

airline tickets



hotel rooms



rental cars



home financing



new cars

priceline.com℠

Name Your Own Price℠

annual report 1999

priceline.com™

800 Connecticut Avenue, Norwalk, Connecticut 06854

“Millions of people... feeling as if they’ve won something when they get their price. And what have they won?

Power.

Freedom.

Control.

It’s priceline.com, man. It’s a natural high.”

–William Shatner, actor, icon, starship captain and priceline.com spokesman

“If saving money is wrong, I don’t want to be right.”

–William Shatner, actor, icon, starship captain and priceline.com spokesman

priceline.com™

Dear Shareholder,

This, our first annual report, gives us a chance to welcome you, our shareholders, and provides an opportunity to more thoroughly discuss the theory and workings of our unique business model.

1999 was a milestone year for our company. In our first full year of operation - and our first full year as a public company – priceline.com became firmly established as one of the leading and fastest growing companies on the Internet. Both consumer and business response to the priceline.com system has been gratifying. And yet, following our strong start, we are confident that our future prospects are even more exciting.

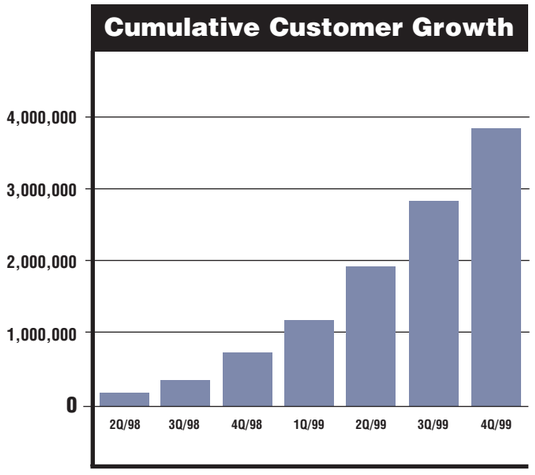


Dan Schulman, President and COO
Richard Braddock, Chairman and CEO

Jay Walker talks more about the theory of the priceline.com business in the following letter, but it is important to note that our distinctive business proposition, uniquely fit to the Internet, is at the core of our early success. We offer important benefits to both buyers and sellers. Our consumers are truly empowered as they use the Internet to name their own price for goods and services, thereby generating savings in pursuit of a "better life". Businesses are able to use our unique pricing system to sell

excess or perishable inventory anonymously, and therefore without affecting their traditional retail prices. In most respects this represents incremental, and therefore highly profitable, business for them.

We view the dramatic growth of our customer base as perhaps our most significant accomplishment in 1999. Our customers grew from 700,000 at the beginning of the year to nearly four million unique users by year-end. Indeed, the growth in that customer base continues to accelerate and now, together with our licensees, exceeds over five million users.



We also continued to build equity in the priceline.com brand, which we view as the major long-term differentiator of priceline.com. Based on independent consumer research, fully two-thirds of all American adults are familiar with the priceline.com Name Your Own Price℠ brand, a level of awareness exceeded only by AOL, Yahoo and amazon.com among Internet companies. Today, priceline.com and amazon.com are in a statistical dead-heat as the number-one most-recognized e-commerce brand. And our awareness is growing even faster since the recent introduction of our first TV campaign.

We deliver on the promise of the priceline.com brand by providing substantial savings to our customers while generating incremental revenue and profitability for our seller partners. Across our many services, from airline tickets to home mortgages to the groceries sold through our licensee, Priceline WebHouse Club, consumers realize substantial savings by agreeing to be flexible while using our Name Your Own Price℠ service. And our seller partners generate incremental revenue without diluting their full price sales, because they offer their products and services behind the priceline.com brand shield.

Brand Awareness Chart

Company	9/98 %	4/99 %	8/99 %	February 2000 %	February 2000 Adults
AOL	79%	83%	88%	**87%**	**170 mm**
Yahoo	51%	70%	76%	**81%**	**159 mm**
Amazon	37%	52%	60%	**69%**	**135 mm**
Priceline	**32%**	**46%**	**55%**	**66%**	**130 mm**
Netscape	49%	58%	65%	**64%**	**125 mm**
eBay	6%	32%	46%	**60%**	**118 mm**
E* Trade	13%	30%	44%	**56%**	**110 mm**
eToys	n/a	22%	26%	**46%**	**91 mm**
Earthlink	n/a	n/a	n/a	**46%**	**91 mm**
MSN	24%	35%	39%	**44%**	**87 mm**

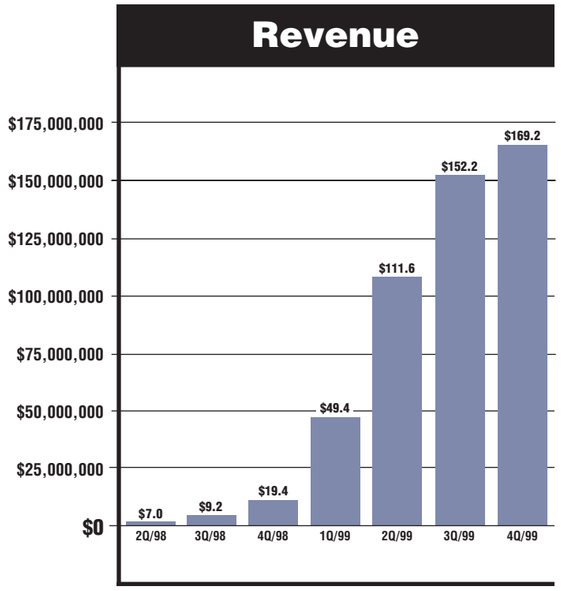
Source:Opinion Research Corp.

As we proved the validity and power of the priceline.com business model, we dramatically increased our results in all of our products and services. Airline ticket sales grew from less than 10,000 tickets per week at the beginning of the year to approximately 70,000 tickets per week by year-end, and have exceeded 100,000 in several weeks early in the new year.

Hotel room night reservations increased even more dramatically, from about 1,000 room nights per week at the beginning of the year to approximately 17,000 room nights per week by year-end and in excess of 30,000 more recently. Our new car sales and home financing services also grew

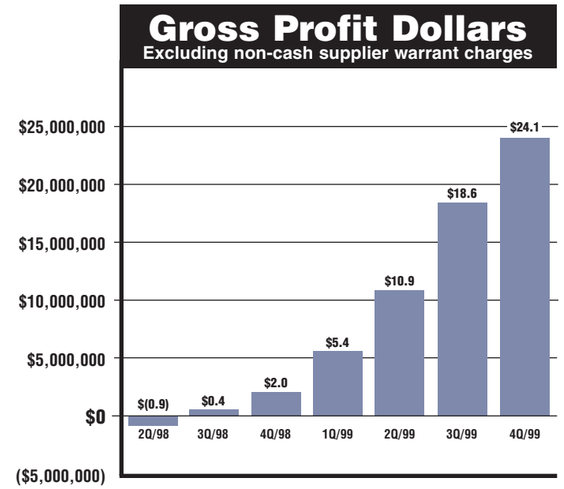
rapidly during the course of 1999. And our momentum continues to build, with each of our product lines' performance currently exceeding their 1999 peaks.

We achieved these results in large part because our seller partners are convinced that priceline.com offers them a unique way to improve sales and profitability. During 1999 we added the full participation of American, Continental, Northwest, United and US Airways. They joined Delta, America West and TWA, so that priceline now enjoys the participation of eight domestic major full service airlines, which provide priceline.com Name Your Own Price℠ customers with access to 84 percent of all unsold seats. Our seller networks in our other services also expanded significantly during the year.



Also during 1999, we leveraged our infrastructure and experience in support of our growth and to reduce the time it takes to launch new products and services. For example, while it took a full year to develop and launch priceline.com's airline ticket service, our rental car product was introduced in a span of 90 days.

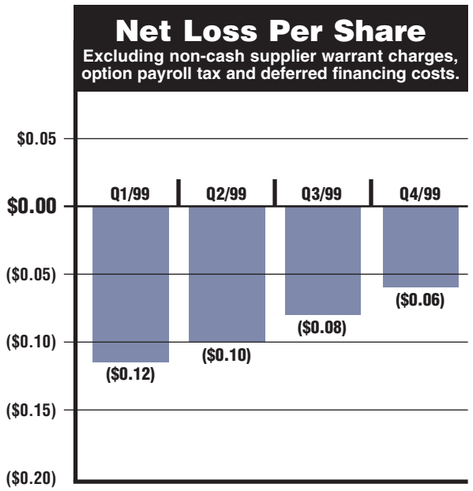
With a growing complement of services and a firm commitment toward profitability, priceline.com demonstrated the power of its financial model in 1999. We had revenue of $482 million in our first full year of operation, and gross profit dollars also increased sharply during the year, reaching $24 million in the fourth quarter (before non-cash supplier warrant charges). Our fourth quarter gross margin (before non-cash supplier warrant charges) of 14.2% set a record for priceline.com. In contrast to many Internet companies, financial discipline and a commitment to achieving steady progress toward profitability are priorities for priceline.com. We reduced operating losses (excluding special charges) in each quarter after making a commitment to steadily decreasing losses at the end of the first quarter of 1999 and expect to continue that progress during the year.



Our other major financial highlight during 1999 was, of course, priceline.com's initial public offering in March 1999. Priceline.com sold 10 million shares at a price of $16.00 per share in an offering that was widely regarded as one of the most successful IPOs in 1999. We are grateful to our shareholders for making it possible.

In order to take advantage of the many opportunities to expand the priceline.com brand and business, we also adopted a flexible business development model during 1999 which allows

us to pursue, in parallel, multiple new offerings across our horizontal model. One aspect of this strategy involved the licensing of the priceline.com name and business model to an independent company called the Priceline WebHouse Club in return for a royalty arrangement and a fully vested, non-forfeitable warrant to acquire a majority of the equity of the WebHouse Club that is exercisable under certain conditions. The Priceline WebHouse Club commenced operations in the New York metropolitan area in November 1999 with a unique consumer proposition – consumers price their own groceries at our Web site and then pick up their items at participating retailers – and has been expanding rapidly since.



As we look forward to 2000, we are excited by our prospects. We have already launched our rental car service, and will soon launch a long distance service. We have also licensed the priceline.com name and business model to Priceline Perfect YardSale, which is beta testing a Name Your Own Price℠ service for used goods in the Atlanta market. And we have announced licensee arrangements in Australia and Asia in conjunction with local operating investors. We plan to offer a range of new services and improvements of existing products and services throughout the year. Our publicly-stated goals include achieving at least $1 billion in revenue while expanding our customer base to at least 10 million unique users during the year, including customers of licensee companies.

All of this is made possible by the extraordinarily dedicated team of people who work at priceline.com. We have continued to add new talent to an already strong management team. So far in 2000, we have added a new General Counsel (Jeff Boyd, formerly the General Counsel of Oxford Health Plans), a new Chief Marketing Officer (Michael McCadden, formerly Executive Vice President of Marketing at Gap) and Heidi Miller (formerly the Chief Financial Officer of Citigroup) as our new Senior Executive Vice President, Strategy, Planning and Administration, and Chief Financial Officer. Ours is a management team which can continue to pace our growth as we aim to become a multi-billion dollar corporation in the near future.



Heidi Miller,
Senior Executive Vice President and CFO

We take great pride in all of priceline.com's accomplishments in 1999, but know that this is just the beginning. We are committed to building a great business and a profitable company that will make a real difference for our customers, seller partners, employees and shareholders. Thank you for your support.

Sincerely,

Richard Braddock
Chairman and CEO

Dan Schulman
President and COO

See "Management's Discussion and Analysis of Financial Condition and Results Operations" and "Information Regarding Forward Looking Statements".

vision

Dear Shareholder:

When I began to work on the idea of priceline.com years ago with a team of inventors at Walker Digital Corporation, my goal was to use the power of the Internet to fundamentally change the way in which many goods and services were priced and sold. Our team of inventors recognized that the Internet enabled consumers for the first time to communicate efficiently to sellers their preferences and true elasticity of demand. The first big idea of priceline.com was that consumers would express flexibility and accept trade-offs (including substitutability among quality brands) if they could realize substantial savings. To demonstrate that this consumer demand was not only flexible but serious, priceline.com required that every offer be guaranteed by a credit card, which would be charged as soon as priceline.com could find a seller willing to meet the customer's conditions.

At the same time, we realized that sellers would often sell their goods or services at below their published retail prices if they could do so without disrupting their retail price structure or existing distribution channels. The second big idea of priceline.com was that the flexibility priceline.com demanded of consumers created a "brand shield", which enabled priceline.com's seller partners to generate incremental sales and profits by accepting offers at below the sellers' retail price. To support this brand and retail price shield, priceline.com would not identify the particular brand being purchased until the offer was accepted and never publish the price at which offers were accepted.

When we launched priceline.com on April 6, 1998 with the sale of leisure airline tickets, no one knew whether consumers would, in fact, participate in a Name Your Own Price℠ program. And no one knew if sellers would, in fact, participate in such a program. Now, more than five million guaranteed offers later from



Jay S. Walker, Founder and Vice Chairman

customers for products ranging from airline tickets to home mortgages to everyday items, we know that consumers will express flexibility in order to get their own price. And with the participation of the top eight major full service airlines and significant participation in other industries that priceline.com serves, we know that seller partners will join priceline.com to accept this guaranteed demand, generally at prices well below the retail "price line."

As Rick Braddock and Dan Schulman described in more detail, priceline.com is already a major force in the travel industry and promises to have a similar effect in the other sectors of the economy in which we plan to participate. Indeed, I believe that the priceline.com business model will find applications in most sectors of the economy, from the most significant purchases in a consumer's life, such as a new car, a home mortgage or a vacation, to everyday purchases such as groceries or gasoline. If we can execute on our vision for priceline.com, I believe we can become one of the largest companies not just on the Internet, but in the domestic and even the international economy.

This is an expansive vision, and I know that we are only at the beginning of our journey. But when I think of how far we have come in the last two years, and the quality of the management team that is dedicated to realizing this dream, I am confident that we can achieve our goals.

Priceline.com has always operated on the premise that if we are to succeed in the long run, we would have to serve the interests of both our customers and our seller partners. To that, I would add the need to also serve the long-term interests of our shareholders. I want to thank you as shareholders, and our customers, seller partners and employees as well, for your confidence in us. We have a unique opportunity to build a truly great business, and we will continue to work tirelessly to achieve that goal.



Jay S. Walker
Founder and Vice Chairman

airline tickets



a highly scalable business model

When priceline.com opened the virtual doors for its airline ticket business on April 6, 1998, the new service sold a mere 47 tickets in the first 24 hours. Still, priceline.com's management team knew that the Company's demand collection model had tremendous scalability. With the significant savings priceline.com can deliver, widespread consumer acceptance was just around the corner.

In early 1999, less than a year after that 47-ticket day, priceline.com sold a record 10,000 tickets in 24 hours, proving the rapid scalability of the model. By the end of the year, 60,000 and 70,000-ticket weeks were not uncommon.

"Traveling with a family of four can be expensive. I've used priceline.com twice in the last two months for my entire family and saved over $1,500. I've already told several others about the great savings."

–Garth Carlson, priceline.com airline service customer

"Priceline.com is an extremely effective sales tool for participating airlines. During 1999, we grew from three to eight major full-service U.S. airlines and 20 international carriers participating in our program, representing the majority of seats flown domestically."

–Tim Brier, President,
priceline.com Travel Services

hotel rooms



"I have used priceline.com for approximately eight hotel rooms in the past six months. I'm always able to get high quality for low rates with priceline.com."

– Steve Boddeker, priceline.com hotel service customer

here a hotel, there a hotel

Every night, hundreds of thousands of U.S. hotel rooms sit empty. Priceline.com's aim in 1999 was to make a dent in that statistic by offering one of the industry's most expansive hotel products, supported by targeted advertising. While most online hotel services remained focused on the nation's top cities, priceline.com expanded to cover over 1,100 cities, towns and resort destinations in all 50 states. The service also developed an inclusive selection of properties from one-star to the most luxurious five-star hotels.

The combination of broad geographic coverage, a deep group of participating hotels and priceline.com's familiar Name Your Own Price℠ concept drove demand and sales to new records in 1999. Over the course of the year, weekly bookings grew from 1,000 room nights a week to 17,000 room nights weekly. In one recent three week period, priceline.com launched a marketing campaign in support of hotels and increased sales an additional 129 percent.

"Priceline.com has shown that we can take a business and, through aggressive service enhancements and marketing, grow it dramatically. Our goal is to eventually occupy one of the top three positions in every industry we service."

–Michael McCadden, Executive Vice President and Chief Marketing Officer, priceline.com

rental cars

speeding new products to market

One of the benefits of an Internet-based business is the ability to utilize existing computer and software infrastructures and development technology to speed the introduction of additional products and services. In 1999, this was a critical factor behind priceline.com's continued horizontal expansion into new product areas.

In 1998, it took 12 months to develop and launch priceline.com's first service for airline tickets. Later that year, the Company cut its average development time in half, bringing its hotel service to market in six months. By 1999, priceline.com developers again halved the Company's new product cycle by developing and deploying a new rental car service in just 90 days. This increased speed to market also enabled priceline.com to shorten its timeline to gross profits from one year for airline tickets to 30 days for rental cars. Priceline.com is now in a position to introduce more new services on an annual basis than it could less than two years ago.



"I travel on business frequently and our corporate travel agent makes the reservations. After they priced the rental car for my recent trip, I wanted to see if I could improve my position without costing the company any more money. With priceline.com, I got a luxury car for less than my boss paid for an intermediate car."

–Bruce Kamp, priceline.com rental car customer

"We're building upon our past successes and leveraging priceline.com's experience and infrastructure to bring new products and services to market even faster. This powerful combination has enabled us to significantly reduce our development-to-launch timeline from 12 months for our airline product to just 90 days for rental cars."

–Ron Rose, Chief Information Officer, priceline.com

home financing

building trust through superior service

With a home mortgage being the largest and most important purchase in a consumer's life, trust is an integral part of the loan process. Priceline.com recognized that the traditional online loan process often didn't live up to that promise by forcing consumers to apply for a mortgage, then wait days or weeks to see if they could actually get the rate and terms they were quoted.

In 1999, priceline.com fundamentally changed the online mortgage landscape by licensing its business model to a newly created entity called PricelineMortgage – the first Internet service that allows consumers to name their own terms for a loan and, in a matter of hours, receive locked-in rates and guaranteed low closing costs. As the year progressed and more consumers discovered PricelineMortgage, applications through the service more than tripled. After test marketing the new service in Florida and New York in 1999, priceline.com expanded the PricelineMortgage service nationwide in the first quarter of 2000.



"Everyone I dealt with was perfect, but the beauty of it was that I hardly had to talk with anyone because I used the Internet. Obtaining my mortgage through priceline.com can't compare to the previous, traditional way of getting a mortgage. Priceline.com was far better! I was very, very pleased!"

—Michael Rupolo, priceline.com mortgage service customer

"Consumers using PricelineMortgage don't have to worry about fluctuating interest rates because, for the first time, they can name their own terms at priceline.com, get guaranteed low closing costs and lock in their own rates in as little as 30 minutes."

–Ben Ness, Senior Vice President, Financial Services, priceline.com

new cars



"(Priceline.com) empowers us – to use a word of the 90s – to make our own decisions, to stand our own ground, to get what we want when we want it."

–Tracy O'Such, priceline.com new car customer

revolutionizing new car buying

Priceline.com puts consumers in the driver's seat in a way no other online car buying service can. Using priceline.com, new car buyers specify the exact vehicle they want right down to the option packages. Then they set their price and let priceline.com do the shopping.

Keeping the consumer's identity protected, priceline.com works to find a local new car dealership willing to sell the vehicle at the consumer's price. No dinnertime sales calls. No haggling. Priceline.com makes it possible for every consumer to have the same chance to get a great deal on a new car – quickly and easily. Priceline.com's new car service is available in most states today and will expand nationwide by mid-2000.

"Priceline.com dramatically changes the car-buying process in ways that benefit new car buyers and dealerships. Car buyers can get their price without the stress associated with traditional car buying. Meanwhile, dealerships know they're getting serious, guaranteed buyers and can sell vehicles with an absolute minimum of up-front work."

–Maryann Keller, President,
priceline.com Automotive Services

the future

priceline.com – a big idea positioned for future growth

This past year provided essential building blocks upon which priceline.com intends to grow over the coming year. We see this growth focusing on several key areas.

New Services

In the next 12 months, priceline.com will add a range of new Name Your Own Price℠ services for long-distance telephone service, vacation packages, cruises, life and automotive insurance and credit cards. Meanwhile, priceline.com's new car and home mortgage services both will expand to full national coverage. Priceline.com's licensee, the Priceline WebHouse Club, will broaden its retail categories to include Name Your Own Price℠ gasoline. In addition, priceline.com intends to commence offering a line of business-to-business services during 2000.

Priceline.com International

In early 2000, priceline.com announced two new initiatives to introduce Name Your Own Price℠ services in Asia and Australia/New Zealand. In addition, priceline.com expects to announce in the future similar international plans for Europe, Japan and Latin America.

Continued Progress Toward Profitability

Priceline.com is committed to growing its customer and revenue bases while making steady progress toward profitability. We remain confident that we are well on our way to delivering a scalable and profitable business for our business partners and our shareholders.

"We are well on our way to creating a highly scalable, profitable business for our shareholders."

– Richard Braddock, Chairman and CEO, priceline.com

SELECTED FINANCIAL DATA

The selected financial data presented below are derived from the financial statements of the Company, and should be read in connection with those statements, which are included herein. All share and per share amounts have been retroactively adjusted to reflect the 1.25:1 stock split during 1999.

	Year Ended December 31,		July 18, (inception) to December 31,
	1999	1998	1997
	(In thousands, except per share amounts)		
Statement of Operations Data:			
Revenues	$ 482,410	$ 35,237	
Cost of revenues:			
Product costs	423,056	33,496	
Supplier warrant costs	1,523	3,029	
Total cost of revenues	424,579	36,525	
Gross profit	57,831	(1,288)	
Operating expenses:			
Warrant costs, net	998,832	57,979	
Sales and marketing	79,577	24,388	$ 441
General and administrative (including $1,812 of option payroll taxes in 1999)	27,609	18,004	1,012
Systems and business development	14,023	11,132	1,060
Total operating expenses	1,120,041	111,503	2,513
Operating loss	(1,062,210)	(112,791)	(2,513)
Other income (expense)	7,120	548	
Net loss	(1,055,090)	(112,243)	(2,513)
Accretion on preferred stock	(8,354)	(2,183)	
Net loss applicable to common shareholders	$(1,063,444)	$(114,426)	$(2,513)
Net loss applicable to common shareholders per basic and diluted common share	$ (7.90)	$ (1.41)	$ (.05)
Weighted average number of basic and diluted common shares outstanding	134,622	81,231	50,834

	As of December 31,		
	1999	1998	1997
		(In thousands)	
Cash and cash equivalents and short-term investments	$ 171,943	$ 53,593	$ 16
Working capital	172,489	49,922	(2,389)
Total assets	441,886	66,572	1,449
Long-term obligations		1,015	51
Total liabilities	39,250	11,296	2,706
Total stockholders' equity	402,636	55,276	(1,257)

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

Priceline.com has pioneered a unique e-commerce pricing system known as a "demand collection system" that enables consumers to use the Internet to save money on a wide range of products and services while enabling sellers to generate incremental revenue. Using a simple and compelling consumer proposition—Name Your Own Price℠—we collect consumer demand, in the form of individual customer offers guaranteed by a credit card, for a particular product or service at a price set by the customer. We then either communicate that demand directly to participating sellers or access participating sellers' private databases to determine whether we can fulfill the customer's offer. Consumers agree to hold their offers open for a specified period of time and, once fulfilled, offers cannot be canceled. We benefit consumers by enabling them to save money, while at the same time benefiting sellers by providing them with an effective revenue management tool capable of identifying and capturing incremental revenues. By requiring consumers to be flexible with respect to brands, sellers and product features, we enable sellers to generate incremental revenue without disrupting their existing distribution channels or retail pricing structures.

Priceline.com was formed in July 1997 and our primary activities during the period prior to launch consisted of recruiting and training employees, developing our business model, implementing systems to support our business model, developing relationships with seller participants and developing the priceline.com brand. We commenced operations in April 1998 with the sale of leisure airline tickets. Since that time, our business has grown significantly and the priceline.com service includes the following products and services:

- leisure airline tickets, provided by ten domestic and 20 international airline participants;
- hotel rooms, which was launched in October 1998, in substantially all major United States markets with more than 15 leading national hotel chains as participants;
- rental cars, which was launched in December 1999, in substantially all major United States markets with three leading rental car chains as participants;
- new automobiles, which was launched on a test basis in the New York metropolitan area in July 1998 and is now offered in 26 states;
- home financing services, which was launched in January 1999 with home mortgage services and now also includes home equity loans and refinancing services.

Priceline.com also is currently planning an expansion of its core Name Your Own Price℠ business model to other areas of e-commerce, including long distance telephone service, cruises and vacation packages.

Through the innovative use of "adaptive marketing programs," priceline.com also markets customer acquisition programs for third parties. These programs facilitate the completion of a higher percentage of successful transactions through the priceline.com service, while generating fee income for the Company. During 1999, the Company increased its number of adaptive marketing partners from one to ten, thus reducing its dependence on any one partner. Priceline.com intends to continue to add adaptive marketing programs so that consumers have a variety of programs from which to choose and priceline.com has a diversified source of adaptive marketing revenues.

Priceline.com has announced several transactions pursuant to which third parties ("Licensees") license the priceline.com name and demand collection system for offering a particular product or service or for offering a number of products or services in a distinct international region. Pursuant to the Licensee transactions, priceline.com generally receives a royalty under the license and may also

receive fees for services and reimbursement of certain expenses. Priceline.com also holds convertible debt or warrants entitling it to acquire a significant percentage of such Licensee's equity securities upon the occurrence of certain events. Unless such equity securities are converted, the results of Licensees will not be included in priceline.com's financial results.

In 1999, priceline.com licensed its name and demand collection system to Priceline WebHouse Club, Inc. ("WebHouse") and agreed to provide certain services to WebHouse. WebHouse offers a Name Your Own Price℠ service for groceries and has announced the planned offering of a service for gasoline. Under the negotiated agreements, priceline.com receives a royalty based on a percentage of WebHouse revenues and compensation at fair value for certain services rendered. As an inducement to enter into a relationship with WebHouse, priceline.com received a warrant to purchase a majority of the shares of WebHouse common stock. The warrants are non-forfeitable, fully vested upon grant, exercisable in five years or earlier upon the occurrence of certain events, and do not require the performance of any additional services. Upon receipt of the warrant in the fourth quarter, priceline.com recognized $188.8 million of income representing the amount of the estimated fair value of the warrants, based on an independent valuation.

In March 2000, the Company entered into an agreement with Alliance Capital Partners, pursuant to which Alliance has formed an operating subsidiary, Priceline Mortgage, for the primary purpose of acting as a broker and/or lender of residential mortgage loans in connection with the priceline.com mortgage service. Priceline.com has agreed to provide $3.62 million of financing to an affiliate of Alliance in the form of a convertible secured note and has agreed to license the "priceline" name and business model for use by Priceline Mortgage. Alliance has agreed to provide management services to Priceline Mortgage, including the procurement of personnel and office space and assistance in obtaining regulatory approvals. A pilot program was launched in early October 1999 and currently is operating in all 50 states.

Because the priceline.com system does not set minimum offer thresholds, and consumers are not charged to make offers for its products, it is expected that we will receive a significant number of unreasonable or "fantasy offers". Accordingly, in addition to analyzing our actual fulfillment rates, we also analyze the percentage of "reasonable" offers that we are able to fill. We consider an offer for an airline ticket, hotel room or rental car to be "reasonable" when it is no more than 30% lower than the lowest generally available advance-purchase fare for the same product. Using this standard, the overall percentage of offers considered reasonable for the year ended December 31, 1999 was approximately 57.0%. The Company measures its "bind" rate as the percentage of reasonable offers that the Company ultimately fulfills. The Company's bind rate for 1999 was 43.6% for all reasonable airline ticket, hotel room and rental car offers.

When making offers for airline tickets through the priceline.com service, consumers are permitted to make only one offer within a seven day period unless they change some feature of their itinerary, such as the date on which or the airport from which they are willing to fly. As a result of the Company's "checkstatus" feature, introduced in April 1999, consumers whose initial requests are not satisfied are permitted to resubmit revised offers that reflect at least one change to their itinerary. Effective with this change, each initial offer and any resubmitted offers are treated as a single offer for purposes of measuring our total offer volume and our offer fulfillment rates. Previously, each had been counted as a separate offer. Therefore, comparisons with prior periods may not be meaningful.

As of December 31, 1999, the Company had an accumulated deficit of $1.18 billion, of which $1.07 billion related to certain non-cash charges arising from equity issuances to a number of participating airlines, its chief executive officer and other parties, as more fully described below, partially offset by the WebHouse warrant income described above. Priceline.com believes that its continued growth will depend in large part on its ability to continue to promote the priceline.com brand and to apply the priceline.com business model to a wide range of products and services.

Priceline.com intends to continue to invest heavily in marketing and promotion, technology and personnel. As a result, it expects to incur additional losses. However, the Company's plans call for reduction of operating losses and improvement in its gross margins in an effort to achieve profitability. Priceline.com's limited operating history makes the prediction of future results of operations difficult, and accordingly, there can be no assurance that it will achieve or sustain revenue growth or profitability.

As of December 31, 1999, the Company had outstanding non-qualified stock options to purchase 27,024,740 shares issued to various employees, consultants and directors pursuant to the Company's 1997 Omnibus Plan and 1999 Omnibus Plan. The options entitle the holders to purchase common stock at a weighted average exercise price of approximately $13.93 per share, subject to adjustment in accordance with the 1997 Omnibus Plan and the 1999 Omnibus Plan. Upon exercise of an option, priceline.com will be required to make payments on behalf of the option holders for certain payroll taxes such as Social Security and Medicare. These payroll taxes will appear as a general and administrative expense on priceline.com's statement of operations and will amount to approximately 1.5% to 2.0% of the difference between the exercise price and the then fair market value of the common stock at the time of exercise. However, upon exercise of outstanding options, priceline.com will be paid the exercise price of the options that are exercised. The total exercise price of the options outstanding at December 31, 1999 is $376.5 million. Priceline.com also will be entitled to an income tax deduction equal to the sum of (1) the difference between the exercise price of the option and the then fair market value of the common stock at the time of exercise and (2) the total amount of payroll tax payments. Such deduction would be utilized to the extent that the Company generates taxable income. The calculation of the payroll tax expense and income tax deduction, and the timing of those events and the receipt of the related cash inflow, is directly dependent upon the exercise of options and the value of shares of priceline.com Common Stock at the time of exercise. As the decision to exercise options is at the sole discretion of the holder of the options, the timing and amount of the expense, income tax deduction and timing of the cash inflows cannot be estimated.

During July 1999, priceline.com issued to Continental Airlines a warrant to purchase common stock that will become exercisable upon the earlier of July 2004 or upon the achievement of certain performance thresholds. However, the agreement does not require Continental to make any performance commitments. Accordingly, priceline.com incurred a non-cash charge of approximately $88.4 million during the third quarter of 1999 representing the fair value of the warrant on the grant date. In November 1999, the Company amended the Continental warrant to allow the exercise price to fall within the range of the warrants issued to other airlines discussed below. Priceline.com incurred a non-cash charge of approximately $3.5 million during the fourth quarter as a result of the warrant amendment.

In August 1998, priceline.com entered into a warrant agreement granting Delta Airlines (''Delta'') the right to purchase up to 18,892,603 shares of common stock at an exercise price of approximately $0.93 per share. Vesting was contingent upon achievement of certain predetermined performance thresholds. However, there was no penalty for failure to provide ticket inventory to satisfy these performance thresholds. Accordingly, no expense was recorded when the warrant was issued. On December 31, 1998, priceline.com amended its agreement with Delta to eliminate the vesting contingencies and fix the number of shares subject to the warrant at 18,619,402. The amended warrant issued to Delta became exercisable at the earlier of seven years or upon the achievement of certain performance thresholds. However, the agreement did not require Delta to make any performance commitments, is non-exclusive and allows Delta to participate in other programs similar to the priceline.com service. Therefore, the Company recorded a non-cash charge of approximately $58.7 million, reflecting the fair value of the Delta warrant on December 31, 1998.

In November 1999, the Company further amended the Delta warrant to provide Delta with a cashless exercise right. Upon the exercise of the warrant, Delta acquired a total of 16,525,834 shares of

Common Stock of priceline.com. In conjunction with that transaction, Delta sold 2,085,767 shares of priceline.com Common Stock to priceline.com's founder and Vice Chairman Jay S. Walker for an aggregate purchase price of $125 million. The Company further gave Delta the right to exchange six million shares of priceline.com Common Stock for six million shares of newly issued convertible preferred stock that may be converted into priceline.com Common Stock on a one-for-one basis. To date, Delta has not elected to exercise the conversion right.

In November 1999, the Company entered into separate Participation Warrant Agreements with each of eight major domestic airlines relating to their inclusion in the Company's leisure airline ticket service. Under the Participation Warrant Agreements, the airlines were granted warrants to purchase a total of 20 million shares of priceline.com Common Stock at exercise prices ranging from $52.625 to $59.933 per share. All warrants were fully vested on the date of grant, but generally are not exercisable until November 2005, subject to acceleration under certain circumstances. Priceline.com incurred additional warrant costs of approximately $1.1 billion during the fourth quarter as a result of the issuance of the warrants.

Results of Operations

Priceline.com did not commence operations until April 1998. Accordingly, discussion of comparisons with the prior year is not meaningful.

Year Ended December 31, 1999

Revenues

	Year Ended December 31, ($000)		%
	1999	1998	Change
Revenues	$482,410	$35,237	1,269%

Revenues for the year ended December 31, 1999 were comprised primarily of: (1) transaction revenues representing the selling price of airline tickets, hotel rooms and rental cars; (2) fee income from adaptive marketing programs offered in connection with our product offerings; (3) ancillary revenues consisting primarily of Worldspan reservation booking fees and customer processing fees; and (4) fee income from our home financing and auto programs.

Revenues increased during 1999 as a result of the substantial development of our unique customer base, repeat purchases by existing customers and the inclusion of the hotel room, rental car, automobile, and home financing services and adaptive marketing programs. The Company has launched certain of its services in select geographic markets and then expanded to other regions. During 1999, the Company's hotel room reservation service expanded from 25 cities to nationwide coverage. The Company's auto program was launched in the New York City area and expanded to cover 26 states at December 31, 1999. The Company's rental car service was launched nationally during the fourth quarter. The Company currently plans to launch its products for long distance telephone services, cruises and vacation packages during 2000. The Company believes each of these products has the potential to increase revenues in 2000.

As of December 31, 1999 priceline.com had a base of approximately 3.8 million unique customers. A unique customer is defined as someone who has made a guaranteed offer for at least one of priceline.com's products. Of the total unique customer base, approximately 3.0 million made their first offer on priceline.com during 1999. During 1999, priceline.com customers made approximately 4.3 million offers for services.

Ancillary revenues for the year ended December 31, 1999 increased as a result of volume driven increases in Worldspan reservation booking fees and the introduction of a customer processing fee in the airline and hotel services. Fee-based income and ancillary revenues represented 8.4% of total revenues for the year ended December 31, 1999.

Product Costs and Gross Profit

	Year Ended December 31, ($000)		%
	1999	1998	Change
Product Costs	$424,579	$ 36,525	1,062%
% of Revenues	88%	104%	
Gross Profit	$ 57,831	$(1,288)	4,590%
Gross Margin	12.0%	(4.0)%	

For the year ended December 31, 1999, product costs were comprised of (1) the cost of airline tickets from our suppliers, net of the federal air transportation tax, segment fees and passenger facility charges imposed in connection with the sale of airline tickets; (2) the cost of hotel rooms from our suppliers, net of hotel tax; and (3) supplier warrant costs that represent a non-cash expense related to the issuance of common stock warrants to one of our airline program participants in January 1999. We anticipate that we will recognize additional non-cash supplier warrant costs in the amount of approximately $381,000 in each of the next four fiscal quarters.

Gross profit is comprised of revenues less cost of revenues. Excluding the effect of non-cash supplier warrant costs for the year ended December 31, 1999, the Company had gross profit of $59.4 million. During 1999, gross profit was positive as a result of the transactional sales volumes that were sold at positive margins, and the launch of products generating fee-based revenues. Because fee-based and ancillary revenues generally do not involve separate costs, these revenues had a disproportionately positive impact on total gross profit and made a substantial contribution to gross profit for the year ended December 31, 1999.

For the year ended December 31, 1999, gross margin increased each quarter as a result of increased sales volume, increased fee-based revenue and decreased sales of tickets that were sold below cost. Fee-based revenues, such as adaptive marketing revenues, ancillary revenues and revenues from financial services and automobiles generate higher margins than transaction revenues, on which the gross margin generated is derived from the spread between customer payments and product costs.

The Company expects that gross profit and gross margin will improve in the first quarter of 2000 as a result of anticipated consumer demand sufficient to allow the Company to increase revenues while selling its products at increasing positive margins. As a result of this anticipated growth, the Company expects the proportion of its gross profit and gross margin attributable to adaptive marketing revenues to decline.

Operating Expenses

Warrant Costs, Net

	Year Ended December 31, ($000)		%
	1999	1998	Change
Warrant Costs, Net	$998,832	$57,979	1,623%

Warrant costs, net consist of the fair value of warrants issued to airline suppliers during 1999, as discussed above. Such costs were partially offset by warrant income of $188.8 million recognized in the fourth quarter as a result of the receipt of warrants to purchase common stock of WebHouse.

Sales and Marketing

	Year Ended December 31, ($000)		%
	1999	1998	Change
Sales & Marketing	$79,577	$24,388	226.3%
% of Revenues	16.5%	69.2%	

Sales and marketing expenses for the year ended December 31, 1999 consisted primarily of: (1) advertising and promotions; (2) credit card processing fees; (3) fees payable to a third party service provider that operates priceline.com's call center; (4) compensation for priceline.com's sales and marketing personnel; and (5) provisions for customer charge-backs (based upon a percentage reflecting priceline.com's historical experience). The Company plans to continue to invest heavily in advertising and other marketing programs and expects that all marketing costs will increase. However, with the exception of processing fees and provisions for customer accommodations and charge-backs, which the Company anticipates will grow proportionately with transaction based revenue, the Company anticipates that the other marketing costs will decrease as a percentage of revenues as the result of anticipated revenue growth.

General and Administrative

	Year Ended December 31, ($000)		%
	1999	1998	Change
General & Administrative	$27,609	$18,004	53.3%
% of Revenues	5.7%	51.1%	

General and administrative expenses for the year ended December 31, 1999 were comprised primarily of compensation for personnel, fees for outside professionals, telecommunications and other overhead costs, including occupancy expense. The year ended December 31, 1999 included a charge of $1,812 relating to option payroll taxes resulting from the exercise of employee stock options. Excluding this expense, general and administrative expense was 5.3% of sales for the year ended December 31, 1999. Excluding this charge, general and administrative expenses increased as a result of increased payroll and overhead costs associated with the expansion of our product offerings and increases in our revenue base.

Systems and Business Development

	Year Ended December 31, ($000)		%
	1999	1998	Change
Systems & Business Development	$14,023	$11,132	26.0%
% of Revenues	2.9%	31.6%	

Systems and business development expenses for the year ended December 31, 1999 were comprised primarily of: (1) compensation to our information technology and product development staff; (2) payments to outside contractors; (3) data communications and other expenses associated with operating priceline.com's Web site; and (4) depreciation and amortization on computer hardware and software. During 1999, systems and business development expenses increased due to increased payroll costs, increased depreciation and amortization resulting from increased capital expenditures and

increased development costs associated with the expansion of priceline.com's product offerings and technological infrastructure. As the Company depends on its web site and internal systems to operate, it expects to continue to invest significantly on the systems and business development area.

In March 1998, the American Institute of Certified Public Accountants issued Statement of Position ("SOP") 98-1, "Accounting for Costs of Computer Software Developed or Obtained for Internal Use." This SOP requires capitalization of certain costs of computer software developed or obtained for internal use. Priceline.com adopted this SOP on January 1, 1999 and, during the year ended December 31, 1999, priceline.com capitalized approximately $13.9 million of computer software developed or obtained for internal use. Amortization of such costs aggregated approximately $1.1 million during the year ended December 31, 1999.

Other Income, Net

	Year Ended December 31, ($000)		%
	1999	1998	Change
Other Income (Net)	$7,120	$548	1,199%

Other income, net, for the year ended December 31, 1999 was primarily comprised of interest income. Interest income on cash and marketable securities increased due to higher cash and cash equivalent balances resulting from our initial public offering of common stock in April of 1999 and our secondary public offering of common stock in August of 1999.

Year Ended December 31, 1998

Priceline.com was formed in July 1997, but did not commence operations until April 1998. Accordingly, comparisons with prior periods are not meaningful.

Revenues

Total revenues for the year ended December 31, 1998 were $35.2 million. Since commencement of operations in April 1998, essentially all revenues consisted of airline ticket sales, hotel room reservations and related adaptive marketing programs. Priceline.com's automobile sales service, which was launched on a test basis in the New York metropolitan area in July 1998, did not contribute materially to revenues during the period.

Product Costs and Gross Profit (Loss)

Cost of revenues for the year ended December 31, 1998 totaled $36.5 million, consisting of product costs of $33.5 million and supplier warrant costs of $3.0 million. Product costs represent the cost of airline tickets from priceline.com's suppliers, net of the federal air transportation tax, segment fees and passenger facility charges imposed in connection with the sale of airline tickets. Supplier warrant costs represent a non-cash expense related to the pro-rata amount of the Delta warrant earned prior to December 31, 1998, the date on which the Delta warrant was amended.

Gross profit (loss), which is comprised of revenues less cost of revenues, was $(1.3) million for the year ended December 31, 1998. Excluding the effect of the non-cash supplier warrant costs, priceline.com would have had gross profit of $1.7 million for the year ended December 31, 1998. In 1998, priceline.com sold a substantial number of tickets below its cost in order to increase airline and adaptive marketing revenues, build a record of successful transactions, and enhance the priceline.com brand. Because the fees generated by adaptive marketing programs have historically involved no separate costs, adaptive marketing revenues had a disproportionately positive impact on priceline.com's total gross margin. The Capital One adaptive marketing program accounted for all of priceline.com's adaptive marketing revenues in 1998.

Operating Expenses

Warrant Cost, net. Warrant costs, net for the year ended December 31, 1998 totaled $58.0 million, or 164.5% of revenues. Supplier start up warrant costs consist of a non-cash charge representing the fair value of warrants issued to certain participating airlines in the priceline.com service in connection with securing the airline's participation in the priceline.com service.

Sales and Marketing. Sales and marketing expenses for the year ended December 31, 1998 totaled $24.4 million, or 69.2% of revenues. The expenses were comprised of: (1) advertising and promotional items; (2) fees payable to a third party service provider, which operates priceline.com's call center; (3) credit card processing fees; (4) provisions for customer credit card charge-backs (based upon a percentage reflecting priceline.com's historical experience); and (5) compensation for priceline.com's sales and marketing personnel.

General and Administrative. General and administrative expenses for the year ended December 31, 1998 totaled $18.0 million or 51.1% of revenues. General and administrative expenses consist primarily of compensation for personnel, fees for outside professionals, telecommunications and other overhead costs, including occupancy expense. In July 1998, priceline.com issued 8,125,000 shares of Common Stock, to the Chairman and Chief Executive Officer that resulted in the recognition of a charge of $6.5 million with respect to these shares. The shares were issued as compensation for agreeing to accept the position.

Systems and Business Development. Systems and business development expenses for the year ended December 31, 1998 totaled $11.1 million, or 31.6% of revenues. Systems and business development expenses are comprised primarily of compensation to priceline.com's information technology and product development staff and payments to outside contractors, data communications and other expenses associated with operating priceline.com's Web site and, to a lesser extent, depreciation on computer hardware and licensing fees for computer software.

Other Income, Net

Other income, net for the year ended December 31, 1998 totaled $548,374, reflecting approximately $633,000 of interest income earned by priceline.com on its cash balances, net of interest expense for the period.

Period Ended December 31, 1997

During the period from its formation in July 1997 through December 31, 1997, priceline.com was engaged in start-up activities and incurred $2.5 million of operating expenses. These operating expenses primarily consisted of investments in technology and personnel related expenses. No revenues were earned during the period.

Liquidity and Capital Resources

At December 31, 1999, the Company had approximately $171.9 million in cash and cash equivalants, and short-term investments.

Net cash used in operating activities was $63.0 million, $40.9 million and $774,000 for the years ended December 31, 1999 and 1998 and for the period July 18 (inception) through December 31, 1997, respectively. Net cash used in operating activities was primarily attributable to net losses.

Net cash used in investing activities was $68.2 million, $6.6 million and $1.3 million for the years ended December 31, 1999 and 1998 and for the period July 18 (inception) through December 31, 1997, respectively. Net cash used in investing activities was primarily related to purchases of property and equipment, and in 1999 for investments in marketable securities.

Priceline.com has certain commitments for capital expenditures as part of its ongoing business cycle. None of these commitments are material to the financial statements either individually or in the aggregate. Capital expenditures, primarily for computer equipment and software, were $27.4 million for the year ended December 31, 1999. As a result of its rapid growth, priceline.com expects to increase capital expenditures for purchased computer hardware, internally developed software, other equipment and leasehold improvements.

Net cash provided by financing activities was $210.8 million, $101.1 million and $2.1 million for the years ended December 31, 1999 and 1998 and for the period July 18 (inception) through December 31, 1997, respectively. Net cash provided by financing activities resulted primarily from the issuance of equity securities referred to below.

In April 1999, priceline.com completed its initial public offering in which it sold 10,000,000 shares of its Common Stock at a price of $16.00 per share. Offering proceeds to priceline.com, net of approximately $11.2 million in aggregate underwriters' discounts and commissions and $4.5 million in related expenses, were approximately $144.3 million. In August 1999, priceline.com completed a public offering in which it sold 1,000,000 shares of its Common Stock at a price of $67.00 per share. Offering proceeds to priceline.com, net of approximately $2.5 million in aggregate underwriters' discounts and commissions and $2.0 million in related expenses, were approximately $62.5 million.

During 1997, priceline.com's initial equity capital of approximately $27.0 million was provided by Mr. Jay S. Walker, other high net worth individuals and a partnership affiliated with General Atlantic Partners, LLC, a private equity firm that invests worldwide in software and information technology companies. An additional $20.0 million was invested by two partnerships affiliated with General Atlantic in July 1998. In December 1998, priceline.com sold equity securities in a private offering to a group of corporate and institutional investors and high net worth individuals for approximately $54.4 million. Included in that group were two partnerships affiliated with General Atlantic; Vulcan Ventures, Incorporated; Liberty PL, Inc., a wholly owned subsidiary of Liberty Media Corporation; Quantum Industrial Partners LDC, a fund managed by Soros Fund Management, LLC and Allen & Company Incorporated. Allen & Company Incorporated also has served as priceline.com's financial advisor.

In April 1999, priceline.com made a $3.3 million loan to Mr. Richard S. Braddock for the payment of taxes related to the issuance to Mr. Braddock of 8,125,000 shares of common stock in August 1998. The loan bears interest at 5.28% per annum. Interest is payable annually and principal is payable in January 2004.

In July 1999, priceline.com made a $6.0 million loan to an executive of the Company, pursuant to the terms of his employment agreement dated June 14, 1999. The loan bears interest annually at 5.82% per annum. In the first quarter of 2000, priceline.com made loans to two executives aggregating $5.0 million, which bear interest at 6.56%. Subject to certain prepayment obligations and to forgiveness in the event of certain changes of control, death, or termination without cause, pursuant to the terms of these loans, accrued interest and principal are payable after five years, but are forgiven under certain circumstances if the executive remains employed by the Company at that time. Upon any forgiveness of the loans, the Company would recognize as compensation expense an amount up to the amount of principal and interest forgiven.

Priceline.com believes that its existing cash balances and liquid resources will be sufficient to fund its operating activities, capital expenditures and other obligations through at least the next twelve months. However, if during that period or thereafter, priceline.com is not successful in generating sufficient cash flow from operations or in raising additional capital when required in sufficient amounts and on terms acceptable to priceline.com, these failures could have a material adverse effect on priceline.com's business, results of operations and financial condition. If additional funds were raised

through the issuance of equity securities, the percentage ownership of its then-current stockholders would be diluted.

Market-related Risks

Priceline.com currently has no floating rate indebtedness, holds no derivative instruments other than through investments in licensees discussed above, and does not earn significant foreign-sourced income. Accordingly, changes in interest rates or currency exchange rates do not generally have a direct effect on priceline.com's financial position. However, changes in currency exchange rates may affect the cost of international airline tickets and international hotel room reservations offered through the priceline.com service, and so indirectly affect consumer demand for such products and priceline.com's revenue. In addition, to the extent that changes in interest rates and currency exchange rates affect general economic conditions, priceline.com would also be affected by such changes.

Recent Accounting Pronouncements

In July 1999, the FASB issued Statement No. 137, "Accounting for Derivative Instruments and Hedging Activities—Deferral of Effective Date of FASB No. 133". The Statement defers for one year the effective date of FASB Statement No. 133, "Accounting for Derivative Instruments and Hedging Activities". The rule now will apply to fiscal quarters of fiscal years beginning after June 15, 2000. In June 1998, SFAS No. 133 "Accounting for Derivative Instruments and Hedging Activities" was issued. The statement will require the recognition of all derivatives as either assets or liabilities in the balance sheet and the measurement of those instruments at fair value. Derivatives that are not hedges must be adjusted to fair value through income. If the derivative is a hedge, depending on the nature of the hedge, changes in the fair value of derivatives will either be offset against the change in fair value of the hedged assets, liabilities, or firm commitments through earnings or recognized in other comprehensive income until the hedged item is recognized in earnings. The ineffective portion of the derivative's change in fair value will be immediately recognized in earnings. The Company has not yet determined the effect of SFAS No. 133 will have on the earnings and financial position of the Company.

In 1999, the Company adopted Statement of Position (SOP) 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use." This standard requires certain direct development costs associated with internal-use software to be capitalized including external direct costs of material and services and payroll costs for employees devoting time to the software projects. These costs are included in software and are amortized over a period not to exceed three years beginning when the asset is substantially ready for use. Costs incurred during the preliminary project stage, as well as maintenance and training costs, are expensed as incurred.

Tax Matters

Federal Air Transportation Tax on Airline Ticket Sales

A Federal transportation tax is imposed upon the sale of airline tickets. The tax is based on a percentage of the cost of transportation, which was 9% for periods prior to October 1, 1998, 8% for the period October 1, 1998 through September 30, 1999 and 7.5% thereafter. The Company has historically interpreted the tax regulations as requiring that the tax be computed based on the amount charged by the airline to priceline.com for the airline ticket and the Company's participating airlines have collected and remitted the tax based on this amounts. The Company applied for a ruling from the Internal Revenue Service (the "Service") confirming this interpretation. In December 1999, the Service indicated to the Company that it was unlikely that a favorable ruling would be issued. The Company subsequently withdrew its ruling request because of the uncertainty of the outcome. Because the Company anticipated the possibility of an adverse ruling on this issue, the Company accrued

approximately $1.9 million relating to the balance of the tax liability for tickets sold prior to that date. The Company believes this accrual to be adequate but there can be no assurance as to the final outcome because a formal ruling has not been issued by the service.

Non-Qualified Stock Options

As of December 31, 1999, we had outstanding non-qualified stock options to purchase 27,024,740 shares issued to various employees, consultants and directors pursuant to the 1997 Omnibus Plan and the 1999 Omnibus Plan. The options entitle holders to purchase common stock at a weighted average exercise price of approximately $13.93 per share, subject to adjustment in accordance with the 1997 Omnibus Plan and the 1999 Omnibus Plan.

Year 2000 Readiness Disclosure

The following disclosure may be deemed "Year 2000 Readiness Disclosure" pursuant to the Year 2000 Information and Readiness Disclosure Act.

Since inception, the Company has dedicated substantial resources to address the potential issues related to Year 2000 programming and related concerns. As a result of these efforts, the Company has not experienced to date any material disruption in its operations in connection with, or following, the transition of Year 2000.

Since the Company was cognizant of Year 2000 issues during the development of its systems and products since inception, specific costs related to Year 2000 issues can not be quantified. There were no material additional costs incurred to make any previously existing product or services Year 2000 compliant.

Information Regarding Forward Looking Statements

"Management's Discussion and Analysis of Financial Condition and Results of Operations", the letters to shareholders and the descriptions of the Company's business contain forward-looking statements. In some cases, readers can identify forward-looking statements by terminology such as "may," "will," "should," "could," "expects," "plans," "anticipates," "believes," "estimates," "predicts," "potential," or "continue," or the negative of such terms or other comparable terminology. These statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance, or achievements to be materially different from any future results, levels of activity, performance, or achievements expressed or implied by such forward-looking statements. Such factors include, among other things, the expansion of our business model both horizontally and geographically and the amount and timing of investments in such expansion; management of our rapid growth; any decline in consumer acceptance of our adaptive marketing programs; adverse changes or interruptions in our relationships with airlines and other product and service providers; security breaches and other systems-related failures; our ability to protect our intellectual property rights, particularly in connection with our pending litigations; legal and regulatory risks; our limited operating history; anticipated losses; the effects of increased competition; and the ability to attract and retain qualified personnel. Additional factors include the rate of growth of the Internet and online commerce; consumer confidence in on-line security of credit card transactions; consumer spending patterns; technological changes; and on-line fraud. In addition, our future operating results are subject to the risks more fully described in the Company's most recent filings with the Securities and Exchange Commission on Form 10-K and Form 10-Q. We undertake no duty to update any of the forward-looking statements, whether as a result of new information, future events or otherwise.

INDEPENDENT AUDITORS' REPORT

To the Board of Directors and Stockholders of
priceline.com Incorporated

We have audited the accompanying balance sheets of priceline.com Incorporated (the "Company") as of December 31, 1999 and 1998, and the related statements of operations, changes in stockholders' equity, and cash flows for the years ended December 31, 1999 and 1998 and the period July 18, 1997 (inception) to December 31, 1997. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the 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, such financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 1999 and 1998, and the results of its operations and its cash flows for the years ended December 31, 1999 and 1998 and the period July 18, 1997 (inception) to December 31, 1997 in conformity with generally accepted accounting principles.



Stamford, Connecticut
January 27, 2000
(March 17, 2000 as to Note 15)

priceline.com Incorporated

BALANCE SHEETS

(In thousands)

	December 31, 1999	December 31, 1998
ASSETS		
Current assets:		
Cash and cash equivalents	$ 133,172	$ 53,593
Short-term investments	38,771	
Accounts receivable, net of allowance for doubtful accounts of $1,961 and $291	21,289	4,177
Related party receivables	508	
Prepaid expenses and other current assets	17,999	2,433
Total current assets	211,739	60,203
Property and equipment, net	28,006	5,927
Related party receivable	8,838	
Warrants to purchase common stock of Priceline WebHouse Club, Inc.	189,000	
Other assets	4,303	442
Total assets	$ 441,886	$ 66,572
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 24,302	$ 5,268
Related party payable		32
Accrued expenses	13,695	4,259
Other current liabilities	1,253	722
Total current liabilities	39,250	10,281
Long term obligations		1,015
Total liabilities	39,250	11,296
Stockholders' equity:		
Common stock, $0.008 par value authorized 1,000,000 and 300,000 shares, respectively; issued and outstanding, 163,867 and 93,225 shares, respectively	1,311	746
Convertible preferred stock, $0.01 par value; authorized 150,000 shares:		
Series A $1.16 liquidation value per share; issued and outstanding 17,289 shares at December 31, 1998		173
Series B $4.00 liquidation value per share; issued and outstanding, 13,837 shares at December 31, 1998		138
Additional paid-in capital	1,581,708	171,158
Accumulated deficit	(1,180,383)	(116,939)
Total stockholders' equity	402,636	55,276
Total liabilities and stockholders' equity	$ 441,886	$ 66,572

See notes to financial statements.

priceline.com Incorporated

STATEMENTS OF OPERATIONS

(In thousands, except per share data)

	Year Ended December 31,		July 18, 1997 (Inception) to December 31,
	1999	1998	1997
Revenues	$ 482,410	$ 35,237	
Cost of revenues:			
Product costs	423,056	33,496	
Supplier warrant costs	1,523	3,029	
Total costs of revenues	424,579	36,525	
Gross profit (loss)	57,831	(1,288)	
Operating expenses:			
Warrant costs, net	998,832	57,979	
Sales and marketing	79,577	24,388	$ 441
General and administrative (including $1,812 of option payroll taxes in 1999)	27,609	18,004	1,012
Systems and business development	14,023	11,132	1,060
Total operating expenses	1,120,041	111,503	2,513
Operating loss	(1,062,210)	(112,791)	(2,513)
Interest income	7,501	548	
Other expense	(381)		
Total other income (expense)	7,120	548	
Net loss	(1,055,090)	(112,243)	(2,513)
Accretion on preferred stock	(8,354)	(2,183)	
Net loss applicable to common stockholders	$(1,063,444)	$(114,426)	$(2,513)
Net loss applicable to common stockholders per basic and diluted common share	$ (7.90)	$ (1.41)	$ (.05)
Weighted average number of basic and diluted common shares outstanding	134,622	81,231	50,834

See notes to financial statements.

priceline.com Incorporated

STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 1999 AND 1998 AND FOR THE PERIOD JULY 18, 1997 (INCEPTION) TO DECEMBER 31, 1997

(In thousands)

	Preferred Stock		Common Stock		Additional Paid-in Capital	Accumulated Deficit	Total
	Shares	Amount	Shares	Amount			
Issuance of common stock and common stock subscriptions			51,670	$ 413	$ 843		$ 1,256
Net loss						$ (2,513)	(2,513)
Balance, December 31, 1997			51,670	413	843	(2,513)	(1,257)
Issuance of common stock and common stock subscriptions			41,555	333	32,663		32,996
Issuance of Series A convertible preferred stock	17,289	$ 173			19,827		20,000
Issuance of Series B convertible preferred stock	13,837	138			54,276		54,414
Accretion on preferred stock					2,183	(2,183)	
Issuance of options to purchase common stock					245		245
Issuance of warrants to purchase common stock					61,121		61,121
Net loss						(112,243)	(112,243)
Balance, December 31, 1998	31,126	$ 311	93,225	$ 746	$ 171,158	$ (116,939)	$ 55,276
Conversion of Series A convertible preferred stock	(17,289)	(173)	21,611	173			
Conversion of Series B convertible preferred stock	(13,837)	(138)	17,297	138			
Accretion on preferred stock					8,354	(8,354)	
Issuance of common stock			11,000	88	208,329		208,417
Exercise of warrants to purchase common stock			19,121	153	1,579		1,732
Exercise of options to purchase common stock			1,613	13	1,654		1,667
Issuance of warrants to purchase common stock					1,190,634		1,190,634
Net loss						(1,055,090)	(1,055,090)
Balance, December 31, 1999			163,867	$1,311	$1,581,708	$(1,180,383)	$ 402,636

See notes to financial statements.

priceline.com Incorporated

STATEMENTS OF CASH FLOWS

(In thousands)

	Year Ended December 31, 1999	Year Ended December 31, 1998	July 18, 1997 (Inception) to December 31, 1997
OPERATING ACTIVITIES:			
Net loss	$(1,055,090)	$(112,243)	$(2,513)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization	5,348	1,860	212
Provision for uncollectible accounts	3,127	581	
Warrant costs, net	1,189,111		
Warrant income	(189,000)		
Equity based compensation		67,866	
Changes in assets and liabilities:			
Accounts receivable	(29,617)	(4,757)	
Prepaid expenses and other current assets	(12,043)	(1,922)	
Restricted bank deposit and bank certificate of deposit		(680)	
Accounts payable and accrued expenses	28,470	8,300	1,227
Other	(3,331)	112	300
Net cash used in operating activities	(63,025)	(40,883)	(774)
INVESTING ACTIVITIES:			
Additions to property and equipment	(27,416)	(6,607)	(1,317)
Minority equity investment	(2,000)		
Investment in marketable securities	(38,771)		
Net cash used in investing activities	(68,187)	(6,607)	(1,317)
FINANCING ACTIVITIES:			
Related party payable		(1,072)	1,104
Issuance of long-term debt		1,000	
Payment of long-term debt	(1,000)		
Principal payments under capital lease obligations	(25)	(22)	(2)
Issuance of common stock and subscription units	211,816	26,495	1,006
Payment received on stockholder note		250	
Issuance of Series A convertible preferred stock		20,000	
Issuance of Series B convertible preferred stock		54,415	
Net cash provided by financing activities	210,791	101,066	2,108
NET INCREASE IN CASH AND CASH EQUIVALENTS	79,579	53,576	17
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	53,593	17	
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 133,172	$ 53,593	$ 17
SUPPLEMENTAL CASH FLOW INFORMATION:			
Cash paid during the period for interest	$ 37	$ 61	$ 1

See notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

1. BUSINESS DESCRIPTION

Priceline.com Incorporated (“priceline.com”, or the “Company”) has pioneered a unique e-commerce pricing system known as a “demand collection system” that enables consumers to use the Internet to save money on a wide range of products and services while enabling sellers to generate incremental revenue. Using a simple and compelling consumer proposition—Name Your Own Price℠—priceline.com collects consumer demand, in the form of individual customer offers guaranteed by a credit card, for a particular product or service at a price set by the customer. The Company then accesses a database of inventory available to the Company for purchase to determine whether priceline.com can fulfill the customer’s offer. Consumers agree to hold their offers open for a specified period of time and, once fulfilled, offers generally cannot be canceled. The Company benefits consumers by enabling them to save money, while at the same time benefiting sellers by providing them with an effective revenue management tool capable of identifying and capturing incremental revenues. By requiring consumers to be flexible with respect to brands, sellers and product features, priceline.com enables sellers to generate incremental revenue without disrupting their existing distribution channels or retail pricing structures.

Walker Digital Corporation (“Walker Digital”), a research and development company, developed the priceline.com service and the business model and related intellectual property rights underlying the priceline.com service, the rights for which were transferred to the Company. Walker Digital had no operations and no revenues related to the assets transferred to priceline.com. Walker Digital was founded and is controlled by the founding stockholder and Vice Chairman of priceline.com. During the years ended December 31, 1999 and 1998, Walker Digital provided the Company with a variety of services including subleasing office facilities to the Company. Charges to the Company for such services aggregated approximately $1,411,000 and $706,000, respectively. In addition, the Company charged Walker Digital $1,800,000 and $384,831 for the years ended December 31, 1999 and 1998, respectively, for certain services, including legal and accounting services and IT infrastructure. Such amounts have been offset against general and administrative expenses in the accompanying statements of operations.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation—The financial statements for all periods presented include the financial statements of priceline.com and Priceline Travel. On March 24, 1999, priceline.com exercised its call option to purchase Priceline Travel for nominal consideration and Priceline Travel was merged into priceline.com. All significant inter-company transactions have been eliminated.

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

Fair Value of Financial Instruments—The Company’s financial instruments, including cash and cash equivalents, accounts receivable-net and accounts payable, are carried at cost which approximates their fair value because of the short-term maturity of these financial instruments. The Company’s investment in Lending Tree, Inc. was valued at cost as there was no market for its securities at December 31, 1999. The Company recognized income for the warrant to purchase common stock of Priceline WebHouse Club, Inc. at estimated fair market value, as determined by an independent valuation firm. The carrying value of the capital lease obligations and long-term debt approximates fair value because the interest

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

rates on these obligations are comparable to the interest rates that could have been obtained at the dates of the respective balance sheets.

Cash and Cash Equivalents, and Short-term Investments—The Company invests excess cash primarily in money market accounts, certificates of deposits, and short-term commercial paper. All highly liquid instruments with an original maturity of three months or less are considered cash equivalents. Marketable securities are considered ''trading securities'' and valued at fair value.

Property and Equipment—Property and equipment are stated at historical cost. Depreciation and amortization of property and equipment is computed on a straight-line basis, generally over the estimated useful lives of the assets or, when applicable, the life of the lease, whichever is shorter.

Impairment of Long-Lived Assets—The Company evaluates the recoverability of its long-lived assets in accordance with Statement of Financial Accounting Standards ''SFAS'' No. 121, ''Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of.'' SFAS No. 121 requires recognition of impairment of long-lived assets in the event the net book value of such assets exceeds the future undiscounted cash flows attributable to such assets.

Software Capitalization—In 1999, the Company adopted Statement of Position (SOP) 98-1, ''Accounting for the Costs of Computer Software Developed or Obtained for Internal Use.'' This standard requires certain direct development costs associated with internal-use software to be capitalized including external direct costs of material and services and payroll costs for employees devoting time to the software projects. These costs are included in software and are amortized over a period not to exceed three years beginning when the asset is substantially ready for use. Costs incurred during the preliminary project stage, as well as maintenance and training costs, are expensed as incurred.

Revenues and Cost of Revenues—The Company recognizes and records revenues in a variety of ways depending on the product or service sold. With respect to airline ticket, hotel room and rental car services, the Company recognizes as revenue the amount received from the customer, net of taxes, and records as the cost of revenue the amount that the Company pays the respective airline or hotel. With respect to its automobile service, the Company earns a fixed fee from both the customer and the seller after the transaction is consummated. With respect to its home financing service, during 1999 the Company received a percentage of the fees earned by third parties in connection with the closing of mortgage loans. Going forward, the mortgage product will be offered through National Mortgage Center LLC (doing business as pricelinemortgage (''pricelinemortgage''), a Company that has been licensed to use the priceline.com demand collection system. The Company also generates revenues through adaptive marketing programs with third parties that pay the Company fees for marketing their customer acquisition programs. Additionally, the Company generates revenues from third party sources, including a customer processing fee for airline, hotel and rental car services, and ancillary reservation booking fees from the Worldspan reservation system for booking of airline flight segments and hotel reservations through the Worldspan system. Consumer processing fees are payable to the Company and recognized as revenue only upon completion of successful transactions.

The manner in which and time at which revenues are recognized differs depending on the product or service sold through the priceline.com service. With respect to airline ticket, hotel room and rental car services, revenues are generated by transactions with customers who make offers to purchase airline tickets and reserve hotel rooms and rental cars supplied to priceline.com by participating sellers. Revenues and related costs are recognized if, and when, the Company accepts and fulfills the

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

customer's offer. Because priceline.com is the merchant of record in these transactions, revenue for these services includes the offer price paid by the customer, net of certain taxes and fees. Airline, hotel and rental car revenues also may include fees from third parties for adaptive marketing programs. With respect to automobile services, fees or other payments payable by the seller and/or the customer are recognized as revenue. With respect to home financing services, the Company receives no fees from consumers. The Company recognizes revenue from fees paid directly by its strategic partner through the operation of its home financing services. Because the Company acts as an intermediary between the customer and the seller in auto and home financing transactions, revenues for these products and services are recorded at the amount of the fee received, and not on the value of the underlying transaction, when the transaction is completed. Automobile and home financing services revenues also may include fees from third parties for adaptive marketing programs.

Priceline.com expressly permits only credit cards as an acceptable form of payment from its consumers. On rare occasions, the Company provides refunds and makes certain customer accommodations to individual customers to satisfy disputes and complaints. The Company accrues for such expected losses and classifies the resulting expense as an addition to the allowance for doubtful accounts. The Company extends customary payment terms to corporate customers such as automobile dealers and adaptive marketing sponsors.

Sales and Marketing—Sales and marketing expenses are comprised primarily of costs of radio and newspaper advertising, costs of the third-party offer-taking call center, credit card processing fees, provisions for customer accommodations and charge-backs, and compensation for the Company's sales and marketing personnel. All sales and marketing costs are expensed as incurred.

Systems and Business Development—Systems and business development expenses are comprised primarily of compensation to the Company's information systems and product development staff and payments to outside contractors, data communications and other expenses associated with operating the Company's Web site, depreciation on computer hardware and licensing fees for computer software. Such costs are expensed as incurred.

Equity-Based Compensation—The Company accounts for stock-based employee compensation arrangements in accordance with provisions of Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees," and complies with the disclosure provisions of SFAS No. 123, "Accounting for Stock-Based Compensation." Under APB Opinion No. 25, compensation expense is based on the difference, if any, on the date of grant, between the fair value of priceline.com's stock and the exercise price of the option.

The Company accounts for equity instruments issued to non-employees in accordance with the provisions of SFAS No. 123 and Emerging Issues Task Force ("EITF") Issue No. 96-18, "Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services." All transactions in which goods or services are the consideration received for the issuance of equity instruments are accounted for based on the fair value of the consideration received or the fair value of the equity instrument issued, whichever is more reliably measurable. The measurement date of the fair value of the equity instrument issued is the earlier of the date on which the counterparty's performance is complete or the date on which it is probable that performance will occur.

Income Taxes—The Company accounts for income taxes in accordance with SFAS No. 109, "Accounting for Income Taxes," which requires recognition of deferred tax liabilities and assets for the

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

expected future tax consequences of events that have been included in the financial statements or tax returns. Under this method, deferred tax liabilities and assets are determined based on the temporary difference between the financial statement and tax basis of assets and liabilities using presently enacted tax rates in effect. Valuation allowances are established when necessary to reduce deferred tax assets to the amounts expected to be realized.

During the period that priceline.com operated as an LLC, it was treated substantially as a partnership for tax purposes and, accordingly, the tax effect of its activities accrued to its members through July 1998.

Net Loss Per Share—The Company computes basic and diluted earnings per share in accordance with Statement of Financial Accounting Standards No. 128 (“SFAS 128”), “Earnings per Share”. SFAS 128 requires the Company to report both basic earnings per share, which is based on the weighted average number of common shares outstanding, and diluted earnings per share, which is based on the weighted average number of common shares outstanding and all dilutive potential common shares outstanding. Since the Company incurred losses for all periods presented, the inclusion of options in the calculation of weighted average common shares is anti-dilutive; and therefore there is no difference between basic and diluted earnings per share.

Business Risk Business risks include the following:

Competition—The markets for the products and services offered on the priceline.com service are intensely competitive. The Company competes with both traditional distribution channels and online services. The Company currently or potentially competes with a variety of companies with respect to each product or services offered. The Company potentially faces competition from a number of large online services that have expertise in developing online commerce and in facilitating Internet traffic. Many competitors have significant competitive advantages. For example, airlines, hotels and other suppliers also sell their products and services directly to consumers and have established Web sites. Internet directories, search engines and large traditional retailers have significantly greater operating histories, customer bases, technical expertise, brand recognition and/or online commerce experience than the Company. In addition, certain competitors may be able to devote significantly greater resources to furthering their business.

Dependence on Airline Industry and Certain Carriers—The Company’s near term, and possibly long term, prospects are significantly dependent upon the sale of leisure airline tickets. Sales of leisure airline tickets represented approximately 85% and 86% of total revenues for the years ended December 31, 1999 and 1998, respectively. As a result, currently the Company is substantially dependent upon the continued participation of the airlines in the priceline.com service in order to maintain and continue to grow its total revenues. Significantly reducing the Company’s dependence on the airlines is likely to take a long period of time and there can be no guarantee that the Company will succeed in reducing that dependence.

Concentration of Credit Risk—Financial instruments, which potentially subject the Company to concentrations of credit risk, are principally bank deposits and accounts receivable. Cash and cash equivalents and marketable securities are deposited with high credit quality financial institutions. Accounts receivable are derived from the revenues earned from customers in the U.S. and are denominated in U.S. dollars. The Company maintains an allowance for uncollectible accounts based upon the expected collectibility of accounts receivable.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Barter Transaction—In 1999, the Company entered into one barter transaction to exchange services for advertising. The transaction was recorded at the estimated fair value of the services expected to be received. Revenue of $375,000 from this transaction was recognized in 1999, when the service was provided and will be expensed during 2000, when the advertising is provided to priceline.com.

Segment Reporting—The Company operates as a single segment and will evaluate additional segment disclosure requirements as it expands its operations. All of the operations and identifiable assets are in the United States.

Reclassification—Certain amounts in prior years' financial statements have been reclassified to conform to the current year presentation.

Recent Accounting Pronouncements

In July 1999, the FASB issued Statement No. 137, "Accounting for Derivative Instruments and Hedging Activities-Deferral of Effective Date of FASB No. 133". The Statement defers for one year the effective date of FASB Statement No. 133, "Accounting for Derivative Instruments and Hedging Activities". The rule now will apply to fiscal quarters of fiscal years beginning after June 15, 2000. In June 1998, SFAS No. 133 "Accounting for Derivative Instruments and Hedging Activities" was issued. The statement will require the recognition of all derivatives as either assets or liabilities in the balance sheet and the measurement of those instruments at fair value. Derivatives that are not hedges must be adjusted to fair value through income. If the derivative is a hedge, depending on the nature of the hedge, changes in the fair value of derivatives will either be offset against the change in fair value of the hedged assets, liabilities, or firm commitments through earnings or recognized in other comprehensive income until the hedged item is recognized in earnings. The ineffective portion of the derivative's change in fair value will be immediately recognized in earnings. The Company has not yet determined the effect of SFAS No. 133 will have on the earnings and financial position of the Company.

3. SHORT-TERM INVESTMENTS

At December 31, 1999, the Company held short term instruments which were classified as trading securities; accordingly, they are carried at fair value on the balance sheet. Net unrealized gains (losses) of $13,000 have been recognized in the financial statements. Marketable securities at December 31, 1999 include the following (in thousands):

	December 31, 1999
	Fair Value
Discounted commercial paper	$22,578
Asset backed securities	3,443
Municipal bonds and notes	12,750
	$38,771

Included in other assets is a $2.0 million equity investment in Lending Tree, Inc., an internet-based home financing service provider. Since the Company owns less than 20% of Lending Tree and does not exert significant influence over the investee, the Company accounts for the investment on the cost basis. In accordance with SFAS No. 115, the Company deems these securities as available for sale. Because there was no readily determinable value for shares of Lending Tree at December 31, 1999, the Company has valued its investment at cost. The Company's home financing service is offered through a joint marketing arrangement with Lending Tree.

4. ACCOUNTS RECEIVABLE

A summary of the activity in the allowance for uncollectible accounts for the years ended December 31, 1999 and 1998 is as follows (in thousands):

	1999	1998
Balance, beginning of year	$ 291	$ —
Provision charged to expense	3,127	581
Charge-offs	(1,457)	(290)
Balance, end of year	$ 1,961	$ 291

5. PROPERTY AND EQUIPMENT

Property and equipment at December 31, 1999 and 1998 consists of the following (in thousands):

	Estimated Useful Lives (years)	1999	1998
Computer equipment and software	3	$33,242	$ 7,034
Office equipment, furniture & fixtures and leasehold improvements	3 to 7	2,173	965
Total		35,415	7,999
Less accumulated depreciation and amortization		(7,409)	(2,072)
Property and equipment, net		$28,006	$ 5,927

Depreciation and amortization expense was approximately $5,337,000, $1,860,000 and $212,000 for the years ended December 31, 1999 and 1998, and for the period July 18, 1997 to December 31, 1997, respectively.

6. LONG TERM DEBT

In April 1998, priceline.com issued a promissory note to an investor for $1,000,000. The promissory note bore interest at a rate of 6% per annum. In connection with the promissory note, priceline.com issued detachable warrants to purchase 62,500 shares of common stock at $0.80 per share. The note was repaid in 1999.

7. STOCKHOLDERS' EQUITY

In March 1999, the Company effected a 1.25:1 stock split. All share and per share amounts have been retroactively adjusted to reflect the stock split.

On July 18, 1997, priceline.com issued 42,990,211 shares of Common Stock for the initial contributed services of the founders. No compensation expense was recognized for the contributed services as priceline.com was in the earliest phases of development. Such services included conceiving the priceline.com business model, developing business strategies and operating plans, initiating contact with airline suppliers and raising capital. There were no employment agreements related to the services initially contributed and/or the shares issued in respect of such shares.

Also, on July 18, 1997, priceline.com issued 6,895,833 shares of Common Stock to Walker Digital in exchange for the transfer by Walker Digital to priceline.com of all the rights, title, and interest in certain patents and patent applications relating to buyer driven commerce.

7. STOCKHOLDERS' EQUITY (Continued)

In April 1998, priceline.com issued warrants to purchase 125,000 shares of Common Stock, at a zero exercise price, to a non-employee in exchange for services rendered to the Company. The estimated fair value of the warrants at the date of grant of $100,000 was based on the value of the equivalent shares as of the grant date, that is 125,000 shares at $0.80 per share, and has been reflected as sales and marketing expense and additional paid-in-capital.

In July 1998, priceline.com issued 8,125,000 shares of Common Stock, to the Chairman and Chief Executive Officer that resulted in the recognition of a charge of $6,500,000 with respect to these shares. The shares were issued as compensation for agreeing to accept the position.

In April 1999, the Company completed an initial public offering in which it sold 10,000,000 shares of its Common Stock, $0.008 par value. Offering proceeds to the Company, net of underwriter discounts and commissions and other related expenses, were approximately $144.3 million. At the time of the offering, shares of the Series A and Series B Preferred Stock were automatically converted, subject to anti-dilution adjustment, into an equal number of shares of Common Stock.

In August 1999, the Company completed a public offering in which it sold 1,000,000 shares of its Common Stock and certain stockholders of the Company sold 3,500,000 shares of common stock at a price of $67.00 per share. Offering proceeds to priceline.com, net of underwriters discounts and commissions and related expenses, were approximately $62.5 million.

8. WARRANTS TO PURCHASE COMMON STOCK

In August 1998, priceline.com entered into a warrant agreement with Delta Air Lines (''Delta'') to purchase up to 18,892,603 shares of Common Stock at an exercise price of approximately $0.93 per share (the ''Delta Warrant'') for agreeing to participate in the priceline.com service. Vesting was contingent upon achievement of certain predetermined performance thresholds. However, there was no penalty for failure to provide ticket inventory to satisfy these performance thresholds. Accordingly, no expense was recorded when the warrant was issued. On December 31, 1998, the Company amended its agreement with Delta to eliminate the vesting contingencies and fix the number of shares subject to the warrant at 18,619,402. The warrants were immediately vested on the date of grant, in that they are not subject to any forfeiture for any reason. The amended Delta Warrant was to become exercisable at the earlier of seven years or over three years upon the achievement of certain performance thresholds. The agreement does not require Delta to make any performance commitments, is non-exclusive and allows Delta to participate in other programs similar to the priceline.com service. Accordingly, the Company recognized approximately $58.7 million of expense based upon the fair value of the warrant on December 31, 1998, of which $3.0 million is included in cost of revenues-supplier warrant costs and $55.7 million is included in expenses-warrant costs, net in the accompanying statements of operations.

In November 1999, the Company further amended the Delta warrant to provide Delta with a cashless exercise right. Upon the exercise of the warrant, Delta acquired a total of 16,525,834 shares of Common Stock of priceline.com. In conjunction with that transaction, Delta sold 2,085,767 shares of priceline.com Common Stock to priceline.com's founder and Vice Chairman Jay S. Walker for an aggregate purchase price of $125 million. The Company further gave Delta the right to exchange six million shares of priceline.com common stock for six million shares of newly issued convertible preferred stock that may be converted into priceline.com stock on a one-for-one basis. To date, Delta has not elected to exercise the conversion right.

8. WARRANTS TO PURCHASE COMMON STOCK (Continued)

On December 31, 1998, priceline.com issued warrants to purchase 937,500 shares of Common Stock, at an exercise price of $3.20 per share, to three airlines in recognition of their being among the original participants in the priceline.com service. Because there are no requirements as to the nature or length of that participation, and the warrants are not subject to forfeiture for any reason, the Company recognized approximately $2.3 million of expense based upon the fair value of the warrants at December 31, 1998. That amount is included in expenses- warrant costs, net in the accompanying statements of operations.

On January 29, 1999, priceline.com issued warrants to an airline to purchase 1,250,000 shares of Common Stock at an exercise price of $6.40 per share. The warrants become exercisable as follows, 50% on January 29, 2000 and 50% on January 29, 2001. The agreement requires the airline to make available to priceline.com airline ticket inventory on certain specified terms and conditions for two years. If the airline does not provide the specified airline ticket inventory, the unexercised warrants are returnable and a substantial penalty will be imposed. The fair value of the warrant of $3.1 million at the grant date was capitalized and will be amortized over the two year period during which services are expected to be provided to the Company.

During July 1999, priceline.com issued to Continental Airlines a warrant to purchase common stock that will become exercisable upon the earlier of July 2004 or upon the achievement of certain performance thresholds. However, the agreement does not require Continental to make any performance commitments. Accordingly, priceline.com incurred a non-cash charge of approximately $88.4 million during the third quarter of 1999 representing the fair value of the warrant on the grant date. In November 1999, the Company amended the Continental warrant to allow the exercise price to fall within the range of the warrants issued to other airlines discussed below. Priceline.com incurred a non-cash charge of approximately $3.5 million during the fourth quarter as a result of the warrant amendment.

In November 1999, the Company entered into separate Participation Warrant Agreements with each of eight major domestic airlines relating to their inclusion in the Company's leisure airline ticket service. Under the Participation Warrant Agreements, the airlines were granted warrants to purchase a total of 20 million shares of priceline.com Common Stock at exercise prices ranging from $52.625 to $59.933 per share. All warrants were fully vested on the date of grant, but generally are not exercisable until November 2005, subject to acceleration under certain circumstances. Priceline.com incurred additional warrant costs of approximately $1.1 billion during the fourth quarter of 1999 as a result of the issuance of these warrants.

9. STOCK OPTION PLANS

In February 1999, the Company adopted the 1999 Omnibus Plan (the "1999 Plan"), which provides for grants of options as incentives and rewards to encourage employees, officers, consultants and directors in the long term success of the Company. In addition, the Company had previously adopted the 1997 Omnibus Plan (the "1997 Plan"). The 1999 Plan and 1997 Plan provide for grants of options to purchase up to 9,375,000 and 23,875,000 shares of Common Stock, respectively, at a purchase price equal to the fair market value on the date of grant. Generally, options from both plans vest over three years from the date of grant. Compensation expense for options granted to non-employees, included in

9. STOCK OPTION PLANS (Continued)

general and administrative, aggregated $0 and $245,063, during the years ended December 31, 1999 and 1998, respectively.

The following summarizes the transactions pursuant to the Plan:

	Shares	Weighted Average Option Price	Option Price Range
Granted during 1998	23,449,219	$ 0.93	$ 0.80-3.20
Forfeited	(189,374)	0.80	0.80
Cancelled	(815,625)	0.80	0.80
Balance at December 31, 1998	22,444,220	$ 0.94	$ 0.80-3.20
Granted during 1999	6,481,833	55.99	3.20-139.25
Exercised	(1,614,697)	1.02	0.80-8.00
Forfeited	(286,616)	20.74	0.80-139.25
Balance at December 31, 1999	27,024,740	$13.93	$0.80-139.25
Exercisable at December 31, 1999	16,708,585		
Exercisable at December 31, 1998	None		
Available for grant at December 31, 1999	4,610,563		
Available for grant at December 31, 1998	1,430,780		

No options were granted during 1997.

The following table summarizes information about stock options outstanding at December 31, 1999:

	OPTIONS OUTSTANDING			OPTIONS EXERCISABLE	
RANGE OF EXERCISE PRICES	NUMBER OUTSTANDING AS OF 12/31/99	WEIGHTED AVERAGE REMAINING LIFE	WEIGHTED AVERAGE EXERCISE PRICE	NUMBER EXERCISABLE AS OF 12/31/99	WEIGHTED AVERAGE EXERCISE PRICE
$ .80–$ .93	19,532,282	8.53	$ .81	16,171,502	$0.80
3.20– 13.00	2,835,458	9.12	5.99	537,083	3.42
46.75– 139.25	4,657,000	9.68	73.83	—	—
$ .80–$139.25	27,024,740	9.07	$13.93	16,708,585	$0.88

Had compensation costs been determined based upon the fair value at grant date, the Company's pro forma net loss and pro forma net loss per share for the years ended December 31, 1999 and 1998 would have been reported as follows (in thousands, except per share amounts):

1999:	Reported	Pro Forma
Net loss	$1,055,090	$1,295,758
Net loss applicable to common shareholders	1,063,444	1,304,112
Basic and diluted loss per common share	7.90	9.69

9. STOCK OPTION PLANS (Continued)

1998:		
Net loss	$ 112,243	$ 114,613
Net loss applicable to common shareholders	114,426	116,797
Basic and diluted loss per common share	1.41	1.44

The fair value of options granted during 1999 was determined on the date of grant using the Black-Scholes method. The weighted average fair value of options granted during 1999 was estimated to be approximately $52.45, based on the following assumptions: volatility of 107%, risk free interest rate of 5.9%, an expected life of 3 years, and no dividends.

The fair value of options granted during 1998 was determined on the date of grant using the minimum value method. The weighted average fair value of options granted during 1998 was estimated to be approximately $0.15, based on the following assumptions: volatility of 0%, risk free interest rate of 6.0%, an expected life of 3 years, and no dividends.

10. TAXES

Income Taxes Through July 31, 1998, priceline.com operated as a limited liability company and income taxes (benefits) accrued to the members. Accordingly, no income taxes (benefits) were reflected in the accompanying financial statements as of December 31, 1997 and for the period then ended. Since converting from an LLC to a corporation in July 1998, the Company has incurred net operating losses of approximately $1.1 billion, and accordingly, no provision for income taxes is reflected in the accompanying statements of operations.

The tax effects of temporary differences that give rise to significant portions of deferred tax assets at December 31, 1999 and 1998 are as follows (in thousands):

	1999	1998
Warrant costs	$488,989	$25,267
Net operating loss carryforwards	459,455	9,348
Start-up costs	2,300	2,988
Other	(2,801)	382
Less valuation allowance	(947,943)	(37,985)
Deferred tax asset, net	$ —	$ —

A valuation allowance for the full amount of the net deferred tax asset was recorded at December 31, 1999 and 1998 and represents the portion of tax operating loss carryforwards and other items for which it is more likely than not that the benefit of such items will not be realized. The

10. TAXES (Continued)

income tax benefit is different from the amount computed using applicable statutory federal rates for the following reasons (in thousands):

	1999	1998
Income tax benefit at federal statutory rate	$369,281	$39,285
Adjustment due to:		
LLC status through July 31, 1998		(7,090)
State taxes and other	64,605	5,790
Increase in valuation allowance	(433,886)	(37,985)
Income tax benefit	$ —	$ —

Federal Air Transportation Tax —A Federal transportation tax is imposed upon the sale of airline tickets. The tax is based on a percentage of the cost of transportation, which was 9% for periods prior to October 1, 1998, 8% for the period October 1, 1998 through September 30, 1999 and 7.5% thereafter. The Company has historically interpreted the tax regulations as requiring that the tax be computed based on the amount charged by the airline to priceline.com for the airline ticket and the Company's participating airlines have collected and remitted the tax based on this amount. The Company applied for a ruling from the Internal Revenue Service (the "Service") confirming this interpretation. In December 1999, the Service indicated to the Company that it was unlikely that a favorable ruling would be issued. The Company subsequently withdrew its ruling request because of the uncertainty of the outcome. Because the Company anticipated the possibility of an adverse ruling on this issue, the Company accrued approximately $1.9 million relating to the balance of the tax liability for tickets sold prior to that date. The Company believes this accrual to be adequate, but there can be no assurance as to the final outcome because a formal ruling has not been issued by the service.

11. LICENSING, MARKETING and TECHNOLOGY AGREEMENTS

In 1999, priceline.com licensed its name and demand collection system to Priceline WebHouse Club, Inc. ("WebHouse") and agreed to provide certain services to WebHouse. WebHouse is an independent company. Under the negotiated agreements, priceline.com receives a royalty based on a percentage of WebHouse revenues and payments for services at estimated fair value. The Company realized $33,777 of royalty revenue in 1999. As an inducement to enter into a relationship with WebHouse, priceline.com received a warrant to purchase a majority of the shares of WebHouse common stock. The warrants are non-forfeitable, fully vested upon grant, exercisable in five years or earlier upon the occurrence of certain events, and do not require the performance of any additional services. Upon receipt of the warrant in the fourth quarter, priceline.com recognized $188.8 million of income representing the amount of the estimated fair value of the warrants, based on an independent valuation. Priceline.com is negotiating a similar arrangement with another independent Licensee, Priceline Perfect Yardsale, Inc. ("Yardsale").

Additionally, priceline.com and WebHouse entered into an Intellectual Property License Agreement, Marketing and Technical Services Agreement and a Services Agreement pursuant to which priceline.com provides certain marketing, technology and other services to WebHouse and receives compensation at fair value for services rendered. Accordingly, WebHouse paid the Company $1.65 million during 1999 under these agreements.

11. LICENSING, MARKETING and TECHNOLOGY AGREEMENTS (Continued)

Priceline.com and Yardsale also entered into a preliminary agreement pursuant to which priceline.com licenses its name and demand collection system and provides certain marketing, technology and other services to Yardsale and receives compensation at fair value for services rendered. The agreements with Yardsale were not in effect until after January 1, 2000.

12. COMMITMENTS AND CONTINGENCIES

Legal Proceedings On January 6, 1999, priceline.com received notice that a third party patent applicant and patent attorney, Thomas G. Woolston, purportedly had filed in December 1998 with the United States Patent and Trademark Office a request to declare an interference between a patent application filed by Woolston and priceline.com's U.S. Patent 5,794,207. Priceline.com currently is awaiting information from the Patent Office regarding whether it will initiate an interference proceeding.

On January 19, 1999, Marketel International Inc. (Marketel), a California corporation, filed a lawsuit against priceline.com, among others. On February 22, 1999, Marketel filed an amended and supplemental complaint. The amended complaint filed by Marketel alleges causes of action for, among other things, misappropriation of trade secrets, breach of contract, conversion, breach of confidential relationship, copyright infringement, fraud, unfair competition and false advertising, and seeks injunctive relief and damages in an unspecified amount. In its amended complaint, Marketel alleges, among other things, that the defendants conspired to misappropriate Marketel's business model, which allegedly was provided in confidence approximately ten years ago. The amended complaint also alleges that four former Marketel employees are the actual sole inventors or co-inventors of U.S. Patent 5,794,207, which was issued on August 11, 1998 and has been assigned to priceline.com. Marketel asks that the patent's inventorship be corrected accordingly.

On February 5, and February 10, 1999, the Company filed their answer and amended answer, respectively, to the amended complaint, in which they denied the material allegations of liability in the complaint. Priceline.com strongly dispute the material legal and factual allegations contained in Marketel's amended complaint and believes that the amended complaint is without merit. Priceline.com intends to defend vigorously against the action. Pursuant to the indemnification obligations contained in the Purchase and Intercompany Services Agreement with Walker Digital, Walker Digital has agreed to indemnify, defend and hold harmless priceline.com for damages, liabilities and legal expenses incurred in connection with the Marketel litigation.

On October 13, 1999, priceline.com filed a complaint in the United States District Court for the District of Connecticut under the caption Priceline.com Incorporated v. Microsoft Corporation and Expedia, Inc., No. 399CV1991 (AWT) alleging that Microsoft Corporation and Expedia, Inc., a subsidiary of Microsoft Corporation, infringe priceline.com's U.S. Patent 5,794,207 by operating the defendants' ''Hotel Price Matcher'' service, and that the defendants' conduct toward priceline.com violated the Connecticut Unfair Trade Practices Act. On December 20, 1999 defendants moved the Court to dismiss the complaint for failure to name a necessary party, Marketel. On March 21, 2000, the presiding judge stated that he intends to deny defendant's motion to dismiss, and that a decision will be forthcoming. On December 23, 1999 the Court granted priceline.com's motion to supplement the complaint to expressly include defendant's ''Flight Price Matcher'' service. In the lawsuit, priceline.com is seeking declaratory relief, permanent injunctive relief and actual and punitive damages.

From time to time the Company has been and expects to continue to be subject to legal proceedings and claims in the ordinary course of business, and including claims of alleged infringement

12. COMMITMENTS AND CONTINGENCIES (Continued)

of third party intellectual property rights by the Company. Such claims, even if not meritorious, could result in the expenditure of significant financial and managerial resources.

The Company is unable to predict the outcome of the legal proceedings referred to above.

Airline Alliances and Relationships Priceline.com has entered into Airline Participation Agreements with twenty-eight airlines for the supply of airline tickets. The Airline Participation Agreements do not commit the airlines to provide tickets for any particular routes or at a discount to their retail prices, but outline the terms and conditions under which tickets may be sold pursuant to fares, rules and availability that the airlines may provide from time to time. The Airline Participation Agreements are generally subject to termination upon 30 days notice by priceline.com or the airline.

Employment Contracts At December 31, 1999, priceline.com had entered into employment agreements with certain members of senior management that provide for minimum annual compensation of approximately $2.4 million in the aggregate. The agreements provide for periods of employment of up to five years. Generally, the agreements provide for the grant of stock options under the 1999 and 1997 Omnibus Plans.

13. BENEFIT PLAN

Priceline.com adopted a defined contribution 401(k) savings plan (the Plan) during 1998 covering all employees who are at least 21 years old and have completed 6 months of service. The Plan allows eligible employees to contribute up to 20% of their eligible earnings, subject to a statutorily prescribed annual limit. The Company may make matching contributions on a discretionary basis to the Plan. All participants are fully vested in their contributions and investment earnings. During the years ended December 31, 1999 and 1998, the Company did not make any matching contributions to the Plan.

14. OTHER RELATED PARTY TRANSACTIONS

The Founder and Vice Chairman of priceline.com also serves as non-executive Chairman of NewSub Services, Inc. (“NewSub”), a direct marketing company co-founded by him. The Company participates in certain adaptive marketing programs with NewSub. During the years ended December 31, 1999 and 1998, the Company recognized revenue of $202,322 and $0, respectively, and sales and marketing expense of $579,338 and $80,799, respectively, related to these programs.

In June 1998, priceline.com issued a promissory note to a Walker Digital for $1,000,000. The promissory note bore interest at a rate of 6% per annum and was due June 30, 1999. The note has been repaid.

In December 1998, priceline.com completed a private placement of Series B Convertible Preferred Stock with several investors, including GAP and Vulcan Ventures Incorporated. Fees of $850,000 have been paid to a company, in which a director a priceline.com is a director and stockholder, in connection with this transaction.

In April 1999, priceline.com made a $3.3 million loan to Mr. Richard S. Braddock for the payment of taxes related to the issuance to Mr. Braddock of 8,125,000 shares of common stock in August 1998. The loan bears interest at 5.28% per annum. Interest is payable annually and principal is payable in January 2004.

14. OTHER RELATED PARTY TRANSACTIONS (Continued)

In July 1999, priceline.com made a $6.0 million loan to an executive of the Company, pursuant to the terms of his employment agreement dated June 14, 1999. The loan bears interest annually at 5.82% per annum. Subject to certain prepayment obligations and to forgiveness in the event of certain changes of control, death, or termination without cause, pursuant to the terms of this loan, accrued interest and principal are payable after five years, but are forgiven under certain circumstances if the executive remains employed by the Company at that time. Upon any forgiveness of the loan, the Company would recognize as compensation expense an amount up to the amount of principal and interest forgiven.

15. SUBSEQUENT EVENTS

In March 2000, the Company entered into an agreement with Alliance Capital Partners, pursuant to which Alliance has formed an operating subsidiary, pricelinemortgage, for the primary purpose of acting as a broker and/or lender of residential mortgage loans in connection with the priceline.com mortgage service. Priceline.com has agreed to provide $3.62 million of financing to an affiliate of Alliance in the form of a convertible secured note and has agreed to license the ''priceline'' name and business model for use by pricelinemortgage. Alliance has agreed to provide management services to pricelinemortgage, including the procurement of personnel and office space and assistance in obtaining regulatory approvals.

In February 2000, the Company announced the resignation of Paul Francis, Executive Vice President and Chief Financial Officer and the hiring of Heidi Miller as Senior Executive Vice President, Chief Financial Officer, Strategy, Planning and Administration.

In the first quarter 2000, priceline.com made loans to two executives aggregating $5.0 million, which bear interest at 6.56%. Subject to certain prepayment obligations and to forgiveness in the event of certain changes of control, death, or termination without cause, pursuant to the terms of these loans, accrued interest and principal are payable after five years, but are forgiven under certain circumstances if the executive remains employed by the Company at that time. Upon any forgiveness of the loans, the Company would recognize as compensation expense an amount up to the amount of principal and interest forgiven.

16. SELECTED QUARTERLY FINANCIAL DATA (Unaudited)

The follow table sets forth certain key interim financial information for the years ended December 31, 1999 and 1998.

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
	(In thousands, except per share amounts)			
1999:				
Revenues	$ 49,411	$111,564	$ 152,222	$ 169,213
Cost of revenue:				
Product costs	43,659	100,664	133,628	145,104
Supplier warrant costs	381	381	381	381
Total cost of revenues	44,040	101,045	134,009	145,485
Gross profit	5,371	10,519	18,213	23,728
Operating expenses:				
Warrant costs, net			88,389	910,443
Sales and marketing	17,138	17,733	21,413	23,293
General and administrative	3,667	5,503	8,390	10,049
Systems and business development	2,184	3,469	4,593	3,777
Total expenses	22,989	26,705	122,785	947,562
Operating loss	(17,618)	(16,186)	(104,572)	(923,834)
Other income (expense)	458	1,929	2,356	2,377
Net loss	(17,160)	(14,257)	(102,216)	(921,457)
Accretion on preferred stock	(8,354)			
Net loss applicable to common stockholders	$(25,514)	$(14,257)	$(102,216)	$(921,457)
Net loss per basic and diluted common share	$ (0.27)	$ (0.10)	$ (0.71)	$ (5.91)
Weighted average common shares outstanding	94,939	142,320	144,501	156,032
1998:				
Revenues		$ 7,022	$ 9,222	$ 18,993
Cost of revenue:				
Product costs		7,943	8,851	16,702
Supplier warrant costs				3,029
Total cost of revenues		7,943	8,851	19,731
Gross profit		(921)	371	(738)
Operating expenses:				
Warrant costs, net				57,979
Sales and marketing	$ 1,130	6,635	8,160	8,463
General and administrative	1,697	3,102	9,400	3,806
Systems and business development	1,926	3,442	2,801	2,962
Total expenses	4,753	13,179	20,361	73,210
Operating loss	(4,753)	(14,100)	(19,990)	(73,948)
Other income (expense)	50	113	142	244
Net loss	(4,703)	(13,987)	(19,848)	(73,704)
Accretion on preferred stock				(2,183)
Net loss applicable to common stockholders	$ (4,703)	$(13,987)	$ (19,848)	$ (75,887)
Net loss per basic and diluted common share	$ (0.08)	$ (0.17)	$ (0.19)	$ (0.81)
Weighted average common shares outstanding	55,487	81,297	105,411	93,168