

TRAVELZOO INC
Form S-1/A
October 09, 2003

As Filed with the Securities and Exchange Commission on October 9, 2003

Registration No. 333-107304

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

PRE-EFFECTIVE AMENDMENT NO. 3 ON FORM S-1

TO

FORM S-3

REGISTRATION STATEMENT

Under

THE SECURITIES ACT OF 1933

TRAVELZOO INC.

(Exact name of registrant as specified in its charter)

DELAWARE

(State or other jurisdiction of
incorporation or organization)

7373

(Primary Standard Industrial
Classification Code Number)

590 Madison Avenue, 21st Floor
New York, New York 10022
(212) 521-4200

(Address, including zip code, and telephone number,
including area code, of registrant's principal executive offices)

Ralph Bartel

Chief Executive Officer
Travelzoo Inc.

590 Madison Avenue, 21st Floor
New York, New York 10022
(212) 521-4200

Fax: (212) 521-4230

(Name, address, including zip code, and telephone number, including area code, of agent for service)

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Approximate date of commencement of proposed sale to the public: From time to time after this registration statement becomes effective.

If any of the securities being registered on this form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, check the following box. ☐

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ☐

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ☐

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ☐

If delivery of the prospectus is expected to be made pursuant to Rule 434, check the following box. ☐

The registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the registrant shall file a further amendment which specifically states that this registration statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until the registration statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.

SUBJECT TO COMPLETION, DATED OCTOBER 9, 2003

354,400 Shares

Common Stock

This prospectus relates to resales of up to 354,400 shares of our common stock, par value \$.01 per share, by the selling stockholders listed in this prospectus starting on page 33.

Subject to the terms and conditions of the underwriting agreement described in this prospectus, Wedbush Morgan Securities has agreed as underwriter to purchase from Ralph Bartel, our Chief Executive Officer, 300,000 shares of common stock owned by him. Such shares are being sold pursuant to this prospectus in blocks of not more than 1,000 and not less than 100 shares. In connection with such underwriting arrangements, Mr. Bartel has agreed to issue to Wedbush Morgan Securities a warrant to purchase up to 30,000 additional shares of our common stock at a purchase price equal to 120% of the price to the public hereunder. The shares offered hereby include the shares issuable upon exercise of that warrant. Wedbush Morgan Securities is not purchasing the shares of common stock offered by selling stockholders other than Mr. Bartel. See Plan of Distribution Underwriting beginning on page 37.

The selling stockholders other than Ralph Bartel or their transferees may sell their shares of common stock from time to time in accordance with the plan of distribution described in this prospectus. See Plan of Distribution Selling Stockholders Other than Mr. Bartel beginning on page 37.

Our shares are included in the OTC Bulletin Board under the symbol TVZO. On October 3, 2003, the last reported sale price of our common stock was \$4.95 per share. We have submitted an application for listing on the NASDAQ SmallCap Market under the symbol TZOO. This offering is intended primarily to allow Travelzoo to satisfy the requirement for listing on the NASDAQ SmallCap Market that we have 300 round lot holders of our common stock. A qualifying round lot holder is a stockholder who owns at least 100 shares of Travelzoo stock. There can be no assurance that we will satisfy all of the other requirements for listing on the NASDAQ SmallCap Market or that our shares will be listed on the NASDAQ SmallCap Market upon consummation of this offering or ever. See Risk Factors beginning on page 6.

Investing in these securities involves risks. You should carefully consider the risk factors beginning on page 6 of this prospectus before purchasing the common stock.

	Per Share	Total
Price to the public ⁽¹⁾	\$ _____	\$ _____
Underwriting discount ⁽¹⁾	_____	_____
Proceeds to the selling stockholders ⁽¹⁾⁽²⁾⁽³⁾	_____	_____

- (1) This refers only to the shares covered by the underwriting agreement with Wedbush Morgan Securities which are held by Ralph Bartel. The shares of the other selling stockholders may be sold at varying prices from time to time, as described under Plan of Distribution.
- (2) Ralph Bartel has granted Wedbush Morgan Securities an option for 45 days to purchase up to an additional 45,000 shares of common stock held by Mr. Bartel at the public offering price per share, less the underwriting discount, solely to cover over-allotments. If such option is exercised in full, the total proceeds to the selling stockholders will be \$_____. See Plan of Distribution Underwriting.
- (3) We intend to pay the expenses of the offering, which are estimated to be \$_____.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or passed upon the adequacy or accuracy of this prospectus. Any representation to the contrary is a criminal offense.

The date of this prospectus is October __, 2003.

To facilitate this offering, the Underwriter may engage in transactions that stabilize, maintain or otherwise affect the market price of our common stock, including overallocating shares of our common stock in connection with this offering and bidding for and purchasing shares of our common stock at a level above that which might otherwise prevail in the open market. Such stabilizing, if commenced, may be discontinued at any time. See Plan of Distribution Underwriting.

SUMMARY

This summary highlights selected information contained elsewhere in this prospectus. This summary does not contain all of the information you should consider before making an investment decision. You should read the entire prospectus carefully, including Risk Factors beginning on page 6, before making an investment decision.

TRAVELZOO INC.

Overview

We are an Internet media company that publishes online advertisements of sales and specials for hundreds of travel companies. We provide airlines, hotels, cruise lines, vacation packagers, and other travel companies with a fast, flexible, and cost-effective way to reach millions of potential consumers. While our products provide advertising opportunities for travel companies, they also provide Internet users with a free source of information on current sales and specials from hundreds of travel companies.

Our products include the *Travelzoo* website, the *Travelzoo Top 20* e-mail newsletter, and the *Weekend.com* e-mail newsletter. Our *Travelzoo* website at <http://www.travelzoo.com> lists sales and specials from approximately 200 travel companies and it reaches 5.1 million Internet users per month. Our *Travelzoo Top 20* is a free weekly e-mail newsletter that highlights attractive sales and specials from selected travel companies. As of September 30, 2003, the *Travelzoo Top 20* newsletter had 5,482,000 subscribers. Our *Weekend.com* newsletter is a free weekly e-mail newsletter that features ideas and travel opportunities for weekends. We launched this product in November 2002 and as of September 30, 2003, it had 1,585,000 subscribers.

More than 200 companies purchase our advertising services, including American Airlines, American Express, Alamo Rent-A-Car, Avis Rent-A-Car, British Airways, Carnival Cruise Lines, Liberty Travel, Delta Air Lines, Expedia, Fairmont Hotels & Resorts, Hilton Hotels, JetBlue Airways, Marriott Hotels, Park Place Entertainment, Southwest Airlines, Starwood Hotels & Resorts Worldwide, Royal Caribbean, United Airlines, and US Airways.

Our revenues are generated from advertising sales. Our revenues have grown rapidly since we began operations in 1998, primarily driven by an increasing number of travel companies listing their sales and specials on the *Travelzoo* website and in the *Travelzoo Top 20* newsletter. For the year ended December 31, 2002, revenues were \$9.8 million compared to \$6.1 million in 2001, an increase of 61%. Net income for 2002 was \$853,071 versus \$363,735 in the prior year. For the six months ended June 30, 2003, revenues increased 92% to \$8.0 million compared to \$4.2 million for the same period last year. For the six months ended June 30, 2003, net income increased to \$981,010 from \$281,620 for the same period last year, an increase of 248%. For the year ended December 31, 2002, our two largest clients accounted for 15% and 14% of our revenues. In the six months ended June 30, 2003, we acquired 1,472,000 new subscribers for our *Travelzoo Top 20* newsletter in addition to the 2,385,000 new subscribers we acquired in 2002.

Our Industry

According to the Newspaper Association of America, travel companies spent \$1.4 billion in 2002 on national advertising in newspapers. We believe that newspapers are currently the main medium for travel companies to advertise their sales and specials. However, we believe that travel companies will increase their spending on Internet advertising of sales and specials due to the following factors: first, market research shows that the Internet has become consumers' preferred information source for travel; second, Internet advertising provides travel companies advantages compared to print advertising such as real-time listings, real-time updates, and performance tracking; third, the Internet allows travel companies to advertise their sales and specials in a fast, flexible, and cost-effective manner that has not been possible before. Fourth, we believe that many travel suppliers prefer to sell their travel services directly to consumers, as an alternative to distribution through travel agents.

Competitive Strengths

We have developed our company to be a leader in the field of online advertising for travel companies. We provide travel companies with the following key features:

- *Real-Time Listings of Special Offers.* Our technology allows travel companies to advertise new special offers on a real-time basis.

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- *Real-Time Updates.* Our technology allows travel companies to update their listings on a real-time basis.
- *Real-Time Performance Reports.* We provide travel companies with real-time tracking of the performance of their advertising campaigns. Our solution enables travel companies to optimize their campaigns by removing or updating unsuccessful listings and further promoting successful listings.
- *Access to Millions of Consumers.* We provide travel companies fast access to millions of travel shoppers.
- *National Reach.* We offer travel companies access to Internet users across the U.S.

Furthermore, our products and services provide consumers information on current special offers with the following key features:

- *Aggregation of Offers from Many Companies.* Our *Travelzoo* website and our *Travelzoo Top 20* e-mail newsletter aggregate information on current special offers from approximately 200 travel companies. This saves the consumer time when searching for travel sales and specials.
- *Current Information.* Compared to newspaper ads, we provide consumers with more current information, since our technology enables travel companies to update their listings on a real-time basis.
- *Search Tools.* We provide consumers with the ability to search for specific special offers.

Growth Strategy

Our objective is to become the largest online publisher of sales and specials for travel companies. Key elements of our strategy include:

- *Build Strong Brand Awareness.* We believe that it is essential to establish a strong brand with Internet users and within the travel industry. We currently utilize an online marketing program to promote our brands to Internet users. In addition, we believe that we build brand awareness by product excellence that is promoted by word-of-mouth. We utilize sponsorships at industry conferences and public relations to promote our brands within the travel industry.
- *Increase Reach.* In order to attract more users to our products, we intend to expand our advertising campaigns as our business grows. We believe that we can also attract more users by product excellence that is promoted by word-of-mouth.
- *Maintain Quality User Base.* We believe that, in addition to increasing our reach, we need to maintain the quality of our user base by producing high quality content.
- *Increase Number of Advertising Clients.* We intend to continue to grow our advertising client base by expanding the size of our sales force.
- *Provide Excellent Service.* We believe it is important to provide our advertising clients with excellent service in terms of the development and placement of their advertisements.

Corporate Information

Our principal business office is located at 590 Madison Avenue, 21st Floor, New York, New York 10022 and our telephone number is (212) 521-4200. Our website is <http://www.travelzoo.com>. Additionally, we have offices in Chicago, Miami, and Mountain View (California). Our local presence in these regions allows us to better source and publish information on travel specials which are relevant to each regional market. In addition, these regional offices provide local proximity for our sales force to better service advertisers.

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RECENT DEVELOPMENTS

On October 6, 2003, we announced the results of our operations for the third quarter of 2003. The following information is taken from that announcement:

**Three Months Ended
September 30,**

**Nine Months Ended
September 30,**

Statements of Operations:	2002	2003	2002	2003
	(unaudited)	(unaudited)	(unaudited)	(unaudited)
Revenues	\$2,538,152	\$4,785,427	\$6,715,356	\$12,790,363
Cost of revenues	90,108	93,645	262,108	257,814
Gross profit	2,448,044	4,691,782	6,453,248	12,532,549
Operating expenses:				
Sales and marketing	1,510,266	2,525,638	3,822,582	6,744,080
General and administrative	521,663	1,115,144	1,646,279	3,074,947
Merger expenses			54,538	
Total operating expenses	2,031,929	3,640,782	5,523,399	9,819,027
Income from operations	416,115	1,051,000	929,849	2,713,522
Interest income	540	3,187	2,027	8,324
Income before income taxes	416,655	1,054,187	931,876	2,721,846
Income taxes	171,071	437,581	404,672	1,124,230
Net income	\$ 245,584	\$ 616,606	\$ 527,204	\$ 1,597,616
Basic and diluted net income per share	\$ 0.01	\$ 0.03	\$ 0.03	\$ 0.08

Balance Sheet Data:	As of December 31, 2002	As of September 30, 2003
	(unaudited)	(unaudited)
Working capital	\$1,339,593	\$3,080,018
Total assets	3,239,594	5,850,198
Long-term debt		
Stockholders' equity	\$1,790,954	\$3,388,570

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THE OFFERING

Common stock offered by the selling stockholders	354,400 shares
Common stock outstanding	19,425,147 shares as of September 30, 2003 (1)
Purpose of offering	To meet the NASDAQ SmallCap Market listing requirement of having 300 round lot holders. A qualifying round lot holder is a stockholder who owns at least 100 shares of Travelzoo stock. There can be no assurance that we will satisfy all of the requirements for listing, including, but not limited to the round lot holder requirement, and become listed on the NASDAQ SmallCap Market. See Risk Factors beginning on page 6.
Selling Stockholders	Of the shares offered hereby, 300,000 shares are held by Ralph Bartel, our Chief Executive Officer (such shares are being sold pursuant to this prospectus in blocks of not more than 1,000 and not less than 100 shares), 24,400 shares are held by charitable organizations to which Mr. Bartel donated such shares, and 30,000 shares are issuable on exercise of a warrant to be issued to Wedbush Morgan Securities by Mr. Bartel pursuant to the underwriting agreement relating to this offering.
Use of proceeds	

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We will not receive any proceeds from the sale of shares offered hereby. All such proceeds will be received by the selling stockholders listed in this prospectus under **Principal and Selling Stockholders** beginning on page 33.

Dividend policy

We have not paid, and do not anticipate paying, dividends on our common stock. See **Price Range of Common Stock and Dividend Information** on page 36.

Risk factors

See **Risk Factors** beginning on page 6, for a discussion of factors you should carefully consider before deciding to invest in our common stock.

OTC Bulletin Board symbol

TVZO

Proposed NASDAQ SmallCap Market Symbol

TZOO

(1) Excludes 2,401,938 options, all of which are currently exercisable at a weighted average exercise price of \$1.12 per share.

Common Stock Ownership and Netsurfer Shares

Travelzoo was originally incorporated as Travelzoo.com Corporation (Travelzoo Bahamas) in the Commonwealth of The Bahamas. In a Netsurfer Stockholder offering, Travelzoo Bahamas issued approximately 2.6 million shares of its common stock to approximately 700,000 visitors who registered on the *Travelzoo* website. No cash payments were required or received for any of the stock issued pursuant to the Netsurfer Stockholder offering. The number of shares issued was doubled as a result of a subsequent two-for-one stock split. In a series of transactions completed in 2002, Travelzoo Bahamas was merged into Travelzoo Inc., a Delaware corporation, and each share of Travelzoo Bahamas was converted into the right to receive one share of common stock of Travelzoo Inc. As of September 30, 2003, 129,664 former stockholders of Travelzoo Bahamas have taken the steps necessary to receive their shares in Travelzoo Inc., and 7,157,960 shares of common stock have been issued. If all former stockholders of Travelzoo Bahamas accept their shares in Travelzoo Inc., an additional 4,137,914 shares of common stock will be issued. These shares are reported as outstanding in our financial statements.

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The following table sets forth summary consolidated financial data for the periods indicated. It is important that you read this information together with the section entitled Management's Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and the notes to those financial statements beginning on page F-1. The historical results are not necessarily indicative of results to be expected for future periods.

SUMMARY FINANCIAL DATA

Statements of Operations:	Period from May 21, 1998 (inception) to December 31, 1998	Year Ended December 31,				Six Months Ended June 30,	
		1999	2000	2001	2002	2002	2003
						(unaudited)	
Revenues*	\$ 84,101	\$954,259	\$3,949,517	\$6,147,938	\$9,847,820	\$4,177,204	\$8,004,936
Cost of revenues	25,362	132,803	282,195	304,081	351,169	172,000	164,169
Gross profit	58,739	821,456	3,667,322	5,843,857	9,496,651	4,005,204	7,840,767
Operating expenses:							
Sales and marketing	1,595	350,720	1,484,495	3,274,747	5,726,557	2,312,316	4,218,442
General and administrative	22,046	326,686	1,201,982	1,354,088	2,293,846	1,124,616	1,959,803
Merger expenses			231,303	332,721	54,538	54,538	

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Total operating expenses	23,641	677,406	2,917,780	4,961,556	8,074,941	3,491,470	6,178,245
Income from operations	35,098	144,050	749,542	882,301	1,421,710	513,734	1,662,522
Interest income				2,702	3,971	1,487	5,137
Income before income taxes	35,098	144,050	749,542	885,003	1,425,681	515,221	1,667,659
Income taxes	6,213	38,646	387,856	521,268	572,610	233,601	686,649
Net income	\$ 28,885	\$105,404	\$ 361,686	\$ 363,735	\$ 853,071	\$ 281,620	\$ 981,010
Basic and diluted net income per share		\$ 0.01	\$ 0.02	\$ 0.02	\$ 0.04	\$ 0.01	\$ 0.05
		As of December 31,				As of June 30,	
Balance Sheet Data:	1998	1999	2000	2001	2002	2002	2003
						(unaudited)	
Working capital	\$ 78,172	\$171,282	\$ 185,734	\$ 425,147	\$1,339,593	\$ 696,634	\$2,455,049
Total assets	107,051	404,796	1,555,506	2,130,730	3,239,594	2,199,753	4,686,308
Long-term debt							
Stockholders' equity	\$ 88,885	\$194,289	\$ 574,148	\$ 937,883	\$1,790,954	\$1,219,503	\$2,771,964

* Revenues in 1998, 1999 and 2000 included commissions revenue of \$26,774, \$61,015 and \$97,451, respectively. Commissions revenue in all other periods was not material.

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RISK FACTORS

You should carefully consider the risks described below and all other information contained this prospectus before making an investment decision. If any of the following risks, or other risks and uncertainties that are not yet identified or that we currently think are immaterial, actually occur, our business, financial condition and results of operations could be materially and adversely affected. In that event, the trading price of our shares could decline, and you may lose part or all of your investment.

Risks Related to Our Financial Condition and Business Model

Our limited operating history makes our business difficult to evaluate.

We were incorporated and began generating revenues in May 1998. Accordingly, we have only a limited operating history for you to consider in evaluating our business. As a young company, we face risks and uncertainties relating to our ability to successfully implement our business plan. You must consider the risks, expenses and uncertainties which can materially affect the business of an early stage company like ours. These risks include uncertainty whether we will be able to:

- increase awareness of the Travelzoo brand;
- attract and retain additional travel companies to list their special offers with us;
- attract additional Internet users to the *Travelzoo* website;
- increase the functionality of our products and services;
- maintain our current business relationships and develop new ones;
- respond effectively to competitive pressures; and
- continue to develop and upgrade our technology.

We cannot assure you that we will sustain profitability.

Although we have been profitable in the past, there is no assurance that we will continue to be profitable. We forecast our future expense levels based on our operating plans and our estimates of future revenues. We may find it necessary to accelerate expenditures relating to our

sales and marketing efforts or otherwise increase our financial commitment to creating and maintaining brand awareness among travel companies and Internet users. 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 generate sufficient revenues to sustain profitability. In this case, the value of Travelzoo's shares could be reduced.

Fluctuations in our operating results may negatively impact our stock price.

Our quarterly operating results may fluctuate significantly in the future due to a variety of factors that could affect our revenues or our expenses in any particular quarter. You should not rely on quarter-to-quarter comparisons of our results of operations as an indication of future performance. Factors that may affect our quarterly results include:

- mismatches between resource allocation and client demand due to difficulties in predicting client demand in a new market;
- changes in general economic conditions that could affect marketing efforts generally and online marketing efforts in particular;
- the magnitude and timing of marketing initiatives;
- the maintenance and development of our strategic relationships;
- the introduction, development, timing, competitive pricing and market acceptance of our products and services and those of our competitors;
- our ability to attract and retain key personnel;
- our ability to manage our anticipated growth and expansion;

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- our ability to attract traffic to our website; and
- technical difficulties or system downtime affecting the Internet generally or the operation of our products and services specifically.

In addition, we plan to significantly increase our operating expenses to expand our sales and marketing, and production departments. If revenues fall below our expectations in any quarter and we are unable to quickly reduce our spending in response, our operating results would be lower than expected and our stock price may fall.

In addition, we are required under generally accepted accounting principles to review our intangible assets for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. We may be required to record a significant expense or charge to earnings in our financial statements in the period any impairment of intangible assets is determined.

We depend on two clients for a substantial part of our revenues.

In the six months ended June 30, 2003, two clients accounted for 13% and 10%, respectively, of our revenues. In the fiscal year ended December 31, 2002, two clients accounted for 15% and 14%, respectively, of our revenues. The loss of one client or both clients may result in a significant decrease in our revenues and results of operations, which could have a material adverse effect on our business.

Our business model is unproven and may not be adaptable to a changing market.

Our current revenue model depends on advertising fees from travel companies using our products. If current clients decide not to continue advertising their sales and specials with us and we are unable to replace them with new clients, our business may be adversely affected. To be successful, we must provide online marketing solutions that achieve broad market acceptance by travel companies. In addition, we must attract sufficient Internet users with attractive demographic characteristics to our products. It is possible that we will be required to further adapt our business model in response to changes in the online advertising market or if our current business model is not successful. If we are not able to anticipate changes in the online advertising market or if our business model is not successful, our business could be materially adversely affected, which could reduce the value of your shares.

We may not be able to obtain sufficient funds to grow our business and any additional financing may be on terms adverse to your interests.

We intend to continue to grow our business, and intend to fund our current operations and our anticipated growth from the cash flow generated from our operations and our retained earnings. However, these sources may not be sufficient to meet our needs. We may not be able to obtain additional financing on commercially reasonable terms, or at all.

If additional financing is not available when required or is not available on acceptable terms, we may be unable to fund our expansion, successfully promote our brand name, develop or enhance our products and services, take advantage of business opportunities or respond to competitive pressures, any of which could have a material adverse effect on our business and the value of your shares.

If we choose to raise additional funds through the issuance of equity securities, you may experience significant dilution of your ownership interest, and holders of the additional equity securities may have rights senior to those of the holders of our common stock. If we obtain additional financing by issuing debt securities, the terms of these securities could restrict or prevent us from paying dividends and could limit our flexibility in making business decisions.

Our business may be sensitive to recessions.

The demand for online advertising may be linked to the level of economic activity and employment in the U.S. and abroad. Specifically, our business is dependent on the spending of travel companies. The current recession has decreased consumer travel and caused travel companies to reduce or postpone their marketing spending generally, and their online marketing spending in particular. If the current economic downturn continues or worsens in the U.S. or abroad, our business and financial condition could be materially adversely affected, which could reduce the value of your shares.

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We may face significant costs with respect to the delivery of paper copies of reports to our stockholders.

The Securities Exchange Act of 1934 requires us to provide paper copies of certain reports to our stockholders who do not consent to receiving electronic delivery. If a significant number of our stockholders do not consent to electronic delivery of stockholder communications or revoke such consent, we may face significant costs related to the printing and mailing of such reports. These costs may drain our resources and may have a material adverse effect on our business and the value of our shares.

Risks Related to Our Markets and Strategy

The Internet is not a proven marketing medium.

The future of our business is dependent on the ongoing acceptance by travel companies of the Internet as an effective marketing tool, and on the ongoing acceptance by consumers of the Internet as a source for information on offers from travel companies. The adoption of online marketing by travel companies, particularly among those that have historically relied upon traditional advertising methods, requires the acceptance of a new way of conducting business, marketing and advertising. Many of our potential clients have little or no experience using the Internet as a marketing tool, and not all Internet users have experience using the Internet to look for travel offers. As a result, we cannot be sure that we will be able to effectively compete with traditional advertising methods. If we are unable to compete with traditional advertising methods, our business and results of operations could be materially adversely affected.

We may experience reduced visitor traffic, reduced revenue and harm to our reputation in the event of unexpected network interruptions caused by system failures.

Our servers and software must be able to accommodate a high volume of traffic. Any substantial increase in demands on our servers will require us to expand and adapt our network infrastructure. If we are unable to add additional software and hardware to accommodate increased demand, we could experience unanticipated system disruptions and slower response times. Any catastrophic failure at our co-location facility could prevent us from serving our web traffic for up to several days, and any failure of our Internet service provider may adversely affect our network's performance. Our clients may become dissatisfied by any system failure that interrupts our ability to provide our products and services to them or results in slower response times. We do not maintain business interruption insurance. Any system failure, including network, software or hardware failure, that causes an interruption in the delivery of our products and services or a decrease in responsiveness of our services could result in reduced revenue and could materially adversely affect our reputation and brand.

We may not be able to develop awareness of our brand name.

We believe that continuing to build awareness of the *Travelzoo* and the *Weekend.com* brand names is critical to achieving widespread acceptance of our business. Brand recognition is a key differentiating factor among providers of online advertising opportunities, and we believe it could become more important as competition in our industry increases. In order to maintain and build brand awareness, we must succeed in our marketing efforts, provide high quality service and increase the number of Internet users with favorable demographics using *Travelzoo* and *Weekend.com*. If we fail to successfully promote and maintain our brands, incur significant expenses in promoting our brands and fail to generate a corresponding increase in revenue as a result of our branding efforts, or encounter legal obstacles which prevent our continued use of our brand names, our business and the value of your shares could be materially adversely affected.

The adoption of legislation regarding the use of pop-up or pop-under ads or the adoption of filter software could adversely affect our business.

As part of our strategy, we currently utilize an online marketing program, including the use of pop-up and pop-under advertisements, to promote our brands to Internet users and sign up subscribers for our e-mail newsletters. To date, governmental regulations have not materially restricted the use of such online marketing. However, the legal and regulatory environment that pertains to the Internet is uncertain and may change. In addition, if filter software programs that limit or prevent advertising from being delivered to an Internet user's computer are widely adopted, our online marketing programs, and in turn our business, could be materially adversely affected.

Our business may be sensitive to events affecting the travel industry in general.

Events like the war with Iraq or the terrorist attacks on the United States in 2001 have a negative impact on the travel industry. We are not in a position to evaluate the net effect of these circumstances on our business. In the longer term, our business might be negatively affected by financial pressures on the travel industry. If the events result in a long-term negative impact on the travel industry, such impact could have a material adverse effect on our business and the value of your shares.

We will not be able to attract travel companies or Internet users if we do not continually enhance and develop the content and features of our products and services.

To remain competitive, we must continually improve the responsiveness, functionality and features of our products and services. We may not succeed in developing features, functions, products or services that travel companies and Internet users find attractive. This could reduce the number of travel companies and Internet users using our products and materially adversely affect our business and the value of your shares.

We may lose business if we fail to keep pace with rapidly changing technologies and clients' needs.

Our success is dependent on our ability to develop new and enhanced software, services and related products to meet rapidly evolving technological requirements for online advertising. Our current technology may not meet the future technical requirements of travel companies. Trends that could have a critical impact on our success include:

- rapidly changing technology in online advertising;
- evolving industry standards, including both formal and de facto standards relating to online advertising;
- developments and changes relating to the Internet;
- competing products and services that offer increased functionality; and
- changes in travel company and Internet user requirements.

If we are unable to timely and successfully develop and introduce new products and enhancements to existing products in response to our industry's changing technological requirements, our business and the value of your shares could be materially adversely affected.

Our business and growth will suffer if we are unable to hire and retain highly skilled personnel.

Our future success depends on our ability to attract, train, motivate and retain highly skilled employees. We may be unable to retain our skilled employees or attract, assimilate and retain other highly skilled employees in the future. We have from time to time in the past experienced, and we expect to continue to experience in the future, difficulty in hiring and retaining highly skilled employees with appropriate qualifications. If we are unable to hire and retain skilled personnel, our growth may be restricted, which could adversely affect our future success and the value of your shares.

We may not be able to effectively manage our expanding operations.

We have recently experienced a period of rapid growth. In order to execute our business plan, we must continue to grow significantly. As of September 30, 2003, we had 37 employees. We expect that the number of our employees will continue to increase for the foreseeable future. This growth has placed, and our anticipated future growth combined with the requirements we face as a public company will continue to place, a significant strain on our management, systems and resources. We expect that we will need to continue to improve our financial and managerial controls and reporting systems and procedures. We will also need to continue to expand and maintain close coordination among our technical, accounting, finance and sales and marketing departments. We may not succeed in these efforts. Our inability to expand our operations in an efficient manner could cause our expenses to grow disproportionately to revenues, our revenues to decline or grow more slowly than expected and otherwise have a material adverse effect on our business and the value of your shares.

Intense competition may adversely affect our ability to achieve or maintain market share and operate profitably.

We compete with large Internet portal sites, such as About.com, America Online, Lycos, MSN and Yahoo!, that offer listings or other advertising opportunities for travel companies. These companies have significantly greater financial, technical, marketing and other resources and larger client bases than we do. In addition, we compete with newspapers, magazines and other traditional media companies that provide online advertising opportunities. We expect to face additional competition as other established and emerging companies, including print media companies, enter the online advertising market.

We believe that there will be rapid business consolidation in the online advertising industry. Accordingly, new competitors may emerge and rapidly acquire significant market share. The development of competing technologies by market participants or the emergence of new industry standards may also adversely affect our competitive position. Competition could result in reduced margins on our services, loss of market share or less use of Travelzoo by travel companies and consumers. If we are not able to compete effectively with current or future competitors as a result of these and other factors, our business could be materially adversely affected.

Loss of any of our key management personnel could negatively impact our business.

Our future success depends to a significant extent on the continued service and coordination of our management team, particularly Ralph Bartel, our Chairman, President, Chief Executive Officer, Chief Financial Officer and Secretary. The loss or departure of any of our officers or key employees could materially adversely affect our ability to implement our business plan. We do not maintain key person life insurance for any member of our management team. In addition, we expect new members to join our management team in the future. These individuals will not previously have worked together and will be required to become integrated into our management team. If our key management personnel are not able to work together effectively or successfully, our business could be materially adversely affected.

We may not be able to access third-party technology upon which we depend.

We use technology and software products from third parties including Microsoft. Technology from our current or other vendors may not continue to be available to us on commercially reasonable terms, or at all. Our business will suffer if we are unable to access this technology, to gain access to additional products or to integrate new technology with our existing systems. This could cause delays in our development and introduction of new services and related products or enhancements of existing products until equivalent or replacement technology can be accessed, if available, or developed internally, if feasible. If we experience these delays, our business and the value of your shares could be materially adversely affected.

Risks Related to the Market for our Shares

We cannot be sure that an active market for our shares will develop or be maintained in the future.

On August 28, 2002, our shares commenced trading on the OTC Bulletin Board. However, there has been only limited trading in the shares since that time, at widely varying prices, and the trading to date has not resulted in an active market for our shares. We cannot assure you that an active market for our shares will be established or maintained in the future. If such market is not established or maintained, stockholders will not be able to readily sell their shares.

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We cannot be sure that our application for listing on the NASDAQ SmallCap Market will be approved.

We have submitted an application for listing on the NASDAQ SmallCap Market under the symbol TZOO. Even if we meet the requirement for 300 round lot holders of our common stock upon consummation of this offering, we would still need to meet the remaining NASDAQ SmallCap Market listing requirements, including our common stock having a minimum bid price of \$4.00 per share. There can be no assurance that our shares will be listed on the NASDAQ SmallCap Market upon consummation of this offering or ever. In the event our shares are not listed on the NASDAQ SmallCap Market, our shares will continue to trade on the OTC Bulletin Board.

We are controlled by a principal stockholder.

Ralph Bartel, who founded Travelzoo and who is our Chairman of the Board, President, Chief Executive Officer, Chief Financial Officer and Secretary, is our largest stockholder, holding approximately 72% of our outstanding shares with options to increase his percentage ownership to 74% on a fully-diluted basis, assuming all former stockholders of Travelzoo Bahamas receive shares of Travelzoo Inc. Based on the number of shares issued as of September 30, 2003 in the merger with Travelzoo Bahamas, Mr. Bartel's shares represent 92% of the outstanding shares. Assuming Mr. Bartel sells all of the shares offered by him hereunder, Mr. Bartel will hold approximately 70% of our outstanding shares, with options to increase his percentage ownership to 73% on a fully-diluted basis. Through his share ownership, he is in a position to control Travelzoo and to elect our entire board of directors.

Investors may face significant restrictions on the resale of our stock due to federal penny stock regulations.

If our shares trade at less than five dollars per share, since the shares are not listed on a recognized national exchange or on NASDAQ, our common stock may be deemed to be a penny stock under Rule 3a51-1 under the Securities Exchange Act of 1934. Compliance with the requirements governing penny stocks may make it more difficult for investors in our common stock to resell their shares to third parties or to otherwise dispose of them.

Section 15(g) of the Exchange Act and Rule 15g-2 under the Exchange Act require broker-dealers dealing in penny stocks to provide potential investors with a document disclosing the risks of penny stocks and to obtain a manually signed and dated written receipt of the document before effecting any transaction in a penny stock for the investor's account. Moreover, Rule 15g-9 promulgated under the Securities Exchange Act of 1934 requires broker-dealers in penny stocks to approve the account of any investor for transactions in such stocks before selling any penny stock to that investor. These requirements significantly increase the time necessary for a broker-dealer to sell a stock and limit the available purchasers for a stock.

Risks Related to Legal Uncertainty

We may become subject to burdensome government regulations and legal uncertainties affecting the Internet which could adversely affect our business.

To date, governmental regulations have not materially restricted use of the Internet in our markets. However, the legal and regulatory environment that pertains to the Internet is uncertain and may change. Uncertainty and new regulations could increase our costs of doing business, prevent us from delivering our products and services over the Internet or slow the growth of the Internet. In addition to new laws and regulations being adopted, existing laws may be applied to the Internet. New and existing laws may cover issues which include:

- user privacy;
- consumer protection;
- copyright, trademark and patent infringement;

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- pricing controls;
- characteristics and quality of products and services;
- sales and other taxes; and
- other claims based on the nature and content of Internet materials.

We may be unable to protect our registered trademark or other proprietary intellectual property rights.

Our success depends to a significant degree upon the protection of the *Travelzoo* brand name. We rely upon a combination of copyright, trade secret and trademark laws and non-disclosure and other contractual arrangements to protect our intellectual property rights. The steps we have taken to protect our proprietary rights, however, may not be adequate to deter misappropriation of proprietary information.

The U.S. Patent and Trademark Office registered the trademark for *Travelzoo* on January 23, 2001. If we are unable to protect our rights in the mark, a key element of our strategy of promoting *Travelzoo* as a brand could be disrupted and our business could be adversely affected. We may not be able to detect unauthorized use of our proprietary information or take appropriate steps to enforce our intellectual property rights. In addition, the validity, enforceability and scope of protection of intellectual property in Internet-related industries is uncertain and still evolving. The laws of other countries in which we may market our services in the future are uncertain and may afford little or no effective protection of our intellectual property. The unauthorized reproduction or other misappropriation of our proprietary technology could enable third parties to benefit from our technology and brand name without paying us for them. If this were to occur, our business could be materially adversely affected.

We may face liability from intellectual property litigation that could be costly to prosecute or defend and distract management's attention with no assurance of success.

We cannot be certain that our products, content and brand names do not or will not infringe valid patents, copyrights or other intellectual property rights held by third parties. While we have a trademark for *Travelzoo*, many companies in the industry have similar names including the word *travel*. We expect that infringement claims in our markets will increase in number as more participants enter the markets. We may be subject to legal proceedings and claims from time to time relating to the intellectual property of others in the ordinary course of our business. We may incur substantial expenses in defending against these third party infringement claims, regardless of their merit, and such claims could result in a significant diversion of the efforts of our management personnel. Successful infringement claims against us may result in monetary liability

or a material disruption in the conduct of our business.

We may be liable as a result of information retrieved from or transmitted over the Internet.

We may be sued for defamation, negligence, copyright or trademark infringement or other legal claims relating to information that is published or made available in our products. These types of claims have been brought, sometimes successfully, against online services in the past. The fact that we distribute information via e-mail may subject us to potential risks, such as liabilities or claims resulting from unsolicited e-mail or spamming, lost or misdirected messages, security breaches, illegal or fraudulent use of e-mail or interruptions or delays in e-mail service. In addition, we could incur significant costs in investigating and defending such claims, even if we ultimately are not liable. If any of these events occur, our business and the value of your shares could be materially adversely affected.

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CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION

The information in this prospectus contains 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. Such statements are based upon current expectations, assumptions, estimates and projections about us and our industry. These forward-looking statements are subject to the many risks and uncertainties that exist in our operations and business environment that may cause our actual results, performance or achievements to be different from those expected or anticipated in the forward-looking statements. Any statements contained herein that are not statements of historical fact may be deemed to be forward-looking statements. For example, words such as may, will, should, estimates, predicts, pot continue, strategy, believes, anticipates, plans, expects, intends, and similar expressions are intended to identify forward-looking state actual results and the timing of certain events could differ significantly from those anticipated in such forward-looking statements. Factors that might cause or contribute to such a discrepancy include, but are not limited to, those discussed elsewhere in this prospectus in the section entitled Risk Factors and the risks discussed in our other Securities and Exchange Commission (SEC) filings. The forward-looking statements included in this prospectus reflect the beliefs of our management on the date of this report. We undertake no obligation to update publicly any forward-looking statements for any reason, even if new information becomes available or other events or circumstances occur in the future.

USE OF PROCEEDS

We will not receive any proceeds from the sale of shares sold by the selling stockholders listed in this prospectus under Principal and Selling Stockholders beginning on page 33.

CAPITALIZATION

The following table sets forth our capitalization as of June 30, 2003:

	As of June 30, 2003*
	(unaudited)
Cash and cash equivalents	\$ 2,343,037
Long-term debt, less current portion	
Stockholders' equity	
Common stock, \$.01 par value, authorized 40,000,000 shares; issued and outstanding 19,425,147 shares	194,251
Additional paid-in capital	(116,078)
Retained earnings	2,693,791
Total stockholders' equity	2,771,964

**As of
June 30, 2003***

Total capitalization

\$ 2,771,964

* Our capitalization will not change as a result of the sale of our stock by the selling stockholders, except for the effect of costs of the offering paid by us, which will reduce our total stockholders' equity.

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SELECTED FINANCIAL DATA

You should read the following selected financial data along with Management's Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and the notes to those financial statements beginning on page F-1. We derived the selected financial data as of and for each of the four years ended December 31, 2002 and the period ended December 31, 1998 from our audited financial statements. We derived the selected financial data as of and for each of the six month periods ended June 30, 2003 and June 30, 2002 from our unaudited financial statements. In our opinion, the unaudited financial information includes all adjustments, consisting only of normal recurring adjustments, considered necessary for a fair presentation of that information. Our results of operations for the six month period ended June 30, 2003 are not necessarily indicative of the results that we may achieve for the full year.

Statements of Operations:	Period from May 21, 1998 (inception) to December 31, 1998	Year Ended December 31,				Six Months Ended June 30,	
		1999	2000	2001	2002	2002	2003
						(unaudited)	
Revenues*	\$84,101	\$954,259	\$3,949,517	\$6,147,938	\$9,847,820	\$4,177,204	\$8,004,936
Cost of revenues	25,362	132,803	282,195	304,081	351,169	172,000	164,169
Gross profit	58,739	821,456	3,667,322	5,843,857	9,496,651	4,005,204	7,840,767
Operating expenses:							
Sales and marketing	1,595	350,720	1,484,495	3,274,747	5,726,557	2,312,316	4,218,442
General and administrative	22,046	326,686	1,201,982	1,354,088	2,293,846	1,124,616	1,959,803
Merger expenses			231,303	332,721	54,538	54,538	
Total operating expenses	23,641	677,406	2,917,780	4,961,556	8,074,941	3,491,470	6,178,245
Income from operations	35,098	144,050	749,542	882,301	1,421,710	513,734	1,662,522
Interest income				2,702	3,971	1,487	5,137
Income before income taxes	35,098	144,050	749,542	885,003	1,425,681	515,221	1,667,659
Income taxes	6,213	38,646	387,856	521,268	572,610	233,601	686,649
Net income	\$ 28,885	\$105,404	\$ 361,686	\$ 363,735	\$ 853,071	\$ 281,620	\$ 981,010
Basic and diluted net income per share		\$ 0.01	\$ 0.02	\$ 0.02	\$ 0.04	\$ 0.01	\$ 0.05
Shares used in computing basic net income per share	9,431,741	19,323,064	19,372,791	19,425,147	19,425,147	19,425,147	19,425,147

Shares used in
computing diluted
net income per share

9,431,741	19,355,147	19,466,810	19,425,147	19,896,353	19,425,147	20,501,602
As of December 31,				As of June 30,		

Balance Sheet Data:

	1998	1999	2000	2001	2002	2002	2003
						(unaudited)	
Working capital	\$ 78,172	\$171,282	\$ 185,734	\$ 425,147	\$1,339,593	\$ 696,634	\$2,455,049
Total assets	107,051	404,796	1,555,506	2,130,730	3,239,594	2,199,753	4,686,308
Long-term debt							
Stockholders' equity	\$ 88,885	\$194,289	\$ 574,148	\$ 937,883	\$1,790,954	\$1,219,503	\$2,771,964

* Revenues in 1998, 1999 and 2000 included commissions revenue of \$26,774, \$61,015 and \$97,451, respectively. Commissions revenue in all other periods was not material.

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

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with, and is qualified in its entirety by reference to, the consolidated financial statements and the notes to those statements beginning on page F-1.

Overview

Travelzoo Inc. is an Internet media company that publishes online advertisements of sales and specials for hundreds of travel companies. As the Internet is becoming consumers' preferred medium to search for travel offers, we provide airlines, hotels, cruise lines, vacation packagers, and other travel companies with a fast, flexible, and cost-effective way to reach millions of potential consumers. Our products include the *Travelzoo* website, the *Travelzoo Top 20* newsletter, and the *Weekend.com* newsletter.

Our revenues are primarily derived from the sale of advertising on our *Travelzoo* website and in our *Travelzoo Top 20* e-mail newsletter.

Critical Accounting Policies

We believe that there are a number of accounting policies that are critical to understanding our historical and future performance, as these policies affect the reported amounts of revenue and the more significant areas involving management's judgments and estimates. These significant accounting policies relate to revenue recognition and the provision for doubtful accounts. These policies, and our procedures related to these policies, are described in detail below.

Revenue Recognition

Substantially all of our revenues are advertising revenues, consisting of fees paid by travel companies to advertise their special offers on the *Travelzoo* website, the *Travelzoo Top 20* e-mail newsletter, and the *Weekend.com* e-mail newsletter. Listing fees are based on placement, number of listings, number of impressions, or number of clickthroughs. Banner advertising rates are based on CPM rates (cost per thousand impressions). Smaller advertising agreements typically \$2,000 or less per month typically renew automatically each month if they are not terminated by the client. Larger agreements are typically related to advertising campaigns and are not automatically renewed.

We recognize advertising revenues in the period in which the advertisement is displayed, provided that evidence of an arrangement exists, the fees are fixed and determinable, no significant obligations remain at the end of the period, and collection of the resulting receivable is deemed probable. If fixed-fee advertising is displayed over a term greater than one month, revenues are recognized ratably over the period. To the extent that any minimum guaranteed impressions are not met during the contract period, we defer recognition of the corresponding revenues until the guaranteed impressions are achieved. Fees for banner advertising and other variable-fee advertising arrangements are recognized based on the number of impressions displayed or clicks delivered during the period.

Under these policies, no revenue is recognized unless persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable, and collection is deemed probable. We evaluate each of these criteria as follows:

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- *Evidence of an arrangement.* We consider a non-cancelable insertion order signed by the client to be evidence of an arrangement.
- *Delivery.* Delivery is considered to occur when the advertising has been displayed and, if applicable, the clickthroughs have been delivered.

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- *Fixed or determinable fee.* We consider the fee to be fixed or determinable if the fee is not subject to refund or adjustment.
- *Collection is deemed probable.* We conduct a credit review for all significant transactions at the time of the arrangement to determine the credit-worthiness of the client. Collection is deemed probable if we expect that the client will be able to pay amounts under the arrangement as payments become due. If we determine that collection is not probable, then we recognize the revenue upon cash collection, provided that the other criteria for revenue recognition have been met.

Provision for Doubtful Accounts

We initially record a provision for doubtful accounts based on our historical experience of write-offs and then adjust this provision at the end of each reporting period based on a detailed assessment of our accounts receivable and allowance for doubtful accounts. In estimating the provision for doubtful accounts, management considers the age of the accounts receivable, our historical write-offs, the credit-worthiness of the client, the economic conditions of the client's industry, and general economic conditions, among other factors. Should any of these factors change, the estimates made by management will also change, which could impact the level of our future provision for doubtful accounts. Specifically, if the financial condition of our clients were to deteriorate, affecting their ability to make payments, additional provision for doubtful accounts may be required.

Results of Operations

The following table sets forth, as a percentage of total revenues, the results of our operations for the years ended December 31, 2002, 2001 and 2000 and the six-month periods ended June 30, 2003 and 2002.

	Year Ended December 31,			Six Months Ended June 30,	
	2000	2001	2002	2002	2003
Revenues:	100%	100%	100%	100%	100%
Cost of revenues	7	5	4	4	2
Gross profit	93	95	96	96	98
Operating expenses:					
Sales and marketing	38	53	58	55	53
General and administrative	30	22	23	27	24
Merger expenses	6	6	1	1	
Total operating expenses	74	81	82	83	77
Income from operations	19	14	14	13	21
Interest income					
Income before income taxes	19	14	14	13	21
Income taxes	10	8	5	6	9
Net income	9%	6%	9%	7%	12%

Six Months Ended June 30, 2003 and June 30, 2002

Acquisition of Subscribers

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In the six months ended June 30, 2003, we acquired 1,472,000 new subscribers for our *Travelzoo Top 20* product through advertising campaigns for the *Travelzoo* brand. Subscription to the *Travelzoo Top 20* e-mail newsletter is free. However, we believe that these additional subscribers add significant value to our company because the additional subscribers may allow us to increase our advertising rates in the future.

The cost related to the acquisition of the new subscribers is included in our advertising expenses. Advertising expenses are included in sales and marketing expenses. For the six months ended June 30, 2003, our advertising expenses were \$2.9 million.

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Revenues

Our total revenues increased to \$4.3 million for the three months ended June 30, 2003, from \$2.2 million for the three months ended June 30, 2002. Our total revenues increased to \$8.0 million for the six months ended June 30, 2003, from \$4.2 million for the six months ended June 30, 2002. The increase in our total revenues was due to signing on new clients and increased spending from existing clients. During the three months ended June 30, 2003, we recognized revenue of \$95,000 related to advertising delivered in the first quarter of 2003 for which collectibility was not probable and therefore recognized on a cash-received basis. During the three months ended June 30, 2003, we did not recognize revenue related to \$35,000 of advertising delivered in the quarter that will be recognized on a cash-received basis since collectibility is not probable.

Cost of Revenues

Cost of revenues consists of network expenses, including fees we pay for co-location services, depreciation of network equipment and salary expenses associated with network operations staff. Our cost of revenues decreased to \$81,000 for the three months ended June 30, 2003, from \$86,000 for the three months ended June 30, 2002. Our cost of revenues decreased to \$164,000 for the six months ended June 30, 2003, from \$172,000 for the six months ended June 30, 2002. As a percentage of revenue, cost of revenues decreased to 2% for the six months ended June 30, 2003 from 4% for the six months ended June 30, 2002. The decrease resulted primarily from an increase in revenues that was not offset by an increase in our network operations costs.

Operating Expenses

- **Sales and Marketing.** Sales and marketing expenses consist primarily of advertising and promotional expenses, public relations expenses, conference expenses, commission expenses, and salary expenses associated with sales and marketing staff. Sales and marketing expenses increased to \$2.3 million for the three months ended June 30, 2003 from \$1.3 million for the three months ended June 30, 2002. Sales and marketing expenses increased to \$4.2 million for the six months ended June 30, 2003 from \$2.3 million for the six months ended June 30, 2002. The increase in sales and marketing expenses was primarily due to the increase in sales and marketing personnel and an increase of our advertising of the *Travelzoo* brand. In the six months ended June 30, 2003 and 2002, advertising expenses accounted for 69% and 67%, respectively, of sales and marketing expenses. Advertising activities during the two periods were of the same type (i.e., online advertising). During the six months ended June 30, 2003 and 2002, \$236,000 and \$226,000, respectively, of advertising services were purchased from our clients under non-barter arrangements.
- **General and Administrative.** General and administrative expenses consist primarily of compensation for administrative and executive staff, fees for professional services, rent, bad debt expense, amortization of intangible assets and general office expense. General and administrative expenses increased to \$903,000 for the three months ended June 30, 2003 from \$562,000 for the three months ended June 30, 2002. General and administrative expenses increased to \$2.0 million for the six months ended June 30, 2003 from \$1.1 million for the six months ended June 30, 2002. General and administrative expenses increased primarily due to an increase in expenses for office space and an increase in expenses for professional services.
- **Merger Expenses.** Merger expenses consist of expenses relating to the registration statement and proxy statement filed with the SEC relating to the merger of Travelzoo.com Corporation into Travelzoo Inc. Merger expenses were \$-0- for both the three months ended June 30, 2003 and June 30, 2002. There were no merger expenses for the six months ended June 30, 2003 compared to \$55,000 for the six months ended June 30, 2002 as the merger was completed in 2002. The expenses consisted mostly of fees for professional legal and accounting services.

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Income Taxes

For the three months ended June 30, 2003, we recorded an income tax provision of \$419,000. For the three months ended June 30, 2002, we recorded an income tax provision of \$101,000. For the six months ended June 30, 2003, we recorded an income tax provision of \$687,000. For

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the six months ended June 30, 2002, we recorded an income tax provision of \$234,000. Our income is generally taxed in the U.S. and our income tax provision reflects federal and state statutory rates applicable to our levels of income and the effect of non-deductible merger expenses in 2002.

Fiscal Years Ended December 31, 2002, 2001 and 2000

Acquisition of Subscribers

In 2002, we acquired 2,385,000 new subscribers for our *Travelzoo Top 20* product through advertising campaigns for the *Travelzoo* brand. Subscription to the *Travelzoo Top 20* e-mail newsletter is free. However, we believe that these additional subscribers add significant value to our company because the additional subscribers allow us to increase our advertising rates.

The cost related to the acquisition of the new subscribers is included in our expenses for advertising campaigns for the *Travelzoo* brand. For the year 2002, our total advertising expenses were \$3.9 million.

Revenues

Our total revenues increased to \$9.8 million for the year ended December 31, 2002 from \$6.1 million for the year ended December 31, 2001 and \$3.9 million for the year ended December 31, 2000. The increase in our total revenues was due to an increase in advertising revenues. Advertising revenue increased to \$9.8 million for the year ended December 31, 2002 from \$6.1 million for the year ended December 31, 2001 and \$3.9 million for the year ended December 31, 2000. The increases resulted primarily from an increase in the number of travel companies advertising on the *Travelzoo* website and in the *Travelzoo Top 20* newsletter.

Cost of Revenues

Cost of revenues consists of network expenses, including fees we pay for co-location services, depreciation of network equipment and salary expenses associated with network operations staff. Our cost of revenues increased to \$351,000 for the year ended December 31, 2002 from \$304,000 for the year ended December 31, 2001 and \$282,000 for the year ended December 31, 2000. As a percentage of revenue, cost of revenues decreased to 4% for the year ended December 31, 2002 from 5% for the year ended December 31, 2001 and 7% for the year ended December 31, 2000. The decreases resulted primarily from an increase in revenues that was not offset by an increase in our network operations costs.

Operating Expenses

- *Sales and Marketing.* Sales and marketing expenses consist primarily of advertising and promotional expenses, public relations expenses, conference expenses, and salary expenses associated with sales and marketing staff. Sales and marketing expenses increased to \$5.7 million for the year ended December 31, 2002 from \$3.3 million for the year ended December 31, 2001 and \$1.5 million for the year ended December 31, 2000. The increases in sales and marketing expenses was due to the decision by our management to hire more experienced sales personnel and increases of our advertising of the *Travelzoo* brand. For the years ended December 31, 2002 and 2001, advertising expenses accounted for 69% and 69%, respectively, of sales and marketing expenses. Advertising activities during the two periods were of the same type (i.e., online advertising).
- *General and Administrative.* General and administrative expenses consist primarily of compensation for administrative and executive staff, fees for professional services, rent, bad debt expense, amortization of intangible assets and general office expense. General and administrative expenses increased to \$2.3 million for the year ended December 31, 2002 from \$1.4 million for the year ended December 31, 2001 and \$1.2 million for the year ended December 31, 2000. General and administrative expenses increased primarily due to increases in expenses for office space. General and administrative expenses for the year ended December 31, 2001 include a credit of \$128,000 for a reduction to the bad debt reserve principally due to the collection of a doubtful account.

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- *Merger Expenses.* Merger expenses consist of expenses relating to the registration statement and proxy statement filed with the SEC relating to the merger of Travelzoo.com Corporation into Travelzoo Inc. Merger expenses decreased to \$55,000 for the year ended December 31, 2002 from \$333,000 for the year ended December 31, 2001 and \$231,000 for the year ended December 31, 2000. The expenses consisted mostly of fees for professional services, primarily legal and accounting.

Intangible Assets

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As of December 31, 2002, our long-lived assets included intangible assets of \$212,000. The intangible assets consist of the weekend.com and the weekends.com Internet domain names. During 2002, we evaluated the recoverability of our intangible assets in accordance with Statement of Financial Accounting Standards No. 144, Impairment of Long-Lived Assets, which required us to assess these assets for recoverability when events or circumstances indicate a potential impairment by estimating the undiscounted cash flows to be generated from the use of these assets. No impairment losses were recorded related to intangible assets in 2002. Any future impairment losses recorded in the future could have a material adverse impact on our financial conditions and results of operations.

Income Taxes

For the year ended December 31, 2002, we recorded an income tax provision of \$573,000. For the years ended December 31, 2001 and 2000, we recorded income tax provisions of \$521,000 and \$388,000, respectively. Our income is generally taxed in the U.S. and our income tax provision reflects federal and state statutory rates applicable to our levels of income and the effect of non-deductible merger expenses in 2000, 2001 and 2002.

Quarterly Financial Information

The following table sets forth, for the periods indicated, our consolidated financial information for the last ten quarters. We prepared this information using our unaudited interim consolidated financial statements that, in our opinion have been prepared on a basis consistent with our annual consolidated financial statements. We believe that these interim consolidated financial statements include all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of this information when read in conjunction with our financial statements and notes to financial statements. The operating results for any quarter do not necessarily indicate the results expected for any future period.

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Full Year
(unaudited, in thousands, except per share amounts)					
2003					
Revenues	\$ 3,714	\$ 4,291	n/a	n/a	n/a
Gross profit	3,630	4,210	n/a	n/a	n/a
Net income	385	596	n/a	n/a	n/a
Basic and diluted net income per share	\$ 0.02	\$ 0.03	n/a	n/a	n/a
2002					
Revenues	\$ 1,966	\$ 2,211	\$ 2,538	\$ 3,133	\$ 9,848
Gross profit	1,880	2,125	2,448	3,043	9,497
Net income	136	146	246	326	853
Basic and diluted net income per share	\$ 0.00	\$ 0.01	\$ 0.01	\$ 0.02	\$ 0.04
2001					
Revenues	\$ 1,311	\$ 1,539	\$ 1,575	\$ 1,723	\$ 6,148
Gross profit	1,234	1,465	1,501	1,644	5,844
Net income	218	70	61	15	364
Basic and diluted net income per share	\$ 0.01				