

Edgar Filing: ZONE 4 PLAY INC - Form 10QSB

ZONE 4 PLAY INC
Form 10QSB
November 14, 2005

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-QSB

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT
OF 1934

For the quarterly period ended September 30, 2005

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT

For the transition period from _____ to _____

Commission file number 000-51255

ZONE 4 PLAY, INC.
(Exact name of small business issuer as specified in its charter)

NEVADA
(State of incorporation)

98-037121
(IRS Employer Identification No.)

103 FOULK ROAD, WILMINGTON, DELAWARE
(972) - 3 - 6471884
(Address and telephone number of principal executive offices)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the last 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 whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act.)

Yes No

The number of shares outstanding of the registrant's Common Stock, \$0.001 par value, was 23,925,010 as of November 14, 2005.

PART I -- FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

ZONE 4 PLAY INC.
AND ITS SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)

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INTERIM CONSOLIDATED FINANCIAL STATEMENTS

AS OF SEPTEMBER 30, 2005

IN U.S. DOLLARS

UNAUDITED

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ZONE 4 PLAY INC. AND ITS SUBSIDIARIES (A DEVELOPMENT STAGE COMPANY)

CONSOLIDATED BALANCE SHEET

U.S. DOLLARS

	SEPTEMBER 30, 2005
	----- UNAUDITED -----
ASSETS	
CURRENT ASSETS:	
Cash and cash equivalents	\$1,362,729
Trade receivables	271,864
Other accounts receivable and prepaid expenses	64,988

TOTAL current assets	1,699,581

SEVERANCE PAY FUND	94,086

PROPERTY AND EQUIPMENT, NET	769,307

TECHNOLOGY, NET	857,306

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TOTAL assets \$3,420,280
=====

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

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ZONE 4 PLAY INC. AND ITS SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)

CONSOLIDATED BALANCE SHEET

U.S. DOLLARS, EXCEPT SHARE DATA

SEPTEMBER 30,
2005

UNAUDITED

LIABILITIES AND STOCKHOLDERS' EQUITY

CURRENT LIABILITIES:

Short-term bank credit	\$ 13,559
Trade payables	319,078
Employees and payroll accruals	342,828
Deferred revenues	111,113
Accrued expenses and other liabilities	61,935

TOTAL current liabilities	848,513

ACCRUED SEVERANCE PAY	276,416

STOCKHOLDERS' EQUITY:

Common stock of \$ 0.001 par value:	
Authorized: 75,000,000 shares at September	
30, 2005; Issued and outstanding:	
23,925,010 shares at September 30, 2005	23,925
Additional paid-in capital	8,894,921
Deferred stock compensation	(914,687)
Accumulated other comprehensive loss	(19,471)
Deficit accumulated during the development stage	(5,689,337)

TOTAL stockholders' equity	2,295,351

TOTAL liabilities and stockholders' equity	\$ 3,420,280
	=====

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

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ZONE 4 PLAY INC. AND ITS SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)

CONSOLIDATED STATEMENTS OF OPERATIONS

U.S. DOLLARS, EXCEPT SHARE DATA

	NINE MONTHS ENDED SEPTEMBER 30,		THREE MONTHS ENDED SEPTEMBER 30,
	2005	2004	2005
			UNAUDITED
Revenues:			
Software applications	\$ 868,332	\$ 432,883	\$ 374,451
Sale of software applications to related party	-	196,000	-
TOTAL revenues	868,332	628,883	374,451
Cost of revenues	40,322	113,296	11,971
Gross profit	828,010	515,587	362,480
Operating expenses:			
Research and development	1,997,539	812,436	740,820
Selling and marketing	689,258	293,563	216,115
General and administrative	904,230	277,726	418,487
TOTAL operating expenses	3,591,027	1,383,725	1,375,422
Operating loss	2,763,017	868,138	1,012,942
Financial income (expenses), net	31,348	(27,471)	13,603
Net loss	\$ 2,731,669	\$ 895,609	\$ 999,339
Basic and diluted net earnings per share	\$ 0.117	\$ 0.049	\$ 0.042

Weighted average number of shares of

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Common stock used in computing basic and diluted net loss per share	23,389,406 =====	18,262,350 =====	23,925,010 =====
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The accompanying notes are an integral part of the consolidated financial statements.

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ZONE 4 PLAY INC. AND ITS SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)

CONSOLIDATED STATEMENTS OF CASH FLOWS

U.S. DOLLARS

	NINE MONTHS ENDED SEPTEMBER 30,		THREE MONTHS SEPTEMBER 30,
	2005	2004	2005
			UNAUDITED
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net loss	\$ (2,731,669)	\$ (895,609)	\$ (999,339)
Adjustments required to reconcile net loss to net cash used in operating activities:			
Depreciation	265,762	32,407	142,314
Loss from sale of property	-	-	-
Decrease (increase) in other accounts receivable and prepaid expenses	(127,003)	34,350	(64,673)
Amortization of deferred compensation	376,480	-	139,735
Increase in trade payables	67,537	53,006	76,969
Increase in employees and payroll accruals	8,382	39,910	53,485
Increase (decrease) in deferred revenues	111,113	(243,500)	98,506
Increase (decrease) in accrued expenses and other liabilities	(131,590)	(131,967)	(26,868)
Accrued severance pay, net	36,947	54,489	12,606
Issuance of Common stock to a service provider	148,500	51,914	-
	(1,975,541)	(1,005,000)	(567,265)
CASH FLOWS FROM INVESTING ACTIVITIES:			

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Purchase of property and equipment	(638,146)	(62,563)	(433,751)
	-----	-----	-----
Net cash used in investing activities	(638,146)	(62,563)	(433,751)
	-----	-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES:			
Issuance of shares in respect of reverse acquisition (1)	-	4,391	-
Issuance of Capital stock	3,846,656	2,173,932	-
Short-term bank credit, net	3,447	(27,662)	3,015
Receipt of short-term loans from stockholders and others	-	50,000	-
Proceeds from short-term loans from stockholders and others	(1,229)	(532,395)	-
	-----	-----	-----
Net cash provided by financing activities	3,848,874	1,668,266	3,015
	-----	-----	-----
Effect of exchange rate changes on cash and cash equivalents	(16,535)	620	(13,869)
	-----	-----	-----
Increase (decrease) in cash and cash equivalents	1,218,652	601,323	(1,011,870)
Cash and cash equivalents at beginning of period	144,077	49,882	2,374,599
	-----	-----	-----
Cash and cash equivalents at end of period	\$ 1,362,729	\$ 651,205	\$ 1,362,729
	=====	=====	=====

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

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ZONE 4 PLAY INC. AND ITS SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)

CONSOLIDATED STATEMENTS OF CASH FLOWS

U.S. DOLLARS

NINE MONTHS ENDED SEPTEMBER 30,		THREE MONTHS ENDED SEPTEMBER 30,	
2005	2004	2005	2004
-----	-----	-----	-----
		UNAUDITED	

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NON-CASH TRANSACTIONS:

Purchase of property and equipment	\$ 42,477	\$ -	\$ 3,511	\$
	=====	=====	=====	=====
Issuance of shares in respect of minority interest in subsidiary	\$1,000,000	\$ -	\$ -	\$
	=====	=====	=====	=====

SUPPLEMENTAL DISCLOSURE OF CASH FLOWS INFORMATION:

Cash paid during the period for:

Interest	\$ 1,040	\$ 651	\$ 389	\$ 1
	=====	=====	=====	=====

(1) On February 1, 2004, the Company was acquired by Zone4Play Inc. (Nevada) through a reverse shell purchase acquisition (see Note 1b).

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

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ZONE 4 PLAY INC. AND ITS SUBSIDIARIES (A DEVELOPMENT STAGE COMPANY)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. DOLLARS, EXCEPT SHARE DATA

NOTE 1:- GENERAL

- a. Zone 4 Play, Inc. ("the Company") was incorporated under the laws of the State of Nevada on April 23, 2002, under the name of Old Goat Enterprises, Inc. On February 1, 2004, the Company acquired (in a reverse merger transaction, see b hereinafter) Zone 4 Play, Inc. ("Zone 4 Play, (Delaware)"), which was incorporated under the laws of the State of Delaware on April 2, 2001 (see b below). The Company develops and markets interactive games applications for Internet, portable devices and interactive TV platforms.

The Company conducts its operations and business with and through its wholly-owned subsidiary, Zone 4 Play, (Delaware), and its wholly-owned subsidiaries, Zone 4 Play, (Israel) Ltd., an Israeli company, which is engaged in research, development and marketing of the applications, Zone 4 Play, (UK) Limited, a United Kingdom corporation, which is engaged in marketing of the applications, and through MixTV Ltd., an Israeli company incorporated in June 2004, which is engaged in mobile messaging TV technologies.

The Company's shares are currently traded on the OTC Bulletin Board under the trading symbol "ZFPI.OB."

- b. According to the agreement dated February 1, 2004 between the Company and Zone 4 Play, (Delaware), the Company issued 10,426,190 shares of

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Common stock to the former holders of equity interests in Zone 4 Play, (Delaware). The acquisition has been accounted for as a reverse acquisition, whereby the Company was treated as the acquiree and Zone 4 Play, (Delaware) as the acquirer - primarily because the stockholders of Zone 4 Play, (Delaware) owned approximately 58% of the Company's Common stock - upon completion of the acquisition. Immediately prior the consummation of the transaction, the Company had no material assets and liabilities, hence the reverse acquisition was treated as a capital stock transaction in which Zone 4 Play, (Delaware) is deemed to have issued the Common stock held by the Company's stockholders for the net assets of the Company. The historical financial statements of Zone 4 Play, (Delaware) became the historical financial statements of the Company.

- c. The Company and its subsidiaries are devoting substantially all of their efforts toward conducting research, development and marketing of their software. In the course of its activities, the Company and its subsidiaries have sustained operating losses and expect such losses to continue in the foreseeable future. The Company and its subsidiaries have not generated sufficient revenues and have not achieved profitable operations or positive cash flows from operations. The Company's accumulated deficit aggregated to \$ 5,689,337 as of September 30, 2005. There is no assurance that profitable operations, if ever achieved, could be sustained on a continuing basis.

The Company plans to continue to finance its operations with a combination of stock issuances and revenues from product sales.

- d. Concentration of risk that may have a significant impact on the Company:

In the nine months ended September 30, 2005, the Company derived 81% of its revenues from 5 major customers (see Note 4b).

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ZONE 4 PLAY INC. AND ITS SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. DOLLARS, EXCEPT SHARE DATA

NOTE 1:- GENERAL (CONT.)

- e. On January 27, 2005, the Company completed a private placement, pursuant to which it sold an aggregate of 2,659,998 shares of Common stock for aggregate gross proceeds of \$ 3,989,999.

Pursuant to the aforementioned private placement, the Company issued to its investment bank 25,000 warrants exercisable until December 31, 2007 at a price of \$ 0.80 per share, and 53,200 warrants exercisable until December 31, 2007 at a price of \$ 1.50 per share.

- f. On January 3, 2005 and April 20, 2005, the Company issued 50,000 and 50,000 shares, respectively, of fully vested Common stock to a service provider, pursuant to a consulting contract. Expenses in the amount of \$ 69,000 and \$ 79,500, respectively, were recorded in the Company's statements of operations, based on the market share price at the grant date.

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- g. On March 10, 2005, the Company signed a stock purchase agreement ("the Agreement") with NetFun Ltd. ("NetFun"), regarding which the closing took place in April 2005. According to the Agreement, the Company acquired the remaining minority interests held by NetFun of 49.9% in its consolidated subsidiary MixTV Ltd. ("MixTV"), for consideration of 625,000 shares of Common stock of the Company, which have a fair value of \$ 1,000,000 based on the average market price of the shares in or about the date of the signing of the Agreement. As a result of the Agreement, the Company holds the entire ownership interest in MixTV. The acquisition was accounted under the purchase method of accounting and, accordingly, the purchase price has been allocated to MixTV's technology. The technology will be amortized over the weighted-average useful life of three years. No other significant net assets were acquired.
- h. On March 31, 2005, the Company granted to each of its non-employee directors, an option under the terms of the Company's option plan, to purchase 192,261 shares of Common stock of the Company at an exercise price of \$ 1.00 per share. Each director's right to exercise such option will vest in three equal annual installments during a period of three years commencing in May 2005, provided that the Company's agreement with such director does not terminate earlier. The Company recorded deferred stock compensation in the amount of \$ 307,618 in respect of those options.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES

- a. The significant accounting policies applied in the annual consolidated financial statements of the Company as of December 31, 2004 are applied consistently in these consolidated financial statements.
- b. These financial statements should be read in conjunction with the audited annual financial statements of the Company as of December 31, 2004 and their accompanying notes.

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ZONE 4 PLAY INC. AND ITS SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. DOLLARS, EXCEPT SHARE DATA

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (CONT.)

- c. Accounting for stock-based compensation:

The Company accounts for stock-based compensation in accordance with the provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB No. 25") and Financial Accounting Standards Board Interpretation No. 44, "Accounting for Certain Transactions Involving Stock Compensation" ("FIN No. 44"). Under APB No. 25, when the exercise price of an employee's options equals or is higher than the market price of the underlying Common stock on the date of grant, no compensation expense is recognized. Under Statement of Financial Accounting Standard No. 123, "Accounting for Stock-Based Compensation" ("SFAS No. 123"),

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pro-forma information regarding net income and income per share is required, and has been determined as if the Company had accounted for its employee stock options under the fair value method of SFAS No. 123.

The fair value of these options is amortized over their vesting period and estimated at the date of grant using a Black-Scholes multiple option pricing model with the following weighted average assumptions for the nine-month periods ended September 30, 2005 and for the year ended 2004:

	NINE MONTHS ENDED SEPTEMBER 30, 2005 UNAUDITED	YEAR ENDED DECEMBER 31, 2004 AUDITED
Risk free interest	2%	2%
Dividend yields	0%	0%
Volatility	0.97	1.11
Expected life (years)	2.1	2.1

	NINE MONTHS ENDED SEPTEMBER 30,	
	2005	2004
	UNAUDITED	
Net loss as reported	\$2,731,669	\$ 895,609
Deduct - stock-based employee compensation expenses included in reported net loss	376,380	-
Add - stock-based compensation expense determined under fair value method for all awards	494,459	-
	-----	-----
Pro forma net loss	\$2,849,748	\$ 895,609
	-----	-----
Basic and diluted net loss per share, as reported	\$ 0.117	\$ 0.049
	-----	-----
Pro forma basic and diluted net loss per share	\$ 0.122	\$ 0.049
	-----	-----

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ZONE 4 PLAY INC. AND ITS SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. DOLLARS, EXCEPT SHARE DATA

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NOTE 3:- BASIS OF PRESENTATION

The accompanying interim consolidated financial statements have been prepared by the Company in accordance with accounting principles generally accepted in the United States and the rules and regulations of the Securities and Exchange Commission, and include the accounts of the Company and its subsidiaries. Certain information and footnote disclosures, normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States, have been condensed or omitted pursuant to such rules and regulations. In the opinion of the Company, the unaudited financial statements reflect all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation of the financial position at September 30, 2005 and the operating results and cash flows for the nine months ended September 30, 2005 and 2004.

The results of operations for the nine months ended September 30, 2005 are not necessarily indicative of results that may be expected for any other interim period or for the full fiscal year ending December 31, 2005.

NOTE 4:- SEGMENTS, CUSTOMERS AND GEOGRAPHIC INFORMATION

Summary information about geographic areas:

The Company manages its business on the basis of one reportable segment (see Note 1 for a brief description of the Company's business) and follows the requirements of SFAS No. 131, "Disclosures About Segments of an Enterprise and Related Information".

- a. The following is a summary of operations within geographic areas, based on the location of the customers:

	NINE MONTHS ENDED SEPTEMBER 30,	
	2005	2004
	UNAUDITED	
England	\$527,006	\$475,693
United states	210,372	125,257
Australia	100,000	-
Israel	27,080	19,236
Others	3,874	8,697
	\$868,332	\$628,883
	=====	=====

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ZONE 4 PLAY INC. AND ITS SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. DOLLARS, EXCEPT SHARE DATA

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NOTE 4:- SEGMENTS, CUSTOMERS AND GEOGRAPHIC INFORMATION (CONT.)

b. Major customer data as a percentage of total revenues:

	NINE MONTHS ENDED	
	SEPTEMBER 30,	
	-----	-----
	2005	2004
	-----	-----
	UNAUDITED	
	-----	-----
Customer A	27%	34%
	=====	=====
Customer B (Related party)	-	31%
	=====	=====
Customer C	-	13%
	=====	=====
Customer D	21%	-
	=====	=====
Customer E	12%	-
	=====	=====
Customer F	11%	*)
	=====	=====
Customer G	10%	*)
	=====	=====

*) Represents an amount lower than 10%.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION.

FORWARD LOOKING STATEMENTS

This quarterly report on Form 10-QSB contains certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 and Federal securities laws, and is subject to the safe-harbor created by such Act and laws. Forward-looking statements may include our statements regarding our goals, beliefs, strategies, objectives, plans, including product and service developments, future financial conditions, results or projections or current expectations. In some cases, you can identify forward-looking statements by terminology such as "may," "will," "should," "expect," "plan," "anticipate," "believe," "estimate," "predict," "potential" or "continue," the negative of such terms, or other comparable terminology. These statements are subject to known and unknown risks, uncertainties, assumptions and other factors that may cause actual results to be materially different from those contemplated by the forward-looking statements. The business and operations of Zone 4 Play, Inc. are subject to substantial risks, which increase the uncertainty inherent in the forward-looking statements contained in this report. We undertake no obligation to release publicly the result of any revision to these forward-looking statements that may be made to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events. Further information on potential factors that could affect our business is described under the heading "Risk Related to Our Business" in Part I, Item 1, "Description of Business" of our Annual Report on Form 10-KSB for the fiscal year ended December 31, 2004. Readers are also urged to carefully review and consider the various disclosures we have made in this document.

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OVERVIEW

Our financial statements are stated in United States Dollars (US\$) and are prepared in accordance with United States Generally Accepted Accounting Principles.

You should read the following discussion of our financial condition and results of operations together with the unaudited financial statements and the notes to unaudited financial statements included elsewhere in this filing.

COMPANY HISTORY

Zone4Play, Inc. (hereinafter referred to as "Zone4Play", "the Company", "us" or "we") was incorporated under the laws of the State of Nevada on April 23, 2002, as Old Goat Enterprises, Inc. On February 1, 2004, Old Goat Enterprises, Inc. issued the shareholders of Zone 4 Play, Inc., a Delaware corporation ("Zone4Play Delaware"), 10,426,190 shares of common stock, in consideration for the entire share capital of Zone4Play Delaware. Immediately after the issuance, the shareholders of Zone4Play Delaware held 58% of the issued and outstanding share capital of Old Goat Enterprises, Inc., and subsequently changed its name to Zone 4 Play, Inc., a Nevada corporation. The transaction was accounted for as a reverse acquisition, whereby Old Goat was treated as the acquired company and Zone4Play Delaware as the acquirer. The historical financial statements of Zone4Play Delaware became our historical financial statements. We conduct our operations through our wholly owned subsidiaries, Zone4Play (Israel) Ltd., an Israeli corporation incorporated in July 2001, Zone4Play (UK) Limited, a United Kingdom corporation incorporated in November 2002, and Zone4Play Delaware. On April 27, 2005, pursuant to an agreement with NetFun Ltd., we increased our ownership percentage of the issued and outstanding share capital of MixTV Ltd. from 50.1% to 100%. Our shares of common stock are currently traded on the OTC Bulletin Board under the trading symbol "ZFPI.OB"

OUR BUSINESS

We are a software and technology developer and provider to companies that service the interactive gaming industry, delivering cross-platform systems that are built for mass participation gaming over mobile devices, TV and the internet. Our software provides and supports play-for-fun and play-for-real interactive games (currently such play-for-real gaming solutions are only provided in the UK where fixed odds gaming are permitted by licensed bookmakers).

We develop five core solutions to companies that offer play-for-real gaming, namely:

- (i) Mobile gaming: the provision of services on mobile devices, including fixed odds games, multiplayer games, sports betting services, scratch cards and exchange betting.
- (ii) Interactive TV gaming: the provision of software and technology supporting fixed odds games, skill games, scratch card services, and multiplayer blackjack and poker.
- (iii) Participating/SMS-TV gaming: the provision of services via the interaction of television broadcasts and mobile text messages, IVR lines or Java Interaction. Services currently include fixed odds games and virtual racing.

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- (iv) Online gaming: the provision of fixed odds and casino games over the internet.
- (v) Multiplayer gaming: multiplayer poker, bingo and blackjack products that allow competition between players who play on mobile devices, Interactive TV or the internet.

We also provide:

- (i) Games for fun: the provision of play-for-fun gaming alternatives on mobile, Interactive TV, participating/SMS-TV and the internet.
- (ii) Games of skill: the provision of play-for-fun games of skill on Interactive TV, participating/SMS-TV and the internet are under development.

Our customers include online gaming operators (Cosmotrade Investments Limited), bookmakers (Eurobet UK Limited, Littlewoods Promotions Limited, The Gaming Channel Limited, Two Way Media Limited), betting exchanges (Betfair [the Sporting Exchange Limited]), cable and satellite television service providers (CSC Holdings Inc., Echostar Satellite L.L.C., RCN Telecom Services), TV gaming channel providers (The Poker Channel Ltd., Channel 5 Broadcasting Ltd.), mobile operators (O2 (online) Ltd.), internet service providers (Chello Broadband N.V. and Commonwealth Telephone Enterprises Inc. [CTE]) and hospitality service providers (LodgeNet Entertainment Corporation). Our technology allows our customers to generate additional revenue from their existing infrastructure and user base by allowing a subscriber to switch from one platform, such as Interactive TV, mobile or internet, to another platform using a single account with the same account balance and user information. One of the key features of our software is its ability to utilize a single account to play a game on mobile, Interactive TV and internet platforms. In addition, our technology allows mobile service providers, TV broadcasters and channels to provide additional content as well as an increased variety of services to their customers.

We enter into license and/or revenue-sharing agreements with our customers under which the customers use our software and technology to offer games to their subscribers and pay us a fixed fee and/or a percentage of the net revenues generated from those games.

We devote substantially all of our efforts toward conducting research, development and marketing of our software. In the course of these activities, we have sustained operating losses and expect such losses to continue in the foreseeable future. To date, we have not generated sufficient revenues to achieve profitable operations or positive cash flow from operations. On September 30, 2005, we had an accumulated deficit of \$5,689,337. There is no assurance that profitable operations, if ever achieved, will be sustained on a continuing basis. During the nine months ended September 30, 2005, we derived approximately 81% of our revenues from five major customers.

RESULTS OF OPERATIONS - THREE MONTHS ENDED SEPTEMBER 30, 2005 COMPARED TO THREE MONTHS ENDED SEPTEMBER 30, 2004

REVENUES AND COST OF REVENUES

Total revenues for the three months ended September 30, 2005 increased by

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167% to \$374,451 from \$140,364 for the three months ended September 30, 2004. All such revenues were from sales of software applications and distribution rights. The increase in revenues from software applications was due to new contracts, such as contracts with Two Way TV Australia Limited, Two Way Media Limited and Winner.com (UK) Limited, and from license revenues from our customer Cosmotrade Investments Ltd., which we did not have in 2004.

Deferred revenues include unearned amounts received under services contracts, and amounts received from customers but not recognized as revenues. Total deferred revenues for the three months ended September 30, 2005 was \$98,506 compared with \$0 for the three months ended September 30, 2004. The increase is mainly due to a new contract with Two Way TV Australia Limited that includes advance payments and deferred revenues as well. The deferred revenues will be included in our revenues at the end of the first year of the contract with Two Way TV Australia Limited.

Cost of revenues for the three months ended September 30, 2005 decreased by 10% to \$11,971 from \$13,372 for the three months ended September 30, 2004. For the three months ended September 30, 2005, gross profit increased by 185% to \$362,480 when compared to gross profit of \$126,992 for the three months ended September 30, 2004. The decrease in the cost of revenues is attributable to the fact that there was a decrease in the servers hosting expenses in the three months ended September 30, 2005 compared with the three months ended September 30, 2004.

RESEARCH AND DEVELOPMENT

Research and development expenses for the three months ended September 30, 2005 increased by 106% to \$740,820 from \$358,915 for the three months ended September 30, 2004. The increase is primarily attributable to the our new projects in the United Kingdom and the United States, which involve adapting our software to new systems and platforms (ITV, mobile, internet, and SMS-TV by our subsidiary ,MixTV Ltd.), recruitment of employees, subcontractors' expenses, increased general and administrative expenses allocated to the research and development department due to its growth and to the amortization of the technology which was acquired on April 2005 by acquiring the minority shares in our SMS-TV subsidiary, MixTV Ltd., and to amortization of deferred compensation related to options which were granted to the relevant employees in December 2004.

SALES AND MARKETING

Sales and marketing expenses for the three months ended September 30, 2005 increased by 52% to \$216,115 from \$142,012 for the three months ended September 30, 2004. The increase in sales and marketing expenses is primarily attributable to marketing efforts made mainly in the United Kingdom and the United States using our Israeli-based team. Sales and marketing expenses consist mainly of labor costs, trade shows, travel expenses to the United Kingdom and the United States, and amortization of deferred compensation related to options which were granted to the relevant employees in December 2004.

GENERAL AND ADMINISTRATIVE

General and administrative expenses for the three months ended September 30, 2005 increased by 200% to \$418,487 from \$139,441 for the three months ended September 30, 2004. The increase in general and administrative expenses is primarily attributable to recruitment of employees, additional legal and audit expenses associated with being a reporting company in the U.S, expenses in relation to the possible admission of our shares to trade on AIM, a market

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operated by the London Stock Exchange plc, and amortization of deferred compensation related to options which were granted to the relevant employees in December 2004, and to non-employees directors in March 2005.

NET LOSS

Net loss for the three months ended September 30, 2005 was \$999,339 as compared to net loss of \$535,276 for the three months ended September 30, 2004. Net loss per share for the months ended September 30, 2005 was \$0.042 as compared to \$0.026 for the three months ended September 30, 2005. The net loss significantly increased for the three months ended September 30, 2005 and the increase is mainly attributable to the increase in the operating expenses. Our weighted average number of shares of common stock used in computing basic and diluted net loss per share for the three months ended September 30, 2005 was 23,925,010 compared with 20,012,050 for the three months ended September 30, 2004. The increase is mainly attributable to issuance of 2,659,998 shares of our common stock which were sold on a private placement in January 2005, to the issuance of 100,000 shares of our common stock which were issued to service provider pursuant to consulting contract, and to issuance of 625,000 shares of our common stock to Netfun Ltd. on April 27, 2005, pursuant to an agreement with Netfun Ltd., under which we increased our ownership percentage of the issued and outstanding share capital of MixTV Ltd. from 50.1% to 100%.

RESULTS OF OPERATIONS - NINE MONTHS ENDED SEPTEMBER 30, 2005 COMPARED TO NINE MONTHS ENDED SEPTEMBER 30, 2004

Our current financial statements reflect MixTV Ltd.'s revenue and losses for the nine months ended September 30, 2005. MixTV Ltd. was formed by us and Netfun Ltd. in June 2004 and therefore only its revenue and losses since the date of its formation have been reflected in the Company's financial statements for the nine month period ended September 30, 2004.

REVENUES AND COST OF REVENUES

Total revenues for the nine months ended September 30, 2005 increased by 38% to \$868,332 from \$628,883 for the nine months ended September 30, 2004. All such revenues were from sales of software applications and distribution rights. For the nine months ended September 30, 2005, revenues from sales of software applications to related parties were \$0, compared with \$196,000 for the nine months ended September 30, 2004. The increase in revenues from software applications was due to new contracts such as Two Way TV Australia, Two way Media Limited and Winner.com (UK) Ltd., and to an increase in penetration with our existing customers such as NDS Limited, and CSC Holdings Inc. (Cablevision) Also in the first nine months of 2005, we had license revenues from our customers, such as Cablevision, Commonwealth Telephone Enterprises Inc (CTE) (to which we supplied internet packages for play-for-fun), and Cosmotrade investments Ltd., which we did not have in 2004.

Deferred revenues include unearned amounts received under services contracts, and amounts received from customers but not recognized as revenues. Total deferred revenues for the nine months ended September 30, 2005 was \$111,113 compared with \$0 for the nine months ended September 30, 2004. The increase is mainly due to a new contract with Two Way TV Australia Limited that includes advance payments and deferred revenues as well. The deferred revenues will be included in our revenues at the end of the first year of the contract with Two Way TV Australia Limited.

Cost of revenues for the nine months ended September 30, 2005 decreased by 64% to \$40,322 from \$113,296 for the nine months ended September 30, 2004. Gross profit increased by 61% for the nine months ended September 30, 2005 to \$828,010 from \$515,587 for the same period in 2004. The decrease in the cost of revenues is attributable to the fact that in the nine months ended September 30, 2004

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there were revenues generated from related party transactions that have not been repeated, nor have any costs been incurred in connection with such revenues, in the nine months ended September 30, 2005.

RESEARCH AND DEVELOPMENT

Research and development expenses for the nine months ended September 30, 2005 increased by 146% to \$1,997,539 from \$812,436 for the nine months ended September 30, 2004. The increase is primarily attributable to the our new projects in the United Kingdom and the United States, which involve adapting our software to new systems and platforms (ITV, mobile internet, and SMS-TV by our subsidiary, MixTV Ltd.), recruitment of employees, subcontractors' expenses, increased general and administrative expenses allocated to the research and development department due to it's growth and to the amortization of the technology which was acquired on April 2005 by acquiring the minority shares in our SMS-TV subsidiary, MixTV Ltd., and to amortization of deferred compensation related to options which were granted to the relevant employees in December 2004.

SALES AND MARKETING

Sales and marketing expenses for the nine months ended September 30, 2005 increased by 135% to \$689,258 from \$293,563 for the nine months ended September 30, 2004. The increase in sales and marketing expenses is primarily attributable to marketing efforts made mainly in the United Kingdom and the United States using our Israeli-based team. Sales and marketing expenses consist mainly of labor costs, trade shows, travel expenses to the United Kingdom and the United States, and amortization of deferred compensation related to options which were granted to the relevant employees in December 2004.

GENERAL AND ADMINISTRATIVE

General and administrative expenses for the nine months ended September 30, 2005 increased by 226% to \$904,230 from \$277,726 for the nine months ended September 30, 2004. The increase in general and administrative expenses is primarily attributable to recruitment of employees, additional legal and audit expenses associated with being a reporting company in the U.S. expenses in relation to the possible admission of our shares to trade on AIM, a market operated by the London Stock Exchange plc, non-cash investor relations expenses and amortization of deferred compensation related to options which were granted to the relevant employees in December 2004, and to non-employees directors, which were granted on March 2005.

NET LOSS

Net loss for the nine months ended September 30, 2005 was \$2,731,669 as compared to net loss of \$895,609 for the nine months ended September 30, 2004. Net loss per share for the months ended September 30, 2005 was \$0.117 as compared to \$0.049 for the three months ended September 30, 2005. The net loss significantly increased for the nine months ended September 30, 2005 and the increase is mainly attributable to the increase in the operating expenses. Our weighted average number of shares of common stock used in computing basic and diluted net loss per share for the nine months ended September 30, 2005 was 23,389,406 compared with 18,262,350 for the nine months ended September 30, 2004. The increase is mainly attributable to issuance of 2,659,998 shares of our common stock which were sold on a private placement in January 2005, to the issuance of 100,000 shares of our common stock which were issued to service provider pursuant to consulting contract, and to issuance of 625,000 shares of our common stock to Netfun Ltd on April 27, 2005, pursuant to an agreement with NetFun

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Ltd., under which we increased our ownership percentage of the issued and outstanding share capital of MixTV Ltd. from 50.1% to 100%.

LIQUIDITY AND CAPITAL RESOURCES

As of September 30, 2005, total current assets were \$1,699,581 and total current liabilities were \$848,513. On September 30, 2005, we had a working capital surplus of \$ 851,068 and an accumulated deficit of \$5,689,337. We finance our operations and plan to continue doing so with a combination of stock issuances and revenues from product sales. We had working capital of \$851,068 on September 30, 2005 compared with a working capital deficit of \$385,993 on December 31, 2004. Cash and cash equivalents on September 30, 2005 were \$1,362,729, an increase of \$1,218,652 from the \$144,077 reported on December 31, 2004. Cash balances increased in the nine months ended September 30, 2005 primarily as a result of a stock issuance, offset by the increase in our net loss for the nine months ended September 30, 2005.

Operating activities used cash of \$1,975,541 in the nine months ended September 30, 2005 and \$567,265 in the three months ended September 30, 2005. Cash used by operating activities in the nine months ended September 30, 2005 results primarily from a net loss of \$2,731,669, a \$8,382 increase in employee payroll accruals, a \$131,590 decrease in accrued expenses and other liabilities offset by a \$376,480 increase in amortization of deferred compensation, \$111,113 increase in deferred revenues, \$265,762 of depreciation and \$148,500 of compensation related to issuance of common stock to a service provider.

Investing activities used cash of \$638,146 in the nine months ended September 30, 2005 and \$433,751 in the three months ended on the same date. Cash used by investing activities in the nine and three months ended September 30, 2005 results from the purchase of computer and software equipment and office furnishings.

Financing activities generated cash of \$3,848,874 during the nine months ended September 30, 2005 and \$3,015 for the three months ended September 30, 2005. Cash provided by financing activities for the nine month period ended September 30, 2005 results primarily from a stock issuance offset slightly by repayments of short term loans.

On January 27, 2005, we completed a private offering to accredited investors under Section 4(2) of the Securities Act of 1933, as amended, pursuant to which it sold an aggregate of 2,659,998 shares of common stock for aggregate gross proceeds of \$3,989,999. We agreed to prepare and file with the SEC a registration statement covering the resale of the common stock for certain investors. The registration statement became effective on April 29, 2005.

OUTLOOK

We believe that our future success will depend upon our ability to enhance our existing products and solutions and introduce new commercially viable products and solutions addressing the demands of the evolving markets. As part of the product development process, we work closely with current and potential customers, distribution channels and leaders in our industry to identify market needs and define appropriate product specifications. Our current anticipated levels of revenue and cash flow are subject to many uncertainties and cannot be assured. In order to have sufficient cash to meet our anticipated requirements for the next twelve months, we may be dependent upon our ability to obtain additional financing. The inability to generate sufficient cash from operations or to obtain the required additional funds could require us to curtail operations.

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ITEM 3. CONTROLS AND PROCEDURES.

EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES - We maintain a system of disclosure controls and procedures that are designed for the purposes of ensuring that information required to be disclosed in our Securities and Exchange Commission ("SEC") reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"), as appropriate to allow timely decisions regarding required disclosures.

As of the end of the period covered by this report, we carried out an evaluation, under the supervision and with the participation of our CEO and CFO, of the effectiveness of our disclosure controls and procedures as defined in Rule 13a-15(e) of the Securities Exchange Act of 1934, as amended. Based on that evaluation, our CEO and CFO concluded that our disclosure controls and procedures are effective.

CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING - There has been no change in our internal control over financial reporting during the third quarter of 2005 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II -- OTHER INFORMATION

ITEM 6. EXHIBITS.

- 10.1 Agreement, dated August 17, 2005 between Two Way TV Australia Limited and Zone 4 Play, Inc., a Delaware corporation and a wholly owned subsidiary of the Company (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on August 23, 2005).
- 10.2 Amended Employment Agreement, dated July 25, 2005, by and between the Zone 4 Play (Israel) Ltd., a wholly-owned Israeli subsidiary of the Company and Shimon Citron (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on July 27, 2005).
- 10.3 Summary of Compensation of the Directors of the Company.
- 31.1 Section 302 Certification of Chief Executive Officer Pursuant to Rule 13a-14(a)/15d-14(a) under the Securities Exchange Act of 1934 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Section 302 Certification of Chief Financial Officer Pursuant to Rule 13a-14(a)/15d-14(a) under the Securities Exchange Act of 1934 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of Chief Executive Officer Pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of Chief Financial Officer Pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

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In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

ZONE 4 PLAY, INC.

Dated: November 14, 2005

By: /S/ Shimon Citron

SHIMON CITRON
President and Chief Executive Officer

Dated: November 14, 2005

By: /S/ Uri Levy

URI LEVY
Chief Financial Officer