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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

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**FORM 10-K**

**FOR ANNUAL AND TRANSITION REPORTS PURSUANT TO SECTIONS 13 OR 15(D)  
OF THE SECURITIES EXCHANGE ACT OF 1934**

**ANNUAL REPORT PURSUANT TO SECTIONS 13 OR 15(D) OF THE  
SECURITIES EXCHANGE ACT OF 1934**

**For the fiscal year ended June 30, 2001**

**OR**

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE  
SECURITIES EXCHANGE ACT OF 1934**

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**Commission File Number: 000-27577**

**HARRIS INTERACTIVE INC.**

(Exact Name of Registrant as Specified in Its Charter)

**Delaware**  
(State or Other Jurisdiction of  
Incorporation or Organization)

**16-1538028**  
(I.R.S. Employer Identification No.)

**135 Corporate Woods, Rochester, NY 14623**  
(Address of Principal Executive Offices)

**Registrant's Telephone Number, Including Area Code: (716) 272-8400**

**Securities registered pursuant to Section (b) of the Act:**

**NONE**

**Securities registered pursuant to Section 12(g) of the Act:**

**Common Stock, par value \$.001 per share**  
(Title of Class)

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

As of August 28, 2001, the aggregate market value of voting stock held by non-affiliates of the registrant was \$30,606,848.

As of August 28, 2001, 34,419,803 shares of the registrant's common stock, par value \$.001 per share, were outstanding.

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**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the registrant's definitive proxy statement (to be filed pursuant to Regulation 14A) for the 2001 Annual Meeting of Shareholders (the "Proxy Statement") are incorporated by reference into Part III hereof.

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## PART I

### Item 1. Business

The discussion in this Form 10-K contains forward-looking statements that involve risks and uncertainties. The statements contained in this Form 10-K that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, including statements regarding expectations, beliefs, intentions or strategies regarding the future. All forward-looking statements included in this document are based on the information available to Harris Interactive Inc. on the date hereof, and Harris Interactive assumes no obligation to update any such forward-looking statement. Actual results could differ materially from the results discussed herein. Factors that might cause or contribute to such differences include, but are not limited to, those discussed in the Risk Factors section of the document. The Risk Factors set forth in other reports or documents Harris Interactive files from time to time with the Securities and Exchange Commission, such as our prospectus dated December 6, 1999 and filed with the Securities and Exchange Commission on December 7, 1999, should also be reviewed.

### Overview

Harris Interactive Inc., a Delaware corporation, and its subsidiaries (together with its subsidiaries “Harris Interactive”, “we”, “our”, “us”, or the “Company”) is a leading market research, polling and consulting firm that uses Internet-based and traditional methodologies to provide our world-wide customers with critical market knowledge in many industries. Known for our HARRIS POLL™, we have over 45 years experience in providing our clients with information about the views, experiences and attitudes of people worldwide. The Company operates as one business segment. Our Internet-based and traditional market research and polling services include:

- research studies conducted on specific issues for specific customers—custom research,
- research studies on issues of general interest developed and sold to numerous clients—multi-client research,
- research conducted for other research firms—service bureau research, and
- outsourced customer relationship services—customer relationship management services.

In September 1997, we began developing our Internet panel and our proprietary technology infrastructure to provide our clients with online market research and polling products and services. As of June 30, 2001, our Internet panel consisted of several million individuals who have voluntarily agreed to participate in our various online market research and polling studies. We believe our Internet panel is larger than those of any of our competitors. Consequently, we believe we are the leading Internet-based market research and polling firm in the world. Our extensive Internet panel and proprietary technology infrastructure enable us to offer Internet-based market research and polling products and services which meet our clients’ needs for fast, comprehensive and accurate information.

Prior to 1999, we provided our market research services exclusively through traditional methodologies, including direct mail, telephone surveys, mall intercepts, focus groups and in-person interviews. We believe, however, that the Internet is changing our industry. Accordingly, we have made, and will continue to make, significant expenditures in the development of our technology platform, our Internet panel and management and staff to lead the transformation of the market research and polling industry to an Internet-based platform.

The HARRIS POLL is a registered trademark of Harris Interactive. This 10-K also includes other trademarks, trade names and service marks of Harris Interactive and of other parties.

### Our Market Opportunity

#### General Overview

Companies are operating in an increasingly complex business environment, characterized by heightened competition, consolidation, globalization of product markets, shortened product life cycles and rapidly changing

consumer preferences. This business environment has escalated the need for accurate and timely information about the preferences, needs, purchase behavior and brand recognition of existing and potential clients. Companies also need continuous tracking capabilities so that they can ascertain product performance and competitive position, monitor consumer satisfaction, measure advertising effectiveness and determine price sensitivity.

Historically, information-gathering and tracking functions in market research have been performed using traditional market research methodologies. The ability of traditional market research methodologies to deliver accurate and objective data rapidly is limited by high data acquisition costs, small sample sizes and the extensive time required to perform the research. As a result, broad-based research projects, which require a large number of survey participants, are prohibitively costly except for companies and organizations with significant resources. The growth and rapid adoption of the Internet is changing the market research and polling industry, making it possible for the first time to survey a very broad, diverse population at low cost and at speeds that are unattainable through any other method.

### **The Internet and its Impact on the Market Research and Polling Industry**

The Internet has emerged as a mass communications and commerce medium enabling millions of people worldwide to gather and share information and conduct business electronically. The use of the Internet as a market research and polling tool is still in its early stages.

Companies first began testing the use of the Internet to conduct market research and polling in 1995, at a time when less than 10 million persons in the United States had access to the Internet and the population on the Internet was not representative of the general population. We believe that, as Internet usage has increased, the demographic composition of those using the Internet has shifted to better reflect the characteristics of the overall population. As a result, with standard market research weighting procedures, the Internet is now a viable medium to conduct market research. We believe that Internet-based market research and polling offers significant advantages over traditional methodologies. These advantages include:

- Versatility—Internet-based market research combines the interactivity of telephone sampling with the visual capabilities of mail surveys. Pictures, graphics, advertising copy and other visual materials can be viewed over the Internet, a feature not available with telephone sampling. With Internet-based methodology, questions and their sequence in surveys can be modified as panelists respond. Mail panel surveys, in contrast, are limited to the order and content in the printed text of the survey.
- Speed—Responses from the online panelists are generally received within several days, while mail panelists' responses are generally received over several weeks. Further, when compared to a telephone survey, the speed advantage of the Internet model becomes greater as sample sizes increase.
- Cost-efficiency—Internet-based market research and polling offers significant cost benefits when compared to traditional market research methodologies. Under traditional methodologies, the sample size of a survey is limited due to the high data collection costs per response. However, utilizing Internet-based market research methods, larger and more robust sample sizes can be used for effectively the same cost, or the same sample size can be used to reduce the overall cost of a study.
- Productivity—The Internet is user-friendly to online panelists because surveys can be completed at the convenience of the participant and can be conducted 24 hours per day, seven days per week. In addition, because online panelists can read questions faster than they can listen, more questions can be asked to panelists in the same amount of time on the Internet than with traditional telephone survey methods. In our experience, a mail survey typically takes approximately six weeks from design to completion. In contrast, Internet surveys can generally be completed in two to seven days.

### **The Harris Interactive Advantage**

We offer a broad suite of Internet-based market research and polling products and services to meet our clients' needs for rapid, comprehensive and accurate information about the opinions, experiences and attitudes of

people worldwide. We possess several key competitive advantages that we believe will enable us to maintain and expand our leading market position in Internet-based research. Our key competitive advantages include:

**Largest Internet Panel.** We have developed what we believe to be the largest Internet panel in the world. As of June 30, 2001, our Internet panel consisted of several million online panelists, who are individuals that have voluntarily agreed to participate in our various online research studies. Our large and diverse Internet panel enables us to:

- conduct a broad range of customer specific or multi-client research studies across a wide set of industries;
- utilize survey sizes that range from a large representative sample of the overall population to targeted subsets;
- market new research products and services through co-branded alliances that we historically could not develop;
- market our online panel to other research firms through the Harris Interactive Service Bureau, enabling us to penetrate new markets in which we do not have relationships or specific expertise.

As our Internet business has matured and our panel size reached a critical mass, we have shifted the focus of our attention from increasing the absolute size of our panel to quality and segmentation of participants. Our change of emphasis enables us to target our investments more specifically toward increases in panel productivity at a reduced cost. As part of these changes, we terminated our agreement to buy names in bulk from Excite@Home in April, 2001. We continue to obtain and buy names from a variety of sources to meet specific needs, and are planning additional investment in expanding our international databases. We also are transforming our entire panel to double opt-in status, enabling us to be removed from the Mail Abuse Prevention System (“MAPS”) black hole list. Along with productivity related activities, we also have created a number of specialty subpanels, enabling us to better meet clients’ specialized needs.

**Proprietary Technology Infrastructure.** A significant amount of computer software and hardware is required to conduct Internet-based market research and polling. Since the beginning of fiscal 1998 through year end fiscal 2001, we have expended approximately \$36.4 million to develop and maintain our technology infrastructure, data analysis techniques, and internal systems and procedures to capitalize on the Internet opportunity within our industry.

Key elements of our technology infrastructure include:

- A high speed customized e-mail system, which enables us to rapidly format, target and deliver over 1,000,000 e-mails per hour, inviting panelists in our database to participate in our online surveys.
- A sophisticated survey engine, which can be programmed to conduct 200,000 interactive, five-minute surveys per hour in any language supported by Microsoft Word.
- An advanced survey dispatcher system, which monitors, controls and allocates all respondent contact and survey results across our servers. In addition, our proprietary dispatcher system gathers real-time statistics on survey starts, suspensions and completions to ensure high quality data collection.
- Customizable multi-language registration and polling system, which allows new and existing panel members to add, delete or update registration information online. In addition, this system, for which a patent application is presently pending, recognizes each panelist’s language preferences and delivers the survey in that language.

We have developed flexible, automated reporting tools which will allow online access to survey information at any time and speed the process of data delivery to clients. We have designed our technology infrastructure to be scalable, which means that it can accommodate the expansion of our business without significant modifications to our existing system design.

Based on our extensive research about Internet research, we have determined that some anomalies occur between the responses from on-line respondents versus the responses from off-line respondents that cannot be reconciled through normal demographic weighting. As such, we have developed proprietary propensity weighting schemes to correct for those anomalies.

Strong Brand Name and Long-Standing Client Relationships. We believe the HARRIS POLL is one of the best known polls operating in the United States today. For over 45 years, the HARRIS POLL has been recognized as providing trusted market research products and services to a broad range of companies, non-profit organizations and governmental agencies. We use a variety of marketing strategies to heighten awareness of and enhance brand recognition of the HARRIS POLL, HARRIS INTERACTIVE and our Internet-based products and services.

Custom Research Division of Yankelovich Partners, Inc. Complimenting the strong brand name HARRIS POLL, in February 2001, the Company acquired the custom research division of Yankelovich Partners, Inc. ("Yankelovich") headquartered in Norwalk, Connecticut. Yankelovich offers a full range of research and consulting services including: product forecasting for the pharmaceutical and other industries, public opinion polling, brand equity studies, and corporate reputation measurement. Yankelovich has a long history of conducting high-quality market research for blue chip clients. We believe their consultative expertise and access to new markets such as retail, telecommunications and media is a key competitive advantage.

### **Our Products and Services**

We are a full-service provider of market research and polling services, utilizing both Internet-based and traditional survey methodologies. Our services are focused upon serving numerous vertical markets, which include, but are not limited to, e-commerce, consumer packaged goods, automotive, financial services, health care, technology and education. By aligning all of our support functions (e.g. sales, marketing, research staff) on specific vertical markets, we can effectively and efficiently deliver the various multi-client and custom services that we offer, while providing industry expertise and consultative support.

Our business model comprises four main sources of revenues:

- custom research;
- multi-client research;
- service bureau research; and
- customer relationship management services;

Our custom research products and services and customer relationship management services are provided using both traditional and Internet-based methodologies. We are transitioning our custom research and polling products and services to Internet-based research. Our remaining products have been developed exclusively using the Internet-based model. During fiscal 2001, 54% of our total revenues were derived from Internet-based products, up from 41% in fiscal 2000 and 10% in fiscal 1999. Through fiscal 1998, all of our revenues were derived from custom research products using traditional market research and polling methodologies. We are dedicating a significant amount of our financial and management resources to developing and marketing additional products and services which utilize our Internet-based methodologies.

The following table summarizes our products and services.

<u>Product Type</u>	<u>Description</u>	<u>Methodology</u>
Custom Research	Market research and polling conducted on an issue specifically identified by a client	Traditional and internet-based
Multi-Client Research	Studies developed for and sold to a large number of clients who have a similar interest in a particular subject area	Internet-based
Harris Interactive Service Bureau	Market research and polling conducted for other market research organizations	Internet-based
Customer Relationship Management Services	Outsourced customer service operations for corporations and organizations	Traditional and Internet-based

### **Custom Research**

For more than 45 years, we have provided custom business and consumer research to a broad range of companies, non-profit organizations and governmental agencies. This wealth of experience has provided us with the foundation to conduct custom research using the Internet to perform efficient, cost-effective data collection. As a result of our long history in providing custom research, we have particular expertise in the following markets:

- office equipment and technology;
- pharmaceuticals;
- healthcare;
- education and public policy; and
- transportation.

We conduct custom research to produce a variety of client-specific surveys and polls, including customer satisfaction surveys, market share studies, new product introduction studies and brand recognition studies. A custom research project comprises three distinct phases:

- design—meetings with our client to discuss the objectives and reasons for the study; determine the research procedure such as a mail, telephone or Internet survey, focus group meetings or personal interviews; identify the population to be surveyed; and design the survey questionnaire or focus group protocol.
- data collection—interviews conducted through the use of computer-aided Internet or telephone interviewing software, by mail or in person, or holding focus group meetings; and follow-up procedures to assure that surveys are returned and interviews are completed.
- analysis and reporting—review of collected data for sufficiency and completeness; segmentation of data for analysis by desired demographic, business or industry characteristics; and preparation and delivery of the report.

We use our proprietary sample design techniques and our questionnaire development process to collect complete and accurate information responsive to the specific inquiries of our clients. We have developed in-depth data collection techniques that enhance the integrity and reliability of our sample database. We also take affirmative steps to assure that our responses are derived from the appropriate decision makers in each particular survey so as to assure the accuracy of our results. As a result, we are able to deliver samplings that represent the desired demographics of our clients based on our significant expertise in assembling appropriate samples and in developing effective survey content.

### **Multi-Client Research**

Multi-client research products are studies that are conducted and sold on a one time or subscription basis to a large number of individuals or companies that have an interest in a particular market segment or research application. To develop our multi-client products, we utilize a rigorous, proprietary, Strategic Marketing Implementation Process (“SMIP”). The SMIP ensures our products are consistent with the Company’s strategic direction, are meaningful in the targeted marketplace, and are of superior value. Our multi-client products are developed on an independent or co-branded basis and are marketed by us. Co-branding involves the development and marketing of a study with another party having a unique experience base in a particular subject or market. Agreements for co-branded studies are negotiated on a case-by-case basis, with revenues generally applied to specified categories of expenses and any profits shared equally. These products enable our clients to conduct research and collect useful data in their areas of expertise that they could not conduct without our Internet panel and technology infrastructure. By combining their expertise, the vast database of Internet respondents, and our Internet-based market research capabilities, we are able to develop and market a product that benefits both parties.

### **Harris Interactive Service Bureau**

Our Harris Interactive Service Bureau (“HISB”) conducts Internet-based market research for other market research firms and other organizations that either do not have the necessary resources to develop Internet-based market research capabilities or that have otherwise chosen not to develop such a capability themselves. Harris Interactive Service Bureau provides us with a revenue-generating source utilizing our data collection capabilities, our proprietary Internet panel and our scalable technology infrastructure. It enables us to penetrate markets or industries in which we do not have relationships or specific expertise. We believe that the Harris Interactive Service Bureau reduces the likelihood that those market research firms and other organizations, which are our clients, will invest significant financial and management resources in developing their own Internet-based market research capabilities.

Harris Interactive Service Bureau clients can access our data collection facilities on a long-term, continuous basis or on a project-by-project basis. During fiscal 2001, the number of market research firms that use HISB increased to 74, up from 37 in fiscal 2000 and 5 at the end of fiscal 1999.

### **Customer Relationship Management Services**

By combining our traditional telephone research capabilities, our experience in customer contact services, and our sophisticated technology infrastructure, we provide high quality customer relationship services to clients. Our customer relationship management practice (“CRM”), assists clients in improving campaign performance using real-time data mining, marketing research, and state-of-the-art CRM technology. Our ISO 9002 certified contact centers offer 24/7, 365 days-per-year services that facilitate CRM campaign management processes. Customized program management and resource optimization help businesses achieve personalization with customers so they can proactively develop account management strategies and recommendations for next-logical product development solutions and marketing actions.

### **Our Clients**

For over 45 years, we have provided high quality market research products and services to a broad range of companies, non-profit organizations and governmental agencies.

For the year ended June 30, 2001, revenues from the Company’s largest customer comprised 12% of total revenues. No other single customer comprised 10% of total revenue. For the year ended June 30, 2000, revenues from the Company’s largest customer comprised 18%. For the year ended June 30, 1999, revenues from the two largest customers comprised 15% and 14% of revenues.

### **Our Sales and Marketing Programs**

We have designed and implemented a broad range of sales and marketing programs, intended to:

- raise the brand awareness of Harris Interactive;

- generate sales leads to add new clients who purchase our products and services;
- recruit new members to expand our Internet panel; and
- support our global network.

Our marketing activities are strategically planned to be fully integrated. Major marketing efforts include public relations, trade show participation, both offline advertising and online promotion, as well as direct marketing.

- **Public Relations.** We rely on our ability to produce and issue press releases for both our Company and clients who desire to make joint releases concerning studies that we have conducted. Our public relations strategy is designed to deploy critical communications in the areas of public affairs and government relations, issues management, and media relations in the United States and globally.
- **Trade Shows.** We have participated and will continue to participate in a large number of industry tradeshows where we share our expertise with attendees to further our position as a global leader in Internet-based research.
- **Offline Advertising.** We use print advertising to promote our brand name and our associated products and services. One of our significant offline promotional activities is our continuous release of the HARRIS POLL results to the public. These results are reported by various national newswire services. Additionally, the Harris Interactive name regularly appears in Time Magazine and on CNN as the research provider for Time/CNN surveys.
- **Online Promotion.** We have agreements with numerous Internet sites, which allow us to place the HARRIS POLL icon on these online portals or websites. The HARRIS POLL icon provides a direct link to the panel registration area of our website.

Other online promotions are undertaken from time to time to recruit special segments to our panel such as senior citizens, minorities, and Information Technology (“IT”) users.

### **Our Competition**

The traditional market research and polling industry is highly competitive. The Internet-based market research and polling industry continues to rapidly evolve. We expect competition to intensify as existing market research firms recognize the significance of the Internet to their business and as other companies already engaged in Internet-based services recognize the potential market.

In both traditional and Internet-based market research and polling business, we compete on the basis of our superior analytical and consultative skills to assist clients in identifying appropriate research issues to examine. This is accomplished through:

- our proprietary sample designs techniques;
- our questionnaire development;
- our in-depth data collection; and
- our ability to deliver samplings that represent the desired demographics of our clients.

We believe that additional competitive factors in the Internet-based market research and polling industry are:

- an ability to project results to the required universe;
- a large and diverse proprietary Internet panel, with geographic scope and demographic depth;
- a scalable proprietary Internet technology platform to provide a variety of services and operational support;
- quality, depth and breadth of products and services offered;
- brand recognition and strong reputation; and
- cost.

In the delivery of both our traditional and Internet-based market research products and services, we compete with numerous market research firms, as well as corporations and individuals that perform market research studies on an isolated basis, many of whom have market shares larger than our own.

We will likely also face competition in the future from other traditional market research firms who move into Internet-based technologies or other companies with access to large databases of individuals with whom they can communicate on the Internet. These companies may, either alone or in alliances with other firms, attempt to penetrate this market.

Many of our current and potential competitors have longer operating histories or significantly greater financial and marketing resources. These competitors may be able to undertake more extensive marketing campaigns for their services, adopt more aggressive pricing policies and make more attractive offers to potential employees, partners and potential customers. Further, our competitors and potential competitors may develop technologies that are superior to ours or that achieve greater market acceptance than our own.

### **Our Intellectual Property and Other Proprietary Rights**

Our success is dependent upon proprietary software technology, research methods, data analysis techniques, and internal systems and procedures that we have developed to address client and Internet-based market research needs. Our intellectual property is essential to our success and we rely on a combination of patent, copyright, trademark and trade secret laws and confidentiality and license agreements with our employees, clients, independent contractors and other third parties to further protect our proprietary rights, software and procedures. We currently have two patents pending. One pending patent covers a multi-location and multi-language registration and polling system being placed on a variety of websites. Our other pending patent covers our CONCEPTLOC encryption system. Additionally, in June 2001, a patent application was filed for a system and method for conducting product configuration research over a computer-based network. Effective trademark, service mark, copyright and trade secret protection may not be available in every country in which our services are made available.

Under the terms of our acquisition of Louis Harris and Associates, we purchased the HARRIS name including HARRIS POLL, for global use except for use in Europe and the European portion of the former Soviet Union (the "Territory"). The prior owner of Louis Harris and Associates sold the HARRIS name for use in the Territory, and those rights are now owned by Taylor Nelson Sofres plc. ("TNS"). In February 2000, we entered into a trade mark license agreement with TNS, which provides us with a non-transferable license to use the names HARRIS ONLINE, HARRIS POLL ONLINE, HARRIS INTERACTIVE, and HARRIS POLL INTERACTIVE within the Territory. Our use of these trademarks is permitted only with reference to the license in connection with market research services involving use of the Internet. We may not otherwise use the HARRIS name in the Territory. The agreement prohibits TNS from using HARRIS ONLINE, HARRIS POLL ONLINE, HARRIS INTERACTIVE and HARRIS POLL INTERACTIVE, or confusingly similar marks within the Territory, and provides that TNS will not contest our use of "HPOL", within the Territory. TNS retains the right to use the HARRIS name within the Territory unless such use indicates a connection with the Internet and is confusingly similar to the marks licensed to us. TNS also retains the right to terminate the license in the event of (i) our insolvency or our breach of the agreement, (ii) the termination of separate agreements between us and TNS relating to our providing TNS with access to our panelist database, and/or (iii) a change of control or sale of substantially all of our business or assets of Harris Interactive in favor of a competitor of TNS; provided however, in the latter two cases we may purchase perpetual rights to the names.

We have licensed in the past, and expect to license in the future, certain of our proprietary rights, such as trademarks or copyrighted material, to third parties. While we attempt to ensure that the quality of our brand is maintained by these licenses, licensees may take actions that might harm the value of our proprietary rights or reputation. The steps taken by us to protect our proprietary rights may not be adequate and third parties may infringe or misappropriate our copyrights, trademarks and similar proprietary rights. In addition, other parties may assert claims of infringement of intellectual property or other proprietary rights against us.

In addition, there can be no assurance that third parties will not independently develop functionally equivalent or superior systems, software or procedures. We believe that our systems, software and procedures and other proprietary rights do not infringe on the proprietary rights of third parties. There can be no assurance,

however, that third parties will not assert infringement claims against us in the future or that any such claim will not require us to enter into materially adverse license agreements or result in protracted and costly litigation, regardless of the merits of such claims.

### Employees

As of June 30, 2001, we employed a total of 560 persons on a full-time basis in addition to 190 full-time and 150 part-time individuals involved in our telephone data collection activities.

None of our employees are represented by a collective bargaining agreement. We have not experienced any work stoppages. We consider our relationship with our employees to be good.

### Executive Officers

The following persons are our executive officers who are not also directors. These individuals have been elected by and are serving at the pleasure of our board of directors:

<u>Name</u>	<u>Age</u>	<u>Position</u>
Dennis Bhame .....	53	Executive Vice President, Human Resources
Arthur E. Coles .....	58	Group President, Health Care and Public Policy
Peter J. Milla .....	42	Senior Vice President, Chief Information Officer
Ronald Knight .....	62	Group President, Business & Consumer Services; Consulting & Brand Management
Bruce A. Newman .....	47	Chief Financial Officer, Secretary and Treasurer
Gregory T. Novak .....	39	Group President, Emerging Markets
Harold E. Quinley .....	58	Group President, Media & Public Relations

The following is a brief account of the business experience of each of the above executive officers:

**Dennis K. Bhame** has served as the Executive Vice President of Human Resources since April 2000. Prior to joining our company, Mr. Bhame spent 16 years at Bausch & Lomb, most recently as Vice President, Global Human Resources, Eyeware Division. He worked as a human resource professional at Burroughs Corporation and Moore Business Forms prior to joining Bausch & Lomb. Mr. Bhame holds a B.S. in Business Management from New Hampshire College.

**Arthur E. Coles** has served as our Group President, Health Care and Public Policy, since July 2000. From June 1999 to June 2000, Mr. Coles was our Executive Vice President of Marketing and Business Development. Mr. Coles was President and Chief Executive Officer of our largest subsidiary from June 1997 to June 1999. Prior to joining our company, Mr. Coles worked for Eastman Kodak Company, where he served as Vice President of Strategic Planning for the Digital Imaging Division. Prior to this, he spent over 30 years at Xerox Corporation in a variety of general management, marketing, and operational roles. Mr. Coles received an M.B.A. from the Rochester Institute of Technology and a B.S. in Mathematics from the State University of New York at Albany.

**Peter J. Milla** has served as our Senior Vice President, Chief Information Officer since September 1999. From 1985 until 1999, Mr. Milla was the Senior Vice President and Chief Information Officer at Response Analysis Corporation and following its acquisition, at Roper Starch Worldwide, where he was responsible for all information technology and data processing activities. From 1983 until 1985, Mr. Milla was on the staff of the National Opinion Research Center (NORC) at the University of Chicago and was responsible for managing the data processing activities on research projects for academic institutions and government agencies. Mr. Milla is currently a member of the Board of Directors of the Council of American Survey Research Organizations (CASRO). He also serves as chair of CASRO's Technology Committee. Mr. Milla holds a B.A. and M.A. from Queens College of the City University of New York.

**Ronald B. Knight** has served as Group President, Business and Consumer Services; Consulting & Brand Management since July 2000. Prior to joining our company, Mr. Knight was the Chief Operating Officer for The Sutherland Group from September 1998 through July 2000. He is the former Vice President and Chief of Staff of Business Operations for Xerox Corporation's Production Systems Group (PSG) where he worked for 30 years. He served as a Lieutenant in the U.S. Navy and worked as a financial analyst for General Motors prior to joining

Xerox Corporation. Mr. Knight holds a B.S. in Business Administration from the University of Rochester, and an M.B.A. from the University of Rhode Island.

**Bruce A. Newman** has served as our Chief Financial Officer, Secretary and Treasurer since January 1986. From July 1980 to January 1986, Mr. Newman served as Treasury Manager of The Case-Hoyt Corporation, a national printer. From July 1975 to August 1979, Mr. Newman worked for PricewaterhouseCoopers LLP. Mr. Newman received a B.S. in Accounting from the State University of New York at Albany and is a Certified Public Accountant.

**Gregory T. Novak** has served as Group President, Strategic Marketing Solutions, since July 2000. From June 1999 through June 2000, Mr. Novak was the President of our Internet Division. From August 1996 to June 1999, Mr. Novak was Vice President/General Manager of Lightnin America's, a unit of GSX. Mr. Novak received an M.S. in Management from Purdue University's Krannert Business School and a B.S. in Mechanical Engineering from the University of Pittsburgh. Mr. Novak is also a graduate of General Electric's Nuclear Power Engineering Program and Corporate Analyst's Training and Development Program.

**Harold E. Quinley** has served as Group President, Media & Public Relations, since February 2001. From 1984 until 2001, Dr. Quinley held various positions with Yankelovich Partners, Inc., including Partner, Senior Partner, and most recently, Executive Vice President. Prior to joining Yankelovich Partners, Inc., Dr. Quinley held various teaching positions at Stanford University, Brown University, San Francisco State University, Manhattanville College and The Graduate School at the New School for Social Research. Dr. Quinley was also the recipient of two Post-Doctoral Grants: Social Science Research Council (1969-1970) and National Endowment for the Humanities (1973-1974). Dr. Quinley received a B.A. from Lawrence University and a Ph.D. from Stanford University.

## **Item 2. Properties**

Our principal office is located in Rochester, New York, under a lease that expires in June 2005. In addition, we lease data collection centers, which include telephone interviewing and customer relationship management services, in Rochester, New York and Boardman, Ohio, and we lease service offices to house our project staff, administrative staff and processing staff, in New York, New York, Chicago, Illinois, Charlotte, North Carolina, Arlington, Virginia, Norwalk, Connecticut, Claremont, California and Washington DC. In August 2001, we closed the Charlotte, North Carolina and Washington DC offices.

We lease all of our facilities and believe our current facilities are adequate to meet our needs for the foreseeable future. We believe additional or alternative facilities can be leased to meet our future needs on commercially reasonable terms.

## **Item 3. Legal Proceedings**

In the normal course of business, we are at times subject to pending and threatened legal actions and proceedings. After reviewing pending and threatened actions and proceedings with counsel, management believes that the outcome of such actions or proceedings is not expected to have a material adverse effect on our financial position or results of operations.

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

No matters were submitted to a vote of security holders during the fourth quarter of fiscal 2001.

## PART II

### Item 5. Market for Registrant's Common Equity and Related Stockholder Matters

#### Market Information

Our common stock has been quoted on the Nasdaq National Market system under the symbol "HPOL" since December 6, 1999. Before then, there was no public market for our common stock. The following quotations are furnished by Nasdaq for the periods indicated. These quotations reflect inter-dealer quotations that do not include retail markups, markdowns or commissions and may not represent actual transactions. The following table shows, for the periods indicated, the high and low bid prices per share of our common stock.

	Price Range of Common Stock	
	High	Low
Year ending June 30, 2001:		
Fourth Quarter .....	3.8000	2.0500
Third Quarter .....	6.0625	2.6250
Second Quarter .....	4.8750	2.5000
First Quarter .....	5.3750	3.1250
Year ending June 30, 2000:		
Fourth Quarter .....	7.8750	3.0000
Third Quarter .....	21.0000	6.0000
Second Quarter (from December 6, 1999) .....	24.0000	13.0000

#### Holdings

At August 28, 2001, the Company's common stock was held by approximately 4,710 shareholders, reflecting shareholders of record or persons holding stock through nominee or street name accounts with brokers.

#### Dividends

We have never declared nor paid any cash dividends on our common stock. We currently anticipate that we will retain any future earnings for the development and operations of our business. Accordingly, we do not anticipate paying any cash dividends on our capital stock in the foreseeable future.

#### Changes in Securities and Use of Proceeds

On December 6, 1999, the Securities and Exchange Commission declared effective the Company's Registration Statement on Form S-1 (No. 333-87311). Pursuant to this Registration Statement, the Company completed an initial public offering of 6,670,000 shares of its common stock. Proceeds to the Company from the offering totaled approximately \$85.5 million, net of offering costs of approximately \$1.4 million.

The Company issued and sold an aggregate of 101,466 shares of its common stock to employees during the fourth quarter of fiscal 2001, upon the exercise of options granted under the Company's 1997 stock option plan, at a price of \$1.26, for an aggregate cash consideration of \$127,847. As to each employee of the Company who was issued the common stock described in this paragraph, the Company relied on Rule 701 under the Securities Act of 1933, as amended. Each person was granted an option to purchase shares of the Company's common stock pursuant to a written contract between such person and the Company, and the Company was eligible to use Rule 701 at the time the options herein reported as exercised were originally granted in accordance with Rule 701(b).

On June 30, 2001, the Company issued an aggregate of 44,438 shares of its common stock as the Company's matching contribution for the 401(k) Plan at a price of \$2.50, which did not constitute a sale under Section 2(3) of the Securities Act of 1933, as amended.

During the period December 6, 1999 through June 30, 2001, the Company used a portion of the proceeds from its public offering as follows: (i) approximately \$44.6 million of net cash used for working capital and general corporate purposes, including capital expenditures (ii) approximately \$11.0 million of net cash used for

the expansion of our Internet panel (iii) approximately \$8.2 million of net cash used for the purchase of the custom research division of Yankelovich and (iv) \$0.5 million of net cash used in connection with the repayment of short-term borrowings.

#### Item 6. Selected Consolidated Financial Data

The following selected consolidated financial data should be read in conjunction with “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and the consolidated financial statements and the notes to those statements and other financial information appearing elsewhere in this Form 10-K. The consolidated financial data for the year ended June 30, 1997 reflects the results of operations and balance sheet data of Gordon S. Black Corporation, our predecessor corporation.

	Year ended June 30,				
	2001	2000	1999	1998	1997
	(In thousands, except per share data and sales growth)				
<b>Statement of Operations Data:</b>					
Revenues from services . . . . .	\$ 60,061	\$ 51,289	\$ 28,965	\$26,290	\$23,327
Cost of services . . . . .	<u>30,764</u>	<u>28,600</u>	<u>19,086</u>	<u>16,618</u>	<u>15,629</u>
Gross profit . . . . .	29,297	22,689	9,879	9,672	7,698
<b>Operating expenses:</b>					
Internet database development expenses . . . . .	7,422	5,647	4,505	2,753	—
Sales and marketing expenses . . . . .	8,475	8,665	1,316	957	513
General and administrative expenses . . . . .	<u>41,115</u>	<u>32,209</u>	<u>13,085</u>	<u>8,855</u>	<u>5,878</u>
Operating (loss) income . . . . .	(27,715)	(23,832)	(9,027)	(2,893)	1,307
Interest and other income (loss), net . . . . .	3,695	2,940	180	(160)	(89)
(Loss) income before income tax . . . . .	(24,020)	(20,892)	(8,847)	(3,053)	1,218
Income tax expense (benefit) . . . . .	<u>—</u>	<u>50</u>	<u>—</u>	<u>(1,114)</u>	<u>490</u>
Net (loss) income . . . . .	(24,020)	(20,942)	(8,847)	(1,939)	728
Accrued dividends on preferred stock . . . . .	<u>—</u>	<u>(738)</u>	<u>(1,176)</u>	<u>—</u>	<u>—</u>
Net (loss) income available to holders of common stock . . . . .	<u>\$(24,020)</u>	<u>\$(21,680)</u>	<u>\$(10,023)</u>	<u>\$(1,939)</u>	<u>\$ 728</u>
(Loss) income per share—basic and diluted . . . . .	<u>\$ (0.70)</u>	<u>\$ (0.93)</u>	<u>\$ (1.01)</u>	<u>\$ (0.16)</u>	<u>\$ 0.06</u>
Weighted average shares outstanding—basic . . . . .	34,239	23,318	9,955	11,903	11,742
Weighted average shares outstanding—diluted . . . . .	34,239	23,318	9,955	11,903	12,372
<b>Selected Operating Data:</b>					
Sales Growth . . . . .	17%	77%	10%	13%	60%
Capital Expenditures . . . . .	7,648	12,092	4,372	977	672
<b>Balance Sheet Data (at end of period):</b>					
Cash, cash equivalents and marketable securities . . . . .	42,491	72,892	108	4	349
Working capital (deficit) . . . . .	44,634	78,698	552	(2,196)	(31)
Total assets . . . . .	85,221	104,452	14,785	9,798	9,721
Long-term debt, excluding current installment . . . . .	—	—	—	400	700
Mandatory redeemable preferred stock . . . . .	—	—	15,876	—	—
Total stockholders’ equity (deficit) . . . . .	71,174	94,350	(8,496)	947	2,392

#### Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations

##### Overview

We provide market research, polling and consulting services to a broad range of companies, non-profit organizations and governmental agencies. Since 1956, we have provided these services utilizing traditional market research and polling methodologies, such as direct mail, telephone-based surveys, mall intercepts, focus

groups and in-person interviews. In September 1997, we began developing our Internet panel and building the technology infrastructure to provide online market research and polling services. In November 1997, we introduced our first Internet-based market research and polling products and services.

We generally perform traditional and Internet-based custom research services on a fixed fee basis in response to client-generated requests. We sell our multi-client research products on a periodic subscription basis, typically quarterly or annually. Harris Interactive Service Bureau performs research for other market research firms on a project-by-project basis in response to requests from those firms. We provide customer relationship management services on an outsourced basis to our clients on a project-by-project basis.

Through fiscal 1998, all of our revenues were derived from custom research projects using traditional market research and polling methodologies. In fiscal 1999, revenues from those sources represented \$26.1 million, or 90% of our total revenues, while revenues from Internet-based products represented \$2.9 million, or 10% of total revenues. During fiscal 2000, revenues from traditional market research and polling methodologies represented \$30.3 million, or 59% of total revenues, while revenues from Internet-based products represented \$21.0 million, or 41% of total revenues. During fiscal 2001, revenues from traditional market research and polling methodologies represented \$27.5 million, or 46% of total revenues, while revenues from Internet-based products represented \$32.6 million, or 54% of total revenues. We consider all of the revenues from a project to be Internet-based whenever 50% or more of the surveys used in the completed project were completed by online panelists over the Internet. We anticipate that revenues derived from Internet-based custom research, multi-client products and Harris Interactive Service Bureau research will continue to represent the dominant portion of our total revenues.

Revenues under fixed fee arrangements are recognized on a percentage of completion method based on the ratio of costs incurred to total estimated costs. These revenues include amounts billed to our clients to cover subcontractor costs and other direct expenses. Provision for estimated contract losses, if any, is made in the period such losses are determined. Subscription revenues are recognized upon delivery of the research product.

Gross margin represents revenues less variable project costs and associated direct labor. Variable project costs related to market research utilizing traditional methodologies include interviewer payroll, subcontractor charges, panelist incentives, telecommunication charges and mailing costs. In contrast, variable costs related to Internet-based market research are nominal. Direct labor costs consist primarily of survey design, analysis, and reporting costs and are comparable for both traditional and Internet-based methodologies. We anticipate that our gross margins will increase as the percentage of revenues we generate from Internet-based products and services increases.

Operating expenses consist primarily of database development costs, sales and marketing, and general and administrative expenses. Database development expenses are the expenses we incur in connection with the ongoing development of our Internet panel. Those costs are expensed as incurred. Sales and marketing expenses consist primarily of personnel and marketing program expenses, public relations advertising and promotion costs, commissions and telemarketing costs and other related expenses. General and administrative expenses consist of salaries, payroll taxes, benefits and related costs for both technology infrastructure development and general corporate functions, occupancy costs and depreciation.

Interest and other income is primarily comprised of income from investments in each period.

We are required to and have in the past recognized compensation expense when we grant options or sell shares to employees at a price less than the fair market value of the shares at the date of grant or sale. In the case of option grants, the difference between the fair market value of the common stock and the exercise price on the grant date of the option is amortized as compensation expense over the vesting period for the option. In the case of a sale of common stock, the compensation expense is recognized on the date of sale. During fiscal 2001, fiscal 2000 and fiscal 1999, we recognized compensation expense in connection with such transactions of approximately \$.4 million, \$1.0 million and \$.02 million, respectively.

Our net losses were \$24.0 million, \$20.9 million, and \$8.8 million in fiscal 2001, fiscal 2000, and fiscal 1999, respectively, resulting primarily from the continued expansion of our business including the addition of new personnel, increased marketing and sales expenses, and higher costs associated with ongoing development of new products, services, and the technology infrastructure and Internet database necessary for our transition from

traditional to Internet-based market research. We believe that as Internet-based revenue continues to grow sharply, becoming an even larger component of total revenue, gross margin will continue to increase and losses will decline.

### Results of Operations

The following table sets forth for the periods indicated our results of operations expressed as a percentage of revenues:

	Year ended June 30,		
	2001	2000	1999
Revenues from services .....	100%	100%	100%
Cost of services .....	51	56	66
Gross margin .....	49	44	34
Internet database development expenses .....	12	11	16
Sales and marketing expenses .....	14	17	4
General and administrative expenses .....	69	63	45
Operating loss .....	(46)	(47)	(31)
Interest and other income, net .....	(6)	(6)	1
Net loss .....	(40)	(41)	(30)

### Fiscal 2001 as Compared to Fiscal 2000

**Revenues from Services.** Total revenue increased 17% from \$51.3 million in fiscal 2000 to \$60.1 million in fiscal 2001. This increase was due primarily to the incremental revenue generated from the Yankelovich custom research group acquired effective February 1, 2001, supplemented by increased usage of our Internet-based market research products and services, which contributed \$32.6 million to total revenue in fiscal 2001, a 55% increase over the prior year. Additionally, total revenues were negatively impacted by the current economic slowdown.

Internet revenue constituted 54% of total revenues in fiscal 2001 as compared to 41% of total revenues in fiscal 2000. This increase was dampened by the impact of the revenue mix acquired from Yankelovich which, prior to its acquisition by us, conducted virtually all of its research using traditional methodologies. However, as a percent of total revenue, Internet revenue for Yankelovich totaled 25% during the fourth quarter of fiscal 2001, its first full quarter since being acquired.

**Gross Margin.** Gross margin increased to 49% in fiscal 2001 from 44% in fiscal 2000, primarily due to the continuing expansion of Internet-related business relative to overall revenue growth.

**Database Development Expenses.** Database development expenses increased 32% to \$7.4 million in fiscal 2001 from \$5.6 million in fiscal 2000. The increase over fiscal 2000 is primarily due to The Planet Project Global Poll initiative, a four day, worldwide poll conducted in November, across all continents in eight languages. This survey was the largest of its type ever conducted and greatly increased our knowledge and expertise related to global research and added modestly to the number of cooperative online respondents worldwide.

**Sales and Marketing.** Sales and marketing expenses decreased slightly to \$8.5 million, or 14% of revenue in fiscal 2001 compared to \$8.7 million, or 17% of revenue, in the prior year. The decrease is primarily attributable to a reduction in marketing expenses, with a focus on specific products, as well as the Company-wide initiative to reduce overall spending.

**General and Administrative.** General and administrative expenses increased to \$41.1 million, or 69% of revenue in fiscal 2001 from \$32.2 million, or 63% of revenue in fiscal 2000. This increase was primarily attributable to increased staffing and occupancy expenses associated with new hires, higher costs associated with our continuing development of new products, services and technologies for the Internet.

**Interest and Other Income, Net.** Net interest and other income totaled \$3.7 million in fiscal 2001 as compared to \$2.9 million in fiscal 2000. The increase was primarily due to a higher average marketable securities balance during fiscal 2001 as compared to the prior year.

### **Fiscal 2000 as Compared to Fiscal 1999**

**Revenues from Services.** Total revenues increased 77% from \$29.0 million in fiscal 1999 to \$51.3 million in fiscal 2000. This increase was primarily due to increased usage of our Internet-based market research products and services, which contributed \$21.0 million to total revenues in fiscal 2000, a 624% increase over the prior year. Internet revenues constituted 41% of total revenues in fiscal 2000 as compared to 10% of total revenues in fiscal 1999.

**Gross Margin.** Gross margin increased to 44% in fiscal 2000 from 34% in fiscal 1999, primarily due to the significant expansion of Internet-related business relative to overall revenue growth.

**Database Development Expenses.** Database development expenses increased 24% to \$5.6 million in fiscal 2000 from \$4.5 million in fiscal 1999. The increase over fiscal 1999 is due to the continued expansion of the Company's online panel at a rate consistent with strategic objectives.

**Sales and Marketing.** Sales and marketing expenses increased 569% to \$8.7 million in fiscal 2000 compared to \$1.3 million in the prior year. The increase is primarily attributable to additional sales and marketing personnel as well as marketing efforts in support of our multi-client research products and Harris Interactive Service Bureau expansion.

**General and Administrative.** General and administrative expenses increased 146% to \$32.2 million in fiscal 2000 from \$13.1 million in fiscal 1999. This increase was primarily attributable to increased staffing and occupancy expenses associated with new hires, higher costs associated with our continuing development of new products, services and technologies for the Internet, and compensation expense related to stock option grants.

**Interest and Other Income, Net.** Net interest and other income totaled \$2.9 million in fiscal 2000 as compared to \$0.2 million in fiscal 1999. The increase was primarily due to increased cash and marketable security balances during fiscal 2000 resulting from a private placement of Class B Preferred Stock in October 1999 and completion of our initial public offering in December 1999.

## Quarterly Results of Operations

The following table presents unaudited consolidated quarterly statement of operations data for the years ended June 30, 2000 and 2001. In management's opinion, this information has been prepared on the same basis as the audited consolidated financial statements and includes all adjustments, consisting only of normal recurring adjustments necessary for the fair presentation of the unaudited information in the periods presented. This information should be read in conjunction with the consolidated financial statements and related notes included under Item 8 of this report and in conjunction with other financial information included elsewhere in this Form 10-K. The results of operations for any quarter are not necessarily indicative of results that may be expected for any future periods.

	Three Months Ended							
	September 30, 1999	December 31, 1999	March 31, 2000	June 30, 2000	September 30, 2000	December 31, 2000	March 31, 2001	June 30, 2001
Revenues from services .....	\$ 9,364	\$12,473	\$14,156	\$15,296	\$12,053	\$14,532	\$15,826	\$17,650
Cost of services .....	6,307	6,950	7,503	7,840	6,301	6,939	8,444	9,080
Gross Profit .....	3,057	5,523	6,653	7,456	5,752	7,593	7,382	8,570
Operating expenses:								
Internet database development expenses .....	905	1,615	1,600	1,527	2,517	2,617	1,633	655
Sales and marketing expenses ..	793	2,067	2,863	2,942	1,913	2,071	2,443	2,048
General and administrative expenses .....	5,121	7,224	9,046	10,818	10,086	9,748	10,045	11,236
Operating loss .....	(3,762)	(5,383)	(6,856)	(7,831)	(8,764)	(6,843)	(6,739)	(5,369)
Interest and other (expense) income, net .....	(71)	401	1,340	1,270	1,138	1,048	818	862
Loss before income taxes .....	(3,833)	(4,982)	(5,516)	(6,561)	(7,626)	(5,795)	(5,921)	(4,507)
Income tax expense .....	—	—	—	50	—	171	—	—
Net loss .....	(3,833)	(4,982)	(5,516)	(6,611)	(7,626)	(5,966)	(5,921)	(4,507)
Accrued dividends on preferred stock .....	(294)	(444)	—	—	—	—	—	—
Net loss attributable to holders of common stock .....	<u>\$(4,127)</u>	<u>\$(5,426)</u>	<u>\$(5,516)</u>	<u>\$(6,611)</u>	<u>\$(7,626)</u>	<u>\$(5,966)</u>	<u>\$(5,921)</u>	<u>\$(4,507)</u>
Basic and diluted net loss per share .....	<u>\$ (0.38)</u>	<u>\$ (0.33)</u>	<u>\$ (0.17)</u>	<u>\$ (0.19)</u>	<u>\$ (0.22)</u>	<u>\$ (0.17)</u>	<u>\$ (0.17)</u>	<u>\$ (0.13)</u>

## Liquidity and Capital Resources

We have financed our operations primarily through bank financing and, more recently, issuances of our common and preferred stock. In December 1999 we completed the initial public offering of 6,670,000 shares of our common stock (including 870,000 shares sold pursuant to the exercise of the Underwriters' over-allotment option), which generated net proceeds of \$85.5 million. Consequently, cash and cash equivalents and marketable securities increased from \$0.1 million at June 30, 1999 to \$72.9 million at June 30, 2000. At June 30, 2001, cash and cash equivalents and marketable securities were \$42.5 million.

Net cash used in operating activities was \$15.5 million for fiscal 2001, \$22.0 million for fiscal 2000 and \$8.2 million for fiscal 1999. Net cash used in operating activities in each of these periods was primarily the result of net losses.

Net cash provided by investing activities was \$2.1 million for fiscal 2001. Net proceeds from sales and maturities of marketable securities of \$17.9 million were partially offset by the \$8.2 million cash outflow to purchase the custom research division of Yankelovich Partners, Inc. in February 2001. Capital expenditures of \$7.6 million primarily supported the development of our Internet infrastructure.

During fiscal 2000 and fiscal 1999, net cash used in investing activities was \$60.9 million and \$4.3 million, respectively. Net cash used in investing activities during fiscal 2000 was attributable to the purchase of investment securities with the proceeds from our initial public offering of common stock, pending the use of these proceeds for working capital, expansion of our Internet panel, and development of new technologies, products,

and services. Additionally, capital expenditures associated with our Internet infrastructure development and facilities expansion were \$12.1 million. During fiscal 1999, net cash used in investing activities was primarily related to capital expenditures associated with our Internet infrastructure development and facilities expansion.

Net cash provided by financing activities was \$.1 million in fiscal 2001, resulting from issuances of common stock and stock options, offset by the repurchase of common stock. During fiscal 2000 and fiscal 1999 net cash provided by financing activities was \$106.7 million and \$12.6 million, respectively. In fiscal 2000, our financing activities primarily consisted of the issuance of common stock in connection with the initial public offering completed in December 1999, with net proceeds of \$85.5 million, as well as a private placement of our Class B preferred stock with net proceeds of \$19.9 million. In fiscal 1999, our financing activities consisted primarily of a private placement of our Class A preferred stock with net proceeds of \$14.1 million in the first quarter, and the issuance of common stock to a long-term participant in our Harris Interactive Service Bureau with net proceeds of \$4.1 million in the fourth quarter. These net proceeds were partially offset by the repurchase of \$3.0 million of common stock from two of our executive officers and several other stockholders, the repayment of \$1.9 million on our line of credit and principal repayments of \$0.7 million on our long-term debt.

Our capital requirements depend on numerous factors, including market acceptance of our products and services, the resources we allocate to the continuing development of our Internet infrastructure and Internet panel, marketing and selling of our services, our promotional activities and other factors. While management anticipates continuing expenditures for property, plant and equipment and working capital requirements throughout fiscal 2002, these expenditures are expected to be lower than fiscal 2001.

### **Recent Developments**

On August 5, 2001, the Company entered into an Agreement and Plan of Merger with Total Research Corporation, located in Princeton, New Jersey. Pursuant to the agreement, Harris Interactive will exchange 1.222 shares of Harris Interactive common stock, par value \$.001 per share, for each outstanding share of Total Research common stock, par value \$.001 per share.

The merger is intended to be a tax free exchange. Consummation of the merger is subject to satisfaction or waiver by the parties of certain closing conditions, including the receipt of regulatory approvals, approvals by the stockholders of Harris Interactive and Total Research, respectively, and other customary closing conditions. The transaction is anticipated to close during the fourth quarter of the calendar year 2001.

On August 6, 2001, the Company also entered into an agreement to acquire Market Research Solutions Limited, a privately owned UK company, headquartered in Oxford, England, in consideration of a combination of cash and shares of Harris Interactive common stock.

### **Recent Accounting Pronouncements**

#### **SAB 101**

In December 1999, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 101 ("SAB 101"), "Revenue Recognition in Financial Statements." SAB 101 provides guidance for revenue recognition under certain circumstances. SAB 101 became effective for our fiscal year beginning July 1, 2000. Implementation of SAB 101 did not require us to change existing revenue recognition policies and therefore did not have a material effect on our financial position or results of operations.

#### **FIN 44**

In March 2000, the Financial Accounting Standards Board issued Interpretation No. 44 ("FIN 44"), "Accounting for Certain Transactions Involving Stock Compensation, an Interpretation of APB Opinion No. 25". FIN 44 clarifies the application of Opinion No. 25 for (a) the definition of employee for purposes of applying Opinion No. 25, (b) the criteria for determining whether a plan qualifies as a noncompensatory plan, (c) the accounting consequence of various modifications to the terms of a previously fixed stock option or award, and (d) the accounting for an exchange of stock compensation awards in a business combination. FIN 44 became effective July 1, 2000, but certain conclusions cover specific events that occur after either December 15, 1998, or

January 12, 2000. The impact of FIN 44 did not have a material effect on our financial position or results of operations.

### **SFAS 141 and SFAS 142**

In July 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standard No. 141 ("SFAS 141"), "Business Combinations" and Statement of Financial Accounting Standard No. 142 ("SFAS 142"), Goodwill and Other Intangible Assets." SFAS 141 requires that all business combinations be accounted for under the purchase method only and that certain acquired intangible assets in a business combination be recognized as assets apart from goodwill. SFAS 142 requires that ratable amortization of goodwill be replaced with periodic tests of the goodwill impairment and that intangible assets other than goodwill and other indefinite lived intangible assets, be amortized over their useful lives. SFAS 141 is effective for all business combinations initiated after June 30, 2001 and for all business combinations accounted for by the purchase method for which the date of acquisition is after June 30, 2001. The provisions of SFAS 142 will be effective for fiscal years beginning after December 15, 2001. The impact of SFAS 141 and SFAS 142 on the Company's financial statements has not yet been determined.

### **Risk Factors**

**If the marketplace does not accept internet-based market research and polling, our growth will be adversely affected.**

The success of our business will depend on our ability to develop and market Internet-based products and services that achieve broad market acceptance by our current and potential clients. These clients must accept the Internet as an attractive and sustainable substitute medium for traditional methodologies of conducting market research to which they are accustomed, such as direct mail, telephone-based surveys, mall intercepts, focus groups and in-person interviews. Since the beginning of fiscal 1998, we have expended \$56.7 million and significant management resources in the development and growth of our Internet-based market research and polling business. We have experienced resistance from some of our clients regarding our Internet-based market research and polling methodologies. These clients expressed concern that Internet users do not yet accurately reflect the overall population, and any resulting information will be inherently biased towards the views, experiences and attitudes of an unrepresentative group. If our current and potential clients do not accept our Internet-based methodologies as reliable and unbiased, our revenues may not meet expectations or may decline, and our business would likely suffer.

**We must continually attract and retain skilled technical, managerial, marketing, sales and other personnel or we will be unable to execute our business strategy.**

Our future success will depend, in part, on our ability to attract, retain and motivate highly skilled technical, managerial, marketing, sales and client support personnel. Competition for these personnel is intense and we may be unable to attract, integrate or retain sufficiently qualified personnel or the number of qualified personnel our business plan assumes. We have experienced in the past, and we expect to continue to experience in the future, difficulty in hiring and retaining highly skilled employees with appropriate qualifications. Our past difficulties in hiring and retaining highly skilled employees have resulted in additional costs for recruitment, compensation and relocation or the provision of remote access to our facilities. In addition, at certain times we have been required to outsource software development for systems improvements, which has resulted in delays in implementation and integration and increased costs. To the extent that we are unable to hire and retain skilled employees in the future, our business would likely suffer.

**We derived 12% of our total revenues from one client in fiscal 2001. If we were to lose, or if there were a material reduction in business from this client, our business would likely suffer.**

Our contract with our largest client is terminable upon notice of 90 days or less, and this client may reduce its use of our services or products at any time. The loss of, or material reduction in business from this client, without replacement, would have a material adverse effect on our business, financial condition and results of operations.

**We have incurred losses in recent years.**

Since the beginning of fiscal 1998 through year end fiscal 2001, we have expended approximately \$56.7 million to develop and maintain our Internet capabilities, comprising of approximately \$20.3 million to develop our Internet panel and approximately \$36.4 million to develop and maintain our technology infrastructure. As a result, we incurred net losses of \$24.0 million in fiscal 2001, \$20.9 million in fiscal 2000 and \$8.8 million in fiscal 1999. We base current and future expense levels on our operating plans and our estimates of future revenues. If our revenues grow at a slower rate than we anticipate, or if our spending levels exceed our expectations or cannot be adjusted to reflect slower revenue growth, we may not be able to achieve profitability. Even if we achieve profitability in the future, we may be unable to sustain or increase profitability on a quarterly or annual basis.

**Fluctuations in our operating results may cause our stock price to decline.**

Our operating results have in the past and may in the future fluctuate significantly from quarter to quarter. In future periods, our results of operations may be below the expectations of public market analysts and investors. In this event, the price of our common stock would likely decline.

Factors that are outside of our control, and that have caused our results to fluctuate in the past or that may affect us in the future, include:

- demand for market research and polling products and services generally;
- seasonal fluctuations due to decreases in requests for market research and polling services during the summer and year-end vacation and holiday periods;
- development of products and services by our competitors;
- technical difficulties or system downtime affecting the Internet generally; and
- fluctuations in general economic conditions or the budgets of our clients.

Factors that are within our control, and that have caused our results to fluctuate in the past or that may affect us in the future, include:

- our relative mix of Internet-based and traditional market research and polling businesses;
- technical difficulties or downtime of individual components of our computer system affecting our operations;
- our ability to maintain a critical mass and scope of our Internet panel commensurate with our use of the panel to develop and sell new products and services to generate revenues; and
- development of our products and services.

The factors listed above may affect both our quarter-to-quarter operating results as well as our long-term success. You should not rely on quarter-to-quarter comparisons of our results of operations as an indication of our future performance or any trend in our performance.

**We have ended our agreements with Excite@Home.**

In June 2001 the Company ended its strategic alliance and multi-year, panel recruitment agreement with Excite@Home. This arrangement had been the single, largest source of new names for the Harris Interactive online panel, having obtained more than 90% of the names in the Internet panel from that relationship. However, prices for double opt-in names have dropped precipitously over the past 18 months, thus allowing the Company to explore other less costly options to expand and replenish the panel. Our success will depend on our ability to develop other reliable sources with which to build and replenish our Internet panel. If we are unable to develop alternative sources of online panelists, our business, financial condition and results of operations would likely suffer.

**If we are unable to maintain adequate size and demographic composition of our Internet panel, or if we are required to spend substantial funds to do so, our business will suffer.**

Our success is highly dependent on our ability to obtain and retain an adequate number of panelists in our Internet panel. Our ability to maintain an adequate online panel or increase revenues through the use of our Internet panel may be harmed if:

- a significant number of our current online panelists decide that they are no longer willing to participate in our surveys;
- we lose our online panelists due to numerous requests for participation and we are required to rely on a limited number of online panelists for numerous surveys on a variety of subjects; or
- our online panelists become frustrated with the layout and design of our questionnaires and, as a result, reduce their participation in our surveys.

If the number of our survey respondents decreases or the demographic composition of our Internet panel narrows, our ability to provide our clients with accurate and statistically projectable information would likely suffer. This risk is likely to increase as our business expands. For example, our Internet panel is surveyed for our own studies as well as for studies conducted by our Harris Interactive Service Bureau, which conducts research for other market research firms. Our business cannot grow and will suffer if we have an insufficient number of panelists to respond to our surveys, or if our panel becomes unreliable because of its size or because it is not representative of the general population.

Our online panelists are not obligated to participate in our surveys and polls and there can be no assurance that they will do so. We occasionally offer incentives to encourage participation in our surveys and to increase the size of our Internet panel.

**We may not be able to compete successfully.**

The markets for our products and services are highly competitive. We compete for clients with market research firms offering Internet-based and traditional market research and polling services. We expect to face competition in the future from other traditional market research firms who develop Internet-related products and services or other companies with access to large databases of individuals with whom they can communicate on the Internet. These companies may, either alone or in alliances with other firms, penetrate the Internet-based market research and polling market.

We do not believe that there are currently any dominant competitors in the Internet-based market research and polling market. However, many of our current and potential competitors have longer operating histories and significantly greater financial and marketing resources. These competitors may be able to undertake more extensive marketing campaigns for their services, adopt more aggressive pricing policies and make more attractive offers to potential employees, strategic partners and customers. Further, our competitors and potential competitors may develop technologies that are superior to ours, or that achieve greater market acceptance than our own. The above factors, either alone or in combination, would likely result in a loss of market share and reduced levels of revenue and profitability.

**Potential acquisitions of or investments in other companies may not be available and may have a negative impact on our business.**

As part of our continued strategy to expand our Internet panel, our technology infrastructure and our products and services, we may acquire or make investments in complementary businesses, services, products or technologies if appropriate opportunities arise. However, we may be unable to identify suitable acquisition or investment candidates at reasonable prices or on reasonable terms. The material risks involved with acquisitions are:

- the difficulties in the integration and assimilation of the operations, technologies, products and personnel of the acquired business;
- the diversion of management's attention from other business concerns;

- the availability of favorable acquisition financing; and
- the potential loss of key employees and/or customers of any acquired business.

Acquisitions may require the use of significant amounts of cash, resulting in the inability to use those funds for other business purposes. Acquisitions utilizing our capital stock could result in potentially dilutive issuances of our capital stock, which could adversely impact the market price of our common stock. Amortization of intangible assets would reduce our earnings, which in turn could negatively impact the price of our common stock. These difficulties could disrupt our ongoing business, distract our management and employees and increase our expenses.

**The loss of the services of one or more of our key personnel could disrupt our operations and result in loss of revenues.**

Our future success depends to a significant extent on the continued services of our key technical and senior management personnel. The loss of the services of any of these persons could seriously harm our business. Although some of our key employees have signed non-competitive agreements, none of our officers or key employees is bound by an employment agreement, and our relationships with our officers and key employees are at will. We do not have “key person” life insurance policies covering any of our employees other than Gordon S. Black.

**We are growing rapidly and if we are not able to effectively manage and support our growth our business strategy might not succeed.**

We have grown rapidly and will need to continue to grow in all areas of our operations to execute our business strategy. Managing and sustaining our growth will place significant demands on management as well as on our administrative, operational, technical and financial systems and controls. If we are unable to manage our growth effectively, we would have to divert resources away from the continued growth of our business and the implementation of our business strategy.

**If we do not keep pace with rapid technological change and the intense competition of the market research and polling industry, we will not be able to successfully implement our business plan.**

The market research and polling industry is characterized by intense competition, frequent new products and service introductions and evolving methodologies. The continued growth of the Internet exacerbates these market characteristics. To succeed, we will need to develop and integrate effectively the various software programs, technologies and methodologies required to enhance and improve our market research product and service offerings and manage our business. Any enhancements or new services or products must meet the requirements of our current and potential clients and achieve significant market acceptance. Our success also will depend on our ability to adapt to rapidly changing technologies by continually improving the performance features and reliability of our products and services. We may experience difficulties that could delay or prevent the successful development, introduction or marketing of new products and services. We could also incur substantial costs if we need to modify our services or infrastructure to adapt to these changes.

**Any failure in the performance of our Internet-based technology infrastructure could harm our business and our reputation.**

Any system failure, including network, software or hardware failure, that causes an interruption in our ability to communicate with our Internet panel or in our ability to collect research data could result in reduced revenue, and could impair our reputation. Our systems and operations are vulnerable to damage or interruption from fire, earthquake, power loss, telecommunications failure, break-ins and similar events. We depend on Verio Collocation, an off-site data security facility, to maintain approximately one-third of our servers at its facility in Rochester, New York, and to protect our systems and operations from the events described above.

We have experienced technical difficulties with downtime of individual components of our computer system in the past and believe that technical difficulties and downtime will continue to occur from time to time in the future. To date, technical difficulties and downtime have had minimal impact on our operations and have usually

been rectified within several hours to 48 hours. Their impact may be more severe in the future. We have no formal disaster recovery plan and our business interruption insurance may not adequately compensate us for any losses that may occur due to any failures in our system and any resulting interruptions in our communications with our Internet panel or in our data collection efforts. In addition, our servers and software must be able to accommodate a high volume of traffic. Any increase in demands on our servers beyond that which we currently anticipate will require us to expand and adapt our network infrastructure. If we were unable to add additional software and hardware to accommodate increased demand, unanticipated system disruptions and slower data collection would likely result.

Moreover, our Internet panel members communicate with us using various Internet service providers. These providers have experienced significant outages in the past, and could experience outages, delays and other difficulties due to system failures unrelated to our systems.

While the impact of these outages in the past has been minimal, any future system delays or failures of service providers to our Internet panel could adversely affect our access to our online panelists, which could have a material adverse effect on our business, financial condition and results of operations.

**Failure or inability to protect our intellectual property could adversely affect our business.**

Our success and ability to compete substantially depend on our internally developed technologies and trademarks, which we protect through a combination of patent, copyright, trade secret and trademark laws. We have trademark registrations for a number of our trademarks, including the HARRIS POLL. If we were prevented from using the HARRIS POLL, our brand recognition and business would likely suffer. We would have to make substantial financial commitments to promote and rebuild our brand identity and loyalty with our clients and members of our Internet panel and re-implement our website.

We have currently pending trademark applications for CONCEPTLOC, STOCKMETER, JOURNAL OF INTERNET RESEARCH, HARRIS INTERACTIVE and HPOL. We also have patent applications currently pending for a multi-location and multi-language registration and polling system and for our CONCEPTLOC encryption system. In June 2001, the Company filed a third patent application for a system and method for conducting product configuration research over a computer-based network. In addition, we may apply for additional trademarks or patents in the future. Our patent or trademark applications may not be approved, or if approved, our patents or trademarks may be successfully challenged by others or invalidated. If our trademark applications are not approved because third parties own these trademarks, our use of these trademarks would be restricted unless we enter into arrangements with the third-party owners, which might not be possible on commercially reasonable terms or at all.

We generally enter into confidentiality or license agreements with parties with whom we do business, and generally control access to and distribution of our technologies, documentation and other proprietary information. Despite our efforts to protect our proprietary rights from unauthorized use or disclosure, parties may attempt to disclose, obtain or use our technologies. The steps we have taken may not prevent misappropriation of our technologies, particularly in foreign countries where laws or law enforcement practices may not protect our proprietary rights as fully as in the United States.

We also rely on off-the-shelf technologies that we license from third parties. "Off-the-shelf" technology refers to generally commercially available software that is not customized for a particular user. These third party licenses may not continue to be available to us on commercially reasonable terms or at all. The inability to use licensed technology important to our business could require us to obtain substitute technology of lower quality or performance standards or at a greater cost. In the future, we may seek to license additional technology to enhance our current technology infrastructure. We cannot be certain that any such licenses will be available on commercially reasonable terms or at all. The loss of any of these technology licenses could result in delays in providing our products and services until equivalent technology, if available, is identified, licensed and integrated.

**Possible intellectual property infringement claims by third parties could be costly.**

We cannot guarantee that infringement or other claims will not be asserted or prosecuted against us in the future, whether resulting from our internally developed intellectual property or licenses or content from third parties. Any future assertions or prosecutions could be time-consuming, result in costly litigation and diversion of technical and management personnel or require us to pay money damages, introduce new trademarks, develop non-infringing technology, or enter into royalty or licensing agreements. Any of those events could substantially increase our operating expenses and potentially reduce our expected revenues. These royalty or license agreements, if required, may not be available on acceptable terms, or at all. Our ability to execute our business strategy will suffer if a successful claim of infringement is brought against us and we are unable to introduce new trademarks, develop non-infringing technology or license the infringed or similar technology on a timely basis.

Moreover, our general liability insurance may not cover, or may not be adequate to cover all costs incurred, in defense of potential trademark infringement claims, or to indemnify us for all liability that may be imposed.

**Any difficulty in accessing additional capital may prevent us from achieving our business objectives.**

We may need to raise additional funds in the future to fund the expansion of our Internet panel and the marketing of our products and services, or to acquire complementary businesses, technologies or services. Any required additional financing may be unavailable on terms favorable to us, or at all. If we raise additional funds by issuing equity securities, current stockholders will experience dilution, which may be significant, to their ownership interest, and such securities may have rights senior to those of the holders of our common stock. If additional financing is not available when required or is not available on acceptable terms, we may be unable to fund the development and expansion of our business, promote our brand name successfully, take advantage of business opportunities or respond to competitive pressures, any of which could have a material adverse effect on our business, financial condition and results of operations.

**Our business is largely dependent on the development and growth of the Internet, which may not grow, or if it does grow, may be unable to support the demands placed on it by this growth.**

If Internet usage in general does not grow, we may be unable to attract additional online panelists to our Internet panel or clients for our Internet-based market research and polling products and services. If Internet usage does continue to grow, the Internet infrastructure may be unable to support the demands placed on it by this growth and its performance and reliability may decline. Varying factors could inhibit future growth or the ability of the Internet infrastructure to adequately support the growth in Internet usage, including:

- inadequate network infrastructure;
- security concerns;
- inconsistent quality of service; and
- unavailability of cost effective, high speed service.

Our Internet panel depends on Internet service providers, online service providers and other website operators for access to the Internet and our websites. Many websites have experienced interruptions in their service as a result of outages and other delays occurring throughout the Internet network infrastructure.

Nielsen//NetRatings reported that the total number of users that had access to the Web during the month of July 2001 (but did not necessarily log on), was approximately 165 million or 58% of the census population, an increase of 6% from one year ago and an increase of 19% from two years ago. If Internet usage declines or grows at a significantly slower rate than projected, our ability to maintain our Internet panel, add further members to our Internet panel and gather research data and information quickly will decrease, which would likely harm our business.

**Changes in government regulation or industry practices could limit our Internet activities or result in additional costs of doing business on the Internet.**

The Internet Tax Freedom Act prohibits states or political subdivisions from imposing taxes on Internet access, unless imposed and enforced prior to October 1, 1998, and multiple or discriminatory taxes on electronic commerce during the period beginning October 1, 1998. The Internet Tax Freedom Act also created the Advisory Commission on Electronic Commerce to examine tax laws that impact electronic commerce.

Any new laws pertaining to the imposition of taxes on Internet access and electronic commerce could adversely affect our business. In February 1999, the Federal Communications Commission issued a declaratory ruling interpreting the Telecommunications Act of 1996 to allow local exchange carriers to receive reciprocal compensation for traffic delivered to information service providers, particularly Internet service providers, on the basis that traffic bound for Internet service providers is largely interstate. As a result of this ruling, the costs of transmitting data over the Internet may increase and our business could suffer.

There are currently few laws or regulations that specifically regulate communications on the Internet. However, we expect more stringent laws and regulations to be enacted due to the increasing popularity and use of the Internet. Any new legislation or regulations or the application of existing laws and regulations to the Internet could limit our effectiveness in conducting Internet-based market research and polling, and increase our operating expenses. In addition, the application of existing laws to the Internet could expose us to substantial liability for which we might not be indemnified by content providers or other third parties. Existing laws and regulations currently address, and new laws and regulations and industry self-regulatory initiatives are likely to address, a variety of issues, including the following:

- e-mail distribution,
- user privacy and expression;
- the rights and safety of children;
- intellectual property;
- information security;
- anti-competitive practices;
- the convergence of traditional channels with Internet commerce;
- taxation and pricing; and
- the characteristics and quality of products and services.

Those laws that do reference the Internet have limited interpretation by the courts and their applicability and scope are not well defined. Any new laws or regulations relating to the Internet could adversely affect our business.

Industry standards related to the Internet are still evolving. Moreover, some private entities have proposed their own standards for communications with, and use of information related to, individuals who use the Internet. Internet service providers also have the ability to disrupt our communications with our panel. Although we believe that we employ responsible practices related to the recruitment of members of our database, communications with our panelists and use of information provided by our respondents, some service providers and/or self appointed industry regulators may not agree. As a result, our communications with our panelists may be disrupted from time to time.

**Internet security concerns could hinder Internet communications and our ability to obtain sufficient and reliable responses from our online panelists.**

The need to transmit confidential information securely over the Internet has been a significant barrier to communications over the Internet. Internet security concerns could cause some online panelists to reduce their participation levels, provide inaccurate responses or terminate their membership in our Internet panel. This could harm our credibility with our current clients. If our clients become dissatisfied, they may stop using our products

and services. In addition, dissatisfied and lost clients could damage our reputation. A loss of online panelists or a loss of clients would hurt our efforts to generate increased revenues.

**We are susceptible to breaches of database security.**

A party who is able to circumvent our security measures could misappropriate the personal information of our online panelists. As a result, we may be required to expend capital and other resources to protect against the threat of such security breaches or to alleviate problems caused by such breaches, which could have a material adverse effect on our business, financial condition and results of operations.

**Potential liability for the use of the personal information or our Internet panel could be costly.**

We could be subject to liability claims by our online panelists for misuses of personal information, such as for unauthorized marketing purposes. These claims could result in costly litigation. In addition, the Federal Trade Commission and state agencies have been investigating various Internet companies regarding their use of personal information. We could incur additional costs and expenses if new regulations regarding the use of personal information are introduced or if our privacy practices are investigated.

**If we are unable to achieve the anticipated global growth of our Internet panel, or if we are unable to overcome other risks of global operations, we will be unable to conduct business on a global level.**

Key components of our strategy are extension of our Internet-based market research and polling products and services to clients globally, expansion of our Internet panel to include global online panelists and development of strategic alliances globally. The following risks are inherent in doing business on a global level:

- export controls relating to encryption technology;
- more restrictive privacy laws;
- unexpected changes in regulatory requirements;
- lower penetration of Internet use globally, which may effect our ability to obtain non-U.S. panel members;
- currency exchange fluctuations;
- problems in collecting accounts receivable and longer collection periods;
- potentially adverse tax consequences;
- political instability; and
- Internet access restrictions.

We have little or no control over these risks. We have encountered more restrictive privacy laws in connection with our business operations in Europe, which have inhibited our ability to develop our European Internet panel. We have also experienced currency exchange fluctuations, the impact of which has not been material. As we increase our global operations, we may experience in the future some or all of these risks, which may have a material adverse effect on our business, financial condition and results of operations.

**We may be subject to liability for publishing or distributing content over the Internet.**

We may be subject to claims relating to content that is published on or downloaded from our websites. We also could be subject to liability for content that is accessible from our website through links to other websites.

Although we carry general liability insurance, our insurance may not cover potential claims of this type, such as defamation or trademark infringement, or may not be adequate to cover all costs incurred in defense of potential claims or to indemnify us for all liability that may be imposed. In addition, any claims of this type, with or without merit, would result in the diversion of our financial resources and management personnel.

**The price of our common stock is likely to be volatile and subject to wide fluctuations.**

The market prices of the securities of Internet-related companies have been especially volatile and these securities may be overvalued. The market price of our common stock is likely to be subject to wide fluctuations. If financial operating results do not improve or improve at a slower rate than we anticipate, or if operating or capital expenditures exceed our expectations and cannot be adjusted accordingly, or if some other event adversely affects us, the market price of our common stock would decline. In addition, if the market for Internet-related stocks or the stock market in general experiences a loss in investor confidence or otherwise falls, the market price of our common stock could fall for reasons unrelated to our business, financial condition and results of operations. Investors might be unable to resell their shares of our common stock at or above the purchase price. In the past, companies that have experienced volatility in the market price of their stock have been the subject of securities class action litigation. If we were to become the subject of securities class action litigation, it could result in substantial costs and a diversion of management's attention and resources.

**Anti-takeover provisions in our charter could delay or prevent an acquisition of the company.**

Our restated certificate of incorporation provides for the division of our board of directors into three classes and provides our board of directors with the power to issue shares of preferred stock without stockholder approval.

This preferred stock could have voting rights, including voting rights that could be superior to that of our common stock, and the board of directors has the power to determine these voting rights. In addition, Section 203 of the Delaware General Corporation Law contains provisions which impose restrictions on stockholder action to acquire our company. The effect of these provisions of our certificate of incorporation and Delaware law provisions could discourage or prevent third parties from seeking to obtain control of us, including transactions in which the holders of common stock might receive a premium for their shares over prevailing market prices.

**Our executive officers, directors, members of their families and entities affiliated with them have significant control of our management and affairs.**

Our executive officers, directors, members of their families and entities affiliated with them, in the aggregate, beneficially own a majority of our common stock. As a result, these stockholders are able to exercise control over all matters requiring approval by our stockholders, including the election of directors and approval of mergers, consolidations, sales of assets, recapitalizations and amendments to our certificate of incorporation. This concentration of ownership may also have the effect of delaying or preventing a change in control of us.

**Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

The carrying values of financial instruments including cash and cash equivalents, marketable securities, accounts receivable and accounts payable, approximate fair value because of the short maturity of these instruments.

We have historically had very low exposure to changes in foreign currency exchange rates. Therefore we have not used derivative financial instruments to manage foreign currency fluctuation risk. As we continue to expand globally, the risk of foreign currency exchange rate fluctuation may increase. Therefore, in the future, we may consider utilizing derivative instruments to mitigate such risks.

**Item 8. Financial Statements and Supplementary Data**

The information required by this item is incorporated by reference to the consolidated financial statements listed in Item 14(a) of Part IV of this Form 10-K.

**Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

None.

### **PART III**

#### **Item 10. Directors and Executive Officers of the Registrant**

Information regarding our directors is incorporated by reference from the section entitled "Election of Directors" in our definitive proxy statement for our annual stockholders' meeting to be held on or before December 31, 2001 (the "2001 Proxy Statement"). Information regarding executive officers who are not directors is set forth in Item 1 of Part I of this report under the caption "Executive Officers."

#### **Item 11. Executive Compensation**

The information required by Item 11 is incorporated by reference from the 2001 Proxy Statement.

#### **Item 12. Security Ownership of Certain Beneficial Owners and Management**

The information required by Item 12 is incorporated by reference from the 2001 Proxy Statement.

#### **Item 13. Certain Relationships and Related Transactions**

The information required by Item 13 is incorporated by reference from the 2001 Proxy Statement.

**PART IV**

**Item 14. Exhibits, Financial Statements Schedules, and Reports on Form 8-K**

(a) List of Documents Filed as part of this Annual Report.

(1) Index to Consolidated Financial Statements

	<u>Page Number in this Report</u>
Report of Independent Accountants. . . . .	F-1
Consolidated Balance Sheets at June 30, 2001 and 2000 . . . . .	F-2
Consolidated Statements of Operations for the years ended June 30, 2001, 2000 and 1999 . . . . .	F-3
Consolidated Statements of Stockholders' Equity for the years ended June 30, 2001, 2000 and 1999 . . . . .	F-4
Consolidated Statements of Cash Flows for the years ended June 30, 2001, 2000 and 1999 . . . . .	F-5
Notes to Consolidated Financial Statements . . . . .	F-6

(2) Index to Financial Statement Schedules

	<u>Page Number in this Report</u>
Schedule II – Valuation and Qualifying Accounts . . . . .	S-1

All other schedules for which provision is made in the applicable accounting regulations of the Securities and Exchange Commission are not required under the related instructions or are inapplicable and therefore have been omitted.

(b) Reports on Form 8-K

None

(c) List of Exhibits

<u>Exhibit Number</u>	<u>Exhibit Title</u>
3.1	Amended and Restated Certificate of Incorporation of the Company (filed as Exhibit 3.1 to Form 10-K filed September 27, 2000 and incorporated herein by reference).
3.2	Bylaws of the Company (filed herewith).
10.1	1999 Long Term Incentive Plan and form of agreements thereto of the Company (filed as Exhibit 10.1 to the Company's Registration Statement on Form S-1 filed September 17, 1999 (Registration No. 333-87311) and incorporated herein by reference).
10.2	1999 Employee Stock Purchase Plan and form of agreements thereto of the Company (filed as Exhibit 10.2 to the Company's Registration Statement on Form S-1 filed September 17, 1999 (Registration No. 333-87311) and incorporated herein by reference).
10.5.1	Confidentiality and Non-Competition Agreement dated September 1, 1999 between the Company and Gordon S. Black (filed as Exhibit 10.5.1 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).
10.5.2	Confidentiality and Non-Competition Agreement dated September 1, 1999 between the Company and David H. Clemm (filed as Exhibit 10.5.2 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).

<u>Exhibit Number</u>	<u>Exhibit Title</u>
10.5.3	Confidentiality and Non-Competition Agreement dated September 1, 1999 between the Company and Leonard R. Bayer (filed as Exhibit 10.5.3 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).
10.6.1	Leases for 135, 155 & 60 Corporate Woods, Rochester, New York dated April 12, 1991 between Gordon S. Black Corporation and Corporate Woods Associates, together with all amendments thereto (filed as Exhibit 10.6.1 to the Company's Registration Statement on Form S-1 filed September 17, 1999 and incorporated herein by reference); amendments dated February 11, 2000, March 14, 2000 and October 1, 2000 (filed herewith).
10.6.2	Lease for 70 Carlson Road, Rochester, New York dated July 1, 1998 between Gordon S. Black Corporation and Carlson Park Associates, together with all amendments thereto (filed as Exhibit 10.6.2 to the Company's Registration Statement on Form S-1 filed September 17, 1999 (Registration No. 333-87311) and incorporated herein by reference).
10.6.3	Lease for 111 Fifth Avenue, New York, New York dated June 9, 1994 between Louis Harris and Associates, Inc. and B.J.W. Associates (filed as Exhibit 10.7 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).
10.6.4	Sublease for 5th Floor, 500 Fifth Avenue, New York, New York dated March 31, 2000 between the Company and New York Life Insurance Company (filed as Exhibit 10.6.4 to Form 10-K filed September 27, 2000 and incorporated herein by reference).
10.7	Registration Agreement dated July 7, 1998 among the Company, Brinson Venture Capital Fund III, L.P., Brinson MAP Venture Capital Fund III Trust and the Virginia Retirement System (filed as Exhibit 10.8 to the Company's Registration Statement on Form S-1 filed September 17, 1999 (Registration No. 333-87311) and incorporated herein by reference).
10.8	Revolving Credit Facility between Gordon S. Black Corporation and Manufacturers and Traders Trust Company dated August 18, 1999 (filed as Exhibit 10.9 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).
10.9	Investment Agreement between Market Facts, Inc. and the Company dated April, 1999 (filed as Exhibit 10.11 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).
10.10	Amended and Restated Investment Agreement between Riedman Corporation and the Company dated October 15, 1991 (filed as Exhibit 10.12 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).
10.11	Investment Agreement among SEQUEL Limited Partnership II and Sequel Entrepreneur's Fund II, L.P. and the Company dated as of October 15, 1995 (filed as Exhibit 10.13 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).
10.12	Investment Agreement between Young & Rubicam Inc. and the Company dated as of October 15, 1999 (filed as Exhibit 10.14 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).
10.14	Amendment No. 1 to the Registration Agreement between the Company and Brinson Map Venture Capital Fund III, Brinson MAP Venture Capital Fund III Trust, BVCF III, L.P., and Virginia Retirement System dated as of October 15, 1999 (filed as Exhibit 10.16 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).

<u>Exhibit Number</u>	<u>Exhibit Title</u>
10.15	Registration Agreement between the Company and Riedman Corporation dated as of October 15, 1999 (filed as Exhibit 10.17 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).
10.16	Registration Agreement among the Company and Sequel Limited Partnership II and Sequel Entrepreneur's Fund II, L.P. dated as of October 15, 1999 (filed as Exhibit 10.18 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).
10.17	Registration Agreement between the Registrant and Young & Rubicam Inc. dated as of October 15, 1999 (filed as Exhibit 10.19 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).
10.18	Registration Agreement between the Registrant and Excite, Inc. dated as of October 15, 1999 (filed as Exhibit 10.20 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).
10.19	Stockholder's Agreement by and among the Company, Brinson MAP Venture Capital Fund III, BVCF III, L.P., Virginia Retirement System, Gordon S. Black, Leonard R. Bayer, David M. Clemm, Excite, Inc., Young & Rubicam Inc., Riedman Corporation, Sequel Limited Partnership II and Sequel Entrepreneur's Fund II, L.P. dated as of October 15, 1999 (filed as Exhibit 10.21 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).
10.20	Research Agreement between the Company and Young & Rubicam Inc. dated October 22, 1999 (filed as Exhibit 10.22 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).
10.21	Consulting Agreement between the Company and James R. Riedman dated April 25, 2001 (filed herewith).
21.	List of Subsidiaries (filed herewith).
23.1	Consent of Independent Accountants (filed herewith).
23.2	Report of Independent Accountants on Financial Statement Schedule (filed herewith).
24.	Power of Attorney (included on page 36 of this Report).

### SIGNATURES

Pursuant to the requirements of section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized on the 31st day of August, 2001.

HARRIS INTERACTIVE INC.

By: /s/ BRUCE A. NEWMAN

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Bruce A. Newman

Title: Chief Financial Officer,  
Secretary, and Treasurer

### POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints, jointly and severally, Bruce A. Newman and Gordon S. Black, and each of them, as his true and lawful attorneys-in-fact and agents, each with full power of substitution, for him, and in his name, place and stead, in any and all capacities, to sign any amendments to this Report on Form 10-K, and to file the same, with Exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite or necessary to be done as fully to all intents and purposes as he or she might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents, or any of them, or their substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

<u>Name</u>	<u>Capacity</u>	<u>Date</u>
<u>/s/ Gordon S. Black</u> Gordon S. Black	Chairman and Chief Executive Officer (Principal Executive Officer)	August 31, 2001
<u>/s/ Bruce A. Newman</u> Bruce A. Newman	Chief Financial Officer, Secretary, and Treasurer (Principal Financial and Accounting Officer)	August 31, 2001
<u>/s/ David H. Clemm</u> David H. Clemm	President, Chief Operating Officer, and Director	August 31, 2001
<u>/s/ Leonard R. Bayer</u> Leonard R. Bayer	Director	August 31, 2001
<u>/s/ Thomas D. Berman</u> Thomas D. Berman	Director	August 31, 2001
<u>/s/ G. Thomas Clark</u> G. Thomas Clark	Director	August 31, 2001
<u>/s/ James R. Riedman</u> James R. Riedman	Director	August 31, 2001
<u>/s/ Benjamin D. Addoms</u> Benjamin D. Addoms	Director	August 31, 2001

## Report of Independent Accountants

To the Board of Directors and Shareholders  
of Harris Interactive Inc.

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, stockholders' equity and cash flows present fairly, in all material respects, the financial position of Harris Interactive Inc. (the "Company") and its subsidiaries at June 30, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended June 30, 2001 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

/s/ PricewaterhouseCoopers LLP

Rochester, New York  
July 27, 2001

**HARRIS INTERACTIVE INC.**  
**CONSOLIDATED BALANCE SHEETS**  
(In thousands, except share and per share amounts)

	<b>June 30,</b>	
	<b>2001</b>	<b>2000</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents .....	\$ 10,585	\$ 23,932
Marketable securities .....	31,906	48,960
Accounts receivable, less allowances of \$383 and \$74, respectively .....	12,722	10,056
Costs and estimated earnings in excess of billings on uncompleted contracts .....	1,888	3,780
Other current assets .....	1,580	2,072
Total current assets .....	58,681	88,800
Property, plant and equipment, net .....	14,983	13,640
Goodwill and other intangibles, less accumulated amortization of \$786 and \$456, respectively .....	8,971	1,094
Other assets .....	2,586	918
Total assets .....	<b>\$ 85,221</b>	<b>\$104,452</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable .....	\$ 4,805	\$ 4,243
Accrued expenses .....	2,863	2,958
Billings in excess of costs and estimated earnings on uncompleted contracts .....	6,379	2,901
Total current liabilities .....	14,047	10,102
Stockholders' equity:		
Preferred stock, \$.01 par value, 5,000,000 shares authorized, no shares issued and outstanding Common stock, \$.001 par value, 100,000,000 shares authorized; 34,614,503 shares issued at June 30, 2001 and 34,111,434 shares issued at June 30, 2000 .....	34	34
Additional paid-in capital .....	128,793	129,113
Unamortized deferred compensation .....	(436)	(2,075)
Accumulated other comprehensive income (loss) .....	184	(133)
Accumulated deficit .....	(56,609)	(32,589)
Less: Treasury stock at cost, 232,700 shares at June 30, 2001 and 0 shares at June 30, 2000 .....	(792)	
Total stockholders' equity .....	71,174	94,350
Total liabilities and stockholders' equity .....	<b>\$ 85,221</b>	<b>\$104,452</b>

The accompanying notes are an integral part of these consolidated financial statements.

**HARRIS INTERACTIVE INC.**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
**(In thousands, except share and per share amounts)**

	<b>Year ended December 31,</b>		
	<b>2001</b>	<b>2000</b>	<b>1999</b>
Revenues from services .....	\$ 60,061	\$ 51,289	\$ 28,965
Cost of services .....	<u>30,764</u>	<u>28,600</u>	<u>19,086</u>
Gross profit .....	29,297	22,689	9,879
Operating expenses:			
Internet database development expenses .....	7,422	5,647	4,505
Sales and marketing expenses .....	8,475	8,665	1,316
General and administrative expenses .....	<u>41,115</u>	<u>32,209</u>	<u>13,085</u>
Operating loss .....	(27,715)	(23,832)	(9,027)
Interest and other income, net .....	<u>3,695</u>	<u>2,940</u>	<u>180</u>
Loss before income taxes .....	(24,020)	(20,892)	(8,847)
Income tax expense .....	<u>—</u>	<u>50</u>	<u>—</u>
Net loss .....	(24,020)	(20,942)	(8,847)
Accrued dividends on preferred stock .....	<u>—</u>	<u>(738)</u>	<u>(1,176)</u>
Net loss attributable to holders of common stock ..	<u>\$ (24,020)</u>	<u>\$ (21,680)</u>	<u>\$ (10,023)</u>
Basic and diluted net loss per share .....	<u>\$ (.70)</u>	<u>\$ (.93)</u>	<u>\$ (1.01)</u>
Weighted average shares outstanding—basic and diluted .....	<u>34,239,393</u>	<u>23,317,847</u>	<u>9,955,261</u>

The accompanying notes are an integral part of these consolidated financial statements.

**HARRIS INTERACTIVE INC.**  
**CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY**  
**(In thousands)**

	Common Stock Outstanding		Additional Paid-In Capital	Unamortized Deferred Compensation	Accumulated Other Comprehensive Income (Loss)	Retained Earnings (Accumulated Deficit)	Treasury Stock	Total Stockholders' Equity (Deficit)
	Shares	Amount						
Balance At June 30, 1998	12,063	\$121	\$ 492			\$ 334		\$ 947
Purchase and retirement of common stock	(2,382)	(24)	(492)			(2,484)		(3,000)
Issuance costs incurred on preferred stock						(594)		(594)
Issuance of common stock	1,190	12	4,147					4,159
Deferred compensation on stock options issued			666	\$ (666)				16
Amortization of deferred compensation				16				
Accrued dividends on preferred stock						(1,176)		(1,176)
Net loss and comprehensive loss						(8,847)		(8,847)
Balance At June 30, 1999	10,871	109	4,813	(650)		(12,767)		(8,495)
Comprehensive loss:								
Net loss						(20,942)		(20,942)
Unrealized losses on marketable securities					\$(127)			(127)
Foreign currency translation					(6)			(6)
Total comprehensive loss								(21,075)
Exercise of options and warrants	2,010	2	696					698
Issuance of common stock under Employee Stock Purchase Plan	28		118					118
Deferred compensation on stock options issued			2,431	(2,431)				
Amortization of deferred compensation				1,006				1,006
Conversion to \$.001 par value stock		(98)	98					
Issuance costs incurred on preferred stock						(56)		(56)
Issuance of common stock	151		811					811
Accrued dividends on preferred stock						(738)		(738)
Conversion of Class A Preferred Stock	11,790	12	14,688			1,688		16,388
Conversion of Class B Preferred Stock	2,591	2	19,998			226		20,226
Initial public offering, net of costs	6,670	7	85,460					85,467
Balance At June 30, 2000	34,111	34	129,113	(2,075)	(133)	(32,589)		94,350
Comprehensive loss:								
Net loss						(24,020)		(24,020)
Unrealized gains on marketable securities					357			357
Foreign currency translation					(40)			(40)
Total comprehensive loss								(23,703)
Exercise of options and warrants	291		318					318
Issuance of common stock under Employee Stock Purchase Plan	145		385					385
Deferred compensation related to cancelled stock options			(1,218)	1,218				
Amortization of deferred compensation				421				421
Repurchase of common stock							\$(792)	(792)
Issuance of common stock	67		195					195
Balance At June 30, 2001	<u>34,614</u>	<u>\$ 34</u>	<u>\$128,793</u>	<u>\$ (436)</u>	<u>\$ 184</u>	<u>\$(56,609)</u>	<u>\$(792)</u>	<u>\$ 71,174</u>

The accompanying notes are an integral part of these consolidated financial statements.

**HARRIS INTERACTIVE INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(In thousands)**

	For the Years ended June 30,		
	2001	2000	1999
Cash flows from operating activities:			
Net loss .....	\$(24,020)	\$ (20,942)	\$ (8,847)
Adjustments to reconcile net loss to net cash used in operating activities—			
Depreciation and amortization .....	6,441	3,584	1,261
Amortization of deferred compensation .....	421	1,006	16
Amortization of premium and discount on marketable securities .....	(493)	(269)	
Loss on disposal of assets .....	152		
(Increase) decrease in—			
Accounts receivable .....	(2,666)	(4,067)	(2,071)
Costs and estimated earnings in excess of billings on uncompleted contracts .....	1,892	(2,074)	(457)
Other current assets .....	492	(1,918)	727
Other assets .....	(1,668)	(316)	(13)
Increase (decrease) in —			
Accounts payable .....	562	2,400	1,666
Accrued expenses .....	(95)	1,158	(848)
Billings in excess of costs and estimated earnings on uncompleted contracts .....	3,478	(569)	363
Net cash used in operating activities .....	(15,504)	(22,007)	(8,203)
Cash flows from investing activities:			
Purchase of custom research division of Yankelovich Partners, Inc. ....	(8,207)		
Purchase of marketable securities .....	(41,838)	(73,860)	
Proceeds from sales and maturities of marketable securities .....	59,742	25,042	
Repayment of loan to officer .....			42
Capital expenditures .....	(7,606)	(12,092)	(4,372)
Net cash provided by (used in) investing activities .....	2,091	(60,910)	(4,330)
Cash flows from financing activities:			
Principal payments under long-term debt .....			(700)
Decrease in short-term borrowings .....		(291)	(1,927)
Net proceeds from initial public offering of common stock ....		85,467	
Net proceeds from issuance of preferred stock .....		19,944	14,105
Repurchase of common stock .....	(792)		(3,000)
Issuance of common stock and stock options .....	898	1,627	4,159
Net cash provided by financing activities .....	106	106,747	12,637
Effect of exchange rate changes on cash and cash equivalents ....	(40)	(6)	
Net (decrease) increase in cash and cash equivalents .....	(13,347)	23,824	104
Cash and cash equivalents at beginning of year .....	23,932	108	4
Cash and cash equivalents at end of year .....	\$ 10,585	\$ 23,932	\$ 108

The accompanying notes are an integral part of these consolidated financial statements.

## HARRIS INTERACTIVE INC.

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Years Ended June 30, 2001, 2000 and 1999  
(In thousands, except share and per share amounts)

#### 1. Business

Harris Interactive Inc. (the "Company") is a leading global market research, polling and consulting firm, using Internet-based and traditional methodologies to provide clients with information about the views, behaviors and attitudes of people worldwide. Known for the HARRIS POLL™, the Company has over 45 years experience in providing clients with market research and polling services including custom, multi-client and service bureau research, in addition to customer relationship management services.

#### 2. Summary of Significant Accounting Policies

##### *Principles of Consolidation*

The accompanying consolidated financial statements include the assets, liabilities and results of operations of its majority-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated.

##### *Cash and Cash Equivalents*

Cash and cash equivalents include highly liquid marketable securities with original maturities of three months or less.

##### *Marketable Securities*

Harris Interactive Inc. accounts for its investments in accordance with Statement of Financial Accounting Standards ("SFAS") No. 115, "Accounting for Certain Investments in Debt and Equity Securities." All investments have been classified as available-for-sale securities as of June 30, 2001. Available-for-sale securities are stated at fair value, with the unrealized gains and losses reported in other comprehensive income (loss). Realized gains and losses on available-for-sale securities are included in interest and other income. The cost of securities sold is based on the specific identification method. Interest and dividends on securities classified as available-for-sale are included in interest income.

##### *Property, Plant and Equipment*

Plant, property and equipment, including improvements that significantly add to productive capacity or extend useful life, are recorded at cost, while maintenance and repairs are expensed as incurred. Depreciation is calculated on the straight-line or accelerated methods over the estimated useful lives of the assets, which are generally 3 to 7 years. Leasehold improvements are amortized on the straight-line method over the estimated useful life of the assets. In accordance with SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of," the Company assesses all long-lived assets, including property, plant and equipment, for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

##### *Goodwill and Other Intangibles*

Goodwill and other intangibles are amortized on a straight-line basis over 15 years. Amortization expense amounted to \$330 in fiscal 2001 and \$103 in each of the fiscal years ended 2000 and 1999.

In accordance with SFAS No. 121, the Company assesses intangible assets for impairment whenever events or circumstances indicate their carrying amounts may not be recoverable. This is accomplished by comparing the expected undiscounted future cash flows of the assets with the respective carrying amounts as of the date of the assessment. Should aggregate future cash flows be less than the carrying value, a write-down would be required, measured as the difference between the carrying value and the fair value of the asset. Fair value is estimated either through independent valuation or as the present value of expected discounted future cash flows. If the

**HARRIS INTERACTIVE INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)**

**Years Ended June 30, 2001, 2000 and 1999**  
**(In thousands, except share and per share amounts)**

**2. Summary of Significant Accounting Policies—(Continued)**

expected undiscounted future cash flows exceed the respective carrying amount as of the date of assessment, no impairment is recognized. There were no impairment charges related to goodwill or other intangible assets recorded during fiscal 2001, 2000, or 1999.

***Computer Software Developed or Obtained for Internal Use***

During the year ended June 30, 2000, the Company adopted the provisions of Statement of Position 98-1, "Accounting for Costs of Computer Software Developed or Obtained for Internal Use" ("SOP 98-1"). SOP 98-1 provides guidance on accounting for the costs of computer software developed or obtained for internal use and new cost recognition principles and identifies the characteristics of internal use software. The adoption of SOP 98-1 did not have a material impact on the Company's results of operations, financial position or cash flows.

***Revenue Recognition***

The Company recognizes revenue from services principally on the percentage of completion method in the ratio that costs incurred bear to estimated cost at completion. Subscription revenues are recognized upon delivery of the research project. Revenues include amounts billed to customers to cover subcontractor costs and other direct expenses. Provision for estimated contract losses, if any, is made in the period such losses are determined.

***Internet Database Development Expenses***

The Company will continue to develop the database of e-mail addresses and use these addresses to conduct marketing research, polling and surveys on behalf of its customers. The costs to acquire these addresses and other external database development costs approximated \$7,422, \$5,647, and \$4,505 in fiscal 2001, 2000, and 1999, respectively. Such costs have been classified as Internet database development expenses in the consolidated statements of operations and are expensed as incurred.

***Concentration of Credit Risk***

Financial instruments which potentially expose the Company to concentrations of credit risk consist principally of accounts receivable as well as costs and estimated earnings in excess of billings on uncompleted contracts.

Credit losses are provided for in the financial statements and have been within management's expectations.

***Income Taxes***

The Company accounts for income taxes using the asset and liability approach which requires recognition of deferred tax liabilities and assets for the expected future tax consequences of temporary differences between the carrying amounts and the tax basis of such assets and liabilities.

This method utilizes enacted statutory tax rates in effect for the year in which the temporary differences are expected to reverse and gives immediate effect to changes in income tax rates upon enactment. Deferred tax assets are recognized, net of any valuation allowance, for deductible temporary differences and net operating loss and tax credit carryforwards.

HARRIS INTERACTIVE INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Years Ended June 30, 2001, 2000 and 1999  
(In thousands, except share and per share amounts)

2. Summary of Significant Accounting Policies—(Continued)

Recent Accounting Pronouncements

*SAB 101*

In December 1999, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 101 (“SAB 101”), “Revenue Recognition in Financial Statements.” SAB 101 provides guidance for revenue recognition under certain circumstances. SAB 101 became effective for the Company’s fiscal year beginning July 1, 2000. Implementation of SAB 101 did not require the Company to change existing revenue recognition policies and therefore did not have a material effect on the Company’s financial position or results of operations.

*FIN 44*

In March 2000, the Financial Accounting Standards Board issued Interpretation No. 44 (“FIN 44”), “Accounting for Certain Transactions Involving Stock Compensation, an Interpretation of APB Opinion No. 25.” FIN 44 clarifies the application of Opinion No. 25 for (a) the definition of employee for purposes of applying Opinion No. 25, (b) the criteria for determining whether a plan qualifies as a noncompensatory plan, (c) the accounting consequence of various modifications to the terms of a previously fixed stock option or award, and (d) the accounting for an exchange of stock compensation awards in a business combination. FIN 44 became effective July 1, 2000, but certain conclusions cover specific events that occur after either December 15, 1998, or January 12, 2000.

The impact of FIN 44 did not have a material effect on the Company’s financial position or results of operations.

*SFAS 141 and 142*

In July 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standard No. 141 (“SFAS 141”), “Business Combinations” and Statement of Financial Accounting Standard No. 142 (“SFAS 142”), “Goodwill and Other Intangible Assets.” SFAS 141 requires that all business combinations be accounted for under the purchase method only and that certain acquired intangible assets in a business combination be recognized as assets apart from goodwill.

SFAS 142 requires that ratable amortization of goodwill be replaced with periodic tests of the goodwill impairment and that intangible assets other than goodwill and other indefinite lived intangible assets, be amortized over their useful lives. SFAS 141 is effective for all business combinations initiated after June 30, 2001 and for all business combinations accounted for by the purchase method for which the date of acquisition is after June 30, 2001. The provisions of SFAS 142 will be effective for fiscal years beginning after December 15, 2001. The impact of SFAS 141 and SFAS 142 on the Company’s financial statements has not yet been determined.

In addition, the standard includes provisions for the reclassification of certain existing recognized intangibles as goodwill, reassessment of the useful lives of existing recognized intangibles, reclassification of certain intangibles out of previously reported goodwill and the identification of reporting units for purposes of assessing potential future impairments of goodwill. SFAS 142 also requires the Company to complete a transitional goodwill impairment test six months from the date of adoption.

The Company is currently assessing the impact of this new statement on the Company’s combined financial position and results of operations and have not yet determined the impact of adoption.

HARRIS INTERACTIVE INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Years Ended June 30, 2001, 2000 and 1999  
 (In thousands, except share and per share amounts)

2. Summary of Significant Accounting Policies—(Continued)

*Reclassifications*

It is the Company's policy to reclassify amounts in prior years' financial statements to conform with the current year's presentation.

*Use of Estimates*

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

*Fair Value of Financial Instruments*

Cash and accounts receivable are valued at their carrying or redemption amounts, which are reasonable estimates of their fair value. The fair value of all other instruments approximates cost.

3. Acquisition of Yankelovich Custom Research Division

In February 2001, the Company acquired the custom research division of Yankelovich Partners, Inc. ("Yankelovich") headquartered in Norwalk, Connecticut, for approximately \$8,207, including acquisition costs. Yankelovich custom research group offers a full range of research and consulting services including: product forecasting for the pharmaceutical and other industries, public opinion polling, brand equity studies, and corporate reputation measurement. In addition to Norwalk, Yankelovich has offices in Claremont, CA and Washington, DC. which was closed in August 2001. The acquisition was accounted for as a purchase, and accordingly, the operating results of Yankelovich custom research division have been included in the Company's consolidated financial statements from the date of acquisition. Goodwill and other intangibles of approximately \$8,100 are being amortized on a straight-line basis over 15 years.

4. Marketable Securities

At June 30, 2001 and 2000, marketable securities consisted of the following:

Type of issue:	2001		2000	
	Cost	Fair Value	Cost	Fair Value
Available-for-sale securities—				
Certificates of deposit . . . . .	\$ —	\$ —	\$ 1,499	\$ 1,496
Commercial paper . . . . .	5,000	5,000	8,013	7,989
Corporate bonds . . . . .	16,507	16,627	32,727	32,628
Government securities . . . . .	10,169	10,279	4,847	4,847
Market auction . . . . .	—	—	2,000	2,000
Total available-for-sale securities . . . . .	<u>\$31,676</u>	<u>\$31,906</u>	<u>\$49,086</u>	<u>\$48,960</u>

HARRIS INTERACTIVE INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Years Ended June 30, 2001, 2000 and 1999  
 (In thousands, except share and per share amounts)

4. Marketable Securities—(Continued)

Gross unrealized gains and losses on available-for-sale securities at June 30, 2001 were \$232 and \$2, respectively. Gross unrealized gains and losses on available-for-sale securities at June 30, 2000 were \$6 and \$132, respectively. The cost and fair value of available-for-sale securities at June 30, 2001 and 2000, by contractual maturity, are shown below:

	2001		2000	
	Cost	Fair Value	Cost	Fair Value
Maturity date:				
Due in one year or less . . . . .	\$22,676	\$22,768	\$29,100	\$29,028
Due after one year through three years . . . . .	9,000	9,138	19,986	19,932
Total available-for-sale securities	<u>\$31,676</u>	<u>\$31,906</u>	<u>\$49,086</u>	<u>\$48,960</u>

There were no material gains or losses from sales of available-for-sale securities during the years ended June 30, 2001 and 2000.

5. Contracts In Progress

Accumulated costs and estimated earnings and billings on contracts in progress at June 30 was as follows:

	2001	2000
Accumulated costs and estimated earnings . . . . .	\$ 17,399	\$ 14,714
Billings . . . . .	(21,890)	(13,835)
	<u>\$ (4,491)</u>	<u>\$ 879</u>

Contracts in progress are included in the accompanying balance sheets under the following captions:

	2001	2000
Costs and estimated earnings in excess of billings on uncompleted contracts . . . . .	\$ 1,888	\$ 3,780
Billings in excess of costs and estimated earnings on uncompleted contracts . . . . .	(6,379)	(2,901)
	<u>\$ (4,491)</u>	<u>\$ 879</u>

6. Property, Plant and Equipment

Property, plant and equipment consists of the following:

	June 30,	
	2001	2000
Furniture and fixtures . . . . .	\$ 5,178	\$ 4,062
Equipment . . . . .	19,792	14,555
Leasehold improvements . . . . .	3,802	2,869
	28,772	21,486
Accumulated depreciation . . . . .	(13,789)	(7,846)
	<u>\$ 14,983</u>	<u>\$13,640</u>

**HARRIS INTERACTIVE INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)**

**Years Ended June 30, 2001, 2000 and 1999  
 (In thousands, except share and per share amounts)**

**6. Property, Plant and Equipment—(Continued)**

Depreciation expense amounted to \$6,111, \$3,481 and \$1,158 in fiscal years 2001, 2000 and 1999, respectively.

The Company has several noncancelable operating leases for office space and office equipment. Future minimum lease payments under noncancelable operating leases as of June 30, 2001 are as follows:

<u>Years Ending June 30:</u>	
2002.....	\$4,560
2003.....	4,325
2004.....	3,974
2005.....	2,824
2006.....	415
2007 and beyond .....	792

Total rental expense for operating leases in 2001, 2000 and 1999 was \$5,121, \$2,749 and \$1,612, respectively.

**7. Business Segment and Geographical Information**

The Company operates as one business segment, primarily in a single domestic market, engaged principally in marketing research, consulting and polling.

For the year ended June 30, 2001, revenues from the Company's largest customer amounted to 12% of revenues. For the year ended June 30, 2000, revenues from the largest customer comprised 18% of revenues. For the year ended June 30, 1999, revenues from the Company's two largest customers comprised 15% and 14% of revenues.

**8. Accrued Expenses**

Accrued expenses consisted of the following at June 30:

	<u>2001</u>	<u>2000</u>
Payroll and withholding expenses .....	\$ 791	\$ 989
Bonuses .....	373	1,513
Accrued Software .....	709	—
Other .....	990	456
	<u>\$2,863</u>	<u>\$2,958</u>

**9. Line of Credit**

The Company maintains a line of credit with a commercial bank providing borrowings up to \$5,000 in fiscal 2001 and fiscal 2000 at prime. The prime rate in effect at June 30, 2001 was 6.75%. Borrowings under this arrangement are due upon demand. There were no borrowings under this agreement at June 30, 2001 and June 30, 2000. The line of credit is collateralized by the assets of the Company.

HARRIS INTERACTIVE INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Years Ended June 30, 2001, 2000 and 1999  
 (In thousands, except share and per share amounts)

10. Income Taxes

Income tax expense (benefit) consists of:

	<u>Current</u>	<u>Deferred</u>	<u>Total</u>
2001:			
Federal .....	\$ —	\$ —	\$—
State .....	—	—	—
	<u>\$ —</u>	<u>\$ —</u>	<u>\$—</u>
2000:			
Federal .....	\$256	\$(256)	\$—
State .....	50	—	50
	<u>\$306</u>	<u>\$(256)</u>	<u>\$50</u>
1999:			
Federal .....	\$ —	\$ —	\$—
State .....	—	—	—
	<u>\$ —</u>	<u>\$ —</u>	<u>\$—</u>

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The valuation allowance increased by \$9,588 and \$11,488 during 2001 and 2000, respectively, primarily related to federal and state net operating loss carryforwards and Internet database development expenses.

The Company continually reviews the adequacy of the valuation allowance and recognizes these benefits only as reassessment indicates that it is more likely than not that the benefits will be realized. The components of deferred income tax assets at June 30 are presented below:

	<u>2001</u>	<u>2000</u>
Deferred tax assets:		
Net operating loss carryforwards .....	\$ 21,011	\$ 12,050
Internet database development expenses .....	3,227	2,906
Financial statement versus tax depreciation .....	86	87
Tax credit carryforwards .....	107	97
Compensation expense accounted for differently between financial reporting and tax purposes .....	723	555
Book expenses currently not deductible for tax purposes .....	174	45
Gross deferred tax assets .....	<u>25,328</u>	<u>15,740</u>
Valuation allowance .....	<u>(24,592)</u>	<u>(15,004)</u>
Net deferred tax assets .....	<u>\$ 736</u>	<u>\$ 736</u>

The New York State and Federal net operating loss carryforwards (“NOLs”) of approximately \$55,691 and \$53,720, respectively, begin to expire in 2019. A change in ownership could create a limitation on the amount of annual income that can be offset by NOLs and credits.

HARRIS INTERACTIVE INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Years Ended June 30, 2001, 2000 and 1999  
 (In thousands, except share and per share amounts)

10. Income Taxes—(Continued)

The differences between income taxes (benefit) at the U.S. statutory rate and the effective rate are summarized as follows:

	<u>2001</u>	<u>2000</u>	<u>1999</u>
Benefit at Federal statutory rate . . . . .	\$(8,167)	\$ (7,104)	\$(3,008)
State income tax benefit, net of Federal income tax . . . .	(1,162)	(1,388)	(435)
Stock option deductions . . . . .	(211)	(2,832)	
Other . . . . .	(48)	(114)	(73)
Valuation allowance . . . . .	9,588	11,488	3,516
	<u>\$ —</u>	<u>\$ 50</u>	<u>\$ —</u>

11. Stockholders' Equity

*Initial Public Offering*

On December 6, 1999, the Securities and Exchange Commission declared effective the Company's Registration Statement on Form S-1. Pursuant to this Registration Statement, the Company completed an initial public offering of 6,670,000 shares of its common stock (including 870,000 shares sold pursuant to the exercise of the Underwriters' over-allotment option) at an initial public offering price of \$14.00 per share (the "Offering"). The Offering was managed by Lehman Brothers, U.S. Bancorp Piper Jaffray, Volpe Brown Whelan & Company, E\*Offering Corp. and Fidelity Capital Markets. Proceeds to the Company, after deduction of the Underwriters' discount and commission, totaled approximately \$85,467, net of offering costs of approximately \$1,367.

*Preferred Stock*

In July 1998, the Company authorized and issued 147,000 shares of Class A Preferred Stock having a par value of \$.01 per share and received proceeds in the amount of \$14,700. The redemption value of Class A Preferred Stock is equal to \$100 per share plus accrued and unpaid dividends. The costs associated with issuing these securities in the amount of \$594 were charged to accumulated deficit due to the fact that the Class A Preferred Stock is required to be carried at redemption value.

In September 1999, the Company authorized 200,000 shares of Class B Preferred Stock having a par value of \$.01 per share. The Company received proceeds of approximately \$1,000 from the issuance of 10,000 shares of Class B Preferred Stock on September 30, 1999.

In October 1999, the Company received proceeds of approximately \$19,000 from the issuance of 190,000 shares of Class B Preferred Stock.

In December 1999, the Company authorized 5,000,000 shares of preferred stock having a par value of \$.01 per share. No shares were issued or outstanding at June 30, 2001 or 2000.

Upon completion of the initial public offering, the Company's Class A and Class B preferred stock was converted into 14,381,445 shares of common stock, and all outstanding shares of preferred stock were cancelled and retired. Upon conversion of the preferred stock, all rights to accrued and unpaid dividends were terminated.

*Common Stock*

In fiscal 2000, the Company amended the Certificate of Incorporation to increase the number of authorized common stock to 100,000,000 shares. At June 30, 2001 and 2000, the Company had outstanding Warrants to

HARRIS INTERACTIVE INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Years Ended June 30, 2001, 2000 and 1999  
 (In thousands, except share and per share amounts)

11. Stockholders' Equity—(Continued)

purchase 67,659 and 104,916 shares, respectively, of common stock at \$1.50 per share. The Warrants expire in July 2003.

*Stock Split*

On September 7, 1999, the Company declared a 28-for-1 stock split. All references in the consolidated financial statements referring to share prices, conversion rates, per share amounts, stock option plans and common stock issued and outstanding have been adjusted retroactively for the 28-for-1 stock split.

*Employee Stock Purchase Plan*

The Company registered 500,000 shares of common stock in March 2000 for issuance under the 1999 Employee Stock Purchase Plan ("ESPP"). The ESPP provides employees with an opportunity to purchase the Company's common stock through payroll deductions. Under the ESPP, the Company's employees may purchase, subject to certain restrictions, shares of common stock at the lesser of 85 percent of the fair value at either the beginning or the end of each offering period. During fiscal years 2001 and 2000, employees purchased 145,143 and 28,672 shares of common stock, respectively. There were no purchases under this plan in fiscal year 1999.

*Treasury Stock*

In December 2000, the Board of Directors approved a share repurchase program authorizing the Company to purchase up to \$5,000 of its common stock at market prices. The amount and timing of any purchase will depend upon a number of factors, including the price and availability of the Company's shares and general market conditions. The Company's purchases of common stock are recorded as "Treasury Stock" and result in a reduction of "Stockholders' Equity". As of June 30, 2001, the Company repurchased 232,700 shares of common stock, at a cost of \$792 under such program.

12. Net Loss Per Share

Basic and diluted net loss per share are computed based on the weighted average number of common shares outstanding during the period. In arriving at the net loss attributable to holders of common stock, preferred stock dividends of \$738 and \$1,176 were added in fiscal 2000 and 1999. Upon conversion of the preferred stock in conjunction with the initial public offering, all rights to accrued and unpaid dividends were terminated. All potentially dilutive securities (see Notes 11 and 13) were excluded from the calculation of diluted net loss per share, as the effect would be anti-dilutive.

The following table sets forth the computation of basic and diluted net loss per share:

	<u>2001</u>	<u>2000</u>	<u>1999</u>
Numerator:			
Net loss .....	\$ (24,020)	\$ (20,942)	\$ (8,847)
Accrued dividends on preferred stock .....	<u>—</u>	<u>(738)</u>	<u>(1,176)</u>
Net loss attributable to holders of common stock .....	<u>\$ (24,020)</u>	<u>\$ (21,680)</u>	<u>\$ (10,023)</u>
Denominator for basic and diluted loss per share – weighted average shares .....	<u>34,239,393</u>	<u>23,317,847</u>	<u>9,955,261</u>
Basic and diluted net loss per share .....	<u>\$ (.70)</u>	<u>\$ (0.93)</u>	<u>\$ (1.01)</u>

HARRIS INTERACTIVE INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Years Ended June 30, 2001, 2000 and 1999  
 (In thousands, except share and per share amounts)

13. Employee Stock Option Plan

The Company has a nonqualified and incentive stock option plan that enables key employees and directors of the Company to purchase shares of common stock of the Company. The Company grants options to key employees to purchase its common stock, generally at fair value as of the date of grant. Options generally vest over a period up to 4 years and expire after 10 years from the date of grant.

The Company registered 2,750,000 shares of common stock for issuance under the 1999 long-term incentive plan. There were 1,433,250 shares available for future grant at June 30, 2001.

During fiscal 2000 and 1999, 617,000 and 266,000 options, respectively, were granted to employees at an amount which was less than the fair value of the common stock as of the grant date.

Accordingly, the Company recorded \$2,431 and \$666 in unamortized deferred compensation in fiscal 2000 and 1999 for such options which vest over 3 to 4 years. Compensation expense is being amortized over the vesting period and unamortized deferred compensation has been recorded as a reduction in stockholders' equity. No such options were granted in fiscal 2001. During fiscal 2001, 2000 and 1999, compensation expense recognized in the consolidated statements of operations amounted to \$421, \$1,006 and \$16, respectively.

Stock option activity is as follows:

	<u>Number of Shares</u>	<u>Weighted Average Price Per Share</u>
Outstanding at June 30, 1998 .....	3,379,600	\$ .35
Granted .....	560,000	1.26
Canceled .....	65,352	.47
Exercised .....	<u>97,048</u>	.37
Outstanding at June 30, 1999 .....	3,777,200	.48
Granted .....	2,288,600	5.88
Canceled .....	126,200	2.93
Exercised .....	<u>1,880,200</u>	.34
Outstanding at June 30, 2000 .....	4,059,400	3.52
Granted .....	653,250	4.25
Canceled .....	600,130	6.21
Exercised .....	<u>254,036</u>	1.25
Outstanding at June 30, 2001 .....	<u>3,858,484</u>	3.38

Options exercisable as of June 30, 2001, 2000 and 1999 amounted to 2,456,572, 2,173,408 and 2,140,712, respectively.

HARRIS INTERACTIVE INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Years Ended June 30, 2001, 2000 and 1999  
 (In thousands, except share and per share amounts)

13. Employee Stock Option Plan—(Continued)

Under the provisions of SFAS No. 123, "Accounting for Stock-Based Compensation," the Company has elected to continue to account for its stock option plan in accordance with the provisions of APB Opinion No. 25. Had compensation cost for the Company's stock option plan been determined consistent with the provisions of SFAS No. 123, the Company's net loss and net loss per share would have been the pro forma amounts indicated below:

	Net Loss Available to Holders of Common Stock		Basic Net Loss Per Share Available to Holders of Common Stock		Diluted Net Loss Per Share Available to Holders of Common Stock	
	As Reported	Pro Forma	As Reported	Pro Forma	As Reported	Pro Forma
	2001	\$(24,020)	\$(25,282)	\$ (.70)	\$ (.74)	\$ (.70)
2000	(21,680)	(22,224)	(.93)	(.95)	(.93)	(.95)
1999	(10,023)	(10,100)	(1.01)	(1.01)	(1.01)	(1.01)

For purposes of this disclosure, the fair value of each option grant was estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions used for grants outstanding in 2001, 2000 and 1999.

	2001	2000	1999
Risk-free interest rate	4.31%	6.28%	4.70%
Weighted average expected life (years)	3	3	3

For option grants made subsequent to the initial public offering, a volatility factor of 110% was used for fiscal 2001 and a volatility factor of 137% was used for fiscal 2000.

The weighted average grant date fair value of options granted in 2001, 2000 and 1999 is summarized below:

	2001		2000		1999	
	Weighted Average		Weighted Average		Weighted Average	
	Fair Value	Exercise Price	Fair Value	Exercise Price	Fair Value	Exercise Price
Options whose exercise price equaled the grant date fair value	\$3.95	\$5.80	\$3.33	\$6.16	\$ .15	\$1.26
Options whose exercise price was less than the grant date fair value	\$6.57	\$4.92	\$4.36	\$4.65	\$2.63	\$1.26

The following represents additional information about stock options outstanding at June 30, 2001:

Options Outstanding			Options Exercisable		
Range of Exercise Prices Per Share	Number Outstanding	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price (Per Share)	Number Exercisable	Weighted Average Exercisable Price (Per Share)
\$ .18 – \$ .47	1,372,000	6	\$ .45	1,372,000	\$ .45
1.26 – 3.70	1,186,734	8	2.95	690,467	2.69
3.75 – 7.06	847,750	9	4.53	125,771	5.23
11.00 – 14.00	452,000	9	11.22	268,334	11.28

HARRIS INTERACTIVE INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Years Ended June 30, 2001, 2000 and 1999  
 (In thousands, except share and per share amounts)

14. 1997 Stock Program

The 1997 Stock Program replaced a similar program enacted in 1993. Under this Program, the Company purchased outstanding shares of common stock and: 1) granted to certain employees the right to purchase shares; and/or 2) designate that a portion of the compensation payable under the Company's bonus plans be paid in common stock. All purchases and sales were made at fair value and occur within six months following the end of the Company's year end.

Transactions under the 1997 Stock Program are as follows:

	2000		1999	
	Number of Shares	Amount	Number of Shares	Amount
Shares purchased or retired . . . . .	—	—	57,540	\$72
Shares issued . . . . .	75,880	\$281	57,540	72

There were no transactions under the 1997 Stock Program for the year ended June 30, 2001.

15. 401(k) Plan

The Company established a 401(k) Plan (the "Plan") effective January 1, 1995. Eligibility to participate in the Plan, including employer matching contributions, if any, is limited to those employees who are at least 21 years of age and have completed one year of employment with at least 1,000 hours of service. However, employees are eligible to contribute to the Plan upon completion of one quarter of service.

Participants may contribute 1% to 18% of compensation. Employer matching contributions are discretionary, and include matching contributions and profit sharing contributions. Matching contribution expense incurred by the Company during 2001, 2000 and 1999 was \$344, \$137 and \$94, respectively.

16. Supplemental Cash Flow Information

Supplemental Disclosure of Cash Flow Information

Cash paid (received) during the year for:

	2001	2000	1999
Interest . . . . .	\$26	\$160	\$ 35
Taxes . . . . .	\$ —	\$ 50	\$(748)

*Non-Cash Financing Activity*

Upon completion of the initial public offering during fiscal 2000, all outstanding shares of preferred stock were converted into 14,381,445 shares of common stock, and all outstanding shares of preferred stock were cancelled and retired.

17. Subsequent Events

On August 5, 2001, the Company entered into an Agreement and Plan of Merger with Total Research Corporation, located in Princeton, New Jersey. Pursuant to the agreement, Harris Interactive will exchange 1.222 shares of Harris Interactive common stock, par value \$.001 per share, for each outstanding share of Total Research common stock, par value \$.001 per share.

**HARRIS INTERACTIVE INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)**

**Years Ended June 30, 2001, 2000 and 1999**  
**(In thousands, except share and per share amounts)**

**17. Subsequent Events—(Continued)**

The merger is intended to be a tax free exchange. Consummation of the merger is subject to satisfaction or waiver by the parties of certain closing conditions, including the receipt of regulatory approvals, approvals by the stockholders of Harris Interactive and Total Research, respectively, and other customary closing conditions. The transaction is anticipated to close during the fourth quarter of the calendar year 2001.

On August 6, 2001, the Company also entered into an agreement to acquire Market Research Solutions Limited, a privately owned UK company, headquartered in Oxford, England, in consideration of a combination of cash and shares of Harris Interactive common stock.

**Schedule II**  
**Valuation and Qualifying Accounts**  
**(In thousands)**

	<u>Balance at beginning of period</u>	<u>Additions charged to earnings</u>	<u>Deductions amounts written off</u>	<u>Balance at end of period</u>
Year ended June 30, 1999				
Deducted in the consolidated balance sheet:				
Trade accounts receivable, allowance for doubtful accounts .....	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$0</u>	<u>\$ 0</u>
Deferred tax valuation allowance .....	<u>0</u>	<u>3,516</u>	<u>0</u>	<u>3,516</u>
Year ended June 30, 2000				
Deducted in the consolidated balance sheet:				
Trade accounts receivable, allowance for doubtful accounts .....	<u>0</u>	<u>74</u>	<u>0</u>	<u>74</u>
Deferred tax valuation allowance .....	<u>3,516</u>	<u>11,488</u>	<u>0</u>	<u>15,004</u>
Year ended June 30, 2001				
Deducted in the consolidated balance sheet:				
Trade accounts receivable, allowance for doubtful accounts .....	<u>74</u>	<u>309</u>	<u>0</u>	<u>383</u>
Deferred tax valuation allowance .....	<u>15,004</u>	<u>9,588</u>	<u>0</u>	<u>24,592</u>

## EXHIBIT INDEX

<u>Exhibit Number</u>	<u>Exhibit Title</u>	<u>Page</u>
3.1	Amended and Restated Certificate of Incorporation of the Company (filed as Exhibit 3.1 to Form 10-K filed September 27, 2000 and incorporated herein by reference).	
3.2	Bylaws of the Company (filed herewith).	
10.1	1999 Long Term Incentive Plan and form of agreements thereto of the Company (filed as Exhibit 10.1 to the Company's Registration Statement on Form S-1 filed September 17, 1999 (Registration No. 333-87311) and incorporated herein by reference).	
10.2	1999 Employee Stock Purchase Plan and form of agreements thereto of the Company (filed as Exhibit 10.2 to the Company's Registration Statement on Form S-1 filed September 17, 1999 (Registration No. 333-87311) and incorporated herein by reference).	
10.5.1	Confidentiality and Non-Competition Agreement dated September 1, 1999 between the Company and Gordon S. Black (filed as Exhibit 10.5.1 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).	
10.5.2	Confidentiality and Non-Competition Agreement dated September 1, 1999 between the Company and David H. Clemm (filed as Exhibit 10.5.2 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).	
10.5.3	Confidentiality and Non-Competition Agreement dated September 1, 1999 between the Company and Leonard R. Bayer (filed as Exhibit 10.5.3 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).	
10.6.1	Leases for 135, 155 & 60 Corporate Woods, Rochester, New York dated April 12, 1991 between Gordon S. Black Corporation and Corporate Woods Associates, together with all amendments thereto (filed as Exhibit 10.6.1 to the Company's Registration Statement on Form S-1 filed September 17, 1999 and incorporated herein by reference); amendments dated February 11, 2000, March 14, 2000 and October 1, 2000 (filed herewith).	
10.6.2	Lease for 70 Carlson Road, Rochester, New York dated July 1, 1998 between Gordon S. Black Corporation and Carlson Park Associates, together with all amendments thereto (filed as Exhibit 10.6.2 to the Company's Registration Statement on Form S-1 filed September 17, 1999 (Registration No. 333-87311) and incorporated herein by reference).	
10.6.3	Lease for 111 Fifth Avenue, New York, New York dated June 9, 1994 between Louis Harris and Associates, Inc. and B.J.W. Associates (filed as Exhibit 10.7 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).	
10.6.4	Sublease for 5th Floor, 500 Fifth Avenue, New York, New York dated March 31, 2000 between the Company and New York Life Insurance Company (filed as Exhibit 10.6.4 to Form 10-K filed September 27, 2000 and incorporated herein by reference).	

<u>Exhibit Number</u>	<u>Exhibit Title</u>	<u>Page</u>
10.7	Registration Agreement dated July 7, 1998 among the Company, Brinson Venture Capital Fund III, L.P., Brinson MAP Venture Capital Fund III Trust and the Virginia Retirement System (filed as Exhibit 10.8 to the Company's Registration Statement on Form S-1 filed September 17, 1999 (Registration No. 333-87311) and incorporated herein by reference).	
10.8	Revolving Credit Facility between Gordon S. Black Corporation and Manufacturers and Traders Trust Company dated August 18, 1999 (filed as Exhibit 10.9 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).	
10.9	Investment Agreement between Market Facts, Inc. and the Company dated April, 1999 (filed as Exhibit 10.11 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).	
10.10	Amended and Restated Investment Agreement between Riedman Corporation and the Company dated October 15, 1991 (filed as Exhibit 10.12 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).	
10.11	Investment Agreement among SEQUEL Limited Partnership II and Sequel Entrepreneur's Fund II, L.P. and the Company dated as of October 15, 1995 (filed as Exhibit 10.13 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).	
10.12	Investment Agreement between Young & Rubicam Inc. and the Company dated as of October 15, 1999 (filed as Exhibit 10.14 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).	
10.14	Amendment No. 1 to the Registration Agreement between the Company and Brinson Map Venture Capital Fund III, Brinson MAP Venture Capital Fund III Trust, BVCF III, L.P., and Virginia Retirement System dated as of October 15, 1999 (filed as Exhibit 10.16 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).	
10.15	Registration Agreement between the Company and Riedman Corporation dated as of October 15, 1999 (filed as Exhibit 10.17 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).	
10.16	Registration Agreement among the Company and Sequel Limited Partnership II and Sequel Entrepreneur's Fund II, L.P. dated as of October 15, 1999 (filed as Exhibit 10.18 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).	
10.17	Registration Agreement between the Registrant and Young & Rubicam Inc. dated as of October 15, 1999 (filed as Exhibit 10.19 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).	

<u>Exhibit Number</u>	<u>Exhibit Title</u>	<u>Page</u>
10.18	Registration Agreement between the Registrant and Excite, Inc. dated as of October 15, 1999 (filed as Exhibit 10.20 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).	
10.19	Stockholder's Agreement by and among the Company, Brinson MAP Venture Capital Fund III, BVCF III, L.P., Virginia Retirement System, Gordon S. Black, Leonard R. Bayer, David M. Clemm, Excite, Inc., Young & Rubicam Inc., Riedman Corporation, Sequel Limited Partnership II and Sequel Entrepreneur's Fund II, L.P. dated as of October 15, 1999 (filed as Exhibit 10.21 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).	
10.20	Research Agreement between the Company and Young & Rubicam Inc. dated October 22, 1999 (filed as Exhibit 10.22 to the Company's Registration Statement on Form S-1/A filed October 26, 1999 (Registration No. 333-87311) and incorporated herein by reference).	
10.21	Consulting Agreement between the Company and James R. Riedman dated April 25, 2001 (filed herewith)	
21.	List of Subsidiaries (filed herewith).	
23.1	Consent of Independent Accountants (filed herewith).	
23.2	Report of Independent Accountants on Financial Statement Schedule (filed herewith).	
24.	Power of Attorney (included on page 34 of this Report).	