatives. During the three months ended September 30, 2008, approximately 61% of our online search revenues came from our search distribution partners, as compared to approximately 58% during the three months ended September 30, 2007.

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Content and distribution costs from continuing operations for the three months ended September 30, 2008 increased to $18.3 million from $15.3 million in the three months ended September 30, 2007, primarily due to increases in revenue from search results delivered through certain of our distribution partners and increases in our revenue sharing rates.

Other operating expenses from continuing operations for the three months ended September 30, 2008 were $21.0 million, a decrease from $24.0 million in the three months ended September 30, 2007. Other operating expenses include expenses related to Systems and network operations, Product development, Sales and marketing, General and administrative, and Depreciation, and exclude Restructuring and other, net. The decrease from the three months ended September 30, 2007 was primarily attributable to decreases in payments made to employees related to the cash distribution to shareholders in May 2007, stock-based compensation expense relating to stock-based incentives provided to our employees, and other operating expenses as a result of our restructuring described above.

In the three months ended September 30, 2008, we recorded a loss on investments of $9.0 million related to the illiquid auction rate securities investments that we held at September 30, 2008. In addition, in the three months ended September 30, 2008, we recorded a loss on investments of $2.1 million related to preferred shares and warrants to purchase shares in a privately-held company.

Other income, net for the three months ended September 30, 2008 was $1.5 million, as compared to $2.8 million in the three months ended September 30, 2007. The decrease was primarily attributable to a decrease in interest income on a lower average balance of investments due to the dividends paid during the second quarter of 2007 and the first quarter of 2008. Additionally, we recorded an income tax expense from continuing operations of $548,000 in the third quarter of 2008, as compared to expense of $3.4 million in the third quarter of 2007.

The operating results of the directory and mobile businesses have been presented as discontinued operations in our unaudited Condensed Consolidated Financial Statements for all periods presented. The process to separately present continuing and discontinued operations relied on certain estimates and assumptions, and the historical results of operations presented in our unaudited Condensed Consolidated Financial Statements do not necessarily reflect the results of operations that would have existed had we provided our search services as a standalone business throughout the periods presented. Due to the rapidly evolving nature of our business, overall market conditions and the process used to separately present continuing and discontinued operations, we believe that period-to-period comparisons of our revenues and operating results are not necessarily meaningful, and can be unreliable as indications of future performance.

Loss from discontinued operations for the three months ended September 30, 2008 was $12,000, as compared to a loss of $5.6 million in the three months ended September 30, 2007. Loss from the sale of discontinued operations was $13,000 in the three months ended September 30, 2008 as compared to zero ($0) for the three months ended September 30, 2007.

Net loss for the three months ended September 30, 2008 was $9.9 million compared to a net loss of $12.3 million in the three months ended September 30, 2007. The decrease in net loss was primarily attributable to the items noted above.

Critical Accounting Policies and Estimates

Management s Discussion and Analysis of Financial Condition and Results of Operations, as well as disclosures included elsewhere in this Quarterly Report on Form 10-Q, are based upon our unaudited Condensed Consolidated Financial Statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingencies.

The SEC has defined a company s most critical accounting policies as the ones that are the most important to the portrayal of the company s financial condition and results of operations, and which require the company to make its most difficult and subjective judgments, often as a result of the need to make estimates of matters that are inherently uncertain. On an ongoing basis, we evaluate the estimates used, including those related to impairment of goodwill, other-than-temporary impairment of investments, revenue recognition, the estimated allowance for sales returns and doubtful accounts, restructuring-related liabilities, accrued contingencies and valuation allowance for our deferred tax assets. We base our estimates on historical experience, current conditions and on various other assumptions that we believe to be reasonable under the circumstances and, based on information available to us at that time, we make judgments about the carrying values of assets and liabilities that are not readily apparent from other sources as well as identify and assess our accounting treatment with respect to commitments and contingencies. Actual results may differ significantly from these estimates under different assumptions, judgments or conditions. We believe the following critical accounting policies involve the more significant judgments and estimates used in the preparation of our unaudited Condensed Consolidated Financial Statements. We also have other accounting policies,

which involve the use of estimates, judgments and assumptions that are significant to understanding our results. For additional information see Item 8 of Part II, Financial Statements and Supplementary Data Note 1: Summary of Significant Accounting Policies of our Annual Report on Form 10-K for the year ended December 31, 2007.

Revenue Recognition

Our revenues are derived from products and services delivered to our search customers. In general, we recognize revenues in the period in which the services are performed. Online search revenue is recorded on a gross basis in accordance with Emerging Issues Task Force Issue 99-19, *Reporting Revenue Gross as a Principal versus Net as an Agent*. We are the primary obligor in the revenue-generating relationships with our search engine customers, we separately negotiate each revenue or unit pricing contract independent of any revenue sharing arrangements and assume the credit risk for amounts invoiced to such customers. We, through our metasearch technology, determine the paid click, content and information directed to our owned and operated Web sites and our distribution partners Web properties. We earn revenue from our search engine customers by providing paid search clicks generated from our distribution partners Web properties based on separately negotiated and agreed-upon terms with each distribution partner.

We recognize amounts due to our distribution partners in the period they are earned and classify such costs as Content and distribution expense in the unaudited Condensed Consolidated Statement of Operations and Comprehensive Loss. See Item 8 of Part II, Financial Statements and Supplementary Data Note 1: Summary of Significant Accounting Policies of our Annual Report on Form 10-K for the year ended December 31, 2007, for a description of products and services and the related revenue recognition policy.

Fair Value Measurements

On January 1, 2008, we adopted Statement of Financial Accounting Standards (SFAS) No. 157, *Fair Value Measurements*, issued by the Financial Accounting Standards Board (FASB). SFAS No. 157 defines fair value, establishes a framework for measuring fair value, and expands required disclosures about fair value measurements. SFAS No. 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Our $31.2 million of available-for-sale securities include $13.0 million of investments which are classified as short-term as of September 30, 2008, in the Level 1 input category, as defined by SFAS No. 157, because active markets and quoted prices exist for those assets. The remainder of our available-for-sale securities is comprised of $18.2 million of auction rate securities (ARS) which are classified as long-term, in the Level 3 category, as defined by SFAS No. 157, because there are significant unobservable inputs associated with those investments. We paid $40.4 million for our ARS. Our ARS are floating rate securities with either long-term maturities or no maturity date which are marketed by financial institutions with auction reset dates primarily at 28 day intervals to provide short-term liquidity. Beginning in August 2007, auctions for the ARS that we held at September 30, 2008 began to fail due to insufficient bids from buyers, which resulted in higher interest rates being earned on those securities. Although we receive regular interest payments on those ARS, we do not expect to be able to receive the principal amounts until one or more of the following events occur: future auctions of those ARS are successful, we sell those securities in a secondary market which is currently not active, or the issuers redeem those ARS.

We determined the ARS fair values by using a discounted cash flow model that relied upon certain unobservable inputs including the holding period and the discount rates applied to future cash flows. The holding period was based on our estimate of when we will be able to access those funds, and the discount rate was based on our estimate of default risk, which in part relied on historical credit default swap rates for the ARS issuers. The significant unobservable inputs used to determine the ARS fair values are consistent with a Level 3 assessment. Changes in our estimates of the Level 3 inputs used to value our ARS may have a material effect on our results of operations.

We review our available-for-sale investment impairments in accordance with the provisions of SFAS No. 115, *Accounting for Certain Investments in Debt and Equity Securities*, and related guidance issued by the FASB and the SEC. We determine the impairment classification of any individual ARS as either temporary or other-than-temporary. The differentiating factors between temporary and other-than-temporary impairments are primarily the length of the time and the extent to which the fair value has been less than cost, the financial condition and near-term prospects of the issuer and the intent and our ability to retain our investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. We record other-than temporary impairments in Gain (loss) on investments, net in our unaudited Condensed Consolidated Statements of Operations and Comprehensive Loss, and we record temporary impairments within Accumulated other comprehensive income in our unaudited Condensed Consolidated Balance Sheets.

At September 30, 2008, we held $13.1 million of ARS which are rated AA and were issued by various insurance companies. Those ARS were rated AAA when we purchased them for $21.4 million. The underlying collateral of those ARS is investment-grade corporate debt and prime-rated mortgage-backed debt. Those ARS are also insured by monoline insurance

companies. In the three and nine months ended September 30, 2008, we have recorded $6.0 million and $8.3 million of other-than-temporary impairments for those ARS. The $8.3 million of other-than-temporary impairments that we recorded in the nine months ended September 30, 2008 included $1.3 million of impairments initially classified as temporary in 2008, and $525,000 of impairments classified as temporary at December 31, 2007.

At September 30, 2008, we held $5.1 million of ARS which are rated from AA to B and were issued by various insurance companies. In the event of default or liquidation of the collateral by the ARS issuer, we are entitled to receive non-convertible preferred shares in the ARS issuer. Those ARS were rated AA when we purchased them for $19.0 million. In the three and nine months ended September 30, 2008, we have recorded $3.0 million and $11.7 million of other-than-temporary impairments for those ARS. The $11.7 million of other-than-temporary impairments that we recorded in the nine months ended September 30, 2008 included $251,000 of impairments classified as temporary at December 31, 2007. We did not record any impairments for our ARS in the three and nine months ended September 30, 2007.

The global financial markets experienced unusual and significant distress during the first nine months of 2008. If the ARS issuers are unable to successfully close future auctions and their credit ratings deteriorate, the fair value of those ARS may continue to decline and we may record further other-than-temporary impairment charges.

As of January 1, 2008, we held warrants to purchase shares in a privately-held company that had a carrying value of $188,000. In the three and nine months ended September 30, 2008, we recorded a decrease in the fair value of those warrants of $94,000, reducing their fair value to $94,000 as of September 30, 2008. The warrants are classified in Other long-term assets, in Level 3, because there are significant unobservable inputs associated with them. The Company considers the warrants to be derivatives, and follows SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities,* as amended and interpreted, which requires that all derivatives be carried at fair value. We account for all derivatives by recognizing the changes in their fair values as gains or losses on investments in our unaudited Condensed Consolidated Statements of Operations and Comprehensive Loss.

At September 30, 2008, we held an equity investment in a privately-held company. In the three and nine months ended September 30, 2008, we recorded an other-than-temporary impairment of that investment of $2.0 million, reducing its carrying value to zero ($0) as of September 30, 2008. We initially recorded that equity investment at fair value and assessed it for impairment periodically thereafter. The lowest level of inputs for measuring the fair value of that asset is Level 3. The unobservable inputs used in the analysis of the fair value of that investment primarily included our estimates of the privately-held company s business prospects and financial condition. We assess our investment in a privately-held company for impairment in accordance with FASB Staff Position FAS 115-1/124-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments* and the SEC s Staff Accounting Bulletin Topic 5M, *Other Than Temporary Impairment of Certain Investments in Debt and Equity Securities*. We did not record any impairment charges for the investment in a privately-held company in the three months ended September 30, 2007.

In the first three quarters of 2008 and 2007, we did not measure the fair value of any of our assets or liabilities other than our cash and cash equivalents, available-for-sale investments, warrants and investment in a privately-held company. We consider the carrying values of our accounts receivable, notes and other receivables, prepaid expenses and other current assets, accounts payable, accrued expenses and other current liabilities and assets and liabilities of discontinued operations to approximate fair values primarily due to their short-term nature.

For additional information see Item 1 of Part I of this Report, Financial Statements Note 2: Fair Value Measurements.

Accounting for Goodwill

SFAS No. 142, *Goodwill and Other Intangible Assets*, requires that goodwill be tested for impairment on an annual basis and between annual tests in certain circumstances. In addition, certain circumstances may require testing for impairment in conjunction with restructuring in accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. On a quarterly basis, we assess whether business conditions indicate that our goodwill may not be recoverable.

Significant judgments required to estimate the fair value of goodwill include estimating future cash flows, determining appropriate discount rates and other assumptions. Changes in these estimates and assumptions could materially affect the determination of fair value for goodwill. At December 31, 2007 and September 30, 2008, we had $43.9 million of goodwill on our balance sheet.

Allowances for Sales and Doubtful Accounts

Our management must make estimates of potential future sales allowances related to current period revenues for our products and services. We analyze historical adjustments, current economic trends and changes in customer demand and acceptance of our products when evaluating the

adequacy of the sales allowances. Estimates must be made and used in connection with establishing the sales allowance in any accounting period.

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The allowance for doubtful accounts is a management estimate that considers actual facts and circumstances of individual customers and other debtors, such as financial condition and historical payment trends. We evaluate the adequacy of the allowance utilizing a combination of specific identification of potentially problematic accounts and identification of accounts that have exceeded payment terms.

Stock-Based Compensation

On January 1, 2006, we adopted SFAS No. 123(R), *Share-Based Payment*, which requires companies to record stock compensation expense for equity-based awards granted, including stock options and restricted stock unit grants, for which expense will be recognized over the service period of the equity-based award based on the fair value of the award at the date of grant. During the three months ended September 30, 2008 and 2007, we recognized $4.2 million and $7.7 million of stock-based compensation expense, respectively.

Calculating stock-based compensation expense relies upon certain assumptions, including the expected term of the stock-based awards, expected stock price volatility, and the expected pre-vesting forfeiture rate. If we use different assumptions due to changes in our business or other factors, our stock-based compensation expense could materially vary in the future.

Discontinued Operations

In accordance with the provisions of SFAS No. 144, *Accounting for the Impairment or Disposal of Long-lived Assets*, the gains (losses) on sale, results of operations and cash flows of the directory and mobile businesses presented for all periods have been reported as discontinued operations. In addition, the assets and liabilities of the mobile business have been classified as assets and liabilities of discontinued operations at December 31, 2007 and September 30, 2008. The process used to separately present continuing and discontinued operations required significant judgment to implement and relied on certain estimates and assumptions. Different estimates and assumptions could materially affect the allocations of gain or loss on sale, results of operations, cash flows, assets and liabilities to the mobile businesses.

Contingencies

We are subject to various legal proceedings and claims and tax matters, the outcomes of which are subject to significant uncertainty. SFAS No. 5, *Accounting for Contingencies*, requires that an estimated loss from a loss contingency should be recorded by a charge to income if it is probable that an asset has been impaired or a liability has been incurred and the amount of the loss can be reasonably estimated. Disclosure of a contingency is required if there is at least a reasonable possibility that a loss has been incurred. We evaluate, among other factors, the degree of probability of an unfavorable outcome and the ability to make a reasonable estimate of the amount of loss. Changes in these factors could materially impact our financial position or our results of operations. See Note 5 to our unaudited Condensed Consolidated Financial Statements for further information regarding contingencies.

Income Taxes

We account for income taxes under the asset and liability method, under which deferred tax assets, including net operating loss carryforwards, and liabilities are determined based on temporary differences between the book and tax bases of assets and liabilities. We periodically evaluate the likelihood of the realization of deferred tax assets, and reduce the carrying amount of the deferred tax assets by a valuation allowance to the extent we believe a portion will not be realized. We consider many factors when assessing the likelihood of future realization of our deferred tax assets, including our recent cumulative earnings experience by taxing jurisdiction, expectations of future taxable income, the carryforward periods available to us for tax reporting purposes, and other relevant factors. The Company currently provides a valuation allowance against deferred tax assets when it is more likely than not that some portion, or all of its deferred tax assets, will not be realized.

In determining our income tax provision for interim periods, we use an estimated annual effective tax rate which is based on our expected annual income, permanent differences between financial and tax reporting and statutory tax rates in the various jurisdictions in which we operate. Each quarter we update our estimate of the annual effective tax rate, and if our estimated tax rate changes we make a cumulative adjustment. We separately recognize any subsequent recognition, derecognition and measurement of a tax position, taken in a previous period, in the quarter in which it occurs.

Historical Results of Operations

For the three months ended September 30, 2008, our net loss was $9.9 million. We have incurred net losses on an annual basis for all but three of the years since our inception. Additionally, we incurred a net loss in the first quarter of 2008 and as of September 30, 2008, have an accumulated deficit of $1.0 billion.

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In light of the rapidly evolving nature of our business and overall market conditions, we believe that period-to-period comparisons of our revenues and operating expenses are not necessarily meaningful, and you should not rely upon them as indications of our future performance.

Results of Operations for the Three and Nine months ended September 30, 2008 and 2007

Revenue. We primarily receive revenues from our content providers, whom we refer to as our customers, when an end user of our Web search services clicks on a paid search link that is provided by a customer and displayed on our owned Web site or displayed on the Web property of a distribution partner. In addition, we earn services revenue from certain distribution partners, such as a fixed monthly fee in exchange for portal infrastructure services.

Revenue for the three and nine months ended September 30, 2008 and 2007 is presented below (amounts in thousands):

	Three months ended September 30,		Change from	Nine months ended September 30,		Change from
	2008	2007	2007	2008	2007	2007
Revenue	$ 39,469	$ 33,852	$ 5,617	$ 119,979	$ 101,479	$ 18,500

The increase in revenue for online search services for the three and nine months ended September 30, 2008 as compared to the three and nine months ended September 30, 2007, is due to an increase in revenue from search results delivered through certain of our distribution partners in the United States and an increase in paid click volume on our owned properties attributable primarily to our direct marketing initiatives. During the three months ended September 30, 2008, approximately 61% of our revenues came from our search distribution partners, as compared to approximately 58% during the three months ended September 30, 2007. During the nine months ended September 30, 2008, approximately 65% of our revenues came from our search distribution partners, as compared to approximately 56% during the nine months ended September 30, 2007.

Seasonality

Revenues from online search services from our owned Web sites are historically affected by seasonal fluctuations in Internet usage, which generally declines in the summer months.

Content and Distribution Expenses. Content and distribution expenses consist principally of costs related to revenue sharing arrangements with our distribution partners, as well as content and data licenses. Content and distribution expenses in total dollars (in thousands) and as a percent of total revenues for the three and nine months ended September 30, 2008 and 2007 are presented below:

	Three months ended September 30,		Change from	Nine months ended September 30,		Change from
	2008	2007	2007	2008	2007	2007
Content and Distribution Expenses	$ 18,265	$ 15,274	$ 2,991	$ 58,119	$ 42,819	$ 15,300
Percent of Revenue	46.3%	45.1%	1.2%	48.4%	42.2%	6.2%

The increase in search content and distribution expenses for the three and nine months ended September 30, 2008 as compared to the three and nine months ended September 30, 2007, is primarily due to an increase in revenue shared with our distribution partners from search results delivered through those distribution partners and increases in our revenue sharing rates with our distribution partners. We anticipate that our search content and distribution expenses will increase in absolute dollars if revenues increase through growth from existing arrangements with our search distribution partners or we add new search distribution partners. If online search revenue generated from our distribution partners increases at a greater rate than revenues generated from our own Web sites, content and distribution expenses as a percentage of revenue will increase. We expect that online search revenue from searches conducted by end users on sites of our distribution partners will continue to be a significant share of our online search revenues for the foreseeable future.

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Systems and Network Operations Expenses. Systems and network operations consists of expenses associated with the delivery, maintenance and support of our services and infrastructure, including personnel expenses, which include salaries, benefits and other employee related costs, stock-based compensation expense, and temporary help and contractors to augment our staffing, communication costs, equipment repair and maintenance, and professional service fees. Systems and network operations expenses in total dollars (in thousands) and as a percent of total revenues for the three and nine months ended September 30, 2008 and 2007 are presented below:

	Three months ended September 30,		Change from	Nine months ended September 30,		Change from
	2008	2007	2007	2008	2007	2007
Systems and Network Operations Expenses	$ 3,238	$ 2,295	$ 943	$ 8,454	$ 6,980	$ 1,474
Percent of Revenue	8.2%	6.8%	1.4%	7.1%	6.9%	0.2%

Systems and network operations expenses increased by $943,000 and $1.5 million to $3.2 million and $8.5 million for the three and nine months ended September 30, 2008, respectively, as compared to $2.3 million and $7.0 million for the three and nine months ended September 30, 2007, respectively. The absolute dollar increase for the three and nine months ended September 30, 2008 as compared to the three and nine months ended September 30, 2007 was primarily due to an increase in personnel expenses, including employee salaries, temporary help, contractors, and stock-based compensation expense, of $653,000 and $1.1 million for the three and nine months ended September 30, 2008, respectively, to construct and migrate to our new data centers, which became necessary following the completion of the sale of our mobile business and our related data center assets.

Product Development Expenses. Product development expenses consist principally of personnel expenses, which include salaries, stock-based compensation expense, benefits and other employee related costs, and temporary help and contractors to augment our staffing, research, development, support and ongoing enhancements of our products and services. Product development expenses in total dollars (in thousands) and as a percent of total revenues for the three and nine months ended September 30, 2008 and 2007 are presented below:

	Three months ended September 30,		Change from	Nine months ended September 30,		Change from
	2008	2007	2007	2008	2007	2007
Product Development Expenses	$ 2,757	$ 2,086	$ 671	$ 7,895	$ 6,849	$ 1,046
Percent of Revenue	7.0%	6.2%	0.8%	6.6%	6.7%	(0.1)%

Product development expenses increased by $671,000 to $2.8 million for the three months ended September 30, 2008 as compared to $2.1 million for the three months ended September 30, 2007. The absolute dollar increase for the three months ended September 30, 2008 as compared to the three months ended September 30, 2007 was primarily due to an increase in personnel expenses, including employee salaries, temporary help, contractors, and stock-based compensation expense, of $784,000 for the three months ended September 30, 2008.

Product development expenses increased by $1.0 million to $7.9 million for the nine months ended September 30, 2008 as compared to $6.8 million for the nine months ended September 30, 2007. The absolute dollar increase for the nine months ended September 30, 2008 as compared to the nine months ended September 30, 2007 was primarily due to an increase in personnel expenses, including employee salaries, temporary help, contractors, and stock-based compensation expense, of $1.4 million for the nine months ended September 30, 2008. This increase was partially offset by a decrease in payments made to employees related to the cash distribution to shareholders in May 2007 of $378,000 for the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007.

Product development costs may not be consistent with revenue trends because they represent key costs to develop and enhance our product offerings.

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Sales and Marketing Expenses. Sales and marketing expenses consist principally of personnel costs, which include salaries, stock-based compensation expense, benefits and other employee related costs, and temporary help and contractors to augment our staffing, advertising, market research and promotion expenses. Sales and marketing expenses in total dollars (in thousands) and as a percent of total revenues for the three and nine months ended September 30, 2008 and 2007 are presented below:

	Three months ended September 30,		Change from	Nine months ended September 30,		Change from
	2008	2007	2007	2008	2007	2007
Sales and Marketing Expenses	$ 6,882	$ 5,518	$ 1,364	$ 16,712	$ 17,008	$ (296)
Percent of Revenue	17.4%	16.3%	1.1%	13.9%	16.8%	(2.9)%

Sales and marketing expenses increased by $1.4 million to $6.9 million for the three months ended September 30, 2008 as compared to $5.5 million for the three months ended September 30, 2007. The absolute dollar increase for the three months ended September 30, 2008 as compared to the three months ended September 30, 2007 was primarily attributable to an increase of $2.3 million in advertising and marketing expense related to our direct marketing initiatives, which was partially offset by a decrease in stock-based compensation expense of $853,000 for the three months ended September 30, 2008.

Sales and marketing expenses decreased by $296,000 to $16.7 million for the nine months ended September 30, 2008 as compared to $17.0 million for the nine months ended September 30, 2007. The absolute dollar decrease for the nine months ended September 30, 2008 as compared to the nine months ended September 30, 2007 was primarily attributable to a $1.7 million decrease in payments made to employees related to the cash distribution to shareholders in May 2007 and a decrease of $1.7 million in stock-based compensation expense. These decreases were partially offset by an increase in advertising and marketing expense of $3.2 million for the nine months ended September 30, 2008.

Sales and marketing expenses may increase in absolute dollars as we continue to invest in marketing initiatives and sales promotions and expand our products, services and distribution channels.

General and Administrative Expenses. General and administrative expenses consist primarily of personnel expenses, which include salaries, benefits and other employee related costs, stock-based compensation expense, professional service fees, which include legal fees, audit fees, SEC compliance costs, which include costs related to compliance with the Sarbanes-Oxley Act of 2002, legal settlements, occupancy and general office expenses, and general business development and management expenses. General and administrative expenses in total dollars (in thousands) and as a percent of total revenues for the three and nine months ended September 30, 2008 and 2007 are presented below:

	Three months ended September 30,		Change from	Nine months ended September 30,		Change from
	2008	2007	2007	2008	2007	2007
General and Administrative Expenses	$ 5,940	$ 12,694	$ (6,754)	$ 18,622	$ 51,893	$ (33,271)
Percent of Revenue	15.0%	37.5%	(22.5)%	15.5%	51.1%	(35.6)%

General and administrative expenses decreased by $6.8 million to $5.9 million for the three months ended September 30, 2008 as compared to $12.7 million for the three months ended September 30, 2007. The absolute dollar decrease for the three months ended September 30, 2008 as compared to the three months ended September 30, 2007 was primarily attributable to a decrease in stock-based compensation expense of $3.2 million, a decrease in professional service fees of $1.5 million, a decrease in personnel related expenses, including employee salaries, of $1.2 million, and a decrease in facilities expense of $519,000.

General and administrative expenses decreased by $33.3 million to $18.6 million for the nine months ended September 30, 2008 as compared to $51.9 million for the nine months ended September 30, 2007. The absolute dollar decrease for the nine months ended September 30, 2008 as compared to the nine months ended September 30, 2007 was primarily attributable to a decrease in payments made to employees related to the cash distribution to shareholders in May 2007 of $16.5 million, a decrease in professional service fees of $7.6 million related to the sale of the directory and mobile businesses before the definitive agreements in connection with the sale of those businesses were signed, a decrease in stock-based compensation expense of $5.5 million, a decrease in litigation settlements of $1.1 million, a decrease in facilities expense of $1.1 million, and a decrease in personnel related expenses, including employee salaries, of $703,000.

Depreciation. Depreciation of property and equipment includes depreciation of network servers and data center equipment, computers, software, office equipment and fixtures and leasehold improvements. Depreciation of property and equipment increased to $2.2 million and $5.4 million for the three and nine months ended September 30, 2008, respectively, compared to $1.4 million and $4.1 million for the three and nine months

ended September 30, 2007, respectively. This increase was primarily due to equipment purchased for the new data centers opened in 2008.

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Restructuring and Other, Net. We recorded total restructuring charges of $558,000 and $1.4 million in the three and nine months ended September 30, 2007, respectively, related to the restructuring plans committed to in 2006 and 2007, and we recorded immaterial adjustments to charges related to those plans in the three and nine months ended September 30, 2008. In future periods, adjustments and additions may be made to the amounts recorded as of September 30, 2008.

Other, net totaled zero ($0) and $1.9 million for the three and nine months ended September 30, 2008 and $65,000 and $3.2 million for the three and nine months ended September 30, 2007, respectively, and consists primarily of the gains on sales of certain non-core assets.

Gain (Loss) on Investments, Net. In the three and nine months ended September 30, 2008, we recorded a loss on investments of $11.0 million and $22.1 million, respectively, which primarily consisted of $9.0 million and $20.0 million recorded the three and nine months ended September 30, 2008, respectively, of other-than-temporary impairments related to our illiquid ARS. In addition, in the three and nine months ended September 30, 2008, we recorded a charge of $2.1 million to reduce the carrying value of certain equity investments in a privately held company. We did not record any material gains or losses on investments recorded in the three and nine months ended September 30, 2007.

Other Income, Net. Other income, net totaled $1.5 million and $6.4 million for the three and nine months ended September 30, 2008, respectively, compared to $2.8 million and $12.5 million for three and nine months ended September 30, 2007, respectively. Other income, net, primarily consists of interest income. The decrease in interest income for the three and nine months ended September 30, 2008, as compared to the three and nine months ended September 30, 2007, was primarily attributable to a lower balance of investments as a result of the aggregate $507.3 million of special dividends paid in May 2007 and January 2008. The decrease in interest income for the nine months ended September 30, 2008 was partially offset by income of $1.1 million related to cash received for the resolution of a bankruptcy claim.

Income Tax Expense. We recorded an income tax expense of $548,000 and $153,000 for the three and nine months ended September 30, 2008, respectively. We recorded an income tax expense of $3.4 million and $10.3 million for the three and nine months ended September 30, 2007, respectively. For each period, the income tax expense included U.S. federal tax, state and foreign taxes. Income tax expense for the three months ended September 30, 2008 differed from the tax expense at the statutory rates primarily due to non-deductible permanent differences and applying a valuation allowance against deferred tax assets arising during the period. Income tax expense for the nine months ended September 30, 2008 differed from the tax expense at the statutory rates primarily due to non-deductible permanent differences, applying a valuation allowance against deferred tax assets arising during the period, and certain one-time items primarily attributable to restructuring. Income tax expense for the three and nine months ended September 30, 2007 differed from the tax expense at the statutory rates due to non-deductible permanent differences and applying a valuation allowance against deferred tax assets.

Income from Discontinued Operations. In the fourth quarter of 2007, we completed the sales of our directory and mobile businesses and have reflected loss from those businesses as loss from discontinued operations. Revenue, loss before taxes, income tax benefit, loss from discontinued operations and loss on sale of discontinued operations for the three and nine months ended September 30, 2008 and 2007 are presented below (in thousands):

	Three months ended September 30,		Nine months ended September 30,	
	2008	**2007**	**2008**	**2007**
Revenue from discontinued operations	$ 45	$ 23,636	$ 125	$ 113,182
Loss from discontinued operations before taxes	(638)	(8,975)	(1,859)	(26,385)
Income tax benefit	626	3,350	536	9,518
Loss from discontinued operations, net of taxes	$ (12)	$ (5,625)	$ (1,323)	$ (16,867)
Loss on sale of discontinued operations, net of taxes	$ (13)	$	$ (208)	$

Liquidity and Capital Resources

As of September 30, 2008, we had cash and marketable investments of $210.4 million, consisting of cash and cash equivalents of $179.2 million, short-term investments available-for-sale of $13.0 million, and long-term investments available-for-sale of $18.2 million. We generally invest our excess cash in high quality marketable investments. These investments include securities issued by U.S. government agencies, certificates of deposit, money market funds, and taxable municipal bonds.

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Commitments and Pledged Funds

The following are our contractual commitments associated with our capital and operating lease obligations (in thousands):

	Remainder of 2008	2009	2010	2011	2012	2013	Total
Operating lease commitments	$ 416	$ 1,641	$ 1,640	$ 1,607	$ 1,659	$ 283	$ 7,246
Capital lease commitments (net of imputed interest and executory costs)	137	551	565	209			1,462
Total	$ 553	$ 2,192	$ 2,205	$ 1,816	$ 1,659	$ 283	$ 8,708

We have pledged a portion of our cash and cash equivalents as collateral for standby letters of credit and bank guaranties for certain of our property leases. At September 30, 2008, the total amount of collateral pledged under these agreements was $5.9 million.

Cash Flows

Net cash provided by operating activities consists of net loss offset by certain adjustments not affecting current period cash flows, and the effect of changes in our operating assets and liabilities. Our net cash flows are comprised of the following for the nine months ended September 30, 2008 and 2007 (in thousands):

	Nine months ended September 30,	
	2008	2007
Net cash used by operating activities from continuing operations	$ (21,576)	$ (14,674)
Net cash provided by investing activities	16,634	133,955
Net cash used by financing activities	(298,788)	(193,989)
Net cash provided (used) by discontinued operations	(15,361)	25,754
Net decrease in cash and cash equivalents	$ (319,091)	$ (48,954)

Net cash used by operating activities was $21.6 million for the nine months ended September 30, 2008, consisting of our net loss of $10.8 million, cash used by changes in our operating assets and liabilities of $59.2 million consisting of a decrease in accrued expenses and other current liabilities which primarily resulted from payments of employee expenses related to the $299.1 million special dividend paid on January 8, 2008 and employee separation payments, a decrease in accounts payable and increases in prepaid expenses and other current assets, and adjustments not affecting cash flows used by operating activities of $3.3 million related to the gain on sale of certain non-core assets and deferred income taxes. Partially offsetting these decreases were changes in our operating assets and liabilities of $11.2 million, consisting of decreases in notes and other receivables, other long-term assets, and accounts receivable and adjustments not affecting cash flows provided by operating activities of $40.4 million, primarily consisting of loss on investments, net, stock-based compensation expense, depreciation, loss from discontinued operations, and loss on the sale of discontinued operations.

Net cash used by operating activities was $14.7 million for the nine months ended September 30, 2007, consisting of our net loss of $40.9 million, changes in our operating assets and liabilities of $13.1 million primarily consisting of decreases in accrued expenses and other current and long-term liabilities and accounts payable, and increases in accounts receivable and adjustments not affecting cash flows provided by operating activities of $3.4 million primarily consisting of the gain on the sale of certain non-core assets. Partially offsetting these decreases is cash provided by changes in our operating assets and liabilities of $2.5 million, consisting of decreases in notes and other receivables, prepaid expenses and other current assets and other long-term assets, and adjustments not affecting cash flows provided by operating activities of $40.2 million, consisting of stock-based compensation expense, loss from discontinued operations, depreciation, restructuring, and deferred income taxes.

Net cash provided by investing activities totaled $16.6 million for the nine months ended September 30, 2008, primarily consisting of the net decrease in short-term investments of $26.0 million and proceeds from the sale of assets of $2.3 million. These increases in cash were partially offset by $10.7 million used to purchase property and equipment and the increase in other long-term assets of $1.0 million.

Net cash provided by investing activities totaled $134.0 million for the nine months ended September 30, 2007, primarily consisting of the net decrease in short-term investments of $137.4 million and proceeds from the sale of assets $2.9 million, partially offset by $4.3 million used to purchase property and equipment and a $2.0 million loan to an equity investee.

Net cash used by financing activities totaled $298.8 million in the nine months ended September 30, 2008, and primarily consisted of the $299.1 million special dividend paid to shareholders in January 2008. Partially offsetting this decrease was cash proceeds of $454,000 from the exercise of stock options and from sales of shares through our employee stock purchase plan.

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Net cash used by financing activities totaled $194.0 million in the nine months ended September 30, 2007 and primarily consisted of the $208.2 million special dividend paid to shareholders in May 2007. Partially offsetting this decrease was cash proceeds of $14.2 million from the exercise of stock options, warrants, and from sales of shares through our employee stock purchase plan.

Net cash used by discontinued operations totaled $15.4 million for the nine months ended September 30, 2008, primarily consisting of loss from discontinued operations of $1.3 million and cash used by decreases in liabilities net of operating assets of discontinued operations of $14.0 million.

Net cash provided by discontinued operations totaled $25.8 million for the nine months ended September 30, 2007, primarily consisting of cash provided by decreases in operating assets net of liabilities of discontinued operations of $56.2 million. This increase was partially offset by the loss from discontinued operations of $16.9 million and $13.6 million to purchase property and equipment.

We plan to use our cash to fund operations, develop technology, advertise, market and distribute our products and application services, and continue the enhancement of our network infrastructure. We may use a portion of our cash for acquisitions, special dividends, or for common stock repurchases.

We believe that existing cash balances, cash equivalents, short term investments and cash generated from operations will be sufficient to meet our anticipated cash needs for working capital and capital expenditures for at least the next 12 months. However, the underlying assumed levels of revenues and expenses may not prove to be accurate. Our anticipated cash needs exclude any payments for pending or future litigation matters. In addition, we evaluate acquisitions of businesses, products or technologies that complement our business from time to time. Any such transactions, if completed, may use a significant portion of our cash balances and marketable investments. If we are unable to liquidate these investments when we need such liquidity for business purposes, as further discussed below, we may need to change or postpone such business purposes or find alternative financing for such business purposes, if available. We may seek additional funding through public or private financings or other arrangements prior to such time. Our ability to raise funds may be adversely affected by a number of factors relating to the Company, as well as factors beyond our control, including weakness in the economic conditions in markets in which we operate and from which we generate revenues, and increased uncertainty in the financial, capital and credit markets. Adequate funds may not be available when needed or may not be available on favorable terms. If we raise additional funds by issuing equity securities, dilution to existing stockholders will result. If funding is insufficient at any time in the future, we may be unable to develop or enhance our products or services, take advantage of business opportunities or respond to competitive pressures, any of which could harm our business.

Illiquid Investments