2000 Annual Report

NTN Communications, Inc.

At the Forefront of Interactive Television and Electronic Entertainment

Dear Fellow Shareholders:

Stanley B. Kinsey
Chairman of the Board
Chief Executive Officer

NTN remains a company whose products are ahead of their Interactive Television (ITV) markets, in both in-home and out-of-home applications. We remain a leader in the out-of-home hospitality content arena, where our growth has us closing in on the network size necessary for profitability. We are also positioned to become a leader in the in-home market, as our goal of becoming a premier game channel on ITV services is nearer today than ever before.

When a company is at the leading edge of a dynamic new industry, its financial results reflect the costs of establishing its position as a leader. They often do not, however, reflect the potential benefits. This is indeed the case for the year 2000, as we invested several million dollars in Internet and ITV initiatives. While our investment in specific Internet initiatives may yet prove successful, the bursting of the Internet “bubble” has adversely affected profitability on a short-term basis.

The good news is that we did not “bet the farm,” but invested somewhat prudently in key initiatives. We believe the capital used to establish a stronger game infrastructure and proof of demand for BUZZTIME™ games was appropriate considering potential current and future opportunities. We became one of the leading game areas of WebTV, the best current test in ITV content, and on Sprint PCS’s Wireless Web mobile phones. These interactive content markets remain very promising, as Tyrone Lam, the President of BUZZTIME, discusses on the inside back cover of this report.

For the NTN Network® division, the year 2000 saw the completion of a two-year, $10 million conversion effort to get our restaurant and sports bar installations onto our new digital technology. With the installation of our 3,000th U.S. site by the end of last year, we began to position the company for growth to the 4,000-site milestone. Mark deGorter, the new President and COO of the NTN Network, and his team are doing an excellent job of strengthening content and service, while focusing operations on lower costs and higher growth. Mark discusses his charter on the inside back cover of this report.

I thank all of our employees for their tireless efforts and contributions to making this company successful. With the maturing of both of our key markets, management remains focused, committed and excited for coming developments. I look forward to reporting to you in the future.

Sincerely yours,

Stanley B. Kinsey
Chairman and CEO

Selected Financial Data

The following tables furnish information with respect to selected consolidated financial data over the past five years.

STATEMENT OF OPERATIONS DATA *(in thousands, except per share data)*

Years Ended December 31,	2000	1999	1998	1997	1996
Total revenue	**$22,048**	$23,748	$24,194	$25,861	$25,711
Total operating expenses	**30,249**	27,549	27,641	38,668	51,566
Operating loss	**(8,201)**	(3,801)	(3,447)	(12,807)	(25,855)
Other income (expense), net	**(940)**	1,303	1,654	350	1
Loss from continuing operations	**(9,141)**	(2,498)	(1,793)	(12,457)	(25,854)
Loss from discontinued operations	**—**	—	—	—	(1,317)
Gain on sale of discontinued operations	**—**	—	—	—	4,219
Income taxes	**—**	—	—	—	—
Loss before cumulative effect of accounting change	**(9,141)**	(2,498)	(1,793)	(12,457)	(22,952)
Cumulative effect of accounting change	**(448)**	—	—	—	—
Net loss	**$(9,589)**	$(2,498)	$(1,793)	$(12,457)	$(22,952)
Accretion of beneficial conversion feature of preferred stock	**—**	—	(758)	—	—
Net loss available to common shareholders	**$(9,589)**	$(2,498)	$(2,551)	$(12,457)	$(22,952)
Basic and diluted net loss per common share:					
Continuing operations	**$(.28)**	$(.09)	$(.10)	$(0.55)	$(1.15)
Discontinued operations	**—**	—	—	—	0.13
Cumulative effect of accounting change	**(.01)**	—	—	—	—
Net loss	**$(.29)**	$(.09)	$(.10)	$(0.55)	$(1.02)
Weighted-average shares outstanding	**33,206**	28,470	26,078	22,696	22,568

BALANCE SHEET DATA *(in thousands)*

December 31,	2000	1999	1998	1997	1996
Total current assets	**$5,808**	$6,387	$8,131	$8,390	$10,655
Total assets	**18,822**	17,287	16,767	20,271	28,504
Total current liabilities	**4,915**	5,466	5,731	8,373	12,775
Total liabilities	**14,740**	15,066	8,442	11,545	18,282
Shareholders' equity	**4,082**	2,221	8,325	8,726	10,222

Management's Discussion and Analysis of Financial Condition and Results of Operations

GENERAL

Management's discussion and analysis of financial condition and results of operations should be read in conjunction with the selected financial data and the consolidated financial statements and notes thereto included elsewhere herein.

RESULTS OF OPERATIONS

Following is a comparative discussion by fiscal year of the results of operations for the three years ended December 31, 2000. We believe that inflation has not had a material effect on the results of operations for the periods presented.

Year Ended December 31, 2000 as Compared to the Year Ended December 31, 1999

Operations for the year ended December 31, 2000 resulted in a net loss of $9,589,000 compared to net loss of $2,498,000 for the year ended December 31, 1999. The operating results for the year ended December 31, 2000 include the implementation of Staff Accounting Bulletin No. 101 ("SAB 101") related to the recognition of installation, training and set up revenues, which resulted in a reduction in revenues of $845,000, an increase in related expense of $282,000 and the cumulative effect on prior years of approximately $448,000. It also includes a charge for the impairment of assets for certain Web development costs and Internet game stations equipment, license and related goodwill in the amount of $1,362,000. The operating results for the year ended December 31, 1999 included a gain of $2,254,000 related to the sale of the assets of our wholly owned subsidiary, IWN, L.P., to eBet Limited for $1,227,000 in cash and 4,000,000 shares of eBet Online stock.

Total revenues decreased 7% to $22,048,000 for the year ended December 31, 2000 from $23,748,000 for the year ended December 31, 1999. This occurred primarily due to decreases in NTN Network revenues, America Online fees, equipment sales and other revenues which were partially offset by an increase in BUZZTIME service revenues.

The following table sets forth certain information with respect to the principal sources of our revenues during the years ended December 31, 2000 and 1999.

(in thousands)

Years Ended December 31,	2000	1999
NTN Network revenues	**$21,406**	$22,250
BUZZTIME service revenues	**540**	383
America Online fees	**—**	600
Equipment sales, net	**—**	84
Other revenues	**102**	431

NTN Network revenues are generated primarily from broadcasting content and advertising to customer locations. The direct costs associated with these revenues include the cost of installing the equipment at the customer location, marketing visits, technical service, freight, telecommunications, sales commission, parts, repairs, and depreciation of the equipment placed in service and materials.

BUZZTIME service revenues are generated primarily from advertising and production services. The direct costs associated with these revenues are license fees and server hosting fees.

America Online fees relate to the fees paid by America Online in connection with an exclusive agreement whereby we provided trivia content in exchange for a fee. There are no direct costs related to these fees.

Equipment sales are sales of our broadcast equipment to customers and foreign licensees.

NTN Network revenues decreased 4% to $21,406,000 for the year ended December 31, 2000 from $22,250,000 for the year ended December 31, 1999. This decrease is primarily due to an accounting policy change in revenue recognition under SAB 101, which decreased revenue by $845,000. Excluding the impact of SAB 101, NTN Network revenue would have increased by less than 1%. During the year ended December 31, 2000, approximately 1,300 digital systems were installed. Included in NTN Network revenues are revenues from our Canadian licensee totaling $1,266,000 and $1,292,000 for the years ended December 31, 2000 and 1999, respectively. NTN Network revenues also include advertising fees. In 2000, we generated revenue of $1.4 million in national and regional advertising, comprised primarily of companies in the wine, beer and spirits category, compared to $892,000 in 1999.

BUZZTIME service revenues increased 41% to $540,000 for the year ended December 31, 2000 from $383,000 for the year ended December 31, 1999. The increase was due to new advertising contracts in 2000.

America Online fees were zero for the year ended December 31, 2000 compared to $600,000 for the year ended December 31, 1999. Our contract with America Online expired on December 1, 1999, at which time a new contract was signed, under which we did not generate revenue from America Online. Under the terms of the new nonexclusive contract, we had access to America Online's 25 million subscribers, allowing promotion of the BUZZTIME Web site on several America Online channels. The new contract with America Online expired on November 30, 2000.

Equipment sales were zero for the year ended December 31, 2000 compared to $84,000 for the year ended December 31, 1999. This decrease was due to the conclusion of the recognition of deferred revenue associated with prior equipment sale-leasebacks in 1999. Prior to 1999, we sold equipment to our customers and through our wholly owned subsidiary, LearnStar.

Other revenue decreased 76% to $102,000 for the year ended December 31, 2000 from $431,000 for the year ended December 31, 1999. Other revenue for the year ended December 31, 1999 included $302,000 of revenue recorded by IWN, Inc. Due to the sale of the assets of IWN, Inc. in August 1999, no such revenue was recorded for the year ended December 31, 2000.

Direct operating costs of services decreased 1% to $11,098,000 for the year ended December 31, 2000 from $11,169,000 for the year ended December 31, 1999. Excluding the increase in expenses related to the SAB 101 adjustment of $282,000, direct cost of services decreased 3% to $10,816,000. This is due to a decrease in depreciation and amortization of approximately $708,000 due to the DOS-based network equipment being fully depreciated by June 2000, which is offset by an increase in depreciation for the capitalized purchases of broadcast equipment associated with the digital network. Installation fees, sales commissions and freight expense decreased an aggregate of approximately $371,000 due to approximately 200 fewer installations in 2000 compared to 1999. Technical site service and playmaker repairs decreased an aggregate of $497,000 due to fewer repairs needed on the newer digital broadcast equipment. At December 31, 2000 there were approximately 2,598 digital sites installed compared to 1,493 sites at December 31, 1999. These decreases were offset by an increase in Internet service provider charges of approximately $248,000 due to additional services needed to support the digital network compared to the DOS-based network. Advertising commissions also increased approximately $287,000 partly due to an increase in advertising revenue and due to the recognition of non-refundable advances when a contract with a sales representative was cancelled. License fees increased approximately $219,000 due to the renewed contract with the NFL, which was approximately $50,000 more in fees than in 1999, and also due to the reversal of an accrued liability and the related expense in 1999 of $180,000 in relation to a settlement. Hosting fees increased approximately $360,000 due to the development of BUZZTIME.com in 2000. Miscellaneous parts expense increased by approximately $139,000 due to additional repairs needed on intelligent data receiver ("IDR") cards and due to less conversions of sites to the digital network compared to 1999. Some of the parts for DOS-based equipment were reused on the digital network, which lowered costs for parts in 1999.

Selling, general and administrative expenses increased 11% to $15,070,000 for the year ended December 31, 2000 from $13,610,000 for the year ended December 31, 1999. Selling, general and administrative expense for the year ended December 31, 2000 included an increase in payroll and related expenses of approximately $2,467,000 relating to an increase in the number of employees for the development and launch of the Internet Web site, interactive television and wireless applications. Office lease expense increased approximately $149,000 due to additional space leased for the sales offices in Carlsbad and San Francisco and warehouse space in Carlsbad. Stock-based compensation increased approximately $393,000 due to the issuance of options and warrants to employees and non-employees. These increased expenses were offset by a decrease in equipment leases of approximately $684,000 due to the conclusion of the leases in 1999. Consulting expenses decreased approximately $148,000 due to Year 2000 remediation efforts in 1999 offset by an increase in consultants for technology and BUZZTIME. Marketing expenses decreased approximately $374,000 due to additional expenses incurred in 1999 to promote the digital network. Additionally, bad debt expenses decreased approximately $304,000 due to improved collections.

Litigation, legal and professional fees decreased 15% to $474,000 for the year ended December 31, 2000 compared to $558,000 for the year ended December 31, 1999 due to additional expense recorded in 1999 for the settlement of litigation.

Depreciation and amortization increased 32% to $1,815,000 for the year ended December 31, 2000 from $1,370,000 for the year ended December 31, 1999 due to increased purchases of computer equipment and software placed in service in 2000.

Impairment charges totaled $1,362,000 for the year ended December 31, 2000 due to the write-off of certain Web development costs for the Internet Web site, BUZZTIME.com, as the focus of BUZZTIME changed to other interactive initiatives, and Internet game station assets, license and related goodwill on the basis that the assets are not recoverable through future cash flows.

Research and development expenses decreased 49% to $430,000 for the year ended December 31, 2000 from $842,000 for the year ended December 31, 1999. The current period expenses result from our research and development related to the next generation of the digital network, wireless and interactive applications and Internet stations. For the year ended December 31, 1999, our research and development efforts related to the second generation of the digital network, Internet stations, and future Internet Web sites.

Interest expense increased 8% to $1,131,000 for the year ended December 31, 2000 from $1,050,000 for the year ended December 31, 1999 primarily due to interest expense recorded for additional capitalized leases acquired in 2000 and interest on the revolving line of credit.

Year Ended December 31, 1999 as Compared to the Year Ended December 31, 1998

Operations for the year ended December 31, 1999 resulted in a net loss of $2,498,000 compared to net loss of $1,793,000 for the year ended December 31, 1998. The operating results for the year ended December 31, 1999 included a gain of $2,254,000 related to the sale of the assets of our wholly owned subsidiary, IWN, L.P., to eBet Limited for $1,227,000 in cash and 4,000,000 shares of eBet Online stock. The operating results for the year ended December 31, 1998 included a gain of $1,643,000 related to the sale of a majority interest in one of our subsidiaries.

Total revenues decreased 2% to $23,748,000 for the year ended December 31, 1999 from $24,194,000 for the year ended December 31, 1998. This occurred primarily due to decreases in BUZZTIME service revenues, America Online fees, equipment sales and other revenues which were partially offset by increases in NTN Network revenues.

The following table sets forth certain information with respect to the principal sources of NTN's revenues during the years ended December 31, 1999 and 1998.

(in thousands)

Years Ended December 31,	**1999**	**1998**
NTN Network revenues	$22,250	$20,973
BUZZTIME service revenues	383	1,131
America Online fees	600	883
Equipment sales, net	84	499
Other revenue	431	708

NTN Network revenues increased 6% to $22,250,000 for the year ended December 31, 1999 from $20,973,000 for the year ended December 31, 1998. This increase is primarily due to an increase in rate charged for the setup, installation and training for the digital network as compared to the original DOS-based network. Subscribers to the NTN Network did, however, decline by 2% from 1998 to 1999. During the year ended December 31, 1999, approximately 1,500 digital systems were installed. Included in NTN Network revenues are revenues from our Canadian licensee totaling $1,292,000 in each of the years ended December 31, 1999 and 1998. We also included advertising fees in NTN Network revenues. In 1999, we sold $892,000 in national and regional advertising, comprised primarily of companies in the wine, beer and spirits category.

BUZZTIME service revenues decreased 66% to $383,000 for the year ended December 31, 1999 from $1,131,000 for the year ended December 31, 1998. The decrease was largely due to the expiration of the trials we performed for Bell Canada in 1998, which generated $670,000 in 1998, that did not occur in 1999.

America Online fees decreased 32% to $600,000 for the year ended December 31, 1999 from $883,000 for the year ended December 31, 1998. We entered into a new contract in the second quarter of 1998 with our Internet partner, America Online. The new contract, which expired December 1, 1999, provided for a flat monthly fee rather than fees based on America Online member usage of our content, which resulted in a reduction of revenue from this source of $283,000 for the year ended December 31, 1999 compared to the year ended December 31, 1998.

Equipment sales decreased 83% to $84,000 for the year ended December 31,1999 from $499,000 for the year ended December 31, 1998. This decrease was due to the conclusion of the recognition of deferred revenue associated with prior equipment sale-leasebacks and also a result of no equipment being sold in 1999. Prior to 1999, we sold equipment to our customers and through our wholly owned subsidiary, LearnStar.

Other revenue decreased 39% to $431,000 for the year ended December 31, 1999 from $708,000 for the year ended December 31, 1998. Other revenue for the year ended December 31, 1998 included $125,000 in sales generated by LearnStar, Inc. As a result of the sale of an 82.5% interest in LearnStar in June 1998, no such revenue was recorded for the year ended December 31, 1999. Additionally, due to the curtailment of operations related to IWN, Inc. in 1998, other revenue decreased by approximately $191,000 for IWN, Inc. for the year ended December 31, 1999 as compared to the year ended December 31,1998.

Direct operating costs of services increased 18% to $11,169,000 for the year ended December 31, 1999 from $9,491,000 for the year ended December 31, 1998. This increase was due to aggregate expenses of approximately $600,000 associated with an increase in the number of sites installed, increased freight expenses associated with shipping equipment to the sites and an increase in the number of sales commissions paid in connection with the rollout of the digital network in 1999. Satellite transmissions costs and Internet service provider charges increased $884,000 due to additional services needed to support the digital network for the year ended December 31, 1999. Depreciation and amortization increased $411,000 due to an acceleration of depreciation of the DOS-based network equipment and capitalized purchases of broadcast equipment associated with the digital network, which are offset by a decrease in amortization of capitalized software. These increases were partially offset by the settlement of an accrued liability for license fees that was less than had been estimated. As a result, we reduced the accrued expenses and direct operating costs of service by approximately $180,000 related to the settlement in 1999. The results for the year ended December 31, 1998 included approximately $360,000 in costs related to the realignment of the satellite dishes at hospitality locations in order to receive broadcast transmissions from the Galaxy III-R satellite when the PanAmSat Galaxy IV satellite failed to operate in May 1998.

Selling, general and administrative expenses decreased 4% to $13,610,000 for the year ended December 31, 1999 from $14,142,000 for the year ended December 31, 1998. Approximately $276,000 in selling, general and administrative expenses were incurred by LearnStar for the year ended December 31, 1998. As a result of the sale of an 82.5% interest in LearnStar in June 1998, no such expenses were recorded for the year ended December 31, 1999. Selling, general and administrative expenses incurred by IWN also decreased by approximately $235,000 in 1999 as a result of the sale of assets of IWN, L.P. in August 1999. Equipment leases decreased approximately $684,000 due to the conclusion of the leases in 1999. Stock-based compensation decreased approximately $61,000 due to the issuance of warrants and options to employees and non-employees which can vary from period to period. Additionally, office lease expense decreased approximately $135,000 due to the sublet of office space beginning in September 1998. Selling, general and administrative expense for the year ended December 31, 1999 included consulting expenses of approximately $415,000 relating to Year 2000 remediation efforts. Additionally, marketing expenses increased approximately $343,000, related to the new digital network which was introduced during the year ended December 31, 1999.

Litigation, legal and professional fees decreased to $558,000 for the year ended December 31, 1999 from $1,658,000 for the year ended December 31, 1998 partially due to the settlement of litigation for which we had accrued a liability of $500,000. The litigation was settled for approximately $340,000. As a result, we reduced the accrued expenses and litigation, legal and professional fee expenses by approximately

$160,000 related to the settlement. Expenses for 1998 include legal expenses incurred in the ordinary course of business, as well as certain litigation expenses which did not recur in 1999.

Depreciation and amortization decreased 16% to $1,370,000 for the year ended December 31, 1999 compared to $1,636,000 for the year ended December 31, 1998 due to assets becoming fully depreciated.

Research and development expenses decreased 18% to $842,000 for the year ended December 31, 1999 compared to $714,000 for the year ended December 31, 1998. The current period expenses result from our research and development efforts related to the second generation of the digital network, Internet stations, and future Internet Web sites. For the year ended December 31, 1998, our research and development efforts focused primarily on the upgrade of the NTN Network to the digital network.

Interest expense increased 263% to $1,050,000 for the year ended December 31, 1999 from $289,000 for the year ended December 31, 1998. The increase was primarily due to interest expense recorded in 1999 related to the 7% senior subordinated convertible notes issued in 1999. We also incurred increased interest expense related to a new revolving line of credit, other notes payable and additional capital leases for equipment acquisitions that did not exist in 1998.

SEGMENT ANALYSIS

Our operations are to develop and distribute interactive entertainment. The segment data presented below includes allocations of corporate expenses.

Revenues generated by the two significant segments are as follows:

Segment	2000		1999		1998	
NTN Network	**$21,406,000**	**98%**	$22,250,000	96%	$20,973,000	91%
BUZZTIME	**540,000**	**2%**	983,000	4%	2,014,000	9%
Total	**$21,946,000**	**100%**	$23,233,000	100%	$22,987,000	100%

NTN Network revenues decreased 4% in 2000 over 1999 primarily due to the implementation of SAB 101, which resulted in a reduction of revenue of $845,000. Excluding the impact of SAB 101, NTN Network revenues would have increased by less than 1%.

NTN Network revenues increased 6% in 1999 over 1998 due primarily to an increase in fees charged for the setup, installation and training for the digital network as compared to the original DOS network.

BUZZTIME revenues decreased 45% in 2000 over 1999 due to a reduction in the fees earned from America Online of $600,000 due to the contract that expired on December 1, 1999, at which time a new contract was signed, under which we did not generate revenue from America Online.

BUZZTIME revenues decreased 51% in 1999 over 1998 due to the expiration of the trial performed for Bell Canada in 1998, which generated $670,000 in 1998, that did not occur in 1999 and a reduction in the fees earned from America Online of $283,000 as a result of entering into a new contract with America Online in the second quarter of 1998, which provided for a flat monthly fee rather than fees based on usage.

Operating income (loss) by segment are illustrated below:

Segment	2000	1999	1998
NTN Network	**$(2,162,000)**	$(1,446,000)	$(473,000)
BUZZTIME	**(6,039,000)**	(2,305,000)	(2,063,000)
Total	**$(8,201,000)**	$(3,751,000)	$(2,536,000)

NTN Network operating income was $0.7 million lower in 2000 over 1999, due to the implementation of SAB 101, which resulted in a decrease to operating income of $1.1 million, offset by a decrease in operating expenses as less sites were installed in 2000 compared to 1999.

BUZZTIME operating loss was $3.7 million higher in 2000 over 1999. Selling, general and administrative expenses increased due to a strengthened focus on BUZZTIME initiatives as a result of increased technology personnel costs related to the Internet Web site, BUZZTIME.com, and other Web and ITV initiatives.

The NTN Network operating income was $1.0 million lower in 1999 over 1998. The decrease in income was a result of additional costs incurred in 1999 to begin converting its hospitality sites from the DOS-based network to the digital network.

BUZZTIME operating loss was $0.2 million higher in 1999 over 1998. Selling, general and administrative expenses increased due to a strengthened focus on BUZZTIME initiatives as a result of increased technology personnel costs related to positioning BUZZTIME for the year 2000.

We will need to raise additional equity or debt financing to execute our business plans for the NTN Network and BUZZTIME, which will call for significant growth. The NTN Network currently generates cash flow sufficient to sustain its operations and to continue funding the operation of

BUZZTIME for the next twelve months if we curtail the development and marketing of BUZZTIME as planned. Based on our projected cash requirements, we will need $3 million in additional financing in order to fund any BUZZTIME growth initiatives. Similarly, we will also need an additional $2 million in financing to grow the NTN Network during the next twelve months to 4,000 sites in the U.S. and Canada. We may not be able to obtain additional financing on terms favorable to us.

LIQUIDITY AND CAPITAL RESOURCES

At December 31, 2000, we had cash and cash equivalents of $2,188,000 and working capital (current assets in excess of current liabilities) of $893,000 compared to cash and cash equivalents of $1,044,000 and working capital of $921,000 at December 31, 1999. Net cash provided by operations was $404,000 and $805,000 for the years ended December 31, 2000 and 1999, respectively. The principal uses of cash in 2000 were to fund our net loss from operations and to fund severance payments totaling $598,000 in compliance with reorganization agreements with former officers. These uses were more than offset by depreciation, amortization and other noncash charges. Net cash used in investing activities was $7,570,000 for the year ended December 31, 2000 and $5,846,000 for the year ended December 31, 1999. Included in net cash used in investing activities for the year ended December 31, 2000 were approximately $8,745,000 in capital expenditures, software and Web site development, which were partially offset by proceeds from the sale of investments available for sale of $538,000 and collection of notes receivable of $138,000. Net cash provided by financing activities was $8,312,000 for the year ended December 31, 2000 and $1,525,000 for the year ended December 31, 1999. Net cash provided by financing activities for the year ended December 31, 2000 included $7,028,000 of proceeds from the issuance of stock, net of offering expenses; $890,000 of proceeds from the exercise of stock options and warrants and borrowings under a new revolving line of credit of approximately $26,624,000, offset by principal payments on the revolving line of credit and note payable of approximately $25,300,000; and $932,000 of principal payments on capital leases.

As of December 31, 2000, we had outstanding 7% senior subordinated convertible notes (convertible notes) of $3,987,000, payable February 1, 2001 and bearing interest at 7% per annum. If we default under the convertible notes, in the discretion of the holders of the convertible notes, the entire outstanding principal amount of the convertible notes and all accrued and unpaid interest will become immediately due and payable in full. In January 2001, we reached agreement with the holders of the convertible notes to extend the maturity date of the aggregate $4 million in promissory notes from February 1, 2001 to February 1, 2003. The promissory notes remain convertible at $1.275 per share, but the terms were modified to reduce the interest rate from 7% to 4% and to permit us to convert up to the full principal amount of the promissory notes into our common stock at maturity at a conversion price of $1.275 per share. In addition, if our common stock closes above $2.50 for more than 20 consecutive trading days, we can force conversion of the promissory notes at $1.275 per share.

In August 1999, we entered into an agreement with Coast Business Credit for a revolving line of credit not to exceed $4,000,000. Interest is charged on the outstanding balance at a rate equal to the prime rate plus 1.5% per annum, but cannot be less than 9% per annum. The line of credit is secured by substantially all of our assets. Total loan fees of $120,000 are payable in three annual installments and are being amortized over the life of the loan, which matures on August 31, 2002. As of December 31, 2000, the maximum of $4.0 million was available to us and approximately $3,919,000 was outstanding under the line. A reduction in our monthly collections or operating income would result in a reduction in availability under our revolving line of credit and further constrain our liquidity. We are currently in negotiations with Coast Business Credit regarding our line of credit.

We raised gross proceeds of $6,000,000 in April 2000 through the underwritten sale of 2,000,000 shares of common stock pursuant to our existing shelf registration. The net proceeds from the sale, which totaled approximately $5,163,000, are being used primarily for working capital and general corporate purposes relating to the launch of our game portal, BUZZTIME, and ongoing conversion of the NTN Network's hospitality locations to our new digital technology. We have approximately $14,000,000 remaining under our existing shelf registration for possible future sale to meet our liquidity needs.

On November 14, 2000, we closed a private equity placement of $2,000,000 with two accredited investors. We sold a total of 1,218,584 shares of common stock to the purchasers. The shares were sold at a purchase price of $1.64125 per share. We also issued warrants to the purchasers to purchase 609,292 shares. Each warrant is exercisable for one share of our common stock at an initial exercise price of $1.64125 per share of common stock. In addition, we agreed to issue to the purchasers, for no additional consideration, additional warrants to purchase 609,292 shares of our common stock at an initial price of $1.64125 per share of common stock in the event we raise less than $5 million in gross proceeds from the sale of our common stock to entities other than the purchasers by May 14, 2001. The exercise price of all warrants will be reset every six months beginning May 14, 2001 to the average closing bid price for the 20 days prior to each sixth-month anniversary if a lower exercise price would result. The warrants have a three-year life starting from the date of issuance.

Pursuant to the terms of the private placement, each purchaser will be issued additional shares of common stock in the event we issue, at any time or from time to time during the six months immediately following November 14, 2000, any common stock or convertible securities without consideration or for a consideration per share less than the original purchase price per share paid by the purchasers. In addition, we also granted the purchasers a limited right of first refusal on subsequent offerings exercisable at the option of each purchaser during the twelve-month period ending November 14, 2001.

In January 2001, we reached an agreement with the purchasers in the November 2000 private placement to revise the terms of the private placement in exchange for the issuance of 350,043 additional shares of our common stock. The revisions eliminated the exercise price reset provisions contained in the warrants as well as the purchasers' rights to receive additional shares of our common stock upon the occurrence of certain events. Furthermore, the purchasers agreed to surrender and cancel their rights to additional contingent warrants to purchase 609,291 shares of our common stock. In connection with this agreement, the employment agreement with Stanley B. Kinsey, our chief executive officer, was extended for one year.

The net proceeds from the offering, which totaled approximately $1,865,000, will be used primarily for working capital and general corporate purposes relating to our further expansion of our digital network and infrastructure and continued BUZZTIME development.

Notwithstanding our raising of $2.0 million in gross proceeds in a privately placed equity offering in November 2000, our liquidity and capital resources remain limited, and this may constrain our ability to operate and grow our business. We will need to raise additional equity or debt financing to execute our business plans for the NTN Network and BUZZTIME, which will call for significant growth. The NTN Network currently generates cash flow sufficient to sustain its operations and to continue funding the operation of BUZZTIME for the next twelve months if we curtail the development and marketing of BUZZTIME as planned. Based on our projected cash requirements, we will need $3 million in additional financing in order to fund any BUZZTIME growth initiatives. Similarly, we will also need an additional $2 million in financing to grow the NTN Network during the next twelve months to 4,000 sites in the U.S. and Canada. We may not be able to obtain additional financing on terms favorable to us.

RECENT ACCOUNTING PRONOUNCEMENTS

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133"), which was amended by Statement of Financial Accounting Standards No. 137 and Statement of Financial Accounting Standards No. 138. SFAS 133 requires companies to recognize all derivatives as either assets or liabilities, with the instruments measured at fair value, and is effective January 1, 2001. The accounting for changes in fair value gains and losses depends on the intended use of the derivative and its resulting designation. The adoption did not have a material impact on our financial condition or our results of operations at January 1, 2001.

RISK FACTORS THAT MAY AFFECT FUTURE RESULTS

Our business, results of operation and financial condition would be adversely affected by a number of factors, including the following:

We have experienced significant losses, and we expect to incur significant net losses in the future.

We have a history of significant losses, including net losses of $9.6 million in 2000, $2.5 million in 1999 and $2.6 million in 1998 and an accumulated deficit of $73.2 million as of December 31, 2000. This compares to a net loss of $4.8 million, excluding the gain on the sale of a subsidiary, for the year ended December 31, 1999. We expect to incur significant operating and net losses for the next four quarters due primarily to our continued development of the BUZZTIME subsidiary.

Our limited liquidity and capital resources may constrain our ability to operate and grow our business.

At December 31, 2000, our current assets exceeded our current liabilities by approximately $893,000. We currently have a revolving line of credit agreement which provides for borrowings of up to $4.0 million. Our availability under the revolving line of credit may be reduced if our monthly collections or operating income falls below certain levels. As of December 31, 2000, the maximum of $4.0 million was available to us and approximately $3,919,000 was outstanding under the line. The line of credit is secured by substantially all of our assets. Notwithstanding our raising of $2.0 million in gross proceeds in a privately placed equity offering in November 2000, our liquidity and capital resources remain limited, and this may constrain our ability to operate and grow our business. Any reduction in availability under our revolving line of credit may further constrain our liquidity.

We will require additional financing to implement our plan to significantly expand the digital network and to develop BUZZTIME into a leading content provider for interactive television platforms.

Although we raised $2.0 million in a privately placed equity offering in November 2000, we will need to raise additional equity or debt financing to execute our business plans for the NTN Network and BUZZTIME, which call for significant growth. The NTN Network currently generates cash flow sufficient to sustain its operations and to continue funding the operation of BUZZTIME for the next twelve months if we curtail the development and marketing of BUZZTIME as planned. Based on our projected cash requirements, we will need $3.0 million in additional financing in order to fund any BUZZTIME growth initiatives. Similarly, we will also need an additional $2.0 million in financing to grow the NTN Network during the next twelve months to 4,000 sites in the U.S. and Canada. We may not be able to obtain additional financing on terms favorable to us.

As part of our financing plan, we will try to obtain a direct investment in BUZZTIME. We will begin growth initiatives only if we succeed in raising capital at an appropriate cost. If additional financing is not obtained, our growth plans will be deferred. If additional financing for BUZZTIME is not obtained and we do not reduce cash expenditures at BUZZTIME sufficiently, we may not be able to sustain the operations of BUZZTIME. If our cash flows are less than anticipated or if we incur unanticipated expenses, we may not be able to continue improvement, development and expansion of our new digital network or pursue our BUZZTIME initiatives. If we receive additional equity financing, it could be dilutive to our stockholders.

We do not comply with the American Stock Exchange guidelines and may be delisted or suspended from trading.

AMEX has published a set of continued listing guidelines that it follows to determine whether an AMEX-listed company should be allowed to continue the trading or listing of its securities on the exchange. Under these guidelines, AMEX will consider suspending or "delisting" a company's securities from the exchange if it has sustained operating or net losses in its five most recent fiscal years and if shareholders' equity falls below $4.0 million. We incurred a net loss of $9,589,000 for the year ended December 31, 2000, representing our sixth consecutive year of losses. As such, we are technically not in compliance with the continued listing guidelines of AMEX. Our equity is $4.1 million at December 31, 2000, but is expected to fall below $4.0 million by the first quarter ending March 31, 2001.

In January 2000 and in May 2000 we received correspondence from AMEX indicating that, despite the fact that NTN does not currently meet the guidelines, AMEX will continue the listing of our common stock pending periodic reviews by AMEX of our quarterly and annual SEC filings and certain other financial information. Our most recent meeting with AMEX officials was in March 2001. To date, AMEX has not taken any action regarding delisting. Still, our common stock may not remain listed on AMEX or any other exchange or quotation system in the future. If our common stock is delisted from AMEX, spreads can often be higher for securities traded on the over-the-counter market, and the execution time for orders may be longer. Thus, removing our stock from AMEX may result in decreased liquidity by making the trading of our stock less efficient.

We are currently involved in litigation matters that could materially impact our profitability.

In February 1998, the plaintiffs filed an action entitled *Dorman vs. NTN Communications, Inc.* in the Superior Court of San Diego County for the State of California against us. The complaint alleged that the directors and former officers devised an "exit strategy" to provide themselves with undue compensation upon their resignation from NTN. The plaintiffs further alleged that defendants made false statements about, and failed to disclose, contingent liabilities (guaranteed compensation to management and the right of an investor in IWN to require NTN to repurchase its investment during 1997) and phantom assets (loans to management) in our financial statements and KPMG LLP's audit reports, all of which served allegedly to inflate the trading price of our common stock. In March 1999, the court granted our motion for summary judgment. On May 13, 1999, the plaintiffs filed a motion for new trial which was denied by the court. On August 20, 1999, plaintiffs filed an appeal of the summary judgment in the Fourth Appellate District of the Court of Appeals for the State of California, which was granted. The court ordered the parties to mediation before a court mediator to be completed in May 2001.

We are involved in two pending lawsuits in Canada, both involving Interactive Network, Inc. Both NTN and Interactive Network have asserted claims involving patent infringement and validity and certain other proprietary rights. The litigation is currently at the discovery stage. In December 2000, the Canadian court ordered the parties to complete discovery in the matter by April 2001, later extended to June 30, 2001. These actions affect only the operations of our Canadian licensee and do not extend to our operations in the United States or elsewhere.

Any or all of the foregoing claims may not be decided in our favor and we are not insured against all claims made. During the pendency of these claims, we will continue to incur the costs of our legal defense.

New products and rapid technological change may render our operation obsolete or noncompetitive.

If we do not compete successfully in the development of new products and keep pace with rapid technological change, we will be unable to achieve profitability or sustain a meaningful market position. The interactive entertainment and game industry is becoming highly competitive and subject to rapid technological changes. We are aware of other companies that are introducing interactive game products on interactive platforms that allow players to compete across the nation. Some of these companies may have substantially greater financial resources and organizational capital than we do, which could allow them to identify emerging trends. In addition, changes in customer tastes may render our network, its content and our technology obsolete or noncompetitive.

The life cycle of our technology may be short, and we may not adequately market our product or identify consumer needs in sufficient time to maximize our revenues.

The emergence of new entertainment products and technologies, changes in consumer preferences and other factors may limit the life cycle of our technologies and any future products and services we develop. Accordingly, our future performance will depend on our ability to:

- identify emerging technological trends in our market;
- identify changing consumer needs, desires or tastes;
- develop and maintain competitive technology, including new product and service offerings;
- improve the performance, features and reliability of our products and services, particularly in response to technological changes and competitive offerings; and
- bring technology to the market quickly at cost-effective prices.

We may not be successful in developing and marketing new products and services that respond to technological and competitive developments and changing customer needs. Such products and services may not gain market acceptance. Any significant delay or failure in developing new or enhanced technology, including new product and service offerings, could result in a loss of actual or potential market share and a decrease in revenues.

We may sell equity interests in BUZZTIME to third parties, which could result in the loss of control of BUZZTIME or devaluation of our equity interest in BUZZTIME.

We believe there may be divergent investment preferences between the strategies pursued by the NTN Network and BUZZTIME and may decide in the future to raise additional financing by issuing and selling equity interests in BUZZTIME to third parties. To enhance the ability of BUZZTIME to raise such financing, we have previously contributed and may contribute in the future certain of our assets to BUZZTIME in order to allow the development of a distinct identity that we believe is necessary for it to effectively grow as a separate concern. These assets include our extensive trivia game show library and our interactive play-along sports games and related intangible assets. However, we are uncertain whether the contribution of assets to BUZZTIME will facilitate such a financing in the future.

From an operational standpoint, we could lose control in BUZZTIME. If we lose control, BUZZTIME may no longer provide adequate support and resources for content and programming for the NTN Network, affecting the ability of the NTN Network to continue its operations. From a financial viewpoint, we could undervalue the stock of BUZZTIME when selling it to third parties or undervalue certain assets transferred to BUZZTIME; this could devalue your holdings in NTN, because we would not receive the fair value for our interest in BUZZTIME.

If our intellectual property practices do not adequately protect our proprietary rights and intellectual property, our business could be seriously damaged.

We rely on a combination of trademarks, copyrights and trade secret laws to protect our proprietary rights in certain of our products. Furthermore, it is our policy that all employees and consultants involved in research and development activities sign nondisclosure agreements. Our competitors may, however, misappropriate our technology or independently develop technologies that are as good as or better than ours. Our competitors may also challenge or circumvent our proprietary rights. If we have to initiate or defend against an infringement claim in the future to protect our proprietary rights, the litigation over such claims could be time-consuming and costly to us, adversely affecting our financial condition.

If we fail to manage our growth effectively, we may lose business and experience reduced profitability.

Continued implementation of our business plan requires an effective planning and management process. Our anticipated future growth will continue to place a significant strain on our management systems and resources. If we are to grow successfully, we must:

- improve our operational, administrative and financial systems;
- expand, train and manage our workforce; and
- attract and retain qualified management and technical personnel.

We plan to continue adding personnel to our technical department. However, competition for qualified personnel is intense, particularly for employees with technical expertise. The success of our business depends on hiring and retaining suitable personnel. If we do not attract and retain qualified employees, we may have difficulty servicing our customers and operating our business.

If our Chief Executive Officer leaves us, our business may be adversely affected.

Our success greatly depends on the efforts of our Chief Executive Officer. Our ability to operate successfully will depend significantly on the services and contributions of the Chief Executive Officer. Our business and operations may be adversely affected if our Chief Executive Officer were to leave.

RISKS ASSOCIATED WITH INTERACTIVE TELEVISION

Our prospects for growth depend on our implementation and use of our new digital network.

Our digital network, introduced in April 1999, has been installed in approximately 2,641 subscriber locations as of January 2001. An additional 319 locations continue to subscribe to the original DOS-based NTN network. We currently plan to continue operating our original NTN network and the digital network in the United States concurrently. Our immediate prospects for growth depend, in part, on the successful operation of the new digital network, our ability to add new product offerings and our sales effort. If we do not fully utilize the new digital system or if the market does not accept it, we will have committed much of our resources to an unsuccessful technology.

The interactive gaming and entertainment industry is becoming highly competitive.

The entertainment business is highly competitive. We compete with other companies for total entertainment related revenues in the marketplace. Our network programming competes generally with broadcast television, direct satellite programming, pay-per-view, other content offered on cable television, and other forms of entertainment. Furthermore, certain of our competitors have greater financial and other resources available to them. With the entrance of motion picture, cable and television companies, competition in the interactive entertainment and multimedia industries will likely intensify in the future. In January 1999, The Walt Disney Company introduced interactive programming broadcast in conjunction with live sporting and other events which competes directly with our programming.

We also compete with other content and services available to consumers through other online service providers. Moreover, the expanded use of online networks and the Internet provide computer users with an increasing number of alternatives to video games and entertainment software. With this increasing competition and rapidly changing factors, we must be able to compete on technology, content and management strategy. If we fail to provide these quality services and products, we will lose revenues to other competitors in the entertainment industry.

We depend on a single supplier of Playmakers®.

We currently purchase our 900 megahertz Playmakers from Climax Technology Co. Ltd., an unaffiliated Taiwanese manufacturer. We are currently soliciting bids for the manufacture of our Playmakers. Unless and until we succeed in establishing additional manufacturing relationships, we will continue to depend on our current sole source supplier of Playmakers. If we lose our supplier, our growth will slow until an alternative supplier is identified.

Communication failures with our subscriber locations could result in the cancellation of subscribers and a decrease in our revenues.

We rely on both satellite and telephone systems to communicate with our subscriber locations. Interruption in communications with our subscriber locations under either system could decrease customer loyalty and satisfaction and result in a cancellation of our services. We have had past disputes with our primary telephone service provider, Global Crossing Telecommunications, Inc. We are presently reviewing alternative telephone service providers and establishing contingency plans; however, such alternative providers and contingency plans have not been finalized.

Our games and game shows are subject to gaming regulations.

We operate online games of skill and chance that, in some instances, reward prizes. These games are regulated in many jurisdictions. The selection of prizewinners is sometimes based on chance, although none of our games require any form of monetary payment. The laws and regulations that govern these games, however, are subject to differing interpretations in each jurisdiction and are subject to legislative and regulatory change in any of the jurisdictions in which we offer our games. If such changes were to happen, we may find it necessary to eliminate, modify or cancel certain components of our products that could result in additional development costs and/or the possible loss of revenue.

If our new digital network and BUZZTIME programming are not accepted by consumers, we are not likely to generate significant revenues or become profitable.

The new digital network and BUZZTIME programming face risks as interactive television products and whether the market accepts interactive television. If interactive television does not become a successful, scalable medium or if the market does not accept trivia and play-along sports games, then we will be unable to draw revenues from advertising, direct-marketing of third-party products, subscription fees and pay-per-play fees. We will also be unable to attract local cable operators to add BUZZTIME programming as a channel to their service.

RISKS ASSOCIATED WITH THE INTERNET

One of our principal business objectives is to increase our direct contact with consumers through our Web sites, BUZZTIME.com and NTN.com. We face the risks described below in operating the Web sites on the Internet.

We face significant Internet competition, and we may not be able to compete against other competitors.

The Internet market is new, rapidly evolving and intensely competitive. We expect this competition to intensify in the future due in part to the minimal barriers to entry and the relatively low cost to launch a new Web site. We will compete with a variety of other entertainment and multimedia companies on the Internet. Some of these competitors can devote substantial resources to Internet commerce in the near future. Our Web sites will also compete with traditional providers of entertainment and multimedia content and services.

Many of our current and potential competitors have large customer bases, greater brand recognition and significantly greater financial, marketing and other resources than we have. In addition, some competitors may be able to obtain services from vendors on more favorable terms, devote greater resources to marketing and promotional campaigns, adopt more aggressive pricing policies, and devote more resources to Web site and systems development than we can.

We may be liable for the content we make available on the Internet.

We make content available on our Web sites and on the Web sites of our advertisers and distribution partners. The availability of this content could result in claims against us based on a variety of theories, including defamation, obscenity, negligence or copyright or trademark infringement. We could also be exposed to liability for third-party content accessed through the links from our Web sites to other Web sites. We may incur costs to defend ourselves against even baseless claims, and our financial condition could be materially adversely affected if we are found liable for information that we make available. Implementing measures to reduce our exposure may require us to spend substantial resources and may limit the attractiveness of our services to users.

RISKS ASSOCIATED WITH OUR COMMON STOCK

Our stock price has been highly volatile, and your investment could suffer a decrease in value.

The trading price of our common stock has been and may continue to be subject to wide fluctuations. The stock price may fluctuate in response to a number of events and factors, such as quarterly variations in operating results, announcements of technological innovations or new products and media properties by us or our competitors, changes in financial estimates and recommendations by securities analysts, the operating and stock price performance of other companies that investors may deem comparable, and news reports relating to trends in our markets. In addition, the stock market in general, and the market prices for Internet-related companies in particular, have experienced extreme volatility that often has been unrelated to the operating performance of such companies. These broad market and industry fluctuations may adversely affect the price of our stock, regardless of our operating performance.

Our charter contains provisions that may hinder or prevent a change in control of our company, which could result in your inability to approve a change in control and potentially receive a premium over the current market value of your stock.

Certain provisions of our certificate of incorporation could make it more difficult for a third party to acquire control of us, even if such a change in control would benefit our stockholders. For example, our certificate of incorporation requires a supermajority vote of at least 80% of the total voting power, voting together as a single class, to amend certain provisions of such document, including those provisions relating to:

- the number, election and term of directors;
- the removal of directors and the filling of vacancies; and
- the supermajority voting requirements of our Certificate of Incorporation.

These provisions could discourage third parties from taking over control of our company. Such provisions may also impede a transaction in which you could receive a premium over then-current market prices and your ability to approve a transaction that you consider in your best interests.

We do not expect to pay dividends during the foreseeable future.

We have never declared or paid any cash dividends on our common stock and anticipate that for the foreseeable future any earnings will be retained for use in our business. Our outstanding revolving line of credit prohibits us from paying cash dividends without obtaining prior approval from the lender.

If the shares of our common stock eligible for future sale are sold, the market price of our common stock may be adversely affected.

Future sales of substantial amounts of our common stock in the public market or the anticipation of such sales could have a material adverse effect on then-prevailing market prices. As of March 14, 2001, there were approximately 8,096,000 shares of common stock reserved for issuance upon the exercise of outstanding stock options at exercise prices ranging from $0.50 to $6.375 per share. As of March 14, 2001, there were also outstanding warrants to purchase an aggregate of approximately 1,750,000 shares of common stock at exercise prices ranging from $0.6875 to $3.75 per share. As of March 14, 2001, there were approximately 3,137,255 shares of common stock reserved for issuance upon the conversion of the senior convertible subordinated notes at a conversion price of $1.275. Additionally, we have approximately $14 million of common stock remaining under our existing shelf registration for possible future sale.

The foregoing options and warrants could adversely affect our ability to obtain future financing or engage in certain mergers or other transactions, since the holders of these options and warrants can be expected to exercise them at a time when we would be able to obtain additional capital through a new offering of securities on terms more favorable than those provided by such options and warrants. For the life of such options and warrants, the holders are given the opportunity to profit from a rise in the market price of our common stock without assuming the risk of ownership. To the extent the trading price of our common stock at the time of exercise of any such options or warrants exceeds the exercise price, such exercise will have a dilutive effect on our stockholders.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to risks related to currency exchange rates, stock market fluctuations, and interest rates. As of December 31, 2000, we owned common stock of an Australian company that is subject to market risk. At December 31, 2000, the carrying value of this investment was $272,000, which is net of a $545,000 unrealized loss. This investment is exposed to further market risk in the future based on the operating results of the Australian company and stock market fluctuations. Additionally, the value of the investment is further subject to changes in Australian currency exchange rates. At December 31, 2000, a hypothetical 10% decline in the value of the Australian dollar would result in a reduction of $27,000 in the carrying value of the investment.

We have outstanding convertible notes which bear interest at 7% per annum and line of credit borrowings which bear a rate equal to the prime rate plus 1.5% per annum, which cannot be less than 9% per annum. At December 31, 2000, a hypothetical one-percentage point increase in the prime rate would result in an increase of $39,000 in annual interest expense.

Independent Auditors' Report

The Board of Directors
NTN Communications, Inc.:

We have audited the accompanying consolidated balance sheets of NTN Communications, Inc. and subsidiaries as of December 31, 2000 and 1999, and the related statements of operations, shareholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2000. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of NTN Communications, Inc. and subsidiaries as of December 31, 2000 and 1999, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2000, in conformity with accounting principles generally accepted in the United States of America.

KPMG LLP

San Diego, California
February 23, 2001

Consolidated Balance Sheets

December 31,	2000	1999
ASSETS		
Current assets:		
Cash and cash equivalents	**$2,188,000**	$1,044,000
Restricted cash	**202,000**	239,000
Accounts receivable — trade, net of allowance for doubtful accounts of $811,000 in 2000 and $2,148,000 in 1999	**1,724,000**	2,541,000
Investments available-for-sale	**272,000**	937,000
Deposits on broadcast equipment	**112,000**	611,000
Deferred costs	**772,000**	—
Prepaid expenses and other current assets	**538,000**	1,015,000
Total current assets	**5,808,000**	6,387,000
Broadcast equipment and fixed assets, net	**11,963,000**	10,470,000
Software development costs, net of accumulated amortization of $6,527,000 in 2000 and $6,356,000 in 1999	**405,000**	138,000
Deferred costs	**565,000**	—
Other assets	**81,000**	292,000
Total assets	**$18,822,000**	$17,287,000
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	**$816,000**	$1,421,000
Accrued expenses	**1,351,000**	1,116,000
Accrual for litigation costs	**57,000**	334,000
Accrual for management severance	**—**	598,000
Accrual for sales tax	**399,000**	382,000
Obligations under capital leases	**579,000**	740,000
Deferred revenue	**1,575,000**	796,000
Note payable	**138,000**	79,000
Total current liabilities	**4,915,000**	5,466,000
Obligations under capital leases, excluding current portion	**83,000**	475,000
Accrual for settlement warrants	**—**	1,793,000
Revolving line of credit	**3,919,000**	2,486,000
7% senior subordinated convertible notes	**3,987,000**	4,705,000
Deferred revenue	**1,804,000**	—
Other long-term liabilities and note payable, excluding current portion	**32,000**	141,000
Total liabilities	**14,740,000**	15,066,000
Shareholders' equity:		
Series A 10% Cumulative Convertible Preferred Stock, $.005 par value, 5,000,000 shares authorized; 161,000 shares issued and outstanding at December 31, 2000 and December 31, 1999	**1,000**	1,000
Common stock, $.005 par value, 50,000,000 shares authorized; 36,046,000 and 29,914,000 shares issued and outstanding at December 31, 2000 and December 31, 1999, respectively	**179,000**	149,000
Additional paid-in capital	**78,153,000**	66,548,000
Accumulated deficit	**(73,234,000)**	(63,645,000)
Accumulated other comprehensive loss	**(545,000)**	(360,000)
Treasury stock, at cost; 111,000 shares at December 31, 2000 and December 31, 1999	**(472,000)**	(472,000)
Total shareholders' equity	**4,082,000**	2,221,000
Total liabilities and shareholders' equity	**$18,822,000**	$17,287,000

See accompanying notes to consolidated financial statements.

Consolidated Statements of Operations

For the years ended December 31,	**2000**	**1999**	**1998**
Revenues:			
NTN Network revenues	**$21,406,000**	$22,250,000	$20,973,000
BUZZTIME service revenues	**540,000**	383,000	1,131,000
America Online fees	**—**	600,000	883,000
Equipment sales, net of cost of sales of $0, $208,000 and $231,000 in 2000, 1999 and 1998, respectively	**—**	84,000	499,000
Other revenues	**102,000**	431,000	708,000
Total revenues	**22,048,000**	23,748,000	24,194,000
Operating expenses:			
Direct operating costs of services	**11,098,000**	11,169,000	9,491,000
Selling, general and administrative	**15,070,000**	13,610,000	14,142,000
Litigation, legal and professional fees	**474,000**	558,000	1,658,000
Depreciation and amortization	**1,815,000**	1,370,000	1,636,000
Impairment charges	**1,362,000**	—	—
Research and development	**430,000**	842,000	714,000
Total operating expenses	**30,249,000**	27,549,000	27,641,000
Operating loss	**(8,201,000)**	(3,801,000)	(3,447,000)
Other income (expense):			
Interest income	**72,000**	116,000	288,000
Interest expense	**(1,131,000)**	(1,050,000)	(289,000)
Gain on sale of interest in subsidiary	**—**	—	1,643,000
Gain on sale of assets of subsidiary	**—**	2,254,000	—
Other	**119,000**	(17,000)	12,000
Total other income (expense)	**(940,000)**	1,303,000	1,654,000
Loss before income taxes and cumulative effect of accounting change	**(9,141,000)**	(2,498,000)	(1,793,000)
Provision for income taxes	**—**	—	—
Cumulative effect of accounting change	**(448,000)**	—	—
Net loss	**(9,589,000)**	(2,498,000)	(1,793,000)
Accretion of beneficial conversion feature on preferred stock	**—**	—	(758,000)
Net loss available to common shareholders	**$(9,589,000)**	$(2,498,000)	$(2,551,000)
Loss per common share — basic and diluted loss before cumulative effect of accounting change	**$(0.28)**	$(0.09)	$(0.10)
Cumulative effect of accounting change	**$(0.01)**	$—	$—
Net loss	**$(0.29)**	$(0.09)	$(0.10)
Weighted average shares outstanding — basic and diluted	**33,206,000**	28,470,000	26,078,000

See accompanying notes to consolidated financial statements.

Consolidated Statements of Shareholders' Equity

For the years ended December 31, 2000, 1999 and 1998

	Series A and B Cumulative Convertible Preferred Stock		Common Stock		Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Compre-hensive Loss	Treasury Stock	Total
	Shares	Amount	Shares	Amount					
Balance, December 31, 1997	231,000	$2,000	23,677,000	$118,000	$70,541,000	$(58,596,000)	—	$(3,339,000)	$8,726,000
Issuance of stock in lieu of dividends	—	—	19,000	—	—	—	—	—	—
Issuance of treasury stock for settlement of litigation	—	—	—	—	(622,000)	—	—	755,000	133,000
Issuance of common stock for settlement of litigation	—	—	1,200,000	6,000	1,194,000	—	—	—	1,200,000
Conversion of Series B preferred stock to common stock	(14,000)	—	2,430,000	12,000	(12,000)	—	—	—	—
Issuance of common stock in exchange for cancellation of options and warrants	—	—	759,000	4,000	(4,000)	—	—	—	—
Issuance of treasury stock in exchange for cancellation of options and warrants	—	—	—	—	(1,181,000)	—	—	1,181,000	—
Accretion of beneficial conversion feature on Series B preferred stock	—	—	—	—	758,000	—	—	—	758,000
Issuance of stock for exercise of warrants and options	—	—	1,000	—	1,000	—	—	—	1,000
Options granted to non-employees	—	—	—	—	58,000	—	—	—	58,000
Net loss	—	—	—	—	—	(2,551,000)	—	—	(2,551,000)
Balance, December 31, 1998	217,000	$2,000	28,086,000	$140,000	$70,733,000	$(61,147,000)	—	$(1,403,000)	$8,325,000
Conversion of Series B preferred stock to convertible note payable	(56,000)	(1,000)	—	—	(5,448,000)	—	—	—	(5,449,000)
Convertible note payable converted to common stock	—	—	793,000	4,000	1,008,000	—	—	—	1,012,000
Issuance of stock for exercise of warrants and options	—	—	334,000	2,000	345,000	—	—	—	347,000
Issuance of treasury stock pursuant to anti-dilution provision	—	—	—	—	(931,000)	—	—	931,000	—
Issuance of stock in lieu of interest	—	—	435,000	2,000	295,000	—	—	—	297,000
Issuance of stock in lieu of dividends	—	—	13,000	—	—	—	—	—	—
Issuance of stock in payment of accrued board compensation	—	—	253,000	1,000	246,000	—	—	—	247,000
Stock options granted below market	—	—	—	—	38,000	—	—	—	38,000
Warrants granted to non-employees	—	—	—	—	262,000	—	—	—	262,000
Unrealized holding loss on investments available-for-sale	—	—	—	—	—	—	(360,000)	—	(360,000)
Net loss	—	—	—	—	—	(2,498,000)	—	—	(2,498,000)
Balance, December 31, 1999	161,000	$1,000	29,914,000	$149,000	$66,548,000	$(63,645,000)	$(360,000)	$(472,000)	$2,221,000
Convertible note payable converted to common stock	—	—	719,000	4,000	913,000	—	—	—	917,000
Issuance of stock for exercise of warrants and options	—	—	2,069,000	9,000	881,000	—	—	—	890,000
Issuance of stock in lieu of interest	—	—	115,000	1,000	321,000	—	—	—	322,000
Issuance of stock in lieu of dividends	—	—	10,000	—	—	—	—	—	—
Issuance of stock in private placements, net of issuance costs	—	—	3,219,000	16,000	7,012,000	—	—	—	7,028,000
Stock options granted below market	—	—	—	—	134,000	—	—	—	134,000
Options and warrants granted to non-employees	—	—	—	—	551,000	—	—	—	551,000
Unrealized holding loss on investments available-for-sale	—	—	—	—	—	—	(185,000)	—	(185,000)
Expiration of settlement warrant obligation	—	—	—	—	1,793,000	—	—	—	1,793,000
Net loss	—	—	—	—	—	(9,589,000)	—	—	(9,589,000)
Balance, December 31, 2000	161,000	$1,000	36,046,000	$179,000	$78,153,000	$(73,234,000)	$(545,000)	$(472,000)	$4,082,000

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows

For the years ended December 31,	2000	1999	1998
Cash flows provided by (used in) operating activities:			
Net loss	**$(9,589,000)**	$(2,498,000)	$(1,793,000)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Depreciation and amortization	**6,296,000**	6,557,000	6,412,000
Provision for doubtful accounts	**442,000**	746,000	850,000
Impairment charges	**1,362,000**	—	—
Cumulative effect of accounting change	**448,000**	—	—
Loss from disposition of equipment and sale of available-for-sale investments, net	**6,000**	(6,000)	240,000
Non-cash compensation charges	**685,000**	292,000	353,000
Accreted interest expense	**206,000**	459,000	211,000
Amortization of deferred revenue	**—**	(85,000)	(1,022,000)
Gain on sale of interest in subsidiary	**—**	—	(1,643,000)
Gain on sale of assets of subsidiary	**—**	(2,254,000)	—
Changes in assets and liabilities:			
Restricted cash	**37,000**	(239,000)	—
Accounts receivable	**375,000**	(816,000)	(627,000)
Prepaid expenses and other assets	**476,000**	(423,000)	(487,000)
Accounts payable and accrued expenses	**(249,000)**	(209,000)	64,000
Deferred revenue	**515,000**	236,000	(382,000)
Management severance and other long-term liabilities	**(606,000)**	(955,000)	(819,000)
Net cash provided by (used in) operating activities	**404,000**	805,000	1,357,000
Cash flows provided by (used in) investing activities:			
Capital expenditures	**(7,188,000)**	(6,814,000)	(3,002,000)
Software development expenditures	**(1,557,000)**	—	(10,000)
Deposits on broadcast equipment	**499,000**	(374,000)	(237,000)
Notes receivable	**138,000**	70,000	(70,000)
Proceeds from sale of investments	**538,000**	—	—
Proceeds from sale of assets of subsidiary	**—**	1,227,000	—
Proceeds from sale of equipment	**—**	45,000	—
Proceeds from sale of interest in subsidiary	**—**	—	1,862,000
Net cash provided by (used in) investing activities	**(7,570,000)**	(5,846,000)	(1,457,000)
Cash flows provided by (used in) financing activities:			
Principal payments on capital leases	**(932,000)**	(1,125,000)	(104,000)
Borrowings from revolving line of credit	**26,624,000**	11,175,000	—
Principal payments on note payable and revolving line of credit	**(25,300,000)**	(8,872,000)	—
Proceeds from issuance of common stock, net of issuance costs	**7,028,000**	—	—
Proceeds from exercise of warrants and options	**890,000**	347,000	—
Net cash provided by (used in) financing activities	**8,310,000**	1,525,000	(104,000)
Net increase (decrease) in cash and cash equivalents	**1,144,000**	(3,516,000)	(204,000)
Cash and cash equivalents at beginning of period	**1,044,000**	4,560,000	4,764,000
Cash and cash equivalents at end of period	**$2,188,000**	$1,044,000	$4,560,000

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows

For the years ended December 31,	2000	1999	1998
Supplemental disclosures of cash flow information:			
Cash paid during the period for:			
Interest	**$602,000**	$249,000	$121,000
Income taxes	**—**	—	—
Supplemental disclosure of non-cash investing and financing activities:			
Issuance of treasury stock pursuant to anti-dilution provision	**—**	$931,000	$1,181,000
Issuance of common stock in payment of interest	**$322,000**	$297,000	—
Issuance of common stock in payment of board compensation	**—**	$247,000	—
Equipment acquired under capital leases	**$379,000**	$1,767,000	$464,000
Equipment and license acquired by issuing note payable	**—**	$361,000	—
Exchange of preferred stock for convertible notes and warrants	**—**	$5,449,000	—
Exchange of convertible notes to common stock	**$917,000**	$1,012,000	—
Issuance of common stock in exchange for cancellation of options and warrants	**—**	—	$4,000
Unrealized holding loss on investments available for sale	**$185,000**	$360,000	—
Sale of assets of subsidiary for cash of $1,227,000 and stock of eBet Online	**—**	$1,297,000	—
Expiration of settlement warrant obligation	**$1,793,000**	—	—

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

For the Years Ended December 31, 2000, 1999 and 1998

(1) ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Description of Business

NTN operates its businesses through two operating divisions: BUZZTIME, Inc.™ (BUZZTIME) and the NTN Network™. BUZZTIME, NTN's wholly owned subsidiary formed in December 1999, owns the exclusive rights to the largest known digital trivia game show library and many unique "TV Play-along" sports games. The NTN Network operates two interactive television (ITV) networks: its original NTN Network and its new Digital Interactive Television (DITV) Network. Both networks broadcast daily a wide variety of popular interactive games, advertisements and informational programming to consumers in approximately 3,450 restaurants, sports bars and taverns throughout North America.

Basis of Accounting Presentation

The consolidated financial statements include the accounts of NTN and its wholly owned subsidiaries, IWN Inc. ("IWN"), IWN, L.P. and BUZZTIME (collectively "NTN" or the "Company"). All significant intercompany balances and transactions have been eliminated in consolidation.

On June 16, 1998, NTN sold an 82.5% interest in its subsidiary LearnStar, Inc. ("LearnStar") to NewStar Learning Systems, L.L.C. ("NewStar") for $1,862,000. The transaction resulted in a gain of $1,643,000, which is included in other income for the year ended December 31, 1998. In 1994, NTN formed IWN to serve as the general partner of IWN, L.P., a limited partnership engaged in the development of interactive technology for gaming applications. IWN has no business or operations apart from its service as the general partner of IWN, L.P. In August of 1999, the assets of IWN, L.P. were sold to eBet Limited for $1,227,000 in cash and 4,000,000 shares of eBet Online stock, which resulted in a gain of $2,254,000.

Cash and Cash Equivalents

For the purpose of financial statement presentation, NTN considers all highly liquid investment instruments with original maturities of three months or less to be cash equivalents. Cash equivalents of $2,188,000 and $860,000 at December 31, 2000 and 1999, respectively, consist of money market accounts.

Restricted Cash

Under the revolving line of credit agreement, all cash receipts are required to be deposited into a restricted cash account. The restricted cash is then transferred to pay down the line of credit.

Broadcast Equipment and Fixed Assets

Broadcast equipment and fixed assets are stated at cost. Equipment under capital leases is stated at the present value of minimum lease payments. Depreciation of fixed assets is computed using the straight-line method over the estimated useful lives of the assets (three to seven years). Depreciation of broadcast equipment is computed using the straight-line method over the estimated useful lives of the assets (three to four years). Amortization of fixed assets under capital leases is computed using the straight-line method over the shorter of the estimated useful lives of the assets or the lease period, and is included in depreciation expense.

Revenue Recognition

NTN recognizes revenue from five sources: NTN Network revenues, BUZZTIME service revenues, America Online revenues, equipment sales and other sources. Revenue is not recognized until collectibility of fees is reasonably assured.

NTN Network revenue is generated primarily from broadcasting content and advertising. Revenues generated from broadcasting content to subscriber locations is recognized ratably over the contract term as the content is broadcast 17 hours a day/seven days a week. Consistent with the terms of advertising agreements, advertising is aired a specified number of times per hour everyday, and therefore revenues are recognized ratable over the contract term. Included in NTN Network revenue are amounts earned under a license agreement with our Canadian licensee, who operates approximately 500 hospitality locations. Revenue under this license agreement is recognized on a monthly basis as broadcast content is aired similarly to NTN Network revenue.

BUZZTIME service and America Online revenues are recognized as the service is provided by NTN.

Equipment sales are recognized when equipment is shipped or transferred to the purchaser.

Other revenue is recognized when all material services or conditions relating to the transaction have been performed or satisfied.

In the fourth quarter of 2000, NTN changed its method of accounting for NTN Network installation, setup and training fees ("installation fees") received from customers, retroactively effective as of January 1, 2000, in accordance with Staff Accounting Bulletin No. 101 ("SAB 101"), "Revenue Recognition in Financial Statements," which provides guidance related to revenue recognition based on interpretations and practices followed by the SEC. Previously, NTN recognized approximately one-half of the installation fees upon customer setup to cover direct expenses of the installation, setup and training and the balance over the life of the contract, which generally is one year. Under the new method, all installation fees billed are deferred and recognized as revenue on a straight-line basis over 36 months, the estimated life of a customer. Installation fees not recognized in revenue have been recorded as deferred revenue in the accompanying consolidated balance sheets. In addition, the direct expenses of the installation, setup and training are deferred and amortized on a straight-line basis over 36 months and are classified as deferred costs on the accompanying consolidated balance sheets. Included in 2000 is revenue of $780,000 and direct expenses of $843,000, that were previously recognized in 1999, 1998 and 1997 under the old method. The pro forma effect of retroactive application on the results of operations for the years ended December 31, 2000, 1999 and 1998 is shown below:

	2000	**1999**	**1998**
Net loss			
As reported	**$9,589,000**	$2,498,000	$2,551,000
Pro forma	**$9,141,000**	$3,951,000	$1,687,000
Net loss per share			
As reported	**$0.29**	$0.09	$0.10
Pro forma	**$0.28**	$0.14	$0.06

Software Development Costs

NTN capitalizes costs related to the development of certain software products. In accordance with Statement of Financial Accounting Standards ("SFAS") No. 86, "Accounting for the Costs of Computer Software to be Sold, Leased, or Otherwise Marketed," capitalization of costs begins when technological feasibility has been established and ends when the product is available for general release to customers. Amortization of costs related to interactive programs is recognized on a straight-line basis over three years.

Web Site Development Costs

NTN capitalizes Web site development costs in accordance with Emerging Issues Task Force Issue No. 00-02, "Accounting for Web Site Development Costs." Costs incurred during the planning and operating stages are expensed as incurred, while costs incurred during the Web site application and infrastructure development stage are capitalized and amortized on a straight-line basis over their expected useful life of three years.

Stock-Based Compensation

On January 1, 1996, NTN adopted SFAS No. 123, "Accounting for Stock-Based Compensation," which permits entities to recognize as expense, over the vesting period, the fair value of all stock-based awards on the date of grant. Alternatively, SFAS No. 123 also allows entities to continue to apply the provisions of Accounting Principles Board ("APB") No. 25, "Accounting for Stock Issued to Employees," and provide pro forma net income and pro forma earnings-per-share disclosures for employee stock options grants made in 1996 and future years as if the fair-value-based method defined in SFAS No. 123 had been applied. NTN has elected to continue to apply the provisions of APB No. 25 and related interpretations and provide the pro forma disclosure provisions of SFAS No. 123.

The company accounts for options and warrants issued to non-employees in exchange for services in accordance with SFAS No. 123 and EITF 96-18, "Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services." The Company estimates the fair value of options and warrants using the Black-Scholes option-pricing model. For agreements which require the achievement of specific performance criteria for the options or warrants to vest, the measurement date is the date at which the specific performance criteria is met. Prior to the measurement dates, options and warrants subject to vesting based on the achievement of specific performance criteria that, based on different possible outcomes, result in a range of aggregate fair values are measured at each financial reporting period at their lowest aggregate then-current fair value, while options and warrants which vest over the service period or at completion of the service period are measured at each financial reporting period at their then-current fair value, for purposes of recognition of costs during those periods. For agreements which provide for services to be rendered without the requirement of specific performance criteria, the company measures the fair value of the options and warrants at the earlier of the date the services are completed or the date the options and warrants vest and are non-forfeitable. Generally, services are not rendered prior to the grant date and the related agreements do not contain performance commitments. Accordingly, the measurement date for compensation expense occurs subsequent to the grant date. From the grant date to the measurement date, compensation expense is estimated at each financial reporting period and is recorded over the service period. The unvested options and warrants continue to be remeasured at each financial reporting period until they vest or until the services are completed. For agreements which provide options and warrants for services already rendered, the options and warrants immediately vest and the measurement date is the date of grant. Modifications that increase the fair value of the warrants are treated as an exchange of the original warrant for a new one. Additional compensation expense related to modifications is recorded over the remaining service period.

Impairment of Long-Lived Assets and Long-Lived Assets to be Disposed of

Long-lived assets and certain identifiable intangibles are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows (undiscounted and without interest) expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

Investments Available-for-Sale

Investment securities consist of equity securities, which are classified as available-for-sale securities. Available-for-sale securities are recorded at fair value, and unrealized holding gains and losses are excluded from earnings and are reported as a separate component of comprehensive income until realized. Realized gains and losses from the sale of available-for-sale securities are determined on a specific-identification basis. A decline in the market value of any available-for-sale security, below cost that is deemed to be other than temporary, results in a reduction in the carrying amount to fair value. The impairment is charged to earnings, and a new cost basis for the security is established.

Fair Value of Financial Instruments

NTN believes that the fair value of financial instruments approximates their carrying value. The following methods and assumptions were used to estimate the fair value of financial instruments:

The carrying values of cash and cash equivalents, restricted cash, investments available for sale, accounts receivable, accounts payable and accrued liabilities approximate fair value because of the short maturity of these instruments. The carrying value of the revolving line of credit approximates its fair value because the interest rate is indexed by current market rates, and the other terms are comparable to those currently available in the market place. The carrying value of the convertible notes approximates their fair value because the interest rate is comparable to rates currently available in the market.

Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Research and Development and Advertising

Research and development and advertising are expensed as incurred. Research and development costs amounted to $430,000, $842,000 and $714,000 in 2000, 1999 and 1998, respectively. Advertising costs amounted to $405,000, $343,000 and $284,000 in 2000, 1999 and 1998, respectively, and are included in selling, general and administrative expenses in the accompanying statements of operations.

Concentration of Credit Risk

NTN provides services to group viewing locations, generally bars and lounges, and to third-party distributors, primarily throughout the United States. In addition, NTN licenses its technology and products to licensees outside of the United States. Concentration of credit risk with respect to trade receivables is limited due to the large number of customers comprising NTN's customer base, and their dispersion across many different industries and geographies. NTN performs ongoing credit evaluations of its customers and generally requires no collateral. NTN maintains an allowance for doubtful accounts to provide for credit losses.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management of NTN to make estimates and assumptions that affect the reported amount of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Basic and Diluted Earnings Per Common Share

NTN computes basic and diluted earnings per share in accordance with SFAS No. 128, "Earnings per Share." Basic EPS excludes the dilutive effects of options, warrants and other convertible securities. Diluted EPS reflects the potential dilution of securities that could share in the earnings of NTN. Options, warrants, convertible preferred stock and convertible notes representing approximately 12,614,000, 15,306,000 and 5,569,000 shares were excluded from the computations of diluted net loss per common share for the years ended December 31, 2000, 1999 and 1998, respectively, as their effect is anti-dilutive.

Reflected in the net loss available to common shareholders for the year ended December 31, 1998 is the accretion of the beneficial conversion feature on the Series B preferred stock in the amount of $758,000. The amount of the beneficial conversion feature was measured at the date of issue of the convertible security as the difference between the conversion price and the market value of the common stock into which the security was convertible. This amount was accounted for as a non-cash dividend on the convertible preferred stock with the same amount credited to additional paid-in capital, allocated over the period from issuance to first convertibility. Therefore, there is no impact to shareholders' equity. The beneficial conversion feature was fully accreted as of June 30, 1998. As described in Note 5 to the consolidated financial statements, NTN entered into an exchange agreement with the holders of the Series B preferred stock.

Reclassifications

Certain items in the 1999 and 1998 consolidated financial statements have been reclassified to conform to the 2000 presentation.

(2) BROADCAST EQUIPMENT AND FIXED ASSETS

Broadcast equipment and fixed assets are recorded at cost and consist of the following:

	2000	**1999**
Broadcast equipment	**$19,149,000**	$14,502,000
Furniture and fixtures	**574,000**	445,000
Machinery and equipment	**7,878,000**	5,080,000
Leasehold improvements	**820,000**	547,000
Equipment under capital lease:		
Broadcast equipment	**1,654,000**	1,589,000
Machinery and equipment	**1,217,000**	902,000
Other equipment	**9,000**	9,000
	31,301,000	23,074,000
Accumulated depreciation and amortization	**(19,338,000)**	(12,604,000)
	$11,963,000	$10,470,000

(3) ASSET IMPAIRMENT

The Internet site, BUZZTIME.com, was developed with the intent of registering a large number of consumers at little cost and converting these registrations into revenue through direct marketing to the member database, sponsorship, ad revenues, subscriptions and third-party licensing. However, in the fourth quarter of 2000, NTN shifted its focus from the Internet initiatives to ITV opportunities and decided not to pursue the direct marketing application of BUZZTIME.com. As a result, the use of BUZZTIME.com as a direct marketing database was abandoned, resulting in an impairment charge of $1,131,000 during the fourth quarter of 2000.

In addition to the write-off of certain Web development costs, NTN also wrote off $231,000 associated with the Internet game station licenses, equipment, and related goodwill on the basis that assets are not recoverable through future cash flows.

(4) COMMON STOCK OPTIONS AND WARRANTS

Options

NTN has two active stock option plans. The 1995 Employee Stock Option Plan (the "Option Plan") was approved by the shareholders in 1995 and was subsequently amended. Under the Option Plan, options for the purchase of NTN's common stock may be granted to officers, directors and employees. Options may be designated as incentive stock options or as nonqualified stock options and generally vest over four years, except, the Board of Directors, at its discretion, can authorize acceleration of vesting periods. Options under the Option Plan, which have a term of up to ten years, are exercisable at a price per share not less than the fair market value on the date of grant. The aggregate number of shares authorized for issuance under the Option Plan as of December 31, 2000 is 10,394,762.

In addition, NTN has issued options pursuant to a Special Stock Option Plan ("Special Plan"). Options issued under the Special Plan are made at the discretion of the Board of Directors and are designated only as nonqualified options. The options generally have a term of up to ten years, are exercisable at a price per share not less than the fair market value on the date of grant and vest over various terms. The aggregate number of shares authorized for issuance under the Special Plan as of December 31, 2000 is 704,000.

The per share weighted-average fair value of stock options granted during 2000, 1999 and 1998 was $2.45, $0.92, and $0.72, respectively. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions: 2000 — dividend yield of 0%, risk-free interest rate of 6.30%, expected volatility of 128.99%, and expected life of 4 years; 1999 — dividend yield of 0%, risk-free interest rate of 5.28%, expected volatility of 124.97%, and expected life of 3.6 years; and 1998 — dividend yield of 0%, risk-free interest rate of 4.69%, expected volatility of 188%, and expected life of 5.2 years. In compliance with APB No. 25, NTN expensed $134,000 and $38,000 in 2000 and 1999, respectively, associated with the grants of 600,000 options in 1999 below market value pursuant to the Option Plan. No options were granted below market value in 2000 pursuant to the Option Plan.

NTN applies APB Opinion No. 25 and related interpretations in accounting for its stock option plans. Accordingly, no compensation cost has been recognized in the consolidated financial statements for the issuance of options to employees pursuant to the Special Plan and the Option Plan unless the grants were issued at exercise prices below market value. Had compensation cost related to employees for NTN's stock-based compensation plans been determined consistent with SFAS No. 123, NTN's net loss and net loss per share applicable to common stock would have been increased to the pro forma amounts indicated below.

	2000	**1999**	**1998**
Net loss			
As reported	**$9,589,000**	$2,498,000	$2,551,000
Pro forma	**$11,509,000**	$3,514,000	$4,365,000
Net loss per share			
As reported	**$0.29**	$0.09	$0.10
Pro forma	**$0.35**	$0.12	$0.17

A summary of stock option activity during 2000, 1999 and 1998 is as follows:

	Special Plan		Option Plan	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding December 31, 1997	1,030,000	$3.01	5,088,000	$3.47
Granted	104,000	2.81	3,290,000	0.93
Exercised	—	—	—	—
Canceled	(430,000)	3.30	(3,721,000)	3.59
Outstanding December 31, 1998	704,000	2.81	4,657,000	1.58
Granted	—	—	3,179,000	0.92
Exercised	—	—	(325,000)	1.04
Canceled	—	—	(1,030,000)	0.95
Outstanding December 31, 1999	704,000	2.81	6,481,000	1.38
Granted	—	—	1,851,000	2.45
Exercised	—	—	(546,000)	1.01
Canceled	—	—	(1,077,000)	1.52
Outstanding December 31, 2000	704,000	$2.81	6,709,000	$1.69
Exercisable as of December 31, 2000	704,000	$2.81	3,681,000	$1.73

A summary of options outstanding and exercisable by exercise price range at December 31, 2000 is as follows:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
Special Plan:					
$2.81	704,000	4 years	$2.81	704,000	$2.81
Option Plan:					
$0.56 – $1.50	3,516,000	8 years	$0.86	2,070,000	$0.87
$1.51 – $3.00	2,827,000	8 years	$2.43	1,359,000	$2.65
$3.01 – $6.50	366,000	5 years	$3.87	252,000	$3.91

In April 1998, the Board of Directors approved the issuance of 564,000 options with exercise price of $1.00 in exchange for the cancellation of various prior employee options under the Option Plan with exercise prices ranging from $2.00 to $6.50. No compensation expense was recorded as a result of the issuance.

In March 1998, NTN issued approximately 277,000 shares of common stock to two former officers in exchange for the surrender and cancellation of certain previously outstanding warrants and options to purchase 1,500,000 shares of common stock at exercise prices ranging from $2.00 to $4.75 per share. The fair market value of the shares issued was approximately $242,000, which was less than the fair value of the warrants and options received in the exchange.

In January 1998, NTN issued approximately 759,000 shares of common stock in exchange for the surrender and cancellation of certain previously outstanding warrants and options to purchase approximately 2,578,000 shares of common stock at exercise prices ranging from $2.00 to $5.75 per share. The fair market value of the shares issued was approximately $900,000, which was less than the fair value of the warrants and options received in the exchange.

In 2000 and 1997, NTN issued various options pursuant to the Special Plan to non-employees to purchase common stock. In compliance with SFAS No. 123 and EITF 96-18, NTN expensed $178,000 and $58,000 in 2000 and 1998, respectively, associated with the grant of 100,000 options in 2000 and 134,000 options in 1997.

Warrants

In 2000, 1999 and 1998, NTN granted 885,000, 1,191,000 and 1,000,000 warrants to non-employees. The 2000 and 1999 warrants were granted under consulting agreements, and the 1998 warrants were granted in connection with the Exchange Agreement entered into in 1998 between NTN and the Series B preferred stock investors, under which the investors agreed to surrender for cancellation their remaining shares of Series B preferred stock in exchange for warrants and 7% senior subordinated convertible notes. NTN expensed $373,000, $262,000 and $0 in 2000, 1999 and 1998, respectively, associated with the grant of these warrants.

The following summarizes warrant activity during 2000, 1999 and 1998:

	Outstanding Warrants	Weighted Average Exercise Prices
December 31, 1997	4,194,000	$3.63
Granted	1,000,000	1.25
Exercised	—	—
Canceled	(2,291,000)	4.02
December 31, 1998	2,903,000	2.49
Granted	1,191,000	1.00
Exercised	(9,000)	0.96
Canceled	(938,000)	2.63
December 31, 1999	3,147,000	1.89
Granted	885,000	1.79
Exercised	(1,626,000)	0.36
Canceled	(404,000)	4.53
December 31, 2000	2,002,000	$1.94
Balance exercisable at December 31, 2000	1,865,000	$1.91

At December 31, 2000, the range of exercise prices and the weighted-average remaining contractual life of outstanding warrants was $0.6875 to $3.75 and 3 years, respectively.

(5) CUMULATIVE CONVERTIBLE PREFERRED STOCK

NTN has authorized 10,000,000 shares of preferred stock. The preferred stock may be issued in one or more series. The only series currently designated are a series of 5,000,000 shares of Series A Cumulative Convertible Preferred Stock ("Series A Preferred Stock") and a series of 85,000 shares of Series B preferred stock.

Series A

At December 31, 2000 and 1999, there were 161,000 shares of Series A Preferred Stock issued and outstanding. The Series A Preferred Stock provides for a cumulative annual dividend of 10 cents per share, payable in semi-annual installments in June and December. Dividends may be paid in cash or with shares of common stock. In 2000, 1999 and 1998, NTN issued approximately 10,000, 13,000 and 19,000 common shares, respectively, for payment of dividends. At December 31, 2000, the cumulative unpaid dividends for the Series A Preferred Stock was approximately $1,300.

The Series A Preferred Stock has no voting rights and has a $1.00 per share liquidation preference over common stock. The registered holder has the right at any time to convert shares of Series A Preferred Stock into that number of shares of NTN common stock that equals the number of shares of Series A Preferred Stock that are surrendered for conversion divided by the conversion rate. The conversion rate is subject to adjustment in certain events and is established at the time of each conversion. During 2000, 1999 and 1998, there were no conversions. There are no mandatory conversion terms or dates associated with the Series A Preferred Stock.

Series B

In October 1997, NTN sold and issued 35,000 shares of Series B preferred stock each to two institutional purchasers ("the Investors") for a total of $7,000,000. As of October 5, 1998, 14,000 shares of the Series B preferred stock (plus accrued dividends) had been converted into 2,430,000 shares of common stock of NTN, leaving 56,000 shares of the Series B preferred stock outstanding. On October 5, 1998, NTN entered into an Exchange Agreement with the Investors pursuant to which they agreed to surrender for cancellation their remaining shares of Series B preferred stock in exchange for warrants and 7% senior subordinated convertible notes (see Note 9). The convertible notes were issued January 11, 1999. The Series B preferred stock was retired in June 1999.

Settlement Warrants

The results for the year ended December 31, 2000 include the reclassification of an accrued liability of approximately $1,793,000 to additional paid-in capital for a potential redemption obligation, relating to warrants issued in connection with the settlement of litigation in 1996 ("Settlement Warrants"), which expired in February 2000. The Settlement Warrants entitled the holder of a Settlement Warrant to purchase a share of common stock at a price of $0.96 during the period ending February 18, 2001. During the period from February 18, 2000 to February 18, 2001, the holders of the Settlement Warrants were to have the right to cause the Company to redeem the Settlement Warrants for a redemption price of $3.25 per Warrant (the "Put Right"); however, this Put Right expired by its terms on February 17, 2000, when the closing price per share of the Company's common stock on the American Stock Exchange reached $4.22 or above for the seventh trading day since the Settlement Warrants were issued. The Company has no further obligation to redeem or repurchase the Settlement Warrants.

(6) RETIREMENT AND SAVINGS PLANS

Defined Contribution Plan

During 1994, NTN established a defined contribution plan which is organized under Section 401(k) of the Internal Revenue Code, which allows employees who have completed at least six months of service or reached age 21, whichever is later, to defer up to 15% of their pay on a pre-tax basis. NTN, at its discretion, may contribute to the plan. For the years ended December 31, 2000, 1999 and 1998, NTN made no such contributions.

(7) INCOME TAXES

For each of the years ended December 31, 2000, 1999 and 1998, there was no provision for current or deferred income taxes. The components that comprise deferred tax assets and liabilities at December 31, 2000 and 1999 are as follows:

	2000	1999
Deferred tax assets:		
NOL carryforwards	**$19,710,000**	$16,711,000
Legal and litigation accruals	**20,000**	3,000
Allowance for doubtful accounts	**324,000**	859,000
Compensation and vacation accrual	**141,000**	337,000
Accrued expenses	**160,000**	902,000
Allowance for equipment obsolescence	**—**	77,000
Deferred revenue	**1,838,000**	247,000
Research and experimentation credit	**221,000**	245,000
Amortization	**111,000**	96,000
Depreciation	**—**	482,000
Charitable contributions	**7,000**	10,000
Total gross deferred tax assets	**22,532,000**	19,969,000
Valuation allowance	**(22,445,000)**	(19,914,000)
Deferred tax assets	**87,000**	55,000
Deferred tax liabilities:		
Capitalized software	**—**	55,000
Depreciation	**87,000**	—
Total deferred liabilities	**87,000**	55,000
Net deferred taxes	**$—**	$—

The reconciliation of computed expected income taxes to effective income taxes by applying the federal statutory rate is as follows:

	2000	1999	1998
Tax at federal income tax rate	**$(3,260,000)**	$(849,000)	$(610,000)
State taxes net of federal benefit	**(575,000)**	(150,000)	(105,000)
Settlement warrants and SFAS 123 charges	**274,000**	99,000	84,000
Nondeductible expenses of IWN	**—**	—	299,000
Sale of LearnStar	**—**	—	(559,000)
Change in valuation allowance	**2,531,000**	(789,000)	3,131,000
Expiration of net operating losses	**517,000**	—	—
Adjustments of net operating loss carryforwards	**435,000**	1,384,000	(2,313,000)
Other	**78,000**	305,000	73,000
	$—	$—	$—

The net change in the total valuation allowance for the year ended December 31, 2000 was an increase of $2,531,000. The net change in the total valuation allowance for the years ended December 31, 1999 and 1998 was a decrease of $789,000 and an increase of $3,131,000, respectively. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. Based on the level of historical operating results and projections for the taxable income for the future, management has determined that it is more likely than not that the portion of deferred tax assets not utilized through the reversal of deferred tax liabilities will not be realized. Accordingly, NTN has recorded a valuation allowance to reduce deferred tax assets to the amount that is more likely than not to be realized.

At December 31, 2000, the Company has available net operating loss carryforwards of approximately $55,544,000 for federal income tax purposes, which began to expire in 2000. The net operating loss carryforwards for state purposes, which began expiring in 1998, are approximately $13,744,000.

(8) COMMITMENTS AND CONTINGENCIES

Operating Leases

NTN leases office and production facilities and equipment under agreements which expire at various dates. Certain leases contain renewal provisions and generally require NTN to pay utilities, insurance, taxes and other operating expenses. Additionally, NTN entered into lease agreements for certain equipment used in broadcast operations and the corporate computer network, some of which involved sale and leaseback transactions. Any deferred gains on sale and leaseback transactions were amortized over the three-year lease terms. Each lease provides an option to NTN to repurchase the equipment at the estimated fair market value at the end of the lease term. All sale and leaseback transactions were completed during 1999, at which time the equipment was purchased. Lease expense under operating leases totaled $475,000, $1,007,000 and $1,505,000, in 2000, 1999 and 1998, respectively, net of sublease income of $149,000 and $157,000 in 2000 and 1999, respectively.

Future minimum lease obligations under noncancelable operating leases, net of expected sublease payments, at December 31, 2000 are as follows:

Year Ending	Lease Payment	Sublease Payments	Net
2001	$651,000	$228,000	$423,000
2002	548,000	246,000	302,000
2003	567,000	162,000	405,000
2004	586,000	78,000	508,000
2005	554,000	23,000	531,000
Thereafter	271,000	—	271,000
Total	$3,177,000	$737,000	$2,440,000

Capital Leases

NTN leases certain equipment under capital leases. Future minimum lease payments under the capital leases together with the present value of the net minimum lease payments as of December 31, 2000 are as follows:

Year Ending	Total
2001	$621,000
2002	74,000
2003	33,000
Total minimum lease payments	728,000
Less amount representing interest ranging from 6% to 23.7%	(66,000)
Present value of net minimum lease payments	662,000
Less current portion	(579,000)
Long-term portion	$83,000

Property held under capital leases is as follows:

	2000	**1999**
Equipment	**$2,871,000**	$2,491,000
Accumulated amortization	**(1,594,000)**	(667,000)
	$1,277,000	$1,824,000

(9) DEBT

Revolving Line Of Credit

NTN has an agreement with Coast Business Credit for a revolving line of credit. Available borrowings are limited to three times annualized trailing six-month EBITDA balance or three times trailing six-month cash collections balance, not to exceed $4,000,000. Interest is charged on the outstanding balance at a rate equal to the prime rate plus 1.5% per annum (effective rate of interest is 9.5% at December 31, 2000), but cannot be less than 9% per annum. The line of credit is secured by substantially all of NTN's assets. Total loan fees of $120,000 are payable in three annual installments and are being amortized over the life of the loan, which matures on August 31, 2002. The unused line of credit at December 31, 2000 was $81,000.

7% Senior Subordinated Convertible Notes

In 1999, NTN reacquired the Series B preferred stock in exchange for convertible notes and warrants. The convertible notes, with a face value of $5,913,000, were issued January 11, 1999 and bear interest at the annual rate of 7% per annum. Interest is due and payable in quarterly installments, in arrears, and the entire principal amount will be due and payable on February 1, 2001. Interest on the convertible notes may be paid in cash or, at NTN's election, in shares of its common stock valued for this purpose at 90% of the average closing bid price of the common stock during the 10 trading days preceding the interest payment date.

At any time after a period of 20 consecutive trading days during which the daily "Market Price" (as defined in the Exchange Agreement) of the common stock equals or exceeds $1.75 (subject to adjustment), NTN may elect, upon 45-days prior written notice, to prepay all or any portion of the convertible notes at a price of 105% of the outstanding principal amount, plus accrued and unpaid interest. The convertible notes will continue to be convertible, however, at any time prior to prepayment in full. The convertible notes must be prepaid in connection with a merger or consolidation of NTN or other "Major Transaction" (as defined in the Exchange Agreement) if the consideration per share of common stock in the Major Transaction is at least $1.50. In such event, the prepayment price will be 105% of the outstanding principal amount of the convertible notes, plus accrued and unpaid interest.

The holders of the convertible notes may convert them at any time, in whole or in part, at their option. The number of shares of common stock issuable upon conversion of each convertible note will be determined by dividing the outstanding principal amount to be converted, plus any accrued and unpaid interest, by the conversion price then in effect. The conversion price will be $1.275 per share, subject to adjustment upon the occurrence of certain events, including stock dividends or subdivisions or reclassifications of the common stock or any sale or issuance of common stock (or of rights or options to subscribe for or purchase common stock) for no consideration or for a consideration per share less than the "Average Market Price" (as defined in the Exchange Agreement) of the common stock. The actual number of shares of common stock issuable upon any conversion of the convertible notes will depend on the conversion price in effect on the relevant conversion date. On November 20, 1999, $1,000,000 of principal plus accrued interest was converted into approximately 793,000 shares of common stock. On March 16 and July 13, 2000, $200,000 and $717,000, respectively, of principal plus accrued interest was converted into approximately 159,000 and 560,000 shares of common stock, respectively. An additional $22,000 and $45,000 of interest expense in 2000 and 1999, respectively, related to the unamortized discount on the converted notes, was recognized upon conversion of the principal.

The convertible notes are subordinate in right of payment to the prior payment of all "Senior Debt" (as defined in the Exchange Agreement). NTN is restricted under the terms of the convertible notes from incurring any Senior Debt in excess of $10,000,000 or any other indebtedness [except Senior Debt and "Subordinated Debt" (as defined in the Exchange Agreement)] in excess of $2,000,000 at any time.

NTN will be in default under the convertible notes if it fails to pay any principal or interest on the convertible notes when due, and in certain other events, including in the event of a material adverse change in the condition, financial or otherwise, or operations of NTN as determined by the holders of the convertible notes in their discretion. If NTN defaults under the convertible notes, in the discretion of the holders of the convertible notes, the entire outstanding principal amount of the convertible notes and all accrued and unpaid interest will become immediately due and payable in full.

On October 5, 1998, in consideration for their entering into the Exchange Agreement on October 5, 1998, NTN issued to each of the Investors a warrant to purchase 500,000 shares of common stock at an initial purchase price of $1.25 per share. The exercise price was subject to adjustment based on future changes in the price of the common stock. The warrants are exercisable at any time on or before February 1, 2001.

The warrants contain certain antidilution provisions that require adjustments. The warrants were exercised on March 24, 2000 in a cashless exercise at a purchase price of $0.005, as the daily market price on each day during any 10 consecutive trading days was equal to or greater than $4.00. A total of 999,096 shares of common stock was issued upon exercise of the warrants.

An allocation has been made between the convertible notes and the warrants based on the relative fair values of the securities at the time of issuance. A discount of approximately $464,000 has been recorded against the convertible notes due to the allocation. As a result of this allocation, NTN is recording interest expense, at an effective interest rate of 11% per year, throughout the terms of the convertible notes which began in the first quarter of 1999. Interest expense of approximately $195,000 and $257,000 has been accreted for the years ended December 31, 2000 and 1999, respectively.

The balance of the convertible notes plus accreted interest at December 31, 2000 is $3,987,000.

In January 2001, NTN reached agreement with the holders of the convertible notes to extend the maturity date of the aggregate $4 million in promissory notes from February 1, 2001 to February 1, 2003. The promissory notes remain convertible at $1.275 per share, but the terms were modified to reduce the interest rate from 7% to 4% and to permit NTN to convert up to the full principal amount of the promissory notes into NTN common stock at maturity at a conversion price of $1.275 per share. In addition, if NTN's common stock closes above $2.50 for more than 20 consecutive trading days, NTN can force conversion of the promissory notes at $1.275 per share.

A registration statement on Form S-3 covering 4,637,516 shares of common stock, some or all of which may be issuable upon conversion of the convertible notes, was declared effective by the Securities and Exchange Commission on January 8, 1999.

Note Payable

NTN purchased equipment and a license agreement related to the Internet stations for $400,000 in April 1999 from Sikander, Inc. A promissory note was issued for $360,000 and cash of $40,000 was paid in relation to this agreement. The note bears interest at 10% per annum and principal is payable in twelve equal quarterly installments of $30,000 plus interest. In December 1999, the agreement was revised and a payment of approximately $123,000 plus interest was paid in December 1999, leaving a balance of approximately $178,000 at December 31, 1999, to be paid in nine quarterly installments of $19,676 beginning on March 31, 2000. Since March 31, 2000, NTN has made no further payments on the promissory note issued to Sikander, Inc. pursuant to this revised agreement. In June 2000, NTN commenced litigation against Sikander, Inc. and related defendants. NTN alleges in its complaint that it is under no obligation to pay any further monies to Sikander, Inc. under the terms of the Wind Up Agreement.

Maturities

Maturities of notes payable at December 31, 2000 are as follows:

Year Ending	Convertible Notes	Note Payable	Total
2001	$3,987,000	$138,000	$4,125,000
2002	—	20,000	20,000
Total obligation	3,987,000	158,000	4,145,000
Less current maturities	—	(138,000)	(138,000)
Long-term obligation	$3,987,000	$20,000	$4,007,000

(10) LEGAL ACTIONS

On June 11, 1997, NTN was included as a defendant in a class-action lawsuit, entitled *Eliot Miller and Jay Iyer, shareholders on behalf of themselves and all others similarly situated vs. NTN Communications, Inc., Patrick J. Downs, Daniel C. Downs, Donald C. Klosterman, Ronald E. Hogan, Gerald P. McLaughlin and KPMG Peat Marwick LLP* ("Miller litigation"), filed in the United States District Court for the Southern District of California. The complaint alleged violations of state and federal securities laws based upon purported omissions from NTN's filings with the Securities and Exchange Commission. More particularly, the complaint alleged that the directors and former officers devised an "exit strategy" to provide themselves with undue compensation upon their resignation from NTN. The plaintiffs further alleged that defendants made false statements about, and failed to disclose, contingent liabilities (guaranteed compensation to management and the right of an investor in IWN to require NTN to repurchase its investment during 1997) and phantom assets (loans to management) in NTN's financial statements and KPMG LLP's audit reports, all of which served allegedly to inflate the trading price of NTN's common stock.

On November 7, 1997, the court granted KPMG LLP's motion to dismiss the plaintiffs' claims against it pursuant to Rule 12(b)(6) of the Federal Rules of Civil Procedure for failure to state a claim upon which relief may be granted.

In April 2000, the court approved the settlement agreement between NTN and the class of plaintiffs in the Miller litigation and dismissed the litigation as to all defendants. The settlement provides that NTN will pay $3,250,000 as allocated per the approved settlement agreement. The settlement payment is fully covered by NTN's liability insurance.

In September 1998, NTN received correspondence from counsel to Microsoft Corporation and related inquiries from the Business Software Alliance ("BSA") and Software Publishers Association ("SPA"), two industry associations, requesting information regarding NTN's use of the MS-DOS operating system in connection with its Playmaker® systems, which at the time were installed in over 2,800 hospitality locations throughout the United States. In response, NTN conducted an internal audit and produced the results to counsel to the three entities. Based on the audit results, it was determined that NTN had insufficient licensing for the MS-DOS operating systems in use in its hospitality locations. The three entities agreed that BSA and SPA would represent the interests of Microsoft Corporation in resolution of the matter. In November 1999, NTN entered into a Settlement Agreement with BSA pursuant to which NTN paid BSA a total of $339,864 in ten equal monthly installments. The tenth and final installment was paid in July 2000. In May 2000, pursuant to the terms of the Settlement Agreement, NTN delivered to BSA a Certification of Compliance certifying the accuracy of the software audit results and that all copies of the relevant software products used by NTN in the course of business are licensed to NTN and are used solely in accordance with such licenses. In addition, in December 1999, NTN entered into a Settlement Agreement with SPA pursuant to which NTN was liable for a total of $25,000 to SPA in two equal installments and purchased sufficient copies of the software to replace infringing copies as needed. The settlement was paid in full in January 2000. In December 2000, NTN provided SPA with a signed statement certifying that NTN is still in compliance with any and all applicable software licensing agreements along with a statement itemizing software purchases made by NTN during the course of the previous year. We previously accrued an amount sufficient to cover the expense of both settlements.

NTN has been involved as a plaintiff or defendant in various previously reported lawsuits in both the United States and Canada involving Interactive Network, Inc. ("IN"). With the court's assistance, NTN and IN reached a resolution of all pending disputes in the United States and agreed to private arbitration regarding any future licensing, copyright or infringement issues which may arise between the parties. There remain two lawsuits involving NTN, its unaffiliated Canadian licensee and IN, which were filed in Canada in 1992. The litigation involves licensing and patent infringement issues. These actions affect only NTN's Canadian operations and its Canadian licensee and do not extend to NTN's operations in the United States or elsewhere. In December 2000, the Federal Court of Canada, Trial Division, ordered the parties to complete discovery in the matter by April 2001, later extended to June 30, 2001. Although they cannot be estimated with certainty, any damages NTN might incur are not expected to be material.

There can be no assurance that any or all of the foregoing claims will be decided in favor of NTN, which is not insured against all claims made. During the pendency of such claims, NTN will continue to incur the costs of defense of same. Other than set forth above, there is no material litigation pending or threatened against NTN.

(11) MANAGEMENT REORGANIZATION

On March 5, 1997, NTN announced a reorganization of its executive management personnel in which Patrick J. Downs resigned as Chief Executive Officer and Chairman of the Board and Daniel C. Downs resigned as President. In addition, three other officers resigned or were terminated in connection with the reorganization ("Reorganization"). NTN entered into separate agreements ("Agreements") with each of the former officers, setting out the terms on which their existing employment contracts with NTN would be settled. In compliance with the Agreements, NTN was to continue to pay the former officers their current annual salaries and other benefits for the remaining terms of their employment agreements with NTN, which were to expire on or before December 31, 1999.

In March 1998, NTN and three of the former officers agreed to an amendment of the Agreements. The Agreements were modified to extend the payment term an additional year to December 31, 2000 and provided for reductions of amounts to be paid in 1998 and 1999 totaling $272,000 and $355,000, respectively. All payments under the agreements have been paid in full at December 31, 2000.

Interest expense totaling $45,000, $34,000 and $56,000 was incurred in 2000, 1999 and 1998, respectively, related to the Agreements.

(12) SUBSEQUENT EVENTS

Revision to Terms of Private Placement Agreement

Pursuant to the terms of the November 2000 private placement, two accredited investors (the "Buyers") will be issued additional shares of common stock in the event NTN issues, at any time or from time to time during the six months immediately following November 14, 2000, any common stock or convertible securities without consideration or for a consideration per share less than the original purchase price per share paid by the Buyers. In addition, NTN also granted the Buyers a limited right of first refusal on subsequent offerings exercisable at the option of each Buyer during the twelve-month period ending November 14, 2001.

In January 2001, NTN and the Buyers reached an agreement to revise the terms of the private placement in exchange for the issuance of 350,043 shares of NTN common stock. The revisions eliminated the exercise price reset provisions contained in the warrants as well as the investors' rights to receive additional shares of NTN common stock upon the occurrence of certain events. Furthermore, the Buyers agreed to surrender and cancel their rights to additional contingent warrants for 609,291 shares of NTN common stock. In connection with this agreement, the employment agreement between NTN and Stanley B. Kinsey, Chief Executive Officer of NTN, was extended for one year.

Extension of Terms for 7% Convertible Notes Payable

In January 2001, NTN reached an agreement with the holders of the convertible notes to extend the maturity date of the aggregate $4 million in convertible notes from February 1, 2001 to February 1, 2003. The promissory notes remain convertible at $1.275 per share, but the terms were modified to reduce the interest rate from 7% to 4% and to permit NTN to convert up to the full principal amount of the promissory notes into NTN common stock at maturity at a conversion price of $1.275 per share. In addition, if NTN's common stock closes above $2.50 for more than 20 consecutive trading days, NTN can force conversion of the promissory notes at $1.275 per share.

(13) SEGMENT INFORMATION

NTN's operations are to develop and distribute interactive entertainment. NTN's reportable segments have been determined based on the nature of the services offered to customers, which include, but are not limited to, revenue from the NTN Network and BUZZTIME divisions. NTN Network revenue is generated primarily from broadcasting content to customer locations through two interactive television networks. NTN Network revenues comprise 97% of NTN's total revenue. Revenue from BUZZTIME is primarily generated from the distribution of its digital trivia game show content and "Play-Along" sports games, as well as revenue related to production services for third parties, and also includes fees generated from the America Online contract that expired in November 1999. Included in the operating loss and depreciation and amortization for both the NTN Network and BUZZTIME is an allocation of corporate expenses, while the related corporate assets are not allocated to the segments. The following tables set forth certain information regarding NTN's segments and other operations:

	2000	**1999**	**1998**
Revenues:			
NTN Network	**$21,406,000**	$22,250,000	$20,973,000
BUZZTIME	**540,000**	983,000	2,014,000
IWN	**—**	302,000	493,000
Other	**102,000**	213,000	714,000
Total revenues	**$22,048,000**	$23,748,000	$24,194,000
Operating income (loss):			
NTN Network	**$(2,162,000)**	$(1,446,000)	$(473,000)
BUZZTIME	**(6,039,000)**	(2,305,000)	(2,063,000)
IWN	**—**	(50,000)	(895,000)
Other	**—**	—	(16,000)
Total operating loss	**$(8,201,000)**	$(3,801,000)	$(3,447,000)
Total assets:			
NTN Network	**$14,012,000**	$12,547,000	$11,816,000
BUZZTIME	**1,776,000**	230,000	1,072,000
IWN	**—**	118,000	367,000
Other	**—**	—	—
Corporate	**3,034,000**	4,392,000	3,512,000
Total assets	**$18,822,000**	$17,287,000	$16,767,000
Capital expenditures and software development costs:			
NTN Network	**$5,138,000**	$5,174,000	$2,383,000
BUZZTIME	**2,623,000**	—	10,000
Corporate	**984,000**	1,640,000	619,000
Total capital expenditures and software development costs	**$8,745,000**	$6,814,000	$3,012,000
Depreciation and amortization:			
NTN Network	**$5,669,000**	$5,478,000	$3,597,000
BUZZTIME	**627,000**	1,065,000	2,096,000
IWN	**—**	14,000	698,000
Other	**—**	—	21,000
Total depreciation and amortization	**$6,296,000**	$6,557,000	$6,412,000

(14) SELECTED QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

The 2000 quarterly financial data, as reported in the Company's previously filed Quarterly Reports on Form 10-Q, has been adjusted to reflect the implementation of SAB 101 in the fourth quarter of 2000, retroactive to January 1, 2000. Periods beginning before January 1, 2000 have not been adjusted as the effect of the change in accounting principle could not be reasonably determined. The March 31, 2000 quarterly financial data, as reported in the Company's previously filed Quarterly Report on Form 10-Q, has been adjusted to reflect the reclassification of the accrual for settlement warrants to additional paid-in capital.

	Three-Month Period Ended				
	March 31, 2000	**June 30, 2000**	**September 30, 2000**	**December 31, 2000**	**Total 2000**
Total revenue	**$5,441**	**$5,225**	**$5,613**	**$5,769**	**$22,048**
Total operating expenses	**7,702**	**7,832**	**6,735**	**7,980**	**30,249**
Operating loss	**(2,261)**	**(2,607)**	**(1,122)**	**(2,211)**	**(8,201)**
Other income (expense), net	**(158)**	**(213)**	**(260)**	**(309)**	**(940)**
Net loss before income taxes and cumulative effect of accounting change	**(2,419)**	**(2,820)**	**(1,382)**	**(2,520)**	**(9,141)**
Income taxes	**—**	**—**	**—**	**—**	**—**
Cumulative effect of accounting change	**—**	**—**	**—**	**(448)**	**(448)**
Net loss	**$(2,419)**	**$(2,820)**	**$(1,382)**	**$(2,968)**	**$(9,589)**
Per share amounts:					
Loss before cumulative effect of accounting change	**$(.08)**	**$(.09)**	**$(.04)**	**$(.07)**	**$(.28)**
Cumulative effect of accounting change	**—**	**—**	**—**	**(.01)**	**(.01)**
Net loss	**$(.08)**	**$(.09)**	**$(.04)**	**$(0.08)**	**$(.29)**
Weighted-average shares outstanding	**30,500**	**33,061**	**34,237**	**35,328**	**33,206**

The fourth quarter of 2000 reflects impairment charges of $1,362,000 due to the write-off of certain Web development costs of the Internet Web site, BUZZTIME.com, and Internet game stations equipment, license and related goodwill.

	Three-Month Period Ended				
	March 31, 1999	**June 30, 1999**	**September 30, 1999**	**December 31, 1999**	**Total 1999**
Total revenue	$5,687	$5,811	$5,887	$6,363	$23,748
Total operating expenses	6,350	6,065	7,385	7,749	27,549
Operating loss	(663)	(254)	(1,498)	(1,386)	(3,801)
Other income (expense), net	(169)	(220)	2,005	(313)	1,303
Net loss before income taxes	(832)	(474)	507	(1,699)	(2,498)
Income taxes	—	—	—	—	—
Net loss	$(832)	$(474)	$507	$(1,699)	$(2,498)
Net loss per share	$(.03)	$(.02)	$.02	$(.06)	$(.09)
Weighted-average shares outstanding	27,875	28,249	28,573	29,167	28,470

The third quarter of 1999 included a gain of $2,254,000 related to the sale of the assets of NTN's wholly-owned subsidiary, IWN, L.P., to eBet Limited for $1,227,000 in cash and 4,000,000 shares of eBet Online stock.

Market for Registrant's Common Equity and Related Stockholder Matters

Our common stock is listed on the American Stock Exchange ("AMEX") under the symbol "NTN." Trading of our redeemable common stock purchase warrants, listed under the symbol "NTN/WS," commenced on the AMEX in February 1998 and expired on February 20, 2001. Set forth below are the high and low sales prices for the common stock and warrants as reported by the AMEX for the two most recent fiscal years:

	Common Stock		Warrants	
	Low	**High**	**Low**	**High**
2001				
First Quarter (through 3/14/01)	$0.5000	$1.2000	$—	$—
2000				
First Quarter	$2.5000	$6.5000	$2.7500	$5.5000
Second Quarter	$1.9375	$4.3750	$1.1250	$3.3750
Third Quarter	$2.1875	$3.1250	$0.7500	$2.2500
Fourth Quarter	$0.5625	$2.5000	$1.5000	$0.0630
1999				
First Quarter	$0.5625	$2.0000	$1.3750	$2.5000
Second Quarter	$0.6250	$1.0000	$1.8750	$2.2500
Third Quarter	$1.0625	$1.3750	$2.0630	$2.6250
Fourth Quarter	$1.1875	$4.7500	$2.5000	$3.8130

On March 14, 2001, the closing price for our common stock as reported on the AMEX was $0.70. As of March 14, 2001, there were approximately 1,863 holders of common stock.

To date, we have not declared or paid any cash dividends with respect to our common stock, and the current policy of our Board of Directors is to retain earnings, if any, after payment of dividends on the outstanding preferred stock to provide for our growth. Consequently, no cash dividends are expected to be paid on our common stock in the foreseeable future. Pursuant to the terms of our line of credit, we may not pay or declare dividends without the prior written consent of the lender.

BUZZTIME™

BUZZTIME, Inc., NTN Communications' wholly owned content subsidiary, is focused on leveraging its extensive content library and interactive television studio to build business relationships within the ITV industry that will result in in-home distribution and a scalable revenue model. With over 15 years of programming made specifically for ITV, BUZZTIME is poised to become the leading game channel on interactive cable television systems. BUZZTIME's revenue will come from cable subscribers, cable operators and advertisers. The BUZZTIME interactive game channel will be sold as a premium cable channel to subscribers or included in a larger ITV programming bundle of services sold by the cable operator.

Industry experts predict that 40 million households will engage in ITV by 2005, with projected subscription and advertising revenues in the billions of dollars (Jupiter, Nielsen). Specifically, "advergaming" revenue – embedded advertising messages within interactive games – is expected to reach $1 billion in 2005. Games will be a major revenue driver, as 32% of consumers show a preference to ITV games and quizzes (MediaPost).

Through existing ITV development and distribution agreements with AT&T Broadband, Microsoft and Sun Microsystems, BUZZTIME is insuring that our channel will be accessible regardless of what ITV technology platforms become standards. We will continue to build the relationships with these key drivers of ITV programming and optimize our content for each platform. In the coming year, look for more partnerships to expand distribution and market trials to prove the BUZZTIME revenue model.

NTN Network®

As the clear market leader in providing engaging, interactive entertainment to the out-of-home hospitality market, we feel greater opportunities exist by leveraging this leadership position among our network of 3,500 sports bars, restaurants, taverns and hotels to the over 250,000 target hospitality locations in the United States alone.

We intend to reach our objectives in the coming year by focusing on four key initiatives.

First, grow revenue through site sales while increasing revenue per site. We will achieve this by concentrating sales and service in the major metropolitan markets with the highest per capita hospitality penetration in an effort to achieve 4,000 locations by year-end, as well as by adding new programs that provide incremental value to our subscribers.

Second, grow our Network advertising business. Delivering over 6 million unique consumers each month, the NTN Network provides a highly targeted, integrated marketing solution for brands looking to reach the active, out-of-home consumer, and will remain a core element of our business.

Third, expand our core trivia and sports content with new offerings. Augmenting our proven, highly popular interactive programs with a focused yet steady flow of new entertainment options will grow the universe of game play within the network to include not only our loyal player base, but also an entirely new group of entertainment-seeking consumers.

Finally, increase our marketing and promotional efforts. Expanding the level of prizing, competitions, and on-premise cross-promotion as well as continuous exposure to the brand will serve to create constant awareness and interest in the camaraderie aspects of our experience – the unique sense of community that keeps our players coming back and spending more.

V. Tyrone Lam
President, BUZZTIME, Inc.

Mark deGorter
President and Chief Operating Officer, NTN Network

Corporate Directory

Board of Directors
Stanley B. Kinsey
Chairman of the Board, Director and Chief Executive Officer, NTN Communications, Inc.

Robert M. Bennett
Chairman of the Board, Bennett Productions, Inc.

Barry Bergsman
President, Intertel Communications, Inc.

Esther Rodriguez
Chief Executive Officer, Rodriguez Consulting Group

Vincent A. Carrino
Founder and President, Brookhaven Capital Management, LLC

Gary Arlen
President, Arlen Communications, Inc.

Corporate Officers
Stanley B. Kinsey
Chief Executive Officer

James B. Frakes
Chief Financial Officer

V. Tyrone Lam
President, BUZZTIME, Inc.

Mark deGorter
President and Chief Operating Officer, NTN Network

Independent Certified Public Accountants
KPMG LLP
750 B Street
San Diego, California 92101

Transfer Agent
American Stock Transfer & Trust Company
59 Maiden Lane
New York, New York 10038

Corporate Counsel
O'Melveny & Myers LLP
400 South Hope Street
Los Angeles, California 90071

Executive Offices
NTN Communications, Inc.
5966 LaPlace Court, Suite 100
Carlsbad, California 92008-8830
Tel 760.438.7400
Fax 760.438.7470

For More Information
Investor Relations Manager
760.438.7400
investor@ntn.com

NTN™ AMEX LISTED

Listed on The American Stock Exchange®
Symbol: NTN

Annual Meeting
The 2001 Annual Meeting of NTN shareholders will be held at 10:00 am on June 29, 2001 at:

La Costa Resort
Costa Del Mar Road
Carlsbad, California 92009

Owners of common stock as of May 1, 2001, the record date of the meeting, will be eligible to vote on matters brought before the meeting.