

2001

THE ANNUAL REPORT



INTERENTAINMENT

Aktienqesellschaft

Key figures (holding)

	2 0 0 1	2 0 0 0
	Million Euro	Million Euro
SALES REVENUES	31.1	87.8
EBIT*	-100.2	16.2
OPERATING INCOME	-6.2	16.2
RESULT BEFORE INCOME TAX*	-94.9	10.7
NET INCOME	-86.8	5.6
AVERAGE OF EMPLOYEES	28	28

* Including the extraordinary result

Key figures of the stock

SECURITIES IDENTIFICATION NUMBER	WKN: 622 360 / ISIN: DE0006223605	
SHARE CAPITAL	15,005,155.09 Euro	
NUMBER OF SHARES	11,739,013	
OFFER PRICE 8.2.1999	36.00 Euro	
	after split (1:2)	18.00 Euro
SHAREHOLDER STRUCTURE AT 31.12.2001	Rüdiger Baeres	52.86%
	Management, Supervisory Board	0.20%
	Free float	46.94%
PRICE AT YEAR END 28.12.2001	2.48 Euro	
HIGHEST PRICE 2001 (18.1.2001)	19.53 Euro	
LOWEST PRICE 2001 (1.10.2001)	2.27 Euro	

Corporate Calender

FINANCIAL STATEMENT PRESS CONFERENCE	May 6, 2002
ANALYST CONFERENCE	May 2002
1 ST QUARTERLY REPORT	May 28, 2002
ANNUAL GENERAL MEETING	July 16, 2002
2 ND QUARTERLY REPORT	August 29, 2002
3 RD QUARTERLY REPORT	November 28, 2002

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Dear
Shareholders,



Rüdiger Baeres,
Chief Executive Officer

The legal dispute with the American film producer Franchise Pictures had a major influence on fiscal year 2001 for Entertainment AG. This is the reason why certain projects which we expected to have completed have been delayed. But, we were still quite active. The company’s agreement with Kopelson Entertainment commenced at the beginning of the year and our first film projects such as “Blackout”, “Fast Forward” and “Decoy” are underway. In autumn of 2001, our American subsidiary moved into the same office building together with Kopelson Entertainment making our collaboration even more efficient.

Developments within our industry in the last few months have shown us how important the decision was to change from a film distributor to a film producer. We are

now at the top of the value chain. Our agreements with Kopelson Entertainment and Paramount Pictures are just one step in this direction. The success of the Markman Hearing is a positive development for SightSound Technologies in which we own just under 25 per cent, and will provide us with an even broader base. SightSound has four important patents for digital video and audio download from all types of telecommunication lines, including the internet.

We have had positive developments in our legal dispute with Franchise Pictures. The Federal District Court in Los Angeles has granted decisions in our favor on various important motions. Simultaneously, we are continuing with our strategy of reaching a settlement in out-of-court negotiations.

ENTERTAINMENT AG

In fiscal year 2001, despite the Franchise problems we were able to achieve a turnover of 31.1 million Euro. The operating income was minus 6.2 million Euro. Allowances for film rights, provisions in connection with the Franchise lawsuit and depreciations led to a loss of minus 86.8 million Euro. All possible risks in connection with the dispute have now been taken into consideration enabling us to look forward to a bright future.

Thank you for the trust that you put in our company even in difficult times and in a tense market environment.

A handwritten signature in black ink, reading "Rüdiger Baeres".

Rüdiger Baeres

Chief Executive Officer
of Entertainment AG

Business 2001



Achim Gerlach,
Chief Financial Officer

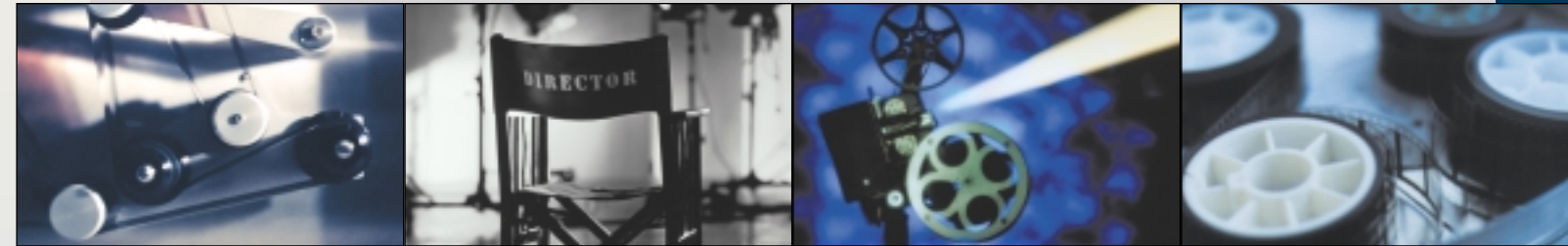
Entertainment is setting up a broader base for itself

The economic environment presented the film industry with a number of challenges in fiscal year 2001. Entertainment AG searched for new ways to position itself better for the long run. The transition from a film rights distributor to a film producer has brought new opportunities. The agreements with Kopelson Entertainment and Paramount Pictures are only the first steps for Entertainment to set up a broader base for its overall business model. In the future, a large portion of the films brought into the cinemas by Entertainment will be a result of internal productions or production

alliances. Entertainment will seek to work with a variety of film producers and form strategic business partnerships in order to produce interesting and commercially viable projects. And the deputy chief executive officer, Stephen Brown, is the company's production expert.

Entertainment AG set up its American subsidiary in 2000 to expand the company's activities in Hollywood and to complete its transition from a film rights distributor to a film producer. Since the autumn of 2001, the company's employees at USA-Entertainment, Inc., have worked in close proximity to Kopelson Entertainment since they now occupy offices in the same building.

Entertainment continues to develop its business model through risk aversion and by maintaining budgetary and creative control of the projects it undertakes to finance and produce. This means that a large portion of the film budget is already covered with pre-sale distribution commitments before production begins. The company balances these pre-sales commitments with its retention of rights in certain territories in order to maximize the best economic outcome. This financing model allows Entertainment to launch large-scale film projects while keeping its financial risk down to a minimum.



New Business Partners

Entertainment and Kopelson Entertainment entered into a two year first-look and co-financing agreement with Paramount Pictures. Paramount will distribute the films produced under the arrangement in all media in North America.

Digital Sales

In the age of the internet, people don't want to wait anymore - that also applies to films and music. Digital technology will revolutionize the manner in which films and music are distributed. Experts forecast that films carried over the internet will replace the video and pay-TV business in the long term. Entertainment has holdings in SightSound Technologies (of just under 25 per cent), giving our media enterprise a cornucopia of opportunities. The prospects for SightSound Technologies have increased after the affirmative ruling of the Markman Hearing in February 2002. The court ruled that the patent for audio and video download via telecommunication lines in the United States that Arthur Hair, the co-founder of SightSound, applied for in 1988 and that was issued in 1993 also applies to the internet.



Merchandising

The field of merchandising with the brandname of "Rudolph" continues to develop in a gratifying fashion. Entertainment has all license rights for the German-speaking countries in Europe for the red-nosed reindeer through its 100% subsidiary, Entertainment Animation & Merchandising GmbH. The second Rudolph film will be coming onto the market in the autumn of 2002 and continued positive growth can be expected.

The Legal Dispute with Franchise Pictures

Civil action was filed by Intertainment against Franchise Pictures in the Federal District Court in Los Angeles at the end of December 2000. Intertainment filed the lawsuit due to Franchise fraudulently inflating film budgets. A ruling is expected at the end of November 2002.

The year 2001 was dominated by the discovery proceedings that will be concluded at the beginning of June 2002. The American discovery proceedings allow certain evidence to be requested from the litigants and from third parties and from depositions. Intertainment has made extensive use of this procedure and has held depositions of witnesses from Franchise Pictures, the Imperial Bank (now Comerica Bank) and the completion bond companies.

The length of proceedings is determined by the scope of documents and interrogations requested by both sides. There were delays because Franchise and Comerica petitioned for a protective order for certain documents from the court for reasons of confidentiality and secrecy. This order does not allow discovery documents to be published and third parties are only granted insight in selective cases.

Recently, Intertainment petitioned the court to reverse the protective order so it could provide important discovery documents to the chartered accountants so they could audit the balance sheet. Without these legal documents a proper balance sheet could not be prepared. As a result, Intertainment requested that the deadline for submitting the annual financial statement and annual report to Deutsche Börse AG be extended, which request was granted.

Separate from the Franchise lawsuit, there were arbitration proceedings at the end of 2001 in connection with the payment of the second installment of 6.5 million USD for the Franchise film Caveman’s Valentine. The National

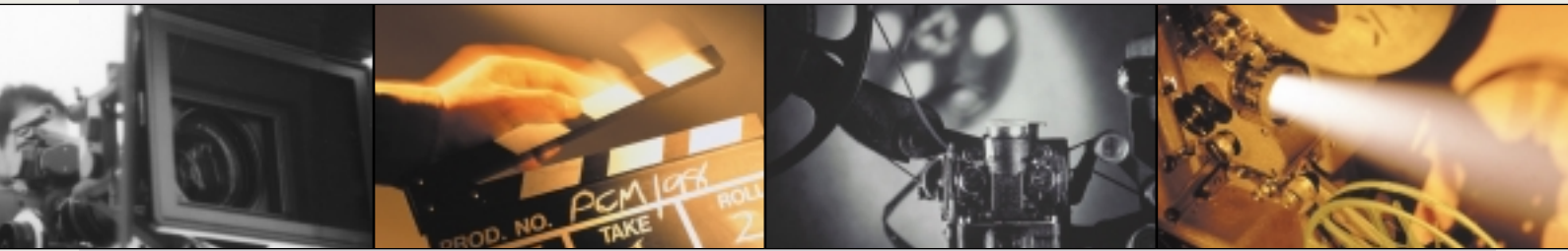
INTERENTAINMENT AG

Bank of Canada, one of the financing banks for this picture, instituted these proceedings after Intertainment objected to payment because the film was not delivered in conformity with the agreement. A judge of the Superior Court of California upheld the arbitration award that set forth that the film should be accepted as delivered and the installment due should be paid. Intertainment has appealed this decision.

The progress of the litigation with Franchise Pictures

December 18, 2000	Negotiations with Andrew Stevens, President and COO of Franchise Pictures, concerning an amicable settlement break down
December 21, 2000	Intertainment takes legal action against Franchise Pictures before the Federal District Court of Los Angeles Franchise Pictures reacts by taking legal action against Imperial Bank
February 20, 2001	Intertainment also takes legal action against Imperial Bank
April 18, 2001	Judge decides that the general case is to be suspended and that priority should be given to the arbitration proceedings against Imperial Bank
May 31, 2001	Intertainment withdraws the law suit against Imperial Bank in order to further pursue the legal proceedings against Franchise Pictures
June 13, 2001	The judge rescinds the temporary suspension of the lawsuit against Franchise Pictures
August 17, 2001	Intertainment files the third version (update) of the statement of claim against Franchise Pictures
August 27, 2001	The date of the hearing is fixed for 10 September 2002. Completion of the discovery stage is scheduled for 27 May 2002
September 20, 2001	The court orders Franchise Pictures to respond to the questionnaires presented by Intertainment on the budgets of the films in dispute The court also grants a petition from Intertainment that obliges the Imperial Bank to release documents
September 25, 2001	The court rejects a petition from Imperial Bank filed because the bank wanted to refuse to release documents to Intertainment for reasons of “confidentiality”
October 13, 2001	The court orders that Film Finances Canada has to submit documents and answer questions on the budgets
October 31, 2001	The case is assigned to a new judge meaning that there are delays in the court dates
December 26, 2001	The judge sets June 3, 2002 as the final date for the discovery proceedings and sets November 19, 2002 as the date for proceedings (ten days for a jury trial)
January 24, 2002	The court orders that Franchise Pictures has to surrender budget documents and imposes monetary sanctions and that Franchise Pictures cannot assert “confidentiality”
January 29, 2002	The court orders monetary sanctions against Franchise Pictures again because they did not answer all questions in connection with the film budget
February 19, 2002	The court orders monetary sanctions against Comerica Bank (earlier known as the Imperial Bank) because it disregarded court orders

THE FILM PROJECTS



Stephen Brown,
Deputy Chief Executive Officer
Chief Executive Business Development

In the autumn of 2001, the American subsidiary of Intertainment AG moved into its new offices on Sunset Boulevard in Hollywood. USA-Intertainment, Inc. is headed by Stephen Brown, the deputy chief executive officer and chief executive business development. When Brown was at Kopelson Entertainment, he was a co-producer and executive producer on ten films, among them such hits as *The Fugitive*, *Seven*, *A Perfect Murder*, *Eraser* and *The Devil's Advocate*.

Intertainment shares the office space with Kopelson Entertainment, enabling Intertainment to work very closely with the Kopelson team on various projects. They include:

Blackout

A very self-confident policewoman suffering from sudden blackouts is investigating a series of murders. To her horror, she discovers that all of the victims are men she had brief relationships with. Finally, the evidence found substantiates the suspicion that she herself could be the murderer.

Shooting is supposed to start for this thriller in the third quarter of 2002. Ashley Judd, who played at Morgan Freeman's side in *"Kiss the Girls"* and with Tommy Lee Jones in *"Double Jeopardy"*, is attached to play the female lead. She will be seen next in German cinemas with Morgan Freeman in *"High Crimes"* in August 2002.

The Film Projects

INTERENTAINMENT AG

Decoy

This thriller is about a good-looking and up-and-coming actress who is hired by a rich woman as a decoy. The woman wants to divorce her husband and hires the actress to seduce him. When the husband is suspected of murder, the police force the actress to help. She soon finds herself in a world of unbridled passions and is horrified when she learns that she is the prime suspect.

*"Seven" © 1995, New Line Productions, Inc. All rights reserved.
Photo by Peter Sorel. Photo appears courtesy of New Line Productions, Inc.*



Producer Arnold Kopelson (left) confers with stars
Brad Pitt (center) and Morgan Freeman (right) on the set
of New Line Cinema's mystery-thriller *"Seven"*

Fast Forward

A CIA man believes that he was in a coma for 18 months. In fact, he was the victim of an intricately planned out deception to get secret information out of him. Suddenly, he's in a world where nothing is what it seems to be.

Window to Atlantis

In this science fiction film project, a father loses his daughter at sea when an alien spaceship crashes nearby. In his desperate search for her, her father gets on the track of a plot by the government that tries to conceal what it knows about the aliens.

All of these projects are part of the first look and co-financing agreement between Intertainment and Paramount Pictures, one of the leading studios in Hollywood. Paramount Pictures pays a portion of the development and production costs of these film projects that are produced jointly with Intertainment AG and Kopelson, and acquires the distribution rights for these films in North America.



Right in the Middle of the Future Market

Digital Distribution

Ordering films via the internet is easier and more convenient than going to a video store and ordering movies online will turn into a multi-billion dollar business. Entertainment is placing its bets on the future market of digital distribution and, with its 24.8% holdings in the Pennsylvania-based SightSound Technologies, Inc., it has positioned itself to capitalize upon a promising opportunity in the American market.

SightSound has Set Milestones for Digital Sales

Since 1995, SightSound has been pursuing the goal of becoming the leading technology enterprise for reliable digital sales of films and music via the internet. In 1995, SightSound was the first company to sell music online. In 1999, the first full-length feature film was sold via the internet. And in the summer of 2000, SightSound was once again the first company in the market that simultaneously launched a film worldwide via the internet. Finally in 2001, SightSound sold the first film in Window Media Format to a digital cinema via the internet. The people at SightSound, particularly its founders Arthur Hair and Scott Sander, are committed to searching for technical innovations in digital online sales.

SightSound is Preparing Itself for the Future of Digital Sales

SightSound benefits from its diversity and innovativeness in the quickly growing and changing market of digital sales. SightSound has focused upon three business areas to be able to efficiently utilise existing synergies: patent licensing, internet platform and e-cinema.

Patent Licensing: SightSound is Successfully Defending its Far-Reaching Patents

SightSound, with its patented application for the digital download of audio and video data through the internet, is ideally positioned to license its system to film studios and other internet portals. Additionally, these patents, assuming they can be asserted in the courts, allow SightSound to charge license fees for every piece of music or motion picture download via the internet.

SightSound's numerous innovations include a portfolio of patents in the digital sales of audio and video data. As early as 1993, Arthur Hair, co-founder of SightSound, received the patent for downloading audio and video through telecommunication lines in the United States. This formed the base for three other patents in digital downloading technology. Since January of 1998 SightSound has had a legal dispute against Bertelsmann's subsidiary CDNow and N2K regarding the enforceability of the patent issued in 1993. This legal dispute will probably be decided in the coming year.

SightSound

SightSound had its first success in its ongoing patent dispute in February 2002. In what is known as the Markman Hearing, the United States District Court in the Western District of Pennsylvania agreed with SightSound Technologies that its patent also extends to internet. Scott Sander, the CEO of SightSound Technologies, sees the court ruling as an important step toward asserting this patent in the long term. The fact that the patent has been confirmed forms the basis for SightSound to resume co-operation talks with the major motion picture film studio.

Internet Platform: Digital Sales of Films is the Future

The technology developed by SightSound makes it possible to offer several hundred-thousand films or pieces of music on a daily basis. The content is encoded and downloaded through the internet platform. The technology enables SightSound to serve the marketplace from the beginning of what is expected to be a period of rapid growth. According to the American market research institute Nielsen/NetRatings, for the first time American internet users spent more time on the web via broadband access than through conventional dial-up connections. 51% of the total 2.3 billion online hours in January of this year were connected by high-speed access. Of course, the majority of high-speed access is established through a computer. However, it is expected that it won't be long until private households will make digital entertainment such as video-on-demand a mass market.

Dynamic development in broadband technology is also expected in the European market. The market researcher Forst & Sullivan believes that high-speed internet services and the burgeoning volume of data will create an enormous demand for broadband access. According to a new analysis, market researchers are expecting with an increase from approximately 3.8 million European subscribers by the end of 2001 to 28.1 million subscribers in 2008. This new technology will gain momentum in Europe beginning in 2003, and will also make video-on-demand a major business.

INTERNET



e-cinema: Billions of Dollars will be Redistributed in the Next Few Years

A study of ScreenDigest says that distributing films cost the big major U.S. studios between 4 and 5 billion US Dollars every year. These costs particularly include postproduction, manufacturing a series of film prints (major films are released on the average with over 1,000 prints) and shipping the material all around the world. Digital sales of films not only means lowering costs for the studios, but it also makes it easier to process the films in postproduction, thus creating greater operating efficiency. Simplified logistics for the cinema operator by digitally reloading the films also makes it possible to launch the films simultaneously all around the world. SightSound has been able to gain initial experience of downloading films via the internet to digital cinemas in 2001 and it will continue to modify its equipment accordingly to increase its attractiveness for the studios.

Rudolph, the Red-Nosed Reindeer is a Star

With more than 150 licensed products, Rudolph, the Red-Nosed Reindeer was once again a star during the 2001 Christmas season. Although competition was particularly great this year, Rudolph was able to position himself well and he's increasingly becoming a significant business sector for Intertainment. Intertainment owns all licensing rights for the German-speaking countries in Europe for the red-nosed reindeer through its wholly-owned subsidiary, Intertainment Animation & Merchandising GmbH. This American classic surpassed all expectations in its third year. Sales of the Rudolph video was in the top ten again during the Christmas season in Germany and it maintained top positions in the sales charts in Austria and Switzerland.

Rudolph's growing success is based upon a longterm networked marketing strategy. This includes a co-operation with UNICEF and optimum integration of licensing and trade partners, thus establishing this character in the family environment. Rudolph was on tour during the entire year with the Kids for Kids campaign and it continues to tour this year as well. Success for Rudolph is also success for UNICEF, the United Nation's children's fund. Rudolph, as the symbol of the Kids for Kids campaign launched by Intertainment, handed over 230,000 Euro to UNICEF in 2001. This means that Rudolph has earned a total of more than one million Euro for disadvantaged children of the earth since he was introduced. The declared goal of the Kids for Kids campaign is to help these children. Under the direction of its managing director Heinz Ehmann, Intertainment Animation & Merchandising is always working on new strategies, looking for appropriate business partners and developing ideas for dynamic events to promote his likeable character.

All of the little and big fans of Rudolph will be looking forward to autumn of 2002. A new adventure of the best known reindeer in the world will be coming into the market in October of 2002 with the title "Rudolph II – Rudolph and the Island of Misfit Toys". Rudolph and his friends go through a series of exciting adventures to save Christmas again. And, as with the first video, well-known actors will be lending their voices to the cartoon characters.



The Development of Shares

The turbulences on the New Market continued in 2001 after an eventful year in 2000. The media sector was greatly affected by the general loss of confidence among investors and the overall weakness in the economy. Intertainment's share price paralleled the comparative indices during the year. In the final analysis, however it closed slightly better than the sector index. For instance, Intertainment's shares lost 48% in the course of the year while the New Market Media & Entertainment Index posted losses of 65% in the same period. The uncertainty of the legal dispute with Franchise Pictures affected the share price as soon as civil action was filed at the end of December 2000. The collapse in the share price and the corresponding lower market capitalisation resulted in the Company's being removed from the Nemax 50 in March of 2001. Furthermore, the fact that shares deposited as collateral for a private guaranty by Rüdiger Baeres, the chief executive officer, were used by the collateralising bank over the stock market in March and April 2001, had a negative effect. Intertainment AG is listed on the New Market and its average daily share turnover was 58,713 on Xetra and 29,246 on the Frankfurt Floor in 2001. The average daily turnover was 8,834 at the other German stock markets.

The profit per share at December 31, 2001 was minus 7.36 Euro. A dividend will not be paid for 2001.

Indicated Stock Price Development from January 2, 2001 to December 28, 2001



Active Financial Communication

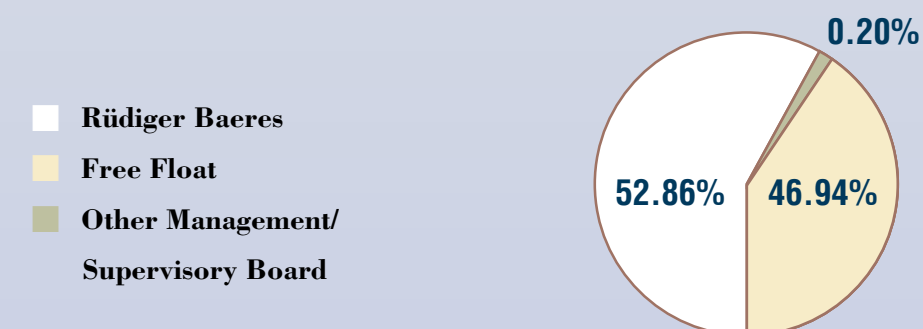
Despite confidentiality restrictions due to its current legal dispute in the United States, Intertainment AG attempted to have open and active financial communication towards the press, analysts, investors and private investors. For example, last year the management board elucidated the company's current position to the financial markets in two analyst conferences, several press conferences and a number of personal conversations. Furthermore, they replied to a number of questions from private investors respecting the principle of fair disclosure.

Capital Measures

The annual general meeting of shareholders in Munich on June 27, 2001 resolved a series of capital measures that gave the management board latitude for action in raising capital. For instance, the annual general meeting created authorised but unissued capital II of up to 383,469 Euro for serving the share option programme for 2001 and it authorised approved capital II of up to 4.3 million Euro and authorised but unissued capital III of a total of 6 million Euro for issuing convertible bonds and/or option bonds.

Furthermore, Intertainment AG had the annual general meeting grant the acquisition of its own shares up to 10% of the capital base. Since none of the reasons for authorising its own shares approved by the annual general meeting were given, the management has to date not made use of this capital market instrument.

Shareholder Structure



Report of the Supervisory Board



Dr. Matthias Heisse, Chairman

During the period under review the Supervisory Board fulfilled all the duties required of it by law and by the company's statutes and continuously consulted with the company's management and monitored its activities. It received regular reports from the Board of Management about the development of the company and about important items of its business and discussed these with the Board of Management. Aside from the general development of the company and important individual items of business, discussions were held especially with regard to decisions relating to company strategy and the internationalization of Intertainment activities. Where required by law or in accordance with the company's statutes, the Supervisory Board gave or withheld its approval – following a thorough examination of the issues involved – of proposals put forward by the Board of Management.

The Supervisory Board devoted special attention, together with the Board of Management, to the questions of the risks arising for the company out of the lawsuit against the Franchise Group, together with other parties, and of the future financing of the company.

The Supervisory Board held seven sessions during the year 2001. In addition, regular meetings took place with the company's Board of Management, in which important issues were discussed and reviewed. The Supervisory Board devoted continuing attention in the course of several sessions to the adjustment of the company's business strategies as a result of fundamental changes in the market, while also working closely with the Board of Management both to promote its continuing focus on the company's function as a producer and to develop new and more far-reaching options for the future.

In its first session on 16th January 2001 the Supervisory Board discussed in detail with the Board of Management the status of the company's lawsuit against Franchise and the effects of this on its suppliers. In addition, planning for the year 2001 was discussed. On 12th February 2001 the Supervisory Board held another session, to discuss mainly the lawsuit against the Franchise Group but also the financing of the company. In the session of 28th March 2001 the Board of Management submitted the company's financial statements for the year 2000 to the Supervisory Board. In the course of this session, a detailed discussion took place of the points raised with regard to the company's balance sheet by the auditors of the Intertainment Group, KPMG Deutsche Treuhandgesellschaft Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, Berlin and Frankfurt-am-Main, for which the Supervisory Board brought in an independent auditor of its own. The Supervisory Board has already provided detailed information about the results of this session as well as about the further investigations of KPMG in its report on the business year 2000 dated 24th April 2001.

The auditors gave a report on the main findings of their investigations in the balance sheet meeting on 24th April 2001. The Supervisory Board approved the results as presented in their report. This was also recorded in the Supervisory Board's report of 24th April 2001 on the business year 2000.

On 27th June 2001 the Board of Management again reported with even more emphasis about the progress of the lawsuit against the Franchise Group and its impact on the company's sub-licensees. In a further joint session of the Board of Management and Supervisory Board on 10th September 2001 the topics discussed included, aside from the current situation of the Franchise lawsuit and the financing of the company, the position with regard to the company's participation in Sight Sound Technologies Inc. as well as various matters relating to the Board of Management. In the session held on 20th December 2001 the Board of Management reported in detail to the Supervisory Board both about the position with regard to the Sight Sound participation and about the progress made with the Franchise lawsuit.



Dr. Ernst Pechtl, Deputy Chairman

INTERENTAINMENT AG

By a resolution passed by the Supervisory Board on 17th September 2001, the appointment of Mr. David Williamson as Member and Deputy Chief Executive Officer of the Board of Management was revoked. With a view to future requirements, the Supervisory Board made some necessary changes in the direction of the company's course and, following a resolution passed during its session of 10th September 2001, appointed Mr. Stephen Brown to be the Deputy Chief Executive Officer of the company's Board of Management. The Supervisory Board wishes nevertheless to thank Mr. David Williamson for his activities on the company's behalf.

The Annual General Meeting of Shareholders on 27th June 2001 chose the KPMG Treuhandgesellschaft Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, Berlin and Frankfurt am Main, to audit the company's results for the year 2001.

In the session held on 26th March 2002 the Board of Management submitted its preliminary figures for the financial statements of the year 2001. During the same session a detailed discussion took place of various balance sheet questions raised by the Board of Management and by KPMG.

In view of the fact that a number of balance sheet questions were still unresolved, the company applied to the Deutsche Börse AG on 26th March 2002 for an extension of the deadline for publication of its financial statements for the business year 2001. The Deutsche Börse accepted this application on 26th March 2002 by approving an extension of the deadline to 29th April 2002.

KPMG has completed its audit of the accounting, annual financial statements and company status report of Intertainment AG as well as of the company's consolidated accounts and group management report for the business year ended 31st December 2001. It has also certified its unqualified approval of the accounting, annual financial statements and management report of Intertainment AG as well as of the company's consolidated accounts and group management report. The auditors gave a verbal report on the main findings of their investigations at the annual balance sheet session held on 25th April 2002. The written report was submitted to the Supervisory Board on 29th April 2002 by the auditors. The Supervisory Board gave its official approval of the results of the auditors' investigations.

In addition, the Supervisory Board examined the financial statements at 31st December 2001, the report on the status of the company, the Board of Management's proposal for the allocation of profits, the consolidated financial statements and the consolidated management report. No objections were raised, with the result that the Supervisory Board has officially approved the company's financial statements, which are herewith adopted. The Supervisory Board has also officially approved the Board of Management's proposal regarding the appropriation of profits.

Both the members of Management and the staff of the company have shown a high degree of commitment in the past year in their endeavours to keep the company progressing despite the challenging market situation and to solve the problems that have arisen. The Supervisory Board would like to express its appreciation and grateful thanks to everyone concerned for their hard work and dedication.

The Supervisory Board, Munich, April 29, 2002

Matthias Heisse

Dr. Matthias Heisse, Chairman of the Board



Dr. Wilhelm Bahner, Member

Consolidated Balance Sheet as at December 31, 2001
in Accordance with the International Accounting Standards (IAS)

INTERENTAINMENT GROUP

ASSETS			
	Item	31.12.2001	31.12.2000
		€	€
A. Fixed assets			
I. Intangible fixed assets	VI.1		
1. Franchises, trademarks and similar rights and assets, as well as licences to similar rights and assets		262,872.62	334,508.35
2. Down payments made		4,860,625.75	0.00
		5,123,498.37	334,508.35
II. Property, plant and equipment			
Other fixed assets fixtures, fittings and equipment		2,554,680.66	528,689.29
III. Financial assets			
Investments		15,036,272.25	20,048,363.00
		22,714,451.28	20,911,560.64
B. Current assets			
I. Inventories	VI.2		
1. Film rights		27,700,378.54	64,008,366.36
2. Merchandise		177,431.38	503,898.09
3. Down payments made		24,569,986.34	6,903,718.14
		52,447,796.26	71,415,982.59
II. Accounts receivable and other assets	VI.3		
1. Trade accounts receivable		54,242,348.43	85,447,647.36
2. Other assets		12,373,039.07	12,898,021.16
		66,615,387.50	98,345,668.52
III. Cash on hand and in bank balances	VI.4		
		14,231,229.85	72,851,361.01
		133,294,413.61	242,613,012.12
C. Deferred taxes	VI.5		
		5,213,782.11	646,169.48
		161,222,647.00	264,170,742.25

Consolidated Balance Sheet as at December 31, 2001
in Accordance with the International Accounting Standards (IAS)

INTERENTAINMENT GROUP

LIABILITIES			
	Item	31.12.2001	31.12.2000
		€	€
A. Shereholder's equity	VI.6		
I. Subscribed capital	VI.6.1	15,005,155.09	15,005,155.09
II. Capital reserves	VI.6.2	149,523,096.82	149,524,596.48
III. Retained earnings	VI.6.3		
Statutory reserve		115,806.59	115,806.59
IV. Profit carried forward		12,311,232.50	6,742,204.98
V. Loss for the year		-86,806,787.35	5,569,027.52
		90,148,503.65	176,956,790.66
B. Provisions	VI.7		
1. Provisions for taxation	VI.7.1	923,956.02	8,523,057.02
2. Other provisions	VI.7.2	11,224,203.37	19,865,697.19
		12,148,159.39	28,388,754.21
C. Liabilities	VI.8		
1. Liabilities due to banks		23,226,641.81	27,096,744.43
2. Down payments received on orders		3,265,691.80	3,968,970.05
3. Trade accounts payable		26,301,508.05	23,418,549.63
4. Other liabilities		3,896,358.87	3,328,505.82
		56,690,200.53	57,812,769.92
D. Deferred tax liabilities		2,235,783.43	1,012,427.46
		161,222,647.00	264,170,742.25

**Consolidated Income Statement for January 1, to December 31, 2001
in Accordance with the International Accounting Standards (IAS)**

INTERENTAINMENT GROUP

	1.1.– 31.12.2001	1.1.– 31.12.2000
	€	€
1. Sales	31,145,496.19	87,810,915.45
2. Other operating income	9,614,979.34	10,114,211.66
	40,760,475.53	97,925,127.11
3. Cost of materials		
a) Cost of film rights and accompanying services	21,727,870.40	53,613,091.33
b) Cost of purchased merchandise	439,943.73	678,334.99
c) Cost of services rendered	331,673.13	550,389.00
	22,499,487.26	54,841,815.32
4. Personnel expenses		
a) Wages and salaries	4,347,336.75	3,052,869.66
b) Social security contributions	146,668.37	169,868.23
	4,494,005.12	3,222,737.89
5. Depreciation on intangible assets and property, plant and equipment	398,820.02	192,785.55
6. Other operating expenses	19,616,061.14	23,509,057.98
7. Depreciation of financial assets	5,012,090.75	0.00
8. Interest income/expense	5,265,274.33	-5,497,916.85
9. Profit/loss on ordinary operations	-5,994,714.43	10,660,813.53
10. Extraordinary income	53,493,922.65	0.00
11. Extraordinary expenses	142,441,573.05	0.00
12. Extraordinary result	-88,947,650.40	0.00
13. Taxes on income	-8,136,815.32	5,090,652.72
14. Other taxes	1,237.84	1,133.29
15. Group net loss (prior year income)	-86,806,787.35	5,569,027.52
16. Retained earnings brought forward/loss carried forward	12,311,232.50	6,742,204.98
17. Group net loss (prior year income)	-74,495,554.85	12,311,232.50
Basic earnings per share	-7.36	0.52
Diluted earnings per share	-7.36	0.52

**Consolidated Statement of Cash Flows for January 1, to December 31, 2001
in Accordance with the International Accounting Standards (IAS)**

INTERENTAINMENT GROUP

	2001	2000
	T€	T€
Net income before extraordinary items	2,141	5,569
Depreciation of fixed assets	399	193
Depreciation of financial assets	5,012	0
Increase (prior year decrease) in provisions	-17,253	11,458
Gain from the retirement of fixed asset items	0	-4
Decrease (prior year increase) in inventories	18,968	-49,347
Decrease (prior year increase) in trade receivables	31,205	-64,936
Increase in other assets	-4,043	-9,515
Decrease in trade accounts payable and other liabilities	4,983	17,709
	41,412	-88,873
Extraordinary items not affecting cash flows	-141,036	0
Extraordinary items affecting cash flows	52,088	0
Cash used for current operations	-47,536	-88,873
Proceeds from asset sales	0	16
Payments made for investments in property, plant and equipment	-7,213	-588
Cash used for investing activities	-7,213	-572
Payments received from capital increases	0	103,850
Payments made to shareholders (dividends)	0	0
Capital increase expenses	0	-2,577
Decrease in liabilities due to banks	-3,870	7,020
Cash used for financing activities	-3,870	108,293
Changes in cash and cash equivalents affecting income	-58,619	18,848
Changes in cash and cash equivalents caused by exchange rates and other factors	-1	44
Cash and cash equivalents at the beginning of the period	72,851	53,959
Cash and cash equivalents at the end of the period	14,231	72,851

Development of the Group-Shareholders' Equity
in Accordance with the International Accounting Standards (IAS)

INTERENTAINMENT GROUP

	Share capital	Capital reserve	Statutory reserve	Distributable profit	Total
	T€	T€	T€	T€	T€
Balance 31.12.1998 (HGB code)	9,296		91	177	9,564
IAS reconciliation					
Adjusting item for legal reorganisation		-7,951		1,549	-6,402
Foreign currency valuation				63	63
Deferred taxation				6	6
Balance 31.12.1998 (IAS)	9,296	-7,951	91	1,795	3,231
Net income 1999				6,701	6,701
IPO	3,098	40,534			43,632
IPO expenses		-1,812			-1,812
Dividend				-1,729	-1,729
Appropriated to revenue reserves			25	-25	0
Balance 31.12.1999	12,394	30,771	116	6,742	50,023
Net income 2000				5,569	5,569
Differences on exchange		44			44
Share exchange	246	19,802			20,048
Capital increase	2,365	101,485			103,850
Capital increase expenses		-2,577			-2,577
Balance 31.12.2000	15,005	149,525	116	12,311	176,957
Net loss 2001				-86,807	-86,807
Differences on exchange		-2			-2
Balance 31.12.2001	15,005	149,523	116	-74,496	90,148

In the financial year 1998 INTERENTAINMENT for the first time produced a reconciliation between the annual financial statements according to the German Commercial Code and according to the International Accounting Standards. The effect of this reconciliation at that time was TEUR 1,618.

Notes to the Consolidated Financial Statements as at December 31, 2001
in Accordance with the International Accounting Standards (IAS)

INTERENTAINMENT GROUP

(I) General Information

The consolidated financial statements of Intertainment Aktiengesellschaft are compiled pursuant to Section 292a of the German Commercial Code (HGB) in accordance with the International Accounting Standards (IAS). They were prepared during the year under review without a reconciliation to HGB. The Company is thus exempted from the requirement to publish consolidated annual financial statements pursuant to the regulations of Section 290 seq. of the German Commercial Code.

The consolidated financial statements are based on uniform accounting and valuation methods with regard to the companies consolidated. Intertainment prepares consolidated financial statements pursuant to the German Commercial Code and adjusts these to the International Accounting Standards on the basis of the IAS adjustments made to the individual financial statements of the companies to be consolidated.

Intertainment prepared a reconciliation to International Accounting Standards for the first time in the 1998 financial year. Taking into account the fact that the incorporation of INTERENTAINMENT Licensing GmbH constitutes a legal reorganisation, the resultant change in profit/loss in 1998 in relation to the financial statements prepared according to the German Commercial Code was TEUR 1,618. We refer to the analysis of shareholder's equity for a detailed explanation of this effect.

The type-of-expenditure format was chosen for the income statement.

(II) Information on the date of consolidation and the companies consolidated (IAS 22)

Intertainment AG and its subsidiaries INTERENTAINMENT Licensing GmbH, Intertainment Animation & Merchandising GmbH and USA-Intertainment Inc. were included in the consolidation.

The Intertainment Group comprises the following companies in which Intertainment AG holds a direct 100% interest:

Notes to the Consolidated Financial Statements as at December 31, 2001
in Accordance with the International Accounting Standards (IAS)

INTERENTAINMENT GROUP

Company	Subscribed capital (previous year) T€	Net result 2001/HGB (previous year) T€	Share %	Description
Intertainment AG, Ismaning	15,005 (15,005)	-20,627 (-9)		The company's purpose is the acquisition and exploitation of film rights, trading in film rights, the production and co-production of films, merchandising, the distribution and dissemination of media content in the audio and video segments using all means of communication, the award of licences, and the execution of related types of business. Financial holding company and counterparty with the producer Arnold Kopelson.
INTERENTAINMENT Licensing GmbH, Ismaning	946 (946)	-70,342 (4,431)	100	The company's purpose is the development of media concepts and trading in film rights.
Intertainment Animation & Merchandising GmbH, Ismaning	358 (358)	35 (-430)	100	The company's purpose is trading in film and merchandising rights with respect to cartoons.
USA-Intertainment Inc., Los Angeles	105 (105)	144 (-14)	100	The company's purpose is to look after contracts with American companies and to search for new film projects, potential licence and production agreements and to exploit these commercially.

The consolidated financial statements were prepared as of the reporting date of the parent company Intertainment AG, Ismaning, namely on December 31, 2001. The annual accounts of the subsidiaries included in the consolidated financial statements were also prepared as of this date.

(III) Methods of consolidation

1. Capital consolidation – first-time consolidation

The capital consolidation was carried out using the book-value method by setting off the book value of the shares against the equity of the subsidiaries included in the consolidated financial statements at the time of their acquisition (IAS 22). Since the 1999 financial year the integration of INTERENTAINMENT Licensing GmbH in the consolidated financial statements has been treated as a legal reorganisation. As a result, the difference arising on capital consolidation was offset directly against the capital reserve. No goodwill was recorded.

Notes to the Consolidated Financial Statements as at December 31, 2001
in Accordance with the International Accounting Standards (IAS)

INTERENTAINMENT GROUP

2. Intercompany eliminations

Accounts receivable and liabilities as well as income and expenditure between the companies included in the consolidated financial statements are eliminated.

3. Elimination of intercompany profits

The intercompany profits arising from business transactions within the Intertainment Group have been eliminated.

4. Currency translation (IAS 21)

The translation of the amounts carried on the balance sheet of USA-Intertainment Inc. at the exchange rate applying on reporting date and the translation of the amounts carried in the income statement at average exchange rates lead to currency translation differences amounting to TEUR 42. These were booked to the shareholder's equity translation reserve and do not affect the income statement. In addition, within the framework of the consolidation of the individual company financial statements, there were currency translation differences amounting to TEUR 51, which were booked to the income statement.

(IV) Accounting and valuation methods

1. Fixed assets

Intangible assets are carried at acquisition cost. If the acquisition cost is attributable to various partial rights, then the cost is allocated on the basis of the anticipated sales revenues. Scheduled depreciation is charged according to the assets' useful commercial life or rate of usage. In the case of software this is 3 to 5 years and for film rights 4 to 7 years. Intertainment compensates producers before projects begin and capitalises these payments and project the costs that have already been incurred as payments on account for intangible fixed assets. These payments are offset against the future production costs of a film project.

Property, plant and equipment is carried at acquisition cost minus depreciation. Depreciable property, plant and equipment are depreciated on a scheduled basis. Depreciation is based on the estimated useful life using the straight-line method. The useful life for fixtures, fittings and equipment is 4 to 10 years. Minor value assets up to an amount of EUR 410 are fully depreciated in the year of acquisition and shown as a disposal.

Financial fixed assets are carried at acquisition cost. Within the framework of an exchange of shares, the cost of acquisition consists of the value of shares given up at the reporting date. A consolidation of the interests where Intertainment does not hold 100% of the shares or voting rights is undertaken according to IAS 28 only if more than 20% of the shares or voting rights are held and a significant influence is exercised.

INTERENTAINMENT GROUP

2. Current assets

The film rights are valued at acquisition cost minus amortisation of exploited partial rights. The costs of financing with borrowed capital are treated as an expense according to IAS 23. The cost of acquisition is allocated to the partial rights cinema, video, video-on-demand, pay-TV and free TV. Films which it is not possible to exploit in the cinema segment are allocated to the remaining partial rights using revised allocation percentages.

Film rights are capitalised at the time of technical acceptance of the delivered film material by an independent laboratory.

The scheduled amortisation of the acquisition cost allocated to the partial rights is based on the decline in economic value of the corresponding licences. The basis of assessment is taken from anticipated sales in the sub-segments in proportion to total sales. Intertainment assumes up to three utilisation cycles with an overall exploitation period of up to 25 years. When stating sales for individual partial rights, the relevant segment is amortised analogously at the previously defined percentage rate.

Within the framework of the loss-free valuation (IAS 2) of film rights carried on the balance sheet, the exploitability of such rights is examined and where appropriate unscheduled amortisation is applied if the forecast proceeds of sale are below the capitalised residual book values. In order to determine the discounted value of the film rights, among other things a valuation report is obtained from an auditor.

Trading stock carried in inventories is carried at cost of acquisition. Goods already delivered for which marketing partners have a right of return continue to be carried by Intertainment at acquisition cost in inventories. Sale is recorded at the time of the expiry of the right of return, which leads to the recording of the cost of materials.

If prior to the technical acceptance of the film material Intertainment makes payments to the film producers, then these are carried as payments on account for film assets. In addition, this position also consists of part-payments for film rights that are the object of the litigation with Franchise Pictures. Intertainment sets aside depreciation reserves to cover the risk that these payments on account are not honoured by performance or that they are not reimbursed in full. In addition, the advance payments made to producers that are offset against the film budgets are also carried under these items.

Trade accounts receivable and other assets are capitalised at the face value. Long-term receivables and assets are capitalised at the present value. Long-term accounts are discounted at 5.5% p.a.. Accounts receivable in foreign currency are carried at the exchange rate pertaining on reporting date.

Cash on hand and credits at banks are carried at face value. Credit balances in foreign currency are shown at the exchange rate applying at reporting date.

INTERENTAINMENT GROUP

Deferred tax assets and liabilities are created (IAS 12) for consolidation adjustments affecting the income statement which are anticipated to reverse-out in subsequent accounting periods (“temporary differences”), as well as for valuation differences between IAS and HGB as well as for losses carried forward that reduce future taxable profit (“tax credits”).

3. Long Term Debt

The tax provisions (IAS 37) comprise the Company’s anticipated tax liabilities computed at current tax rates.

Other provisions are made if a past event imposes a current legal or factual obligation on Intertainment, an outflow of resources of economic utility is likely to occur to meet such obligations, and a reliable estimate of the amount of the obligation is possible.

Short-term liabilities are carried at face value, long-term liabilities at the present value. Intertainment discounts long-term liabilities at 5.5% p.a.. Foreign currency liabilities are carried on the basis of IAS 21 at the exchange rate pertaining on the reporting date.

4. Recognition of sales as revenue

With respect to the recognition as revenue of sales of film rights that have the potential for a major cinema launch, a fundamental distinction is made between the possibilities of selling sub-licences and the exploitation of the licences by Intertainment itself.

In the case of a sale of a sub-licence (usually in the case of “all-rights deals” and “TV” sales) sales are recognised as revenue when a binding contractual relationship has been created between Intertainment and the sub-licensee. This is the case in particular if:

- acceptance of the sub-licensed film rights exists,
- the licence fee for each sub-licensed film right is known,
- the cost of each sub-licensed film right is known and
- there is an adequate probability that the economic benefit, namely the licence fee, will accrue to Intertainment on due date.

In the case of own utilisation (usually in the cinema, video and pay TV segments) of the film rights by Intertainment, sales are recognised as revenue at the time of utilisation of the corresponding partial right. The utilisation of the video segment begins as a rule six months after the cinema launch.

In the case of merchandise, sales are recognised as revenue in the reporting year in which the merchandise is sold to the retail segment. In the case of merchandise for which the retailers hold a right of return to Intertainment, sales are only recognised as revenue when the right of return has expired. Until this point in time the merchandise continues to be carried under inventories.

INTERENTAINMENT GROUP

(V) Explanation of the differences between HGB and IAS

According to Section 292a II N° 4b of the German Commercial Code (HGB), the following differences exist between the German Commercial Code and IAS:

1. Valuation of foreign currency balances

According to IAS 21 foreign currency positions, particularly accounts receivable and liabilities, are stated at the exchange rate pertaining on reporting date. Under HGB, the principle of caution applies, as a result of which unrealised gains on exchange are not recorded. This reconciliation results in a difference of TEUR 566 (previous year TEUR 1,718).

2. Expenses of the capital increase

Expenses incurred in connection with the capital increase are charged directly against the capital reserve under IAS (SIC 17), and do not, as is the case under HGB, accrue to the income statement. In the year under review, the pre-tax expenses of the capital increase were TEUR 0 (previous year TEUR 4,444).

3. General bad debt provision

Under IAS no general bad debt charge is formed for trade receivables. According to HGB a 1% provision is formed on the basis of the principle of caution (previous year 2%), which corresponds to an amount of TEUR 556 (previous year TEUR 946).

4. Withdrawal of goodwill amortisation

The incorporation of INTERENTAINMENT Licensing GmbH in Intertainment AG in the financial year 1998 is not covered by IAS 22. Accordingly, in economic terms this is not a “business combination”, but a legal reorganisation of the Intertainment group. As a result, this incorporation does not create goodwill and amortisation of TEUR 651 under HGB (previous year TEUR 651) is eliminated. Under HGB the difference resulting from the capital consolidation, which is not capable of distribution between the group balance sheet items, is to be shown as goodwill under intangible assets. The goodwill is equal to the difference between the cost of acquiring the shares in the subsidiary and shareholders’ equity at the time of first consolidation. The goodwill is amortised starting from the first consolidation date over its probable useful life of ten years in accordance with HGB Section 309, paragraph 1, sentence 2 in conjunction with HGB Section 255, paragraph 4, sentence 3.

5. Discounting of long-term liabilities

Under HGB long-term liabilities are carried at the amount repayable. According to IAS, this position is carried at the present value calculated with a discounting factor of 5.5% p.a.. The difference is TEUR 3,209 (previous year TEUR 0).

INTERENTAINMENT GROUP

6. Capitalisation of compensation to producers and project costs

According to HGB, intangible fixed assets produced by the company for its own use are to be charged as expense; according to IAS, by contrast, these must be capitalised, which corresponds to an amount to be capitalised of TEUR 4,762 (previous year TEUR 0).

7. Deferred tax assets and liabilities

In accordance with IAS 12 and with due regard for current tax relief legislation, the tax effect arising from the re-statement in accordance with the International Accounting Standards is calculated at a tax rate of 38%. There are also underlying individual tax rates for effects attributable to past accounting periods. Under IAS, deferred tax assets and liabilities are also formed for loss carry forwards. In the year under review, deferred tax income (previous year tax expense) arose mainly from the revaluation of the loss carry forwards and is TEUR 3,344 (previous year TEUR -366).

(VI) Notes to the consolidated balance sheet

1. Fixed assets

For a presentation of the development of fixed assets we refer to the attached statement of asset additions and disposals.

Intangible assets include mainly cartoon film rights of Intertainment Animation & Merchandising GmbH, which are amortised in accordance with their expected economic life.

In the year under audit, Intertainment made payments on account for producer compensation of TEUR 4,491 (TEUR 0) and for other project costs of TEUR 271 (previous year TEUR 0). These payments on account are offset against the films produced in the future.

Fixed assets in the form of fixtures, fittings and equipment are also depreciated on the basis of their useful economic life.

The financial assets position shows the 24.84% interest in SightSound Technologies Inc.. In FY 2001 amortisation of TEUR 5,012 was charged against this, corresponding to 25% of the cost of acquisition. This amortisation is attributable to the decrease in the present value of SightSound Technologies’ potential earnings resulting from increased risk mark downs. In this connection, account was taken of the increased sector and company risks as well as of the greater uncertainty of the media markets.

Notes to the Consolidated Financial Statements as at December 31, 2001
in Accordance with the International Accounting Standards (IAS)

INTERENTAINMENT GROUP

2. Inventories

The value of the film rights at reporting date was TEUR 27,701 (previous year TEUR 64,008), which corresponds to a decline of TEUR 36,307. The film rights developed as follows:

	Financial year 2001	Financial year 2000
	T€	T€
Book values 1 January	64,008	20,069
Additions	42,692	76,205
Scheduled amortisation	-5,393	25,977
Unscheduled amortisation	-62,221	6,289
Disposals	-11,385	0
Book values 31 December	27,701	64,008

The additions of TEUR 31,915 consist of newly-acquired film rights, including for film “Caveman’s Valentine”, which was technically accepted in the fourth quarter. In the financial year 2002 court of arbitration proceedings between the financier of the film rights (National Bank of Canada) on the one hand and Intertainment as well and Completion Bond on the other hand that the film was correctly delivered in the fourth quarter of 2001. Intertainment had previously disputed this. This arbitration means that Intertainment is obliged to pay the second instalment. Irrespective of this decision and the confirmation of proper acceptance it entails, this film remains the object of litigation with Franchise Pictures. No statement was made in the court of arbitration on the inflated budget alleged by Intertainment.

The other additions amounting to TEUR 10,777 primarily entail film rights sold in previous years, which reverted in the year under review to Intertainment. These film rights were subjected to non-scheduled amortisation in the year under review. In the income statement the offsetting position is shown under the extraordinary result as this item is a direct result of the legal action with Franchise Pictures LLC.

The scheduled amortisation refers to current film utilisation in the year under review. TEUR 2,575 of the unscheduled amortisation of film rights is shown under material costs and the remaining amount under extraordinary expenses in the year under audit. This amortisation is a direct result of the legal action with Franchise Pictures as the public discussion of the inflated budgets for Franchise Pictures films has substantially worsened the marketing opportunities for the film rights. Within the framework of the no-loss valuation, therefore, the film rights were written off, and their anticipated sales proceeds are below the capitalised costs of the corresponding film right. In order to reflect the changed market conditions in Germany, a film rights valuation report was prepared by an external auditor assessing the market price. This report, among other things, is the basis for the revaluation.

Notes to the Consolidated Financial Statements as at December 31, 2001
in Accordance with the International Accounting Standards (IAS)

INTERENTAINMENT GROUP

The disposals of film assets result from the disposal of film rights and a price concession on the film “Whole Shebang”.

Merchandise held for sale worth TEUR 177 (previous year TEUR 504) mainly comprises merchandising articles, videos and DVDs.

Payments on account of TEUR 24,570 (previous year TEUR 6,904) consist of payments of the first instalment for film rights of Franchise Pictures that are directly connected with the pending legal action against Franchise Pictures. For the films that are the object of the pending legal action against Franchise Pictures, Intertainment paid the first instalment and reports this amount reduced by depreciation reserves as a payment on account for film rights. Payments on accounts developed as follows:

	Financial year 2001	Financial year 2000
	T€	T€
1 January	6,904	0
+ Additions from payments on account to Franchise Pictures	+87,576	0
+ Other additions	0	6,904
- Disposals from payments on account to Franchise Pictures	-5,925	0
- Depreciation reserve (risk provisioning)	-63,985	0
31 December 2001	24,570	6,904

The additions to payments on account for films of Franchise Pictures are spread essentially over the film rights Get Carter, 3000 Miles to Graceland, The Pledge, Angel Eyes, Viva las Nowhere, Driven, Heist and Caveman’s Valentine.

The disposals of payments on account for films of Franchise Pictures result from the film Caveman’s Valentine, which was technically accepted in the fourth quarter of 2001 and transferred to film assets. In this connection we refer to the comments on events since accounting date (c.f. item VIII, 14).

The depreciation reserves are set aside on the one hand for possible exploitation losses on the disputed film rights which may lead to Intertainment not receiving a complete repayment of the payments on account. On the other hand, additional risk provisioning is made for the continuing litigation with Franchise Pictures.

INTERENTAINMENT GROUP

3. Accounts receivable and other assets

Trade accounts receivables amounting to TEUR 47,075 (previous year TEUR 32,707) have a remaining term of more than one year. These long-term receivables are directly related to the sale of free TV rights as the payment periods are directly connected to the availability of the corresponding films. The TEUR 2,466 decline in the discount amount (previous year increase TEUR -5,936) is shown under interest income (previous year interest expense). In the year under review receivables of TEUR 25,710 (previous year TEUR 0) were written off because of reversals in connection with the Franchise Pictures litigation.

Other assets consist mainly of tax refunds of TEUR 8,579, payments for producer services TEUR 2,260 and input tax not due TEUR 1,371.

4. Cash and cash equivalents

Cash and cash equivalents consist of TEUR 10,459 (previous year TEUR 66,234) of time deposits and of TEUR 3,772 (previous year TEUR 6,614) of current account balances and cash on hand. The time deposits have terms of less than one year.

5. Deferred tax assets and liabilities

Tax deferrals have been created in respect of consolidation adjustments affecting income that are expected to reverse out in subsequent accounting periods as well as in respect of valuation differences between HGB and IAS and loss carry forwards. The amount shown in the balance sheet results from an estimated tax rate of 38% for trade and corporation and corporation tax and individual tax rates for effects attributable to past accounting periods. We also refer to VII.8.

6. Shareholders' equity

6.1 Subscribed capital

By resolution of the Supervisory Board dated April 17, 2000, and entry in the Trade Register on May 23, 2000, the share capital was increased by TEUR 246 because of the share exchange with SightSound Technologies Inc. (previously SightSound.com Inc.).

As a result of the capital increase carried out in the financial year 2000, which was resolved by the Supervisory Board on July 17, 2000, and July 27, 2000, and entered in the Trade Register on July 18, 2000, and August 2, 2000, the share capital was increased by TEUR 2,365 to a total of TEUR 15,005 and is now made up of 11,739,013 no-par-value shares in issue.

The subscribed capital was not changed for the financial year 2001 compared to the previous year.

INTERENTAINMENT GROUP

Authorised unissued capital

The Management Board is authorised until January 28, 2004, subject to the consent of the Supervisory Board, to increase the share capital by TEUR 3,203 (authorised capital) and by June 26, 2006, by a further TEUR 4,300 (authorised capital II) by the single or multiple issue of new no-par-value bearer shares for contribution in cash or in kind. The Management Board specifies in consultation with the Supervisory Board the conditions of the share issue.

The Management Board is also authorised, subject to the agreement of the Supervisory Board, to bar in whole or in part the exercise of the stock option of the shareholders regarding the authorised capital and the authorised capital II in the following cases:

- to equalise peak amounts
- to obtain contributions in kind
- if the capital increase on the basis of capital contributions does not exceed TEUR 1,500 of the share capital and the issue price of the shares does not significantly exceed the market price
- if this is necessary in order to be able to grant the holders of the warrant-linked bonds and convertible bonds a subscription right to the extent to which they would be entitled after exercising the option right

Contingent capital

The contingent capital I as at December 31, 2001 amounts to TEUR 511. The contingent capital increase will only be carried out if the holders of subscription rights issued by Intertainment AG as authorised by the General Meeting of Shareholders on January 18, 1999, and on the basis of the amended authorisation of the General Meeting of Shareholders of July 9, 1999, make use of these subscription rights. New shares created by the exercise of subscription rights participate in profit from the beginning of the financial year in which they are created.

In addition, there also exists contingent capital II amounting to TEUR 383, which serves to grant option rights to employees, the Management Board and the Management of the Company or affiliated companies according to the terms of the resolution of the General Meeting of Shareholders on June 27, 2001 (Stock Option Programme 2001). The new shares participate in profit from the beginning of the financial year in which they are created by exercise of option rights.

The Company's share capital is increased by a further contingent TEUR 6,002 (contingent capital III). The contingent capital increase serves to grant rights to the holders or creditors of warrant-linked bonds and convertible bond issued up to June 26, 2006, by the Company or by a company in which the Company holds a direct or indirect interest. The new shares participate in profit from the beginning of the financial year in which they are created by exercise of the conversion or option rights or by fulfilment of conversion obligations.

Notes to the Consolidated Financial Statements as at December 31, 2001
in Accordance with the International Accounting Standards (IAS)

INTERENTAINMENT GROUP

6.2 Capital reserves

The capital reserves as at reporting date amounted to TEUR 149,523 (pr. year TEUR 149,525). The change is the result of the different offsetting of currency translation differences compared to the previous year.

6.3 Revenues reserves

The revenues reserves refer exclusively to the statutory reserves of Intertainment AG.

7. Provisions

7.1 Provisions for taxation

The provisions for taxation developed as follows in the year under review:

Description	1.1.2001	Utilised	Added	31.12.2001
	T€	T€	T€	T€
Trade tax	648	0	206	854
Corporation tax	7,465	7,455	60	70
Solidarity surcharge	410	410	0	0
Total	8,523	7,865	266	924

The addition to the corporation tax reserve in the year under review refers to the full amount to the tax charge at USA-Intertainment Inc.

Notes to the Consolidated Financial Statements as at December 31, 2001
in Accordance with the International Accounting Standards (IAS)

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7.2 Other provisions

Description	1.1.2001	Utilised	Released	Added	31.12.2001
	T€	T€	T€	T€	T€
Licence sales	6,314	6,314	0	4,250	4,250
Litigation risks	1,099	383	153	2,505	3,068
Outstanding invoices	97	97	0	2,788	2,788
Personnel	196	196	0	520	520
License fees	465	465	0	249	249
Marketing expenses	11,415	11,415	0	0	0
Potential losses	199	199	0	0	0
Miscellaneous	80	80	0	349	349
Total	19,865	19,149	153	10,661	11,224

The provision for licence sales results from disputes related to the settlement of film licence sales agreements.

The provision for litigation risks encompasses the estimated costs still to be incurred for the pending legal action with Franchise Pictures LLC.

The provisions for outstanding invoices consist of payment obligations for goods delivered and services rendered in the year under review and not yet paid for.

The provision for personnel relates to vacation not yet taken and severance payments.

The provision for license fees relates to licences exploited during the year under review for which corresponding fees are payable to the licensor.

TEUR 787 (TEUR 0) of the provisions have a remaining term of more than one year.

8. Liabilities

Trade accounts payable result in the main from the acquisition of licences. Accounts payable for film rights are recorded in a manner analogous to the capitalisation of the film rights on acceptance of the delivered film material by an independent laboratory. Accounts payable in foreign currency are stated at the exchange rate on the balance sheet date.

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Long-term liabilities of TEUR 20,441 are discounted by TEUR 3,209.

Liabilities to banks consist of loans (TEUR 22,996) and current account balances (TEUR 231).

TEUR 16,359 of the loans are due to HypoVereinsbank AG and TEUR 6,637 to BHF Bank. They are subject to variable interest which is geared to base interest rates. Both loans are due by June 30, 2004, at the latest.

The assignment of the utilization rights, of the material and assignment of accounts receivable under sales agreements have been agreed to with the banks. We also refer to the notes on liability at item VIII 5.

(VII) Notes on the group income statement

1. Sales

Sales amounting to TEUR 31,145 (previous year TEUR 87,811) are made up as follows:

	Financial year 2001	Financial year 2000
	T€	T€
Sale of film rights	28,365	83,771
Sale of visual media	1,709	3,040
Other sales	1,118	1,122
Sales deductions	-47	-122
Total	31,145	87,811

The sales deductions relate essentially to bonuses and discounts granted.

2. Other operating income

This item essentially comprises exchange gains of TEUR 4,935 (previous year TEUR 4,291) and payments received for producer services amounting to TEUR 3,712 (previous year TEUR 0).

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3. Cost of materials

The cost of materials consists primarily of the amortisation of the exploited or sold film rights at TEUR 5,393 (previous year TEUR 25,977), unscheduled amortisation of film rights TEUR 2,575 (previous year TEUR 6,289), marketing costs TEUR 12,618 (previous year TEUR 20,494), cost of visual media and merchandising articles for sale TEUR 390 (previous year TEUR 679) and licensor shares TEUR 350 (previous year TEUR 640).

4. Other operating expenses

This item mainly includes expenses for losses on exchange TEUR 4,269 (previous year TEUR 6,108), legal and consultancy costs of TEUR 6,401 (previous year TEUR 2,582), assumption of current fixed costs from producers TEUR 2,049 (previous year TEUR 0) and bank charges of TEUR 627 (previous year TEUR 1,412).

5. Amortisation of financial assets

Amortisation of TEUR 5,012 was charged against the investment in SightSound Technologies Inc. in the year 2001.

6. Net interest income/expense

The net interest income includes interest income of TEUR 7,336 (previous year TEUR 4,320) and interest expenses of TEUR 2,071 (previous year TEUR 9,818).

7. Extraordinary result

Intertainment reports all items directly connected with the legal action against Franchise Pictures under the extraordinary result as a case of fraud is involved.

7.1 Extraordinary income

The extraordinary income as of December 31, 2001, amounted to TEUR 53,494 (previous year TEUR 0).

In the financial year 2001 Franchise Pictures LLC or the presenting bank presented the documents for the payment of letters of credit for the films Get Carter, 3000 Miles to Graceland, The Pledge, Angel Eyes, Driven, Heist and Caveman’s Valentine. Despite Intertainment’s protest, a bank decided to disburse the corresponding amounts and then declared that it was prepared to waive claims against Intertainment Licensing GmbH subject to certain conditions. This waiver of claims outstanding creates extraordinary income of TEUR 52,088 (previous year TEUR 0). A provision was formed (IAS 39.63) for the balance sheet assets connected with the assessment base underlying the waiver of claims outstanding. In addition, extraordinary income arises from payments of damages of TEUR 1,406 (previous year TEUR 0).

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7.2 Extraordinary expenses

Extraordinary expenses of TEUR 142,442 (previous year TEUR 0) result mainly from the unscheduled amortisation of film rights of TEUR 59,646 (previous year TEUR 0), the reserve for payments on account of TEUR 63,985 (previous year TEUR 0), the reversal of licence sales of TEUR 8,620 (previous year TEUR 0), provision for licence sales TEUR 4,250 (previous year TEUR 0), and the addition to provisions for legal and consultancy costs for the litigation with Franchise of TEUR 3,465 (previous year TEUR 0).

8. Taxes

Intertainment reports an overall tax income of TEUR 8,137 (previous year tax expense of TEUR 5,091), which is made up as follows:

	Financial year 2001	Financial year 2000
	T€	T€
Current income taxes	+4,793	-2,374
Deferred tax income (prior year tax expense)	+3,344	-2,717
Total	+8,137	-5,091

Taxes on income result in particular from the refund of corporation tax due to the dividend payment made for 2000 in 2001 by Intertainment Licensing GmbH to Intertainment AG. The dividend payment reduced the corporation tax rate from the standard rate of 40% to the 30% tax rate as levied on distributions. The corporation tax paid can be offset at Intertainment AG.

The Group’s German companies are subject to an average municipal income tax of approx. 16% of the trading profit, which is deductible against corporation tax. The corporation tax rate as of the assessment period 2001 is uniformly 25%, plus a 5.5% Solidarity Surcharge on corporation tax. In the previous year, the corporation tax rate for retained earnings was 40% and for distributed earnings 30%. Deferred tax is calculated at an average tax rate of 38%. The calculation of income tax in the USA is based on the local laws and regulations.

The deferred taxes are calculated according to IAS 12. Accordingly, tax relief and expenses likely to accrue in the future are accounted for temporary differences between the book values carried in the consolidated financial statements and the taxable values of assets and liabilities.

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Anticipated tax savings resulting from the use of loss carry forwards deemed to be realisable are capitalised. The deferred tax assets are carried as the amount that appears probable based on the expectations regarding future profits and the time of reversal of temporary booking differences. Tax rebate claims of TEUR 100 based on the old corporation tax system can be realised by distributing future profits by December 31, 2016.

The following deferred tax assets and liabilities on the balance sheet accrue to reporting and valuation differences in the individual balance sheet items:

	31.12.2001		31.12.2000	
	Asset	Liability	Asset	Liability
	T€	T€	T€	T€
Loss carry forwards	5,039		114	
Intangible assets	174		532	
Payments on account		1,810		0
Trade receivables		426		607
Accounts payable trade		0		405
Total	5,213	2,236	646	1,012

Deferred tax assets on loss carry forwards consist of:

	31.12.2001	31.12.2000
	T€	T€
Corporation tax	3,065	114
Trade tax	1,974	0
Total	5,039	114

The loss carry forwards can be carried forward without restriction. No deferred tax assets were carried for losses of approximately EUR 71 million (corporation tax) and approximately EUR 78 million (trade tax).

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Transfer from anticipated to actual income tax expense (IAS 12.81c.ii)

	31.12.2001	31.12.2000
	T€	T€
Pre-tax profit before extraordinary items	-5,997	10,661
Extraordinary result	-88,948	0
Other taxes	1	1
Pre-tax profit	-94,944	10,662
Anticipated tax rate (38%)	-36,079	0
Anticipated tax rate (54%)	0	5,757
Tax difference with respect to foreign interests in earnings	-22	-3
Deferred tax assets not recorded because of depreciation of loss carry forwards	27,780	0
Repercussions of the changes in tax rates	-543	-224
Capital increase expenses offset against capital reserves at the distribution rate (42%)	0	-533
Reduction of corporation tax resulting from internal group distribution	-1,211	0
Other differences	1,938	94
Total	-8,137	5,091

The tax asset of TEUR 7,624 accrues to the extraordinary result.

(VIII) Other information

1. Segmental reporting

Intertainment has two possible business segments, consisting on the one hand of film rights dealing and on the other of merchandising. Segmental reporting is dispensed with on the basis of the exemption for reasons of company size pursuant to IAS 14.35. Nor are revenues broken down geographically as this is not possible on the basis of the incomplete information available. Own utilisation of the most important film rights for the segments cinema, video and pay TV us carried out by the distribution partners Warner Brothers or 20th Century Fox. Intertainment receives all figures from its distribution partners.

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2. Earnings per share

Under IAS 33 earnings per share are calculated by dividing the result for the accounting period by the weighted average number of shares in issue.

Earnings per share on a total number of 11,793,013 shares and a loss for the year (previous year profit for the year) of TEUR -86,807 (previous year TEUR 5,569) as at December 31, 2001, are EUR -7.36 (previous year EUR 0.52); the dilution effect is not visible because of the limited issue of options (previous year EUR 0.52).

3. Employee participation scheme

The Management Board is authorised until January 18, 2004, subject to the approval of the Supervisory Board, to offer to employees or members of the Management Board and members of the Management of affiliated companies share options in respect of no-par-value bearer shares. The options are to be valid for no more than five years. The right to subscribe and the number of subscription rights is determined for members of the Management Board of the Company solely by the Supervisory Board and in other cases by the Management Board in conjunction with the Supervisory Board. Shareholders have no statutory subscription right. The exercise price of the subscription rights in the Company is set annually as the average closing price of a share in the Company on the Frankfurt stock exchange on the date of the decision by the competent bodies. Subject to the applicable waiting period and exercise conditions, the subscription rights may be exercised annually during the fourth and subsequent 15 market days after the ordinary General Meeting of Shareholders and after announcement of the results for the third quarter. Up to 25% of the subscription rights may be exercised for the first time two years after the date of granting of the subscription rights; a further 25% may be exercised in each of the following three years. If options are not exercised by this last date, they will expire without substitution. The subscription rights may only be exercised if the average cash price of a share in the Company on the Frankfurt stock exchange in the first five market days after the ordinary General Meeting of Shareholders has risen by at least 30% in relation to the average cash price of a share in the Company taken as a basis for the exercise price on issue of the subscription rights.

The share options developed as follows in financial year 2001:

Options in issue as at January 1, 2001	302.000
Options granted in 2001	40.000
Options exercised	0
Options lapsed	4.000
Options in issue as at December 31, 2001	338.000
Options still available	62.000

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4. Other financial commitments

As at December 31, 2001, Intertainment reported the following future payment obligations:

Description	Remaining term up to 1 year	Remaining term more than 1 year	Total
	T€	T€	T€
Commitments arising from film productions	8,475 (pr. year 6,979)	32,204 (pr. year 38,654)	40,679 (pr. year 45,633)
Commitments arising under leasing/rental contracts	1,457 (pr. year 312)	4,616 (pr. year 990)	6,073 (pr. year 1,302)
Payment obligations for film rights	0 (pr. year 176,618)	0 (pr. year 0)	0 (pr. year 176,618)
Total	9,932 (pr. year 183,909)	36,820 (pr. year 39,644)	46,752 (pr. year 223,553)

Commitments arising from film productions

The commitments arising from film productions relate to payments to be made to producers.

Other commitments under lease contracts

The Intertainment Group leases motor vehicles and various office facilities, which are all covered by “operating leasing”.

Rent for office premises

The obligations from rental agreements relate to the business premises in Ismaning and in Los Angeles. The contracts have a fixed term of 5 years in each case. The tenancy agreement for the business premises in Ismaning ends on June 14, 2005, and that in Los Angeles on April 30, 2006.

Payment obligations in respect of film rights

The financial obligations in respect of film rights reported as at December 31, 2001, no longer exist as Intertainment has decided because of the current litigation not to pay the second instalment for the films concerned. In the event that Franchise Pictures’ financing banks file arbitration court proceedings for payment of the second instalment regarding the film rights in dispute, the banks would be obliged in the event of an arbitration decision in their favour to offset the revenues from the exploitation of these film rights against Intertainment’s payment obligation. Intertainment assumes that the revenues from such exploitation are significantly higher than any obligation to pay the second instalment.

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Irrespective of a possible court of arbitration decision the film rights remain the subject of litigation with Franchise Pictures. Only in these proceedings will a final decision be made regarding the fraud with the inflated budgets.

5. Other liabilities

As a result of the financing of the film rights by banks and the corresponding extension of credit lines, the film rights and the associated receivables of Intertainment with regard to the exploitation of these licences have been assigned to the banks as security.

The assignments of accounts receivable of Intertainment Licensing GmbH to HypoVereinsbank AG totalling TEUR 16,052 (previous year TEUR 87,243) and to BHF Bank of TEUR 14,811 (previous year TEUR 9,037) are to be seen in this context.

In addition, Intertainment AG gave HypoVereinsbank AG a guarantee of TEUR 16,361 (previous year TEUR 0) serving as security for the credit line of Intertainment Licensing and which is due on 30.06.2004.

For the rental of the office premises in Ismaning Intertainment AG gave a guarantee of TEUR 76 (previous year TEUR 76). Moreover, there exists a letter of credit for TUSD 1,000 (previous year TUSD 0) for the rental obligations relating to the office premises in Los Angeles.

6. Financial instruments

As a hedge against currency risks, in particular in respect of the US dollar, Intertainment enters into forward ex-change contracts. This derivative financial instrument is used solely to secure the underlying basic transactions. They cannot, therefore, be classified as speculative transactions, since there is a close relationship in terms of amount and timing between the underlying and hedging transactions. At the balance sheet date there were no forward exchange contracts.

7. Additional disclosures with regard to the cash-flow statement in accordance with IAS 7

During the year under audit tax payments of TEUR 7,865 (previous year TEUR 13,825) were made by Intertainment; tax refunds of TEUR 10,093 (previous year TEUR 1,067 became payable).

Interest payments made in the fiscal year 2001 amounted to TEUR 2,071 (previous year TEUR 2,020) and interest payments received TEUR 1,661 (previous year TEUR 2,362).

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8. Organisation

Management	Ernst Rüdiger Bäres, Munich (Chairman)
Board	David Charles Williamson, Munich (Deputy Chairman) / until September 17, 2001
	Hans-Joachim Gerlach, Berlin (Finance Director)
	Stephen Joel Brown (Business Development Director)

Mr. Ernst Rüdiger Bäres has sole power of attorney. David Charles Williamson, Hans-Joachim Gerlach and Stephen Joel Brown each have power of attorney when acting jointly with another Member of the Management Board.

The Deputy Chairman David C. Williamson left the Management Board as of September 17, 2001. Stephen Brown, Business Development Director and CEO of the subsidiary in the USA was appointed to succeed him. At the same time, the Chairman of the Board Rüdiger Bäres assumed responsibility for the legal department.

The remuneration of the Management Board for the calendar year 2001 amounted to TEUR 2,213 (previous year TEUR 1,304).

Supervisory	Dr. Matthias Heisse, Lawyer, Munich (Chairman)
Board	Dr. jur. Ernst Pechtl, Diplom Kaufmann, Berg (Deputy Chairman)
	Dr. Wilhelm Bahner, Diplom-Kaufmann in Munich / as of May 7, 2001
	Dr. Andreas Bohn, Diplom-Kaufmann in Munich / until May 7, 2001

During the year under review Dr. Matthias Heisse also was a member of the supervisory board of Firestorm AG, Munich and for the period 22.06.2001 to 22.08.2001 at QW-Pension Capital AG, Würzburg. Dr. jur. Ernst Pechtl was also a member of the supervisory boards of MedCon AG, Cologne, of Wegold Edelmetalle AG, Wendelstein, of Solidline AG and Core and More AG in the financial year 2001. Dr. Wilhelm Bahner was member of the supervisory board of QW-Pension Capital AG, Würzburg, until August 2001.

Supervisory Board compensation for the financial year 2001 amounted to TEUR 25 (previous year TEUR 22).

9. Relationships with related parties

Under IAS 24 the subsidiaries INTERENTAINMENT Licensing GmbH, Intertainment Animation & Merchandising GmbH and USA-Intertainment Inc. are classified as related parties of Intertainment AG. Intertainment AG holds 100% of the voting rights and shares in all these companies. The nature of the relationship of the undertakings to each other lies among other things in the fact that USA-Intertainment Inc. provides services in Los Angeles for the German subsidiaries, thus resulting in accordance with the cost-plus method in a cost allocation to the respective receiver of the service. In the year under review expenses of USA Intertainment Inc. of TEUR 2,929 (previous year TEUR 1,295) were assumed by INTERENTAINMENT Licensing .

Notes to the Consolidated Financial Statements as at December 31, 2001
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INTERENTAINMENT GROUP

In addition, INTERENTAINMENT Licensing GmbH charged services as follows:

Intertainment AG	TEUR	29 (pr. year 103)
<u>Intertainment Animation & Merchandising GmbH</u>	<u>TEUR</u>	<u>139 (pr. year 120)</u>

The liquidity of the group companies is ensured by means of clearing accounts with Intertainment AG, which bear interest at market rates. At December 31, 2001, Intertainment AG showed the following accounts receivable from the subsidiaries:

INTERENTAINMENT Licensing GmbH	TEUR	98,552 (pr. year 75,310)
Intertainment Animation & Merchandising GmbH	TEUR	2,511 (pr. year 2,500)
<u>USA Intertainment Inc.</u>	<u>TEUR</u>	<u>2,721 (pr. year 1,611)</u>

Mr Rüdiger Bäres is to be regarded as related party, holding 52.9% of the voting rights in Intertainment AG at the balance sheet date.

During the year under audit fees amounting to TEUR 650 (pr. year TEUR 444) were paid in the context of a separate consultancy agreement to the ARCON firm of lawyers, in which Dr. Heisse is a partner (German Stock Corporation Act (AktG), Section 114). In addition, fees of TEUR 83 (previous year TEUR 0) were paid on the basis of a separate consulting contract to Pechtl GmbH.

10. Share ownership and options

	Shares	Options
Management Board		
Rüdiger Baeres	6,205,635	0
David C. Williamson / until 17.09.2001	48,500	125,000
Achim Gerlach	10,000	100,000
Stephen Brown	0	50,000
Supervisory Board		
Dr. Matthias Heisse	12,980	0
Dr. Ernst Pechtl	0	0
<u>Dr. Wilhelm Bahner</u>	<u>0</u>	<u>0</u>

As at December 31, 2001, the Company did not own any of its own shares.

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11. Litigation with Franchise Pictures

At the end of December 2000, INTERENTAINMENT Licensing GmbH filed an action before the District Court (Federal Court) in Los Angeles against Franchise Pictures LLC, Franchise Pictures Inc., their Chairman and CEO Elie Samaha, President and COO Andrew Stevens, various production companies of the Franchise group and other parties. At the end of February 2001 INTERENTAINMENT Licensing GmbH extended the action in that Imperial Bank (as of October 2001 Comerica Bank) domiciled in Inglewood, USA, was included as defendant. In May 2001 the action against Imperial Bank was withdrawn in order to be able to pursue the action against Franchise Pictures.

Within the framework of film contract running over several years, INTERENTAINMENT Licensing GmbH declared it was prepared to buy the European rights for at least 60 Franchise films over a period of 5 years. As security for the financing banks, but also as security for INTERENTAINMENT Licensing GmbH, Franchise Pictures was contractually obliged to provide a completion bond for each film. INTERENTAINMENT Licensing GmbH in return undertook to acquire the European rights for 47% of the budget secured by the completion bond (bonded budget).

According to the action filed, Franchise Pictures provided INTERENTAINMENT Licensing GmbH with fraudulent budgets which led to additional expenses of USD 75 million for license fees for a package of 26 films.

Within the framework of the discovery proceedings, INTERENTAINMENT continues to prepare itself systematically for the main proceedings, which are currently scheduled for November 19, 2002. In the course of the ten scheduled days of hearings the evidence will be presented to a jury. The American discovery proceedings (pursuant to Rules 26 seq. of the Federal Rules of Civil Procedure = FRCP) allows – unlike in Germany – certain evidence to be demanded by the opposing party and also by third parties. According to Rule 34 FRCP, out-of-court hearings of the parties and witnesses may also be demanded (depositions, Rules 27 seq. FRCP). The length of the proceedings depends on the scope of the documents or hearings demanded by the parties. So far, it has been possible by way of several court injunctions to force Franchise Pictures and Imperial Bank to release several budget documents. The court has imposed several fines on Franchise Pictures for delaying release of such documents. The lawyers of INTERENTAINMENT Licensing GmbH have continued and will continue to hear a large number of witnesses from Franchise Pictures, Imperial Bank and the completion bond companies within the framework of depositions.

On the other hand, charges have been brought against INTERENTAINMENT Licensing GmbH and the Board Chairman of Intertainment AG, Rüdiger Bäres, by Franchise Pictures for not fulfilling verbal undertakings and not making payments in connection with the acquisition of film rights. INTERENTAINMENT Licensing GmbH dismissed the charges as fully unfounded. Nor did any further tangible evidence emerge in 2001 to justify a different conclusion.

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12. Employees

In the financial year 2001 the Group employed on average 28 persons (pr. year 28).

13. Registered office

The registered office of Intertainment AG is Osterfeldstraße 84, 85737 Ismaning.

14. Post-balance-sheet events

No events have occurred since reporting that might prevent the annual financial statements as at December 31, 2001 providing a true and fair representation.

In the financial year 2002 it was decided in the course of court-of-arbitration proceedings relating to the film “Caveman’s Valentine” between the financier of the film rights (National Bank of Canada) on the one hand and INTERENTAINMENT Licensing GmbH as well as the completion bond (Film Finances Canada) on the other hand, that this film was delivered properly in the fourth quarter of 2001. INTERENTAINMENT Licensing GmbH had previously disputed this. The result of this arbitration entails for INTERENTAINMENT Licensing GmbH an obligation to pay the second instalment. Independently of this decision and the associated confirmation of proper delivery (with reservation as to a contrary appeal decision), this film remains part of the litigation with Franchise Pictures. The arbitration court made no statement on the inflated budgeted alleged by INTERENTAINMENT Licensing GmbH.

No further insights are available on the pending litigation with Franchise Pictures.

Following the positive decision for SightSound Technologies in the so-called Markman Hearing against the Bertelsmann subsidiaries CDNow and NSK in February 2002, the earnings potential of SightSound for Intertainment has been confirmed. The court supported SightSound’s view that the patent held by SightSound for the digital downloading of audio and music files via telecommunication lines in the USA also applies to the Internet.

A decision relating to the enforceability of the patents is expected next year.

Intertainment AG, April 29, 2002

Rüdiger Baeres
– Board Chairman

Stephen Brown
– Deputy Chairman

Achim Gerlach
– Finance Director

Development of Fixed Assets (Gross)

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Cost of Purchase or Manufacture					
	1.1.2001	Additions	Disposals	Reclassi- fication	31.12.2001
	T€	T€	T€	T€	T€
I. Intangible assets					
1. Franchises, industrial and similar rights and assets as well as licences to similar rights and assets	475	2	0	3	480
2. Down payments made	0	4,860	0	0	4,860
	475	4,862	0	3	5,340
II. Tangible assets					
Other equipment, plant fixtures and fittings	719	2,351	20	-3	3,047
III. Financial assets					
Investments	20,048	0	0	0	20,048
	21,242	7,213	20	0	28,435

Development of Fixed Assets (Gross)

INTERENTAINMENT GROUP

Accumulative Depreciation and Amortisation					Book Value	
	1.1.2001	Depreciation in the financial year	Reclassi- fication	Disposals	31.12.2001	
	T€	T€	T€		T€	31.12.2000 T€
	140	76	1	0	217	263
	0	0	0	0	0	4,860
	140	76	1	0	217	5,123
	190	323	-1	20	492	2,555
	0	5,012	0	0	5,012	15,036
	330	5,411	0	20	5,721	22,714

INTERENTAINMENT GROUP

I. Development in financial year 2001

Intertainment continues orientation towards film production

Intertainment focused its efforts in financial year 2001 on its reorientation towards film production. Intertainment has developed from a pure rights dealer into a film producer, which places it in a position at the beginning of the value-added chain. The systematic continuation of this strategy means that in the future the bulk of Intertainment’s films will be produced by the company itself or by production alliances. The foundations of this strategy lie in the co-production agreement with Paramount Pictures, the exclusive agreement with the producer Arnold Kopelson and the distribution agreements with the major studios Warner Brothers and 20th Century Fox.

Investments in film production

As early as the beginning of 2001 Intertainment signed a two-year first look and co-financing agreement for the Kopelson production facilities with the American production company Paramount Pictures. Paramount Studios, which bear part of the development costs for the productions, thus acquire the marketing rights in all media segments for North America.

After the actors’ strike in Hollywood in summer 2001 Intertainment intensified its co-operation with the producer Arnold Kopelson. This is based on the exclusive five-year agreement between Intertainment and Kopelson Entertainment signed in May 2000. The agreement envisages the production of at least ten films and has a prolongation option. This contract assures Intertainment of access to an extensive range of high-quality film material. In October 2001 the employees of USA-Intertainment, Inc. and the Kopelson Entertainment team moved together into new business premises in order to enhance the efficiency of project work and to pool the creative resources of the two companies. The investments in the first projects in the year under review result from advance payments for producer compensation and the acquisition of material rights, which will later be charged to the corresponding film budget.

Rudolph again successful in the third year of utilisation

Intertainment Animation & Merchandising GmbH was able to successfully exploit the licence for “Rudolph with the Red Nose” for the third consecutive year. Once again, a large number of new merchandising products were added to the range for the successful Christmas character “Rudolph” in the financial year.

Litigation against Franchise Pictures and its repercussions

The lawsuit pending against Franchise Pictures since December 2000 in respect of fraudulently inflated budgets seriously impacted the development of Intertainment’s business activities in the year under review. The film titles that are the object of the litigation and for which Intertainment has made significant advance payments cannot be exploited by the company. Intertainment assumes that it is no longer possible to acquire the film rights in dispute as Franchise Pictures has transferred these to Warner Brothers.

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Not least, the dispute also had repercussions on the valuation of the film assets at the end of the year. Intertainment made an unscheduled depreciation charge against the film assets as the public discussion surrounding the inflated budgets for films from Franchise Pictures has materially worsened the films’ marketing opportunities.

In addition, contracts with licencees were terminated because of the legal action as it was not possible to deliver the disputed films, and the films that had already been delivered were no longer attractive for the licensees if the contract as a whole could not be fulfilled.

The details of the litigation are explained in detail in the notes to the consolidated financial statements (c.f. Notes item VIII, 11).

In the 2002 financial year a decision was made in the court of arbitration proceedings between Intertainment and the financier of the film rights (National Bank of Canada) that the film “Caveman’s Valentine” had been properly delivered in the fourth quarter of 2001, which Intertainment had previously disputed. This arbitration means that Intertainment is obliged to pay the second instalment. Irrespective of this decision and the confirmation of proper delivery that it entails, this film remains part of the litigation with Franchise Pictures. No statement was made in the court of arbitration on the inflated budgets alleged by Intertainment.

Employees and Management

In the financial year 2001 Intertainment employed an average of 28 employees. These were engaged at the company’s registered offices in Ismaning near Munich and at USA-Intertainment, Inc. with registered offices in Los Angeles, USA. The work force thus remained virtually unchanged on the previous year. There were personnel changes in the Management Board and the Supervisory Board during the financial year. The Deputy Chairman David C. Williamson left the Management Board on September 17, 2001. Stephen Brown, Business Development Director and CEO of USA-Intertainment, Inc., was appointed as his successor. The Annual General Meeting of June 27, 2001, appointed Dr. Ernst Pechtl as Supervisory Board member as successor to Martin Schürmann, and Dr. Wilhelm Bahner as successor to Dr. Andreas Bohn.

II. Assets, financial and earnings position

The overall assets, financial and earnings position is heavily influenced by the pending litigation with Franchise Pictures. For this reason, Intertainment decided to pool the transactions concerned under the extraordinary result in the income statement.

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Assets

The financial situation on the assets side is largely characterised by the acceptance of the film rights and on trade receivables. The bulk of the TEUR 36,307 reduction in the value of the film rights is due to non-scheduled depreciation as the legal disputes have greatly worsened the conditions of sale. The market prices were significantly below the capitalised costs and it was thus necessary to write down various film rights, without sales having been made. Intertainment had a valuation report prepared by an independent auditor assessing the market prices. The payments on account made for film rights amounted to TEUR 24,570 and increased particularly as a result of payments to Franchise Pictures. The trade receivables decreased by TEUR 31,206, which is mostly attributable to the reversal of receivables from film rights sales because of reversed transactions. The licensees were not prepared to accept the films at the inflated amounts budgeted because of the problems resulting from the legal disputes with Franchise Pictures.

On the liabilities side other provisions were reduced by TEUR 8,642 as a result of offsetting the marketing costs for film rights against claims against the distribution partners. Liabilities increased by TEUR 2,883 as a result of the acquisition of film rights including “Caveman’s Valentine”. The shareholders’ equity as at December 31, 2001, is TEUR 90,148.

Financial situation

The company’s liquidity decreased compared to the previous year by TEUR 58,620, which was attributable to the acquisition of or payments on account for film rights, producer compensation payments made and the payment of amounts due to banks and tax liabilities.

Earnings situation

In the financial year 2001 Intertainment generated sales from the video and DVD and pay TV exploitation of the films “Art of War”, “Whole Nine Yards” and “Battlefield Earth”. In addition, sales were also generated in the Animation & Merchandising segment from the marketing of “Rudolph”. Sales in the film rights dealing segment declined significantly compared to the year-earlier period. On the one hand, this is because Intertainment is not able to generate any exploitation revenues from the film rights in dispute because of the pending litigation. On the other hand, the structural changes in the European media landscape and the steep falls in advertising receipts at the TV broadcasters are also responsible for the fact that Intertainment was not able to make any significant TV sales in the year under review in Germany or in Europe.

The earnings situation was greatly influenced in financial year 2001 by the extraordinary result. Extraordinary income is TEUR 53,494 and the extraordinary expense TEUR 142,442.

INTERENTAINMENT GROUP

The extraordinary income is essentially attributable to the waiver of claims outstanding by a bank amounting to a total TEUR 52,088, which is directly connected to the litigation. The bank and Intertainment had agreed on the waiver of claims after the bank had paid claims under a letter of credit that Intertainment had previously disputed. In connection with the litigation it was necessary to revalue the film assets. The non-scheduled depreciation of the film rights entailed a charge of TEUR 62,221 under the extraordinary expense item. In addition, payments on account totalling TEUR 63,985 were also written off and licence sales totalling TEUR 8,620 were reversed. This effect also influences the extraordinary charge.

The investment in SightSound Technologies Inc. was written down in the year under review by TEUR 5,012, which corresponds to 25% of the cost of acquisition. This is attributable to the reduced value of SightSound Technologies’ potential earnings, which results from the increased risk mark-downs. In this connection, account was taken of the increased sector and company risks as well as the increased uncertainty of the media markets.

In its financial year 2001 Intertainment reported a loss for the year of TEUR 86,807 and an accumulated net loss of TEUR 74,496.

IV. Future development of the Group

Expansion of the Film Production division

Intertainment will continue to pursue systematically the strategy embarked on in the past year and continue to focus on film-rights dealing and film production. In addition, its extensive film library still contains a large number of free-TV rights that could be sold in the current financial year throughout Europe. Intertainment AG, together with USA-Intertainment, Inc., will further expand film production this year. At the present, implementation of the first pro-duction projects with Kopelson Entertainment is being intensified.

New Rudolph film will stimulate the Christmas business

Intertainment Animation & Merchandising will launch the new Rudolph film “Rudolph II” as a video in time for this year’s Christmas business. It is also planned to sell the free-TV rights to “Rudolph – the Red Nosed Reindeer” following the successful video exploitation during the last three years. Finally, a large number of new merchandising articles are to appear at the retailers.

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The development of SightSound Technologies

In February 2002, SightSound Technologies, Inc. obtained a positive decision in the so-called Markman Hearing. The court had confirmed that the patent held by SightSound for the digital download of video and music files via telecommunication lines also applies to the Internet. The still pending lawsuit against the Bertelsmann subsidiaries CDNow and N2K concerns the assertion of the patents. A decision is expected next year.

Litigation will continue to influence future development

The company’s future development will continue to be influenced by the evolution of the lawsuit with Franchise Pictures. Within the framework of the discovery proceedings Intertainment is preparing itself systematically for the main proceedings, which are currently scheduled for November 19, 2002. In the course of the ten scheduled days of hearings the evidence will be presented to a jury. The American discovery procedure allows – unlike in Germany – certain evidence to be demanded by the adverse party and by third parties. Out-of-court hearings of the parties and witnesses may also be demanded. The length of this procedure depends on the scope of the documents or hearings demanded by the two parties. Regardless of this, an out-of-court settlement is still possible.

Investments

In the current financial year Intertainment will continue to invest in the development of film projects. The future financing of the Kopelson film projects is to be secured partly by the company’s own resources, bank loans or film funds. Security is provided in the form of advance sales of individual country or regional rights to major studios or independent distributors. With Paramount Pictures major studio has already been involved in the financing of the film projects.

Result

The result to be expected for the financial year 2002 depends on whether Intertainment can complete a film project with Kopelson Entertainment in the current year. The outcome of the lawsuit against Franchise Pictures is also of considerable importance.

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V. Risks of future development

The future development of the company entails certain risks. Intertainment has examined its business processes and identified, analysed and valued the resultant risks and has developed measures to minimise these within the framework of permanent risk monitoring. On this basis, it will continue to develop and add to the risk control system for the identification of hazardous influences.

Below, the main risks are described that result from the operational business activities of the film rights dealing and film production segments and from the subsidiaries.

Sector-related risks

As a media company Intertainment is also active in the film licensing business. This segment counts a large number of competitors, particularly in the European market. The mounting competitive pressure may result in changes in the price level, a fall in sales figures, narrower profit margins and a deterioration of the company’s market position. The trend towards consolidation in the media industry may lead to a concentration in the European sales market, which would make it more difficult to sell licences. The sale of television licences is ultimately also dependent on the development of advertising receipts at the television broadcasters, as the financial year 2001 clearly shows.

Acquisition and exploitation of film rights

Licence rights are usually acquired prior to the start of production. The success of a film is difficult to forecast at this point in time. The company attempts to minimise this risk by appropriate know how among its employees, casting for the principle roles and an analysis of the script.

Dependency on distribution partners

An important competitive advantage is the possibility to distribute films throughout Europe via the majors. If these distribution agreements were to be terminated, this could have substantial negative repercussions on the company’s financial situation and its operating earnings.

Budgeting risk

The irregular intervals at which film licences are awarded and film material is received mean that profits may fluctuate significantly. Within the budgeting framework this may led to substantial difficulties in defining the precise point in time of the corresponding film rights acquisitions or sales.

Financing of future growth and liquidity risk

Film production, the purchase of further film rights and the expansion of business activities into new sales regions require substantial financial resources. Moreover, the company’s liquidity depends greatly on the development of the lawsuit between INTERTAINMENT Licensing GmbH and Franchise Pictures. Intertainment plans to ensure its liquidity from its own resources, bank loans, film funds and advance sales of individual film rights.

INTERENTAINMENT GROUP

Currency risk

Exchange-rate fluctuations between the US dollar and the euro may have repercussions on business activities, and may influence the financial and earnings situation and particularly profit margins as a result of currency gains or losses. These currency risks are minimised by hedging incoming and outgoing payments with regard to amount and maturity by opposite hedging transactions.

The risk of further arbitration proceedings

INTERENTAINMENT Licensing GmbH faces the risk that the financing banks of Franchise Pictures file court of arbitration proceedings against Intertainment for payment of the second instalment with regard to the film rights in dispute. In the event that a court of arbitration decides in favour of a bank, then this bank will be obliged to offset the revenues from the exploitation of the disputed film rights against Intertainment's financial obligation. Intertainment assumes that the revenue from the exploitation of these film rights is significantly higher than its potential financial obligation to pay the second instalment. Irrespective of possible court of arbitration proceedings the disputed films remain the object of the pending lawsuit with Franchise Pictures. Only in these proceedings will a definitive decision be made on regarding the fraudulently inflated budgets.

Risks from the Franchise Pictures lawsuit

If INTERENTAINMENT Licensing GmbH loses the lawsuit against Franchise in the first instance in November 2002, it has the possibility of appealing against the decision. The appeal proceedings would take another 18-24 months. The further financing of the costly proceedings could have substantial negative repercussions on the company. If INTERENTAINMENT Licensing GmbH wins the action against Franchise in the first instance, then Franchise may also appeal. As in all court proceedings there is a risk that despite an incumbent decision on the sued party, enforcement of the decision remains without success.

Risks from the investment in SightSound Technologies, Inc.

The pending litigation against the Bertelsmann subsidiaries CDNow and N2K involves the assertion of patents. A decision is expected next year and is of great importance for future earnings development. The financial situation is currently difficult, whereby adequate financial resources have so far been furnished by the shareholders. This may entail substantial opportunities, but also significant risks with respect to the investment's book value. Intertainment AG expects that SightSound Technologies will report a positive earnings development once it has overcome its start-up problems.

Liability risks

Intertainment AG guarantees a bank the repayment of a loan to a subsidiary. The guarantee activating event depends on the repayment of the loan amount as of June 30, 2004, and the fulfilment of further conditions.

Intertainment AG, Munich, April 29, 2002

The Management Board

INTERENTAINMENT GROUP

Independent Auditor's Report

We have audited the consolidated financial statements, comprising the balance sheet, the income statement and the statements of changes in shareholders' equity and cash flows as well as the notes to the financial statements prepared by Intertainment Aktiengesellschaft, Ismaning, Munich, for the business year from January 1 to December 31, 2001. The preparation and the content of the consolidated financial statements in accordance with International Accounting Standards (IAS) are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit of the consolidated financial statements in accordance with German auditing regulations and German generally accepted standards for the audit of financial statements prescribed by the Institut der Wirtschaftsprüfer (IDW). Those standards require that we plan and perform the audit such that it can be assessed with reasonable assurance whether the consolidated financial statements are free of material misstatements. Knowledge of the business activities and the economic and legal environment of the Group and evaluations of possible misstatements are taken into account in the determination of audit procedures. The evidence supporting the amounts and disclosures in the consolidated financial statements are examined on a test basis within the framework of the audit. The audit includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements give a true and fair view of the net assets, financial position, results of operations and cash flows of Intertainment Aktiengesellschaft for the business year in accordance with International Accounting Standards.

Our audit, which also extends to the group management report prepared by the Company's management for the business year from January 1 to December 31, 2001, has not led to any reservations. In our opinion on the whole the group management report provides a suitable understanding of the Group's position and suitably presents the risks of future development. In addition, we confirm that the consolidated financial statements and the group management report for the business year from January 1 to December 31, 2001, satisfy the conditions required for the Company's exemption from its duty to prepare consolidated financial statements and the group management report in accordance with German law.

Munich, April 29, 2002

KPMG Deutsche Treuhand-Gesellschaft
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

Dr. Bartels-Hetzler Matzinger
- German Public Auditor - German Public Auditor

Group Income Statement for the 4th Quarter 2001
in accordance with the International Accounting Standards (IAS)

INTERENTAINMENT GROUP

	1.1.–31.12.2001	1.10.–31.12.2001
	T€	T€
1. Sales	31,145	11,473
2. Other operating income	9,615	1,202
	40,760	12,675
3. Cost of materials		
a) Cost of film rights	-21,728	-8,927
b) Cost of purchased merchandise and services rendered	-772	-54
	-22,500	-8,981
4. Personnel expenses		
a) Wages and salaries	-4,347	-1,089
b) Social security contributions	-147	-27
	-4,494	-1,116
5. Depreciation on intangible assets and property, plant and equipment	-399	-232
6. Other operating expenses	-19,616	-1,568
7. Operating income	-6,249	778
8. Depreciation of financial assets	-5,012	-5,012
9. Interest income	7,336	4,558
10. Interest expense	-2,071	-505
11. Interest income/expense	5,265	4,053
12. Extraordinary income	53,494	7,132
13. Extraordinary expenses	-142,442	-109,336
14. Extraordinary result	-88,948	-102,204
15. Profit/loss before tax	-94,944	-102,385
16. Taxes on income	8,138	10,960
17. Other taxes	-1	0
18. Group net income/loss	-86,807	-91,425
<i>Number of shares</i>	<i>11,739,013</i>	
Basic earnings per share	-7.36	
Earnings before interest and tax (EBIT)*	-100,209	-106,438

* Including the extraordinary result

Group Income Statement for the 4th Quarter 2000
in accordance with the International Accounting Standards (IAS)

INTERENTAINMENT GROUP

	1.1.–31.12.2000	1.10.–31.12.2000
	T€	T€
1. Sales	87,811	13,522
2. Other operating income	10,114	-1,255
	97,925	12,267
3. Cost of materials		
a) Cost of film rights	-53,613	-13,592
b) Cost of purchased merchandise and services received	-1,229	-1,027
	-54,842	-14,619
4. Personnel expenses		
a) Wages and salaries	-3,053	-1,246
b) Social security contributions	-170	24
	-3,223	-1,222
5. Depreciation on intangible assets and property, plant and equipment	-193	-51
6. Other operating expenses	-23,509	-12,611
7. Operating income	16,158	-16,236
8. Depreciation of financial assets	0	0
9. Interest income	4,320	1,323
10. Interest expense	-9,818	-682
11. Interest income/expense	-5,498	641
12. Extraordinary income	0	0
13. Extraordinary expenses	0	0
14. Extraordinary result	0	0
15. Profit/loss before tax	10,660	-15,595
16. Taxes on income	-5,090	8,728
17. Other taxes	-1	0
18. Group net income/loss	5,569	-6,867
Earnings before interest and tax (EBIT)	16,157	-16,236

Balance Sheet as at December 31, 2001

INTERENTAINMENT AG

ASSETS	31.12.2001	31.12.2000
	€	€
A. Fixed assets		
I. Intangible assets		
Franchises, industrial and similar rights and assets as well as licenses to such rights and assets	36,318.46	75,421.64
II. Fixed assets		
Other plant, fixtures, fittings and equipment	2,909.43	5,237.00
III. Financial assets		
1. Shares in affiliated companies	9,359,172.32	9,359,172.32
2. Investments	15,036,272.25	20,048,363.00
	24,434,672.46	29,488,193.96
B. Current assets		
I. Inventories		
Film rights	18,361,815.09	0.00
I. Trade accounts receivable and other assets		
1. Trade receivables	13,795,216.67	0.00
2. Amounts due from affiliated companies	103,784,316.55	79,420,998.63
3. Other assets	9,506,618.64	11,128,015.31
III. Balances at banks	11,267,111.46	58,435,332.74
	156,715,078.41	148,984,346.68
	181,149,750.87	178,472,540.64

Balance Sheet as at December 31, 2001

INTERENTAINMENT AG

LIABILITIES	31.12.2001	31.12.2000
	€	€
A. Shareholders' equity		
I. Subscribed capital	15,005,155.09	15,005,155.09
II. Capital reserves	161,820,547.57	161,820,547.57
III. Retained earnings		
Statutory reserve	115,806.59	115,806.59
IV. Reported net loss (pr. year profit)	-20,165,271.53	461,540.32
	156,776,237.72	177,403,049.57
B. Provisions		
1. Provision for taxations	853,592.59	647,565.48
2. Other provisions	1,503,198.13	174,350.54
	2,356,790.72	821,916.02
C. Liabilities		
1. Liabilities due to banks	0.00	32,917.53
2. Trade accounts payable	21,682,493.80	54,096.59
3. Other liabilities	334,228.63	160,560.93
	22,016,722.43	247,575.05
	181,149,750.87	178,472,540.64

Income Statement

for the Period January 1, to December 31, 2001

INTERENTAINMENT AG

	2001	2000
	€	€
1. Sales	613,550.26	0.00
2. Other operating income	3,902,348.44	57,498.05
	4,515,898.70	57,498.05
3. Cost of materials		
a) Expenses for film rights and related goods and services	320,361.44	0.00
b) Cost of services rendered	4,491,113.86	0.00
	4,811,475.30	0.00
4. Personnel expenses		
a) Wages and salaries	2,104,822.16	1,380,289.61
b) Social security, pension provision and other benefits		
– of which for pensions € 3,012.12 (pr. year € 2,689.55)	26,377.64	45,083.53
	2,131,199.80	1,425,373.14
5. Depreciation of tangible and intangible fixed assets	41,430.73	39,759.67
6. Other operating expenses	5,690,075.10	7,392,811.79
7. Income from investments	11,482,885.24	3,614,833.60
8. Depreciation of financial assets	5,012,090.75	0.00
9. Net interest paid	-1,876,166.98	-5,181,854.95
10. Result on ordinary operations	188,679.24	-3,758.00
11. Extraordinary expenses	20,779,865.23	0.00
12. Taxes on income	35,625.84	6,008.51
13. Net loss	-20,626,811.83	-9,766.51
14. Profit brought forward from the previous year	461,540.30	471,306.81
15. Net reported loss (pr. year profit)	-20,165,271.53	461,540.30

Notes for the Financial Year 2001

INTERENTAINMENT AG

I. General Information

Intertainment AG has been listed on the “Neuer Markt” section of the Frankfurt stock exchange since February 18, 1999. The company is a large public limited company as defined by Section 267, paragraph 3, sentence 2 of the German Commercial Code (HGB). The annual financial statements of Intertainment AG have been compiled in accordance with the provisions of the HGB and the German Stock Corporation Act. The type-of-expenditure format was selected for the income statement.

II. Accounting and valuation methods

1. Fixed assets

Intangible fixed assets and property, plant and equipment have been stated at cost less scheduled straight-line depreciation.

In determining the depreciation use is made of the simplification rule in EstR R 44, paragraph 2. Low-value acquisitions up to EUR 410 are fully written off in the year of acquisition and shown as disposals in the analysis of fixed assets.

Financial assets are stated at the value of the investment in kind/cash or at acquisition cost. In the case of an exchange of shares the cost of acquisition is determined in accordance with the value of the relinquished shares.

2. Current assets

Film rights are valued at cost of acquisition or at the lower attributable value. The film rights are capitalised at the time of technical acceptance of the delivered film material by an independent laboratory. The total cost of acquisition is allocated to the partial rights cinema, video, pay TV and free TV according to these segments’ shares in the proceeds. Intertainment assumes up to three utilisation cycles in the free TV segment stretching over a period of 25 years.

The scheduled amortisation of the film licences is carried out on utilisation of the corresponding segment in the corresponding utilisation period.

Within the framework of the no-loss valuation of film licences these are examined for their exploitability and if appropriate subjected to unscheduled amortisation if the forecast proceeds of sale is below the capitalised residual book values. In order to determine the earnings-discounted value of the rights among other things a valuation report is obtained from an external auditor.

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Trade-term receivables and other assets are carried at the nominal amount. The general credit risk on trade accounts receivable is taken into account in the form of a general bad debt charge of 1%. Long-term non-interest-bearing receivables are discounted at 5.5%.

Amounts receivable in foreign exchange are valued at the exchange rate pertaining at the time of the creation of the claim or at a lower exchange rate pertaining on reporting date.

Cash and cash equivalents are stated by the Company at the nominal amount. Credit balances in foreign currency on current accounts are valued at the rate applying at reporting date, in the case of time deposits at the rate applying at reporting date or the lower rate applying at the time of booking.

3. Long-term debt

Provisions are determined on the basis of sound business judgement and take account of all identifiable risks.

Liabilities are carried at the amount repayable. Liabilities in foreign currency are carried at the exchange rate pertaining on the date of receipt of invoice or a higher rate applying at reporting date.

III. Notes to the balance sheet

1. Fixed assets

For the presentation of the development of fixed assets, please refer to the enclosed analysis of fixed assets.

Financial fixed assets include the following shares in affiliated companies:

Investment	Registered office	% interest	Shareholders' equity 31.12.2001	Result for the year
INTERENTAINMENT Licensing GmbH	Munich	100	TEUR -69,394	TEUR -70,342
Intertainment Animation & Merchandising GmbH	Munich	100	TEUR 209	TEUR 35
USA Intertainment Inc.	Los Angeles/USA	100	TEUR 305	TEUR 144
SightSound.com, Inc. *	Pittsburgh/USA	24,8	TEUR -2,941	TEUR -9,555

* The shareholders' equity and deficit of SightSound Technologies Inc., relate to the unaudited annual financial statements for the year ending September 30, 2001, prepared according to the General Accepted Accounting Principles (US GAAP).

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Amortisation of TEUR 5,012 was charged against the investment in SightSound Technologies Inc. in the 2001 financial year. This corresponds to 25% of the cost of acquisition. This depreciation charge was made because of the decreased present value of SightSound Technologies' potential earnings resulting from the increased risk mark-downs. Account was taken in this connection of the increased sector and company risks as well as of great uncertainty in the media markets.

2. Film rights

The film rights and licences at reporting date amounted to TEUR 18,362. The development compared to the previous year is as follows:

January 1, 2001	TEUR	0
Additions	TEUR	35,955
Scheduled amortisation	TEUR	-49
Unscheduled amortisation	TEUR	-17,544
December 31, 2001	TEUR	18,362

Additions consist of film rights newly acquired during the year under review.

The scheduled amortisation relates to current film utilisations in the financial year.

The non-scheduled amortisation of film rights is reported in the review period under extraordinary expenses. This amortisation is a direct result of the litigation with Franchise Pictures LLC and the public discussion of the inflated budgets for films of Franchise Pictures which has substantially worsened the marketing opportunities for the film rights. Within the framework of the loss-free valuation, therefore, those film rights were written down whose anticipated sales proceeds are below the capitalised costs of the corresponding film right. In order to take account of the changed market conditions in Germany, a film-rights valuation report was drafted by an independent auditor to assess the market prices. This report, among other things, provides the basis for the valuation.

3. Receivables, other assets and cash and cash equivalents

Trade receivables amounting to TEUR 13,795 include long-term receivables with a residual term of more than one year amounting to TEUR 3,028. Intertainment has formed a general provision of TEUR 141 for the general credit risk.

Accounts receivable from affiliated companies exist in respect of INTERENTAINMENT Licensing GmbH to the amount of TEUR 98,552, Intertainment Animation & Merchandising GmbH to the amount of TEUR 2,511 and USA Intertainment Inc. to the amount of TEUR 2,721. This exclusively involves clearing accounts bearing interest at 8% p.a. All accounts receivable have a residual term of less than one year.

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Other assets consist of tax refunds of TEUR 5,876, compensation for producer services TEUR 2,260 and input tax not due of TEUR 1,371.

Cash and cash equivalents result from time deposits of TEUR 10,459 and current account balances of TEUR 808. The time deposits are fully due in the financial year 2002.

4. Shareholders' equity

The subscribed capital at reporting date was unchanged on the previous year at TEUR 15,005 and is divided into 11,739,013 no-par-value shares. The capital reserves amount to TEUR 161,821 and the statutory reserve TEUR 116. As at December 31, 2001, the Company shows a loss of – TEUR 20,165. As at December 31, 2001, the Company had approved capital I of TEUR 3,203, approved capital II of TEUR 4,300, contingent capital of TEUR 511, contingent capital II of TEUR 383 and contingent capital III of TEUR 6,002. The shareholders' equity developed as summarised in the table below in the year under review:

	Balance at 1.1.2001	Result for the year	Balance at 31.12.2000
	TE€	TE€	TE€
Subscribed capital	15,005	0	15,005
Capital reserves	161,821	0	161,821
Retained earnings	116	0	116
Net reported loss (pr. year profit)	462	-20,627	-20,165
Shareholders' equity	177,404	-20,627	156,777

The share options of FY 2001 developed as follows:

Options issued as of January 1, 2001	302.000
Options granted in 2001	40.000
Lapsed options	4.000
Options issued as of December 31, 2001	338.000

5. Long-term debt

The provision for taxation of TEUR 854 comprises the trade tax for the fiscal year 1998, which arose before the company entered into the parent-subsidiary legal agreement which transfers these tax liabilities to the parent company.

The other provisions relate essentially to provisions for outstanding invoices amounting to TEUR 670, for personnel amounting to TEUR 511 and film project expenses amounting to TEUR 271.

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Trade accounts payable result mostly from the acquisition of film rights and as at reporting date amount to TEUR 21,682, of which an amount of TEUR 20,441 has a residual term of more than one year.

The other liabilities of TEUR 334 include among other things liabilities to the tax office for wage tax and church tax of TEUR 65, social security liabilities of TEUR 3 and value added tax of TEUR 251 payable on the basis of fiscal integration with the parent company for value added tax purposes. The entire amount has a residual term of less than one year.

IV. Notes on the income statement

1. Sales

Sales of TEUR 614 (previous year TEUR 0) are generated from the sale of film rights.

2. Other operating income

Other operating income is made up mainly of payments received for producer services at TEUR 3,712 and exchange rate gains of TEUR 158.

3. Cost of materials

The cost of materials consists of producer compensation paid amounting to TEUR 4,491 and of film project expenses of TEUR 271.

4. Other operating expenses

This item includes in particular the expenses for cost refunds for producers TEUR 2,049, legal and consulting costs of TEUR 1,369, bank charges of TEUR 595, investor relations consultancy costs of TEUR 378 and costs for the General Meeting of Shareholders of TEUR 400.

5. Income from investments

The income from investments comes completely from affiliated companies and relates to the dividend payment by INTERENTAINMENT Licensing GmbH on December 17, 2001, of TEUR 11,483.

6. Amortisation of financial assets

Amortisation of TEUR 5,012 was charged against the investment in SightSound Technologies Inc. in the past financial year.

INTERENTAINMENT AG

7. Net interest income

Interest income comes mainly from the interest paid on clearing accounts at the subsidiaries INTERENTAINMENT Licensing GmbH, Intertainment Animation & Merchandising GmbH and USA-Intertainment Inc. at 8% p.a. amounting to TEUR 408 and bank interest of TEUR 1,484. The interest expense of TEUR 16 results from bank interest. As at December 31, December 2001, Intertainment AG waived payment of interest for FY 2001 by INTERENTAINMENT Licensing GmbH.

8. Extraordinary result

This item includes the waiver of claims outstanding against Intertainment Licensing GmbH of TEUR 3,236 for interest in the previous year (unrelated to the accounting period) and unscheduled amortisation on the film assets of TEUR 17,544. The amortisation is attributable to the loss-free valuation of the film assets and a direct consequence of the litigation with Franchise Pictures.

V. Other information

1. Other financial obligations

The Company reports future payment obligations for producer compensation of TEUR 40,678, of which an amount of TEUR 8,475 has a term of up to one year.

2. Other liabilities

In the financial year 2001 Intertainment AG gave Hypo Vereinsbank AG a guarantee for TEUR 16,361 to secure the credit line of Intertainment Licensing GmbH which is due on 30.06.2004. The credit was made available as of December 31, 2001, to an amount of TEUR 16,358. For the leasing of the office premises in Ismaning the company gave a guarantee of TEUR 76. In addition, there exists a letter of credit of TEUR 1,000 for die rental obligations for the office premises in Los Angeles.

In order to remedy the overindebtedness of Intertainment Licensing GmbH, Intertainment AG relegated its claims as shown on the current account of TEUR 71,000 behind the claims of other creditors.

3. Employees

The Company employed an average of five employees in the financial year.

INTERENTAINMENT AG

4. Management structure

The following were Members of the **Management Board** in the financial year:

- Ernst Rüdiger Bäres, Munich (Chairman)
- David Charles Williamson, Munich (Deputy Chairman, Legal Director) / until September 17, 2001
- Hans-Joachim Gerlach, Berlin (Finance Director)
- Stephen Brown, Los Angeles (Business Development Director)

The Deputy Chairman David C. Williamson left the Management Board on September 17, 2001. Stephen Brown, Business Development Director and CEO of the subsidiary in the USA, was appointed as his successor. At the same time, the Board Chairman Rüdiger Bäres takes responsibility for the Legal Department.

The remuneration for the Management Board for the financial year 2001 at Intertainment AG amounted to TEUR 1,273.

The following belonged to the **Supervisory Board** in the financial year 2001:

- Dr. Matthias Heisse, Lawyer in Munich (Chairman)
- Dr. jur. Ernst Pechtl, Diplom-Kaufmann, Berg (Deputy Chairman)
- Dr. Wilhelm Bahner, Diplom-Kaufmann in Munich / as of 07.05.2001
- Dr. Andreas Bohn, Diplom-Kaufmann in Munich / until 07.05.2001

In the year under review, Dr. Matthias Heisse in addition was a member of the Supervisory Board of Firestorm AG, Munich and for the period 22.06.2001 to 22.08.2001 at QW-Pension-Capital, Würzburg. In the financial year 2001 Dr. Jur. Ernst Pechtl was also a member of the Supervisory Board of MedCon AG, Cologne, of Wegold Edelmetalle AG, Wendelstein, of Solidlinie Ag and of Core and More AG. Dr. Wilhelm Bahner was a member of the Supervisory Board of QW-Pension Capital AG, Würzburg, until August 2001.

Supervisory Board remuneration of TEUR 25 was paid in the financial year.

5. Consolidated accounts

Intertainment Aktiengesellschaft with registered office in Ismaning prepares consolidated accounts including its subsidiaries.

Intertainment AG, Ismaning near Munich, April 29, 2002

Rüdiger Baeres	Stephen Brown	Achim Gerlach
– Managing Director	– Deputy Chairman	– Finance Director

Development of Fixed Assets (Gross)

INTERENTAINMENT AG

	Acquisition Costs
	1.1.2001 / 31.12.2001
	T€
I. Intangible assets	
Franchises, industrial rights and similar rights and assets as well as licences in such rights and assets	117
II. Fixed assets	
Other plant, fixtures, fittings and equipment	6
III. Financial assets	
1. Shares in affiliated companies	9,359
2. Investments	20,048
	29,407
	29,530

Development of Fixed Assets (Gross)

INTERENTAINMENT AG

Accumulative Amortisation			Book value	
1.1.2001	Depreciation in the financial year	31.12.2001	31.12.2001	31.12.2000
T€	T€	T€	T€	T€
41	39	80	37	76
1	2	3	3	5
0	0	0	9,359	9,359
0	5,012	5,012	15,036	20,048
0	5,012	5,012	24,395	29,407
42	5,053	5,095	24,395	29,488

INTERENTAINMENT AG

I. Business activities and development

Intertainment Aktiengesellschaft expanded its business activities significantly during its financial year 2001 and is thus no longer a pure financial holding company.

For the first time, operations were geared to film production; Intertainment Aktiengesellschaft thus places its self systematically at the beginning of the value-added chain. Its co-film production and co-film financing activities are based on the contract signed with Kopelson Entertainment in 2000 according to which at least ten films are to be produced in the next five years. A start was made on the implementation of the first joint projects based on this agreement in the year under review. The films are to be financed among other things from the company’s own resources, by bank loans, film funds and advance sales of individual country and regional rights to major studios or independent distributors. Moreover, revenues from marketing various film rights will be reinvested in these projects. Intertainment AG was able to recruit its first large partner in January 2001 in the form of the American production company Paramount Pictures. Paramount Pictures has signed a two-year first look and co-financing agreement with Intertainment AG for the Kopelson productions and received the marketing rights for the productions in all media segments for North America.

In addition, Intertainment Aktiengesellschaft was engaged for the first time in the year under review in the film rights dealing segment. As the parent company of Intertainment Licensing GmbH, Intertainment Animation & Merchandising GmbH and USA-Intertainment Inc., Intertainment AG continues to fulfil the function of a financial holding company. It holds 100% of all subsidiaries.

Subsidiaries

Intertainment Licensing GmbH, which is specialised in film-rights dealing, reported sales from the video/DVD exploitation of the films “Art of War”, “Whole Nine Yards” and “Battlefield Earth” in the year under review. Sales from the film rights dealing business declined steeply compared to the year-earlier period on account of the lack of film exploitation owing to the litigation pending since the end of December 2000 against Franchise Pictures in respect of fraudulently inflated film budgets. In addition, the structural changes in the European media landscape and the collapse in advertising receipts at the TV broadcasters were also responsible for the fact that Intertainment Licensing GmbH was not able to make any significant TV sales in Germany or Europe in the past financial year. Intertainment Licensing GmbH closes the financial year 2001 with a loss for the year of TEUR -70,342. The main reason for this result is to be found in the exceptional influences exerted by the legal dispute with Franchise Pictures. These include the extraordinary income resulting particularly from a waiver of claims outstanding by a bank amounting to TEUR 52,088. On the other hand, non-scheduled depreciation of film rights of TEUR 42,102 and the write-offs on payments on account on film rights of TEUR 63,985 led to significant extraordinary charges. The write-downs made in the annual financial statements as at 31.12.2001 take account of all risks arising from the legal disputes with Franchise Pictures.

USA-Intertainment, Inc., Los Angeles, is responsible for assessing and selecting film projects. The focus of its activity in financial year 2001 was the performance of services for Intertainment Licensing GmbH, particularly the

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generation of future business in Los Angeles by looking after production and film rights distribution. In the future, it is planned to implement the co-production and co-financing agreement with Kopelson Entertainment and Paramount Pictures. In order to increase the efficiency of co-operation, the employees of USA-Intertainment, Inc. and of Kopelson Entertainment moved into shared business premises in Los Angeles in the year under review.

Intertainment Animation and Merchandising GmbH closed the financial year 2001 with a net profit of TEUR 35. The “Rudolph With the Red Nose” licence was already successfully exploited in the third year. The company added a large number of new products to the merchandising segment in the year under review.

Since the financial year 2000 Intertainment AG has held 24.8 % in the American company SightSound Technologies, Inc., Pennsylvania, and regards this investment as a pure financial investment. SightSound Technologies is a provider of download technologies for the media industry for the commercial exploitation of feature films and music via the Internet. The company owns several “business patents” which – provided they can be asserted in the pending court proceedings – will entitle the company to levy licence fees for each Internet commercial download in the USA.

Capital measures

The Shareholders’ Annual General Meeting held on June 27, 2001, approved several capital measures. A contingent capital II of up to TEUR 383 was approved to service the Stock Option Programme 2001. In addition, the AGM also approved contingent capital II of up to EUR 4.3 million and a contingent capital III totalling EUR 6 million for the issue of convertible and/or warrant-linked bonds. Finally, Intertainment AG had the AGM approve its purchase of up to 10% of its share capital.

II. Asset, finance and earnings situation

The asset and earnings situation in the financial year 2001 is as follows:

Within the framework of the financial situation the assets side is mostly affected by the book values of investments of TEUR 24,435 and the amounts due from affiliated companies of TEUR 103,784. For the first time Intertainment AG has a film rights library worth TEUR 18,362 and trade receivables of TEUR 13,795. On the liabilities side trade accounts payable increased significantly as a result of rights purchases to TEUR 21,682. The shareholders’ equity did not change apart from the current result for the year.

The financial situation is determined mainly by the reduction of financial resources resulting from financing the subsidiaries and operating activities associated with film production.

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The earnings situation is characterised essentially by the income from subsidiaries resulting from the dividend paid by Intertainment Licensing GmbH of TEUR 11,483 and the extraordinary result of TEUR -20,780. The extraordinary result comes from non-scheduled depreciation on film rights of TEUR 17,544 and a waiver of claims against Intertainment Licensing GmbH for interest payable in the previous year of TEUR 3,236. In connection with the litigation between Intertainment Licensing GmbH and Franchise Pictures the film assets had to be revalued. A valuation report was prepared by an independent auditor for these film assets and their potential future earnings formed the basis for the no-loss revaluation of the film rights.

A depreciation charge of TEUR 5,012 was made for the SightSound Technologies Inc. investment in the year under review. This corresponds to 25% of the cost of acquisition. This charge is attributable to the discounted value of SightSound Technologies’ potential earnings resulting from the increased risk mark-downs. In this connection the increased sector and company risks and the increased uncertain in the media markets was also taken into account.

As at December 31, 2001, Intertainment Aktiengesellschaft reports a net loss of TEUR 20,627 and an accumulated loss of TEUR 20,165.

III. Future development of the company

In the current financial year **Intertainment AG** intends to further expand film production together with USA-Intertainment and the production partners Kopelson Entertainment and Paramount Pictures. Intensive work is currently being carried out on the implementation of several projects. This realignment requires substantial financial resources. Intertainment AG will minimise the risk of film production by way of extensive rights regarding production and territorial advance sales.

In addition, Intertainment AG will continue its film rights dealing activities and will market the film rights it acquired in financial year 2001.

Earnings at Intertainment AG also depend on future developments at its subsidiaries and investments as these affect the value of investment book values and receivables. The future development of the subsidiaries is described below.

The future development of **INTERENTAINMENT Licensing GmbH** is heavily dependent on the outcome of the pending legal disputes with Franchise Pictures. Regardless of this, INTERENTAINMENT Licensing GmbH will continue to pursue its film rights dealing activities. Its film library still includes a large number of free-TV rights that could be marketed in the current financial year throughout Europe.

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At the end of December 2000 INTERENTAINMENT Licensing GmbH filed a suit before the District Court (Federal Court) in Los Angeles against Franchise Pictures LLC, Franchise Pictures Inc., its Chairman and CEO Elie Samaha, its President and COO Andrew Stevens, various production companies of the Franchise group and other parties. At the end of February 2001 INTERENTAINMENT Licensing GmbH extended the suit to include Comerica Bank (previously Imperial Bank) with registered offices in Inglewood, USA. In May 2001 it withdrew the action against Comerica Bank in order to be able to continue the court proceedings against Franchise Pictures.

Within the framework of film contract covering several years, INTERENTAINMENT Licensing GmbH declared it was prepared to acquire the European rights for at least 60 Franchise films over a period of 5 years. As security for the financing banks, but also as security for INTERENTAINMENT Licensing GmbH, Franchise Pictures was obliged by contract to sign a completion bond for each film. In return, INTERENTAINMENT Licensing GmbH undertook to acquire the European rights for 47% of the budget secured by the completion bond (“bonded budget”). The action alleges that Franchise Pictures fraudulently inflated by several million dollars its budgets vis-à-vis INTERENTAINMENT Licensing GmbH. Overall, the budgets thus allegedly inflated by Franchise entail for INTERENTAINMENT Licensing GmbH “additional expenses of 75 million dollars” and “fraudulently inflated” license fees for a package of 26 films.

Within the framework of the discovery proceedings INTERENTAINMENT continues to prepare itself systematically for the main proceedings, which are currently scheduled for November 19, 2002. In the course of the ten days of scheduled hearings evidence will be presented to a jury. The American discovery procedure (according to Rules 26seq Federal Rules of Civil Procedure = FRCP) allows – unlike in Germany – certain evidence to be demanded by the adverse party and by third parties. According to Rule 34 FRCP out-of-court hearings of the parties and witnesses may also be demanded (depositions, Rules 27seq FRCP). The length of these proceedings depends on the scope of the documents or hearings demanded by the two parties. So far, several court orders have obliged Franchise Pictures and Imperial Bank to release several documents. The court has repeatedly imposed fines on Franchise Pictures for the late release of documents. The attorney of INTERENTAINMENT Licensing GmbH have continued and will continue within the framework of depositions to hear many witnesses from Franchise Pictures, Imperial Bank and the completion bond companies. Regardless of this, there could be possibilities for an out-of-court settlement.

INTERENTAINMENT Licensing GmbH and the Board Chairman of Intertainment AG Rüdiger Baeres have been sued personally by Franchise Pictures for failing to comply with verbal undertakings and failing to make payments in connection with the acquisition of film licences. INTERENTAINMENT Licensing GmbH rejects the action as completely unfounded; in 2001 no further facts emerged allowing a different conclusion.

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USA-Intertainment, Inc., Los Angeles, is responsible for the implementation of the production projects with Kopelson Entertainment and Paramount Pictures and as the source for the procurement of high-quality film material in Los Angeles. USA-Intertainment Inc. will continue to fulfil its function as a service provider for the Intertainment Group.

Intertainment Animation and Merchandising GmbH is to launch the new Rudolph film “Rudolph II” as a video accompanied by new merchandising articles in time for the Christmas business. In addition it is planned to see the free-TV rights to “Rudolph the Red Nosed Reindeer”.

In February 2002 SightSound Technologies, Inc. obtained a positive decision in the so-called Markman Hearing. The court had confirmed that the patent held by SightSound for the digital download of video and music files via telecommunication lines also applies to the Internet. The pending litigation against the Bertelsmann subsidiaries CDNow and N2K involves the assertion of the patents. A decision is expected next year.

IV. Risks of future development

The future development of the company entails certain risks. Intertainment AG has examined its business processes and identified, analysed and valued the resultant risks and has developed measures to minimise these within the framework of permanent risk monitoring. On this basis, it will continue to develop and add to the risk control system for the identification of hazardous influences.

Below, the main risks are described that result from the operational business activities of the film rights dealing and film production segments and from the subsidiaries.

Sector-related risks

As media companies Intertainment AG, INTERENTAINMENT Licensing GmbH and Intertainment Animation & Merchandising GmbH are also active in the film licensing business. This segment counts a large number of competitors, particularly in the European market. The mounting competitive pressure may result in changes in the price level, a fall in sales figures, narrower profit margins and a deterioration of the company’s market position. The trend to-wards consolidation in the media industry may lead to a concentration in the European sales market, which would make it more difficult to sell licences. The sale of television licences is ultimately also dependent on the development of advertising receipts at the television broadcasters, as the financial year 2001 clearly shows.

Acquisition and exploitation of film rights

Licence rights are usually acquired prior to the start of production. The success of a film is difficult to forecast at this point in time. The company attempts to minimise this risk by appropriate know how among its employees, casting for the principle roles and an analysis of the script.

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Dependency on distribution partners

An important competitive advantage is the possibility to distribute films throughout Europe via the majors. If these distribution agreements were to be terminated, this could have substantial negative repercussions on the company’s financial situation and its operating earnings.

Budgeting risk

The irregular intervals at which film licences are awarded and film material is received mean that profits may fluctuate significantly. Within the budgeting framework this may lead to substantial difficulties in defining the precise point in time of the corresponding film rights acquisitions or sales.

Financing of future growth and liquidity risk

Film production, the purchase of further film rights and the expansion of business activities into new sales regions require substantial financial resources. Moreover, the company’s liquidity depends greatly on the development of the lawsuit between INTERENTAINMENT Licensing GmbH and Franchise Pictures. Intertainment plans to ensure its liquidity from its own resources, bank loans, film funds and advance sales of individual film rights.

Currency risk

Exchange-rate fluctuations between the US dollar and the euro may have repercussions on business activities, and may influence the financial and earnings situation and particularly profit margins as a result of currency gains or losses. These currency risks are minimised by hedging incoming and outgoing payments with regard to amount and maturity by opposite hedging transactions.

Risk of further court of arbitration proceedings

INTERENTAINMENT Licensing GmbH faces the risk that the financing banks of Franchise Pictures file court of arbitration proceedings against Intertainment for payment of the second instalment with regard to the film rights in dispute. In the event that a court of arbitration decides in favour of a bank, then this bank will be obliged to offset the revenues from the exploitation of the disputed film rights against Intertainment’s financial obligation. Intertainment assumes that the revenue from the exploitation of these film rights is significantly higher than its potential financial obligation to pay the second instalment. Irrespective of possible court of arbitration proceedings the disputed films remain the object of the pending lawsuit with Franchise Pictures. Only in these proceedings will a definitive decision be made on regarding the fraudulently inflated budgets.

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Risks from the Franchise Pictures lawsuit

If INTERENTAINMENT Licensing GmbH loses the lawsuit against Franchise in the first instance in November 2002, it has the possibility of appealing against the decision. The appeal proceedings would take another 18–24 months. The further financing of the costly proceedings could have substantial negative repercussions on the company. If INTERENTAINMENT Licensing GmbH wins the action against Franchise in the first instance, then Franchise may also appeal. As in all court proceedings there is a risk that despite an incumbent decision on the sued party, enforcement of the decision remains without success.

Risks from the investment in SightSound Technologies, Inc.

The pending litigation against the Bertelsmann subsidiaries CDNow and N2K involves the assertion of patents. A decision is expected next year and is of great importance for future earnings development. The financial situation is currently difficult, whereby adequate financial resources have so far been furnished by the shareholders. This may entail substantial opportunities, but also significant risks with respect to the investment’s book value. Intertainment AG expects that SightSound Technologies will report a positive earnings development once it has overcome its start-up problems.

Liability risks

Intertainment AG guarantees a bank the repayment of a loan to a subsidiary. The guarantee activating event depends on the repayment of the loan amount as of June 30, 2004, and the fulfilment of further conditions.

Ismaning, Munich, April 29, 2002

The Managing Board

INTERENTAINMENT AG

Independent Auditor’s Report

We have audited the annual financial statements, together with the bookkeeping system, and the management report of the Intertainment Aktiengesellschaft for the business year from January 1, 2001 to December 31, 2001. The maintenance of the books and records and the preparation of the annual financial statements and management report in accordance with German commercial law are the responsibility of the Company’s management. Our responsibility is to express an opinion on the annual financial statements, together with the bookkeeping system, and the management report based on our audit.

We conducted our audit of the annual financial statements in accordance with § 317 HGB “Handelsgesetzbuch: German Commercial Code” and the German generally accepted standards for the audit of financial statements prescribed by the Institut der Wirtschaftsprüfer in Deutschland (IDW). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the annual financial statements in accordance with German principles of proper accounting and in the management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Company and evaluations of possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the internal control system relating to the accounting system and the evidence supporting the disclosures in the books and records, the annual financial statements and the management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the annual financial statements and management report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

In our opinion, the annual financial statements give a true and fair view of the net assets, financial position and results of operations of the Company in accordance with German principles of proper accounting. On the whole the management report provides a suitable understanding of the Company’s position and suitably presents the risks of future development.

Munich, April 29, 2002

KPMG Deutsche Treuhand-Gesellschaft
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

Dr. Bartels-Hetzler	Matzinger
– German Public Auditor	– German Public Auditor

Notes

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