

SPARK NETWORKS INC
Form 10-K
March 22, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE FISCAL YEAR ENDED DECEMBER 31, 2016

OR

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

FOR THE TRANSITION PERIOD FROM TO

COMMISSION FILE NO. 001-32750

SPARK NETWORKS, INC.

(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

DELAWARE	20-8901733
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

11150 Santa Monica Boulevard, Suite 600,

Los Angeles, California	90025
(Address of principal executive offices)	(Zip Code)

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE: (310) 893-0550

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

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Title of Each Class	Name of Each Exchange on which Registered
Common Stock, par value \$0.001 per share	NYSE MKT
Preferred Share Purchase Rights	NYSE MKT

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT:

None.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definitions of "accelerated filer," "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer

Non-accelerated filer Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No

The aggregate market value of the voting and non-voting common equity (which consists solely of shares of common stock) held by non-affiliates of the registrant as of June 30, 2016 was approximately \$40,992,324 based on \$1.58, the closing price of the registrant's common stock on the NYSE MKT on June 30, 2016.

The registrant had 32,001,046 shares of outstanding common stock, par value \$0.001 per share, as of March 16, 2017.

Information required by Items 10, 11, 12, 13 and 14 of Part III are incorporated by reference from the Proxy Statement for the registrant's 2016 Annual Meeting of Stockholders. Except with respect to information specifically incorporated by reference in the Form 10-K, the Proxy Statement is not deemed to be filed as part hereof.

SPARK NETWORKS, INC.

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CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This annual report on Form 10-K, including the sections entitled “Risk Factors,” “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and “Business,” contains forward-looking statements that involve substantial risks and uncertainties. All statements other than statements of historical facts contained in this annual report on Form 10-K, including statements regarding our future financial position, business strategy and plans and objectives of management for future operations, are forward-looking statements. In some cases, you can identify forward-looking statements by terminology such as “believes,” “expects,” “anticipates,” “intends,” “estimates,” “may,” “will,” “continue,” “should,” “plan,” “predict,” “potential” or the negative of these terms or other similar expressions. We have based these forward-looking statements on our current expectations and projections about future events and financial trends that we believe may affect our financial condition, results of operations, business strategy and financial needs. Our actual results could differ materially from those anticipated in these forward-looking statements, which are subject to a number of risks, uncertainties and assumptions described in the “Risk Factors” section and elsewhere in this annual report on Form 10-K, regarding, among other matters:

- our ability to attract members to our websites, convert members into paying subscribers and retain our paying subscribers;
- the highly competitive nature of our business;
- our ability to keep pace with rapid technological change and enhance existing or introduce new services;
- the strength of our existing brands and our ability to maintain and enhance those brands;
- our ability to effectively manage our operations and attract and retain qualified personnel;
- the hiring of a new management team, including the CEO and CTO;
- our management services agreement with PEAK6 Investments, L.P.
- the geo-political instability in Israel;
- our dependence upon the telecommunications infrastructure and our networking hardware and software infrastructure;
- effectively protecting our internet and domain names and participating rights;
- the effect of new interpretation of existing laws and regulations on our operations; and
- other factors referenced in this annual report on Form 10-K and other reports.

You should not rely upon forward-looking statements as predictions of future events. We cannot assure you that the events and circumstances reflected in the forward-looking statements will be achieved or occur. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. Moreover, neither we nor any other person assume responsibility for the accuracy and completeness of the forward-looking statements. Except as required by law, we undertake no obligation to update publicly any forward-looking statements for any reason after the date of this annual report on Form 10-K to conform these statements to actual results or to changes in our expectations.

You should read this annual report on Form 10-K, and the documents that we reference in this annual report on Form 10-K and have filed as exhibits with the Securities and Exchange Commission, completely and with the understanding that our actual future results, levels of activity, performance and achievements may materially differ from what we expect. We qualify all of our forward-looking statements by these cautionary statements.

ADDITIONAL INFORMATION

We are required to file annual, quarterly and current reports, proxy statements and other information with the SEC. You can read our SEC filings over the Internet at the SEC's website at <http://www.sec.gov>. You may also read and copy any document we file with the SEC at its public reference facilities at 100 F Street, N.E. Washington, DC 20549. You may also obtain copies of the documents at prescribed rates by writing to the Public Reference Section of the SEC at 100 F Street, N.E., Washington, DC 20549. Please call the SEC at 1-800-SEC-0330 for further information on the operation of the public reference facilities.

We maintain a corporate website at www.spark.net. You may access our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed with, or furnished to, the SEC pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, (the "Exchange Act") with the SEC free of charge at our website as soon as reasonably practicable after such material is electronically filed with, or furnished to, the SEC. The reference to our web address is provided for informational purposes only and does not constitute incorporation by reference of the information contained on this website.

PART I

ITEM 1. BUSINESS

Unless the context otherwise requires, the terms “Company,” “Spark,” “we,” “us,” and “our” refer to Spark Networks, Inc., a Delaware corporation and its subsidiaries. The Company was incorporated on April 20, 2007.

Our Business

Spark Networks, Inc., is a leader in creating communities that help individuals form life-long relationships with others that share their interests and values. The Company’s core properties, JDate and ChristianMingle, are communities geared towards singles of the Jewish and Christian faiths. Through the Company’s websites and mobile applications, the Company helps members search for and communicate with other like-minded individuals.

Along with these two core brands, we also operate a number of other niche-focused and international websites and mobile applications and maintain a physical presence in the United States. Information regarding the geographical source of our revenue and data on our reportable segments can be found in Note 10 to our Consolidated Financial Statements included in this annual report.

Our online singles properties provide users with three key services: (1) searching for compatible individuals with whom to potentially form long-term relationships; (2) validating compatibility through profiles, viewing photographs and understanding likes and characteristics; and (3) communicating via one of our numerous communications platforms designed to foster relationships.

Like many on-line businesses, we have experienced a significant shift in our member base from desktop usage to mobile usage, and now offer mobile applications across all of our core properties. To further accelerate our mobile offerings, we completed the acquisition of Smooch Labs, Inc. (“Smooch Labs”), the owner of the millennial Jewish mobile-only dating application JSwipe, in October 2015. Through this acquisition, we have broadened our reach to younger members of the Jewish community, who traditionally were not JDate subscribers.

Membership on our online singles websites or mobile applications is free and allows registered members to post personal profiles and take advantage of our search and validation features. With the exception of JSwipe, which employs a freemium model, the ability to initiate communication with other members requires payment, typically a monthly subscription fee which, along with advertising sales, represents our primary source of revenue. We typically offer discounted subscription rates to those members who subscribe for periods longer than one month. Subscriptions renew automatically until subscribers terminate them.

In August 2016, we entered into a purchase agreement with PEAK6 Investments, L.P. (“PEAK6”), pursuant to which we issued and sold to PEAK6 an aggregate of 5,000,000 shares of common stock of the Company at a purchase price of \$1.55 per share. We also issued a warrant to PEAK6 to purchase up to 7,500,000 shares of common stock of the Company at an exercise price of \$1.74 per share pursuant to the terms of a warrant agreement.

In connection with the execution of the purchase agreement, the Company entered into a Management Services Agreement dated as of August 9, 2016 with PEAK6, pursuant to which PEAK6 provides certain marketing, technology, strategy, development and other services to the Company over a five-year term, for a cash fee of \$1.5 million per year (the “Management Fee”), which will be paid on a quarterly basis in an amount of \$375,000 per quarter. The Management Fee excludes reimbursement of marketing costs as described below, which are costs in addition to the Management Fee.

At its discretion, PEAK6 may invoice each quarter for an amount different than the contractual amount, however, the amounts cannot exceed the contractual amount of \$375,000 per quarter, other than for marketing costs as described below. If the quarterly invoice is for an amount less than the contractual amount, PEAK6 does not have the right to bill any additional fees in any future period, as the amounts invoiced represent the full amount due for the services provided by PEAK6 to the Company for each specific quarter.

During the year ended December 31, 2016, PEAK6 invoiced the Company a Management Fee of \$560,000, representing the full amount due for services expected to be provided through the period ended February 28, 2017, excluding marketing costs as described below. The Management Fee may increase up to the contractual amount in future periods. The Management Fee expense is included within technical operations, development, and general and administrative expenses in the Consolidated Statements of Operations and Comprehensive Loss. For the year ended December 31, 2016, Management Fee expense to PEAK6 was \$393,000. The prepaid expenses balance related to the Management Fee was \$167,000 at December 31, 2016.

In addition, in the event that PEAK6 partners or employees are engaged to provide marketing or marketing related services to the Company either as replacement of Company employees or other external marketing resources engaged by the Company or as if they were Company employees, then the Company will reimburse PEAK6 for the actual costs incurred by such PEAK6 partners or employees. The amount to be reimbursed in any year by the Company for such marketing or marketing related services shall not exceed the lesser of “Saved Company Marketing Costs” or \$1.8 million. “Saved Company Marketing Costs” is defined as the aggregate amount of fully burdened costs to the Company of the sales and marketing employees and external marketing resources (consulting or otherwise) that provided marketing or similar services to the Company that are replaced or reduced by the Company or PEAK6 partners or employees. The amounts reimbursed to PEAK6 for marketing and marketing related services are included as sales and marketing expense in the Consolidated Statements of Operations and Comprehensive Loss. For the year ended December 31, 2016, the Company has expensed \$259,000 for sales and marketing services performed by PEAK6.

The Management Services Agreement may be terminated by the Company at its convenience upon at least 60 days’ prior written notice at any time after August 9, 2019, and may be terminated for cause at any time by PEAK6 or the Company upon the occurrence of certain events as set forth in the Management Services Agreement. Upon termination for convenience, the Company shall pay PEAK6 any unpaid quarterly payments that are due on or before the termination date and amounts due for certain costs and expenses incurred in connection with the Management Services Agreement. Upon termination for “cause” by PEAK6, the Company shall pay PEAK6 any unpaid quarterly payments that are due on or before the termination date, all Management Fees that would have been paid by the Company to PEAK6 in the first three years of the agreement less amounts actually paid, and the Warrant shall vest immediately without regard to any vesting conditions. Upon termination for cause by the Company, PEAK6 shall pay the Company an amount equal to the aggregate amount of all Management Fees paid by the Company during the term of the Management Services Agreement.

The common stock of Spark Networks, Inc. is traded on the NYSE MKT.

Our Industry

Our primary businesses are in the online personals industry, which we believe fulfills significant needs for single adults looking to meet a companion. Traditional methods such as printed personals advertisements, offline dating services and public gathering places often do not meet the needs of single people. Printed personals advertisements offer individuals limited personal information and interaction before meeting. Offline dating services are time-consuming, expensive and offer a smaller number of potential partners. Public gathering places such as restaurants, bars and other social venues provide a limited opportunity to learn about others prior to an in-person meeting. In contrast, online personals services facilitate interaction between singles by allowing them to screen and communicate with a large number of potential companions before they meet in-person. With features such as detailed personal profiles, email, mobile chat and instant messaging, this medium allows users to communicate with other singles at their convenience and affords them the ability to meet multiple people in an anonymous, convenient and secure setting.

The online personals industry in the United States has experienced significant growth in recent years. According to a Pew Research study released in early 2016, the percentage of the U.S. population using online personals websites or mobile applications grew approximately 40% from 11% in 2013 to 15% in 2015. Members of the millennial generation (individuals under 35 years old) tend to have the highest usage of online or mobile personals sites. However, members of older age groups represent approximately 60% of total users.

Our Competitive Strengths

The dating industry is very competitive and has no single, dominant brand. We compete primarily with other companies that provide similar dating and matchmaking products, including the Match Group, which operates the Match.com, OkCupid, Plenty of Fish, and Tinder properties, and eHarmony and Zoosk. In addition to other online dating brands, we compete indirectly with offline dating services, such as in-person matchmakers, and social media platforms. Arguably, our biggest competition comes from the traditional ways that people meet each other, and the choices some people make to not utilize dating products or services.

We believe our ability to compete is predicated upon the following:

◆ **Affinity-Focused Communities.** We believe singles are more likely to interact, find friends and form lasting relationships with like-minded individuals who share common values, beliefs, traditions and cultural upbringings. For this reason, the majority of our websites and mobile applications are targeted to specific religious, ethnic, geographic and special interest groups. We believe our targeted communities enjoy greater word-of-mouth recognition and consumer loyalty relative to non-targeted communities. This community affinity also affords us the opportunity to work alongside leaders within these communities, and increase the strength of our brands through powerful endorsements.

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Strength of the JDate and ChristianMingle Brands. We believe JDate and ChristianMingle, with their strong brand recognition, are valuable assets. The strength of these brands have been derived both through paid advertising but also by the numerous successes we have been responsible for in the form of marriages between our customers. According to a 2015 Survata industry survey, both JDate and ChristianMingle were responsible for more marriages within their respective Jewish and Christian communities than any other online personals site. We believe the size and strength of each of our key brands allows us to market to and serve each of the Jewish and Christian communities profitably.

- **Multiple Business Models.** With the acquisition of JSwipe, we have broadened our product offerings to include a “freemium”, mobile-only offering that complements our subscription-driven platforms. The addition of this mobile-only application to our portfolio has furthered our reach with millennial users, which constitutes a highly active segment of the online personals industry.

Customer Service Focus. Our multi-lingual call center and email support teams monitor our sites for fraudulent activity, assist members with billing questions, help members complete personal profiles and answer technical questions. We believe the quality of our customer service increases member satisfaction, which increases the number and percentage of members that become and remain paying subscribers.

Our Online Personals Services

Our core subscription online personals services offer single adults a convenient and secure setting for meeting other singles. Visitors to our websites or mobile applications are encouraged to become registered members and post profiles. Posting a profile is a process in which visitors are asked various questions about themselves, including information such as their tastes in food, hobbies and desired attributes of potential partners. Members may also post photos of themselves. Members can perform detailed searches of other profiles and save their preferences, and their profiles can be viewed by other members. In most cases, for a member to initiate email and instant message communication with others, that member must purchase a subscription. A subscription affords access to the paying subscribers’ on-site email, mobile chat, and instant messaging systems, enabling such subscribers to communicate with other members and paying subscribers. Our subscription fees are charged on a monthly basis, with discounts for longer-term subscription purchases.

For our “freemium” mobile application, JSwipe, users can install our applications for free and register via Facebook authentication. These applications use “right swipes” to indicate interest in another user. If there is mutual interest between two users, the application facilitates a forum for communication. In 2016, JSwipe launched unique, paid premium features to better help users find matches.

Online Personals Websites & Applications. We believe we are a relatively unique company in the online personals industry because we operate websites and mobile applications targeted at specific religious, ethnic, geographic and special interest groups. We currently offer websites and mobile applications primarily in English, Hebrew and French. Some of our properties, organized by segment, are as follows:

Online Personals Property	Target Audience
Jewish Networks	
JDate.com	Jewish singles
JSwipe	Jewish singles (millennials)

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JDate.co.uk	Jewish singles
JDate.fr	Jewish singles (French speakers)
JDate.co.il	Jewish singles (Hebrew speakers)
Cupid.co.il	Jewish singles (Hebrew speakers)

Christian Networks

ChristianMingle.com	Christian singles
CrossPaths	Christian singles (millennials)
ChristianMingle.co.uk	Christian singles
ChristianMingle.com.au	Christian singles
Christiansingles.com	Christian singles

Other Networks

AdventistSinglesConnection.com	Adventist singles
BBWPersonalsPlus.com	Big beautiful women and admirers
BlackSingles.com	African-American singles
CatholicMingle.com	Catholic singles

DeafSinglesConnection.com	Deaf singles
LDSMingle.com	Mormon singles
LDSSingles.com	Mormon singles
MilitarySinglesConnection.com	Military singles
SilverSingles.com	Mature singles
Spark.com	Non-targeted

Platform Features. We offer different ways for our members to communicate including:

On-Site Email. We provide all paying subscribers with private message centers. These personal on-site email boxes offer features such as customizable folders for storing correspondence, the ability to know when sent messages were read, as well as block and ignore functions, which allow paying subscribers to control future messages from specific paying subscribers.

Hot Lists and Favorites. “Hot Lists” enable members to see who is interested in them and to save those favorite members in which they have an interest. Lists include (1) who has viewed their profile, (2) their favorites and (3) who has emailed them. Members can maintain their favorites on a list and add their own customized notes.

Mobile Chat. Members can utilize our mobile applications to communicate with each other through in-app mobile messaging.

Instant Message. Paying subscribers can use our instant messaging system to communicate with other subscribers in real-time. This allows subscribers to communicate directly with another subscriber online at the same time instantly.

Ice Breakers. Members can send pre-packaged opening remarks, referred to on the sites as “flirts” and “smiles,” to other members or paying subscribers.

Click! Our patented Click! feature - Secret Admirer connects members who think they would be compatible with each other. A member clicks “yes,” “no” or “maybe” in another member’s profile. When two members click “yes” in each other’s profiles, our patented feature sends an email to both of them alerting them of the match.

Media Properties. We operate four different media properties primarily focused on serving the Christian community. These properties are designed to strengthen the Christian community and extend our relationship with our ChristianMingle users. Revenue generated from these properties today is driven by online advertising; however, we may develop other revenue streams on these or future complementary properties such as subscription services and merchandise sales. Our current portfolio of media properties include:

Media Property	Primary Content
Believe.com	Christian lifestyle portal
Faith.com	Inspirational videos
DailyBibleVerse.com	Send a daily bible verse
ChristianCard.net	Christian eCard and wallpaper site

Business Strategy

We intend to grow revenue by driving additional traffic to our websites and mobile applications, increasing the number and percentage of our members who convert to paying subscribers, and expanding advertising sales on select properties.

Drive traffic. We believe there are opportunities to drive additional traffic to our websites through integrated and targeted marketing initiatives within the communities we serve.

Integrated and targeted marketing. We believe targeting potential members with consistent and compelling marketing messages, delivered through a broad mix of marketing channels, will be effective in driving more traffic and a higher percentage of relationship-oriented singles to our websites. We intend to use a variety of channels to build our brands and increase our base of subscribers including online and offline advertising, customer relationship management tools, public relations, promotional alliances and special events.

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Increase Conversion Rates. We believe a growth opportunity lies in our ability to convert more of our members into paying subscribers. We plan to achieve this increase in conversion by focusing on:

• **Improved member features.** We believe enhanced member communications is a key component to growing our business. We continue to focus on improving and enhancing our platform features and functionality to encourage communication among members. We have also invested in our search and matching capabilities to further improve the user experience of our members. As engagement with these features increases, members have an increased likelihood of finding a compatible partner. We believe that by driving more user connections, we are able to raise customer satisfaction and, in turn, drive organic awareness of our websites and mobile applications.

- **Improved testing and optimization.** Efforts to modernize our technological infrastructure began in 2015 when we deployed a number of tools that allowed us to more efficiently optimize key product features and marketing initiatives. We believe that continuous improvement is key to both providing the best possible experience for our members and maximizing the return on our marketing investments.

• **Leveraging strong customer service.** Each time a member or a potential member is in touch with our customer service center by email or phone, he or she represents a potential new or returning paying subscriber. We continuously train our customer service personnel on identifying these opportunities and capturing these sales.

Sales and Marketing

We engage in a variety of marketing activities intended to drive consumer traffic to our websites and allow us the opportunity to introduce our products and services to prospective visitors, members and subscribers. Our marketing efforts are focused online and offline. Our online marketing approach employs a combination of banner and other display advertising. We also rely on search engine marketing and direct email campaigns to attract potential members and paying subscribers, and use a network of online affiliates, through which we acquire traffic.

We supplement our online marketing by employing a variety of offline marketing and business development activities. These include print, television, public relations, event sponsorship and promotional alliances. We believe a more consistent, targeted marketing message, delivered through an array of available marketing channels, will improve consumer awareness of our brands, drive more traffic to our websites and, therefore, increase the number of visitors, members and paying subscribers.

Customer Service

Our multi-lingual call center and email support teams monitor our sites for fraudulent activity, assist members with billing questions, help members complete personal profiles and answer technical questions. Customer service representatives receive ongoing training in an effort to better personalize the experience for members and paying subscribers who call or email us and to capitalize on upselling opportunities.

Technology

Our internal product teams are focused on the development and maintenance of products in addition to building and managing our software and hardware infrastructure. We intend to continue investing in the development of new products, such as mobile applications, and enhancing the efficiency and functionality of our existing products and infrastructure.

Our network infrastructure and operations are designed to deliver high levels of availability, performance, security and scalability in a cost-effective manner. We operate web and database servers co-located at a third party data center facility in Irvine, California.

Intellectual Property

We rely on a combination of patent, trademark, copyright and trade secret laws in the United States and other jurisdictions, as well as confidentiality procedures and contractual provisions to protect our proprietary technology and our brands. We also enter into confidentiality and invention assignment agreements with our employees and consultants and confidentiality agreements with other third parties.

Spark Networks, Spark, JDate, ChristianMingle and BlackSingles.com are registered trademarks in the United States. Spark Networks, JDate and ChristianMingle are registered trademarks in the EU. JDate and ChristianMingle are registered trademarks in Australia. JDate is also a registered trademark in Israel and Canada. Our rights to these registered trademarks are perpetual as long as we use them and renew them periodically. We also have a number of other registered and unregistered trademarks. We hold two United States patents for our Click! technology, the first of which expired on January 24, 2017, that pertain to an automated process for confidentially determining whether people feel mutual attraction or have mutual interests. Click! is important to our business in that it is a method and apparatus for detection of reciprocal interests or feelings and subsequent notification of such results. The patents describe the method and apparatus for the identification of a person's level of attraction and the subsequent notification when the feeling or attraction is mutual.

Competition

We operate in a highly competitive environment with minimal barriers to entry. We believe the primary competitive factors in creating a community on the Internet are functionality, brand recognition, reputation, critical mass of members, member affinity and loyalty, ease-of-use, quality of service and reliability. We compete with a number of large and small companies, including vertically integrated Internet portals and specialty-focused media companies that provide online and offline products and services to the markets we serve. Our principal online personals services competitors include Match Group, which operates the Match.com, OkCupid, Plenty of Fish, and Tinder properties, and eHarmony and Zoosk. In addition, we face competition from new entrants that have recently offered free and freemium mobile applications such as Bumble and Hinge, as well as social networking sites such as Facebook.

Government Regulation

Our business is regulated by diverse and evolving laws and governmental authorities in the United States and other countries in which we operate. We are subject to laws and regulations related to Internet communications, privacy, consumer protection, security and data protection, intellectual property rights, commerce, taxation, entertainment, recruiting and advertising. These laws and regulations are becoming more prevalent, and new laws and regulations are under consideration by the United States Congress, state legislatures and foreign governments. Any failure by us to comply with existing laws and regulations may subject us to liabilities. New laws and regulations governing such matters could be enacted or amendments may be made to existing regulations at any time that could adversely impact our services. Plus, legal uncertainties surrounding domestic and foreign government regulations could increase our costs of doing business, require us to revise our services, prevent us from delivering our services over the Internet or slow the growth of the Internet, any of which could materially adversely affect our business, financial condition and results of operations.

Employees

As of December 31, 2016, we had 66 full-time and 43 part-time employees. Virtually all of our part-time employees are dedicated to our customer service department. We are not subject to any collective bargaining agreements and we believe our relationship with our employees is good.

ITEM 1A. RISK FACTORS

You should carefully consider the risks described below together with all of the other information included in this report before making an investment decision. The risks described below are the material risks that we are currently aware of that we are facing. In addition, other sections of this report may include additional factors that could adversely impact our business and operating results. If any of the following risks actually occurs, our business, financial condition or results of operations could be materially adversely affected. In that case, the trading price of our common stock could decline and you may lose all or part of your investment.

Risks Related to Our Business

Our growth rates may decline and our operating margins could deteriorate; our business, financial condition and results of operations may be adversely affected by a slowdown or contraction in the economy.

Between 2007 and 2010, and during 2014 through 2016, our revenue declined and it may decline again in the future. It is possible our operating margins will deteriorate if revenue growth does not exceed planned increases in expenditures for all aspects of our business in an increasingly competitive environment, including sales and marketing, development, technical operations and general and administrative expenses.

Our member and paying subscriber base is composed of individual consumers and in the event of a continued prolonged economic downturn in the United States or in our international markets in which spending by individual consumers drops significantly, our current and potential subscribers may be unable or unwilling to subscribe to our services and our business may be negatively affected. In addition, the current or future tightening of credit in financial markets could result in a decrease in demand for our products and services if subscribers do not have access to credit. To the extent the overall economy deteriorates or does not improve, we may lose existing members and paying subscribers and fail to attract new members and paying subscribers, which could adversely affect our business, financial condition and results of operations.

Our business has recently undergone significant changes, including management, personnel and business changes. If we do not effectively and successfully adapt to these changes, it could have a material adverse effect on our business.

During our third fiscal quarter of 2016, we appointed a new Chief Executive Officer and Chief Technology Officer, as well as two new members to our board of directors. In addition, we have implemented certain steps to streamline our business and control costs. As a result, we are also making significant operational changes. These significant changes have created additional pressures on existing personnel, and we have been working to adapt to operating our business in a manner that differs meaningfully from prior periods. We cannot provide assurance that these changes will lead to the desired results. If we do not effectively and successfully adapt to these changes, it could have a material adverse effect on our business.

If we do not successfully implement our new information technology platform, our financial performance could be adversely affected.

We have undertaken a process of transforming our technological infrastructure and implementing new systems that will impact our applications and websites. Implementing new systems carries substantial risk, including implementation delays, cost overruns, disruption of operations, potential loss of data or information, and lower customer satisfaction resulting in lost customers or sales. If we do not implement these systems successfully, our ability to perform key business processes could be disrupted and our financial performance could be adversely affected.

We have significant operating losses and we may incur additional losses in the future.

We have historically generated significant operating losses. As of December 31, 2016, we had an accumulated deficit of approximately \$(65.9) million. We incurred net loss of approximately \$(6.9), (\$1.4) and (\$1.1) million for the years ended December 31, 2016, 2015 and 2014, respectively. If our revenue does not grow at a substantially faster rate than our operating expenses, or if our operating expenses are higher than we anticipate, or if our revenue continues to decline but our operating expenses increase, we may not be profitable and we may incur additional losses, which could be significant.

We need to maintain or increase our number of average paying subscribers to maintain or increase our current level of revenue.

The majority of our revenue is generated by internet users that pay us a subscription fee. One of our key performance metrics focuses on the average number of paying subscribers in a given period. The number of monthly average paying subscribers is calculated as the sum of the paying subscribers at the beginning and end of the month, divided by two. Average paying subscribers for periods longer than one month are calculated as the sum of the average paying subscribers for each month, divided by the number of months in the period. Internet users, in general, and users of online personals services specifically, freely navigate and use the services offered by a variety of websites. We cannot assure you that our monthly average paying subscriber numbers will remain at consistent levels, and they may decrease in the future, thus decreasing our revenue. In 2016, average paying subscribers decreased 12.4% and revenue also decreased 27.1% compared to 2015. If we do not constantly attract new paying subscribers at a faster rate than subscription terminations, our average paying subscribers will decrease and we will not be able to maintain or increase our current level of revenue.

Our business depends on establishing and maintaining strong brands and if we are not able to maintain and enhance our brands, we may be unable to expand or maintain our member and paying subscriber bases.

We believe that establishing and maintaining our brands is critical to our efforts to attract and expand our member and paying subscriber bases. We believe that the importance of brand recognition will continue to increase, given the growing number of Internet sites and the low barriers to entry for companies offering online personals services. To attract and retain members and paying subscribers, and to promote and maintain our brands in response to competitive pressures, we may have to substantially increase our financial commitment to creating and maintaining distinct brand loyalty among these groups. If visitors, members and paying subscribers to our websites and our affiliate and distribution associates do not perceive our existing services to be of high quality, or if we introduce new services or enter into new business ventures that are not favorably received by such parties, the value of our brands could be diluted, thereby decreasing the attractiveness of our websites to such parties. As a result, our results of operations may be adversely affected by decreased brand recognition.

Our growth and profitability rely, in part, on our ability to attract and retain users through cost-effective marketing efforts. Any failure in these efforts could adversely affect our business, financial condition, and results of operations.

Attracting and retaining users for our dating products involves considerable expenditures for online and offline marketing. Historically, we have had to increase our marketing expenditures over time in order to attract and retain users and sustain our growth.

Evolving consumer behavior can affect the availability of profitable marketing opportunities. For example, as traditional television viewership declines and as consumers spend more time on mobile devices rather than desktop computers, the reach of many of our traditional advertising channels is contracting. Similarly, as consumers communicate less via email and more via text messaging and other virtual means, the reach of email campaigns designed to attract new and repeat users (and retain current users) for our dating products is adversely impacted. To continue to reach potential users and grow our businesses, we must identify and devote more of our overall marketing expenditures to newer advertising channels, such as mobile and online video platforms, as well as targeted campaigns in which we communicate directly with potential, former, and current users via new virtual means. Generally, the opportunities in and sophistication of newer advertising channels are relatively undeveloped and unproven, and there can be no assurance that we will be able to continue to appropriately manage and fine-tune our marketing efforts in response to these and other trends in the advertising industry. Any failure to do so could adversely affect our business, financial condition, and results of operations.

Moreover, the Company is currently reworking its technology systems to provide for an ability to enable it to better track the success and profitability of marketing efforts. It may be determined that none of the current or historical marketing channels or efforts are profitable, which would lead the Company to a position where it needs a completely new marketing strategy. There can be no assurances that the Company will be able to identify or implement a marketing strategy that profitably adds customers. In such a case, our business, operations and prospects would be materially and negatively impacted.

If our efforts to attract new members, convert members into paying subscribers and retain our paying subscribers are not successful, our revenue and operating results will suffer.

Our future growth depends on our ability to attract new members, convert members into paying subscribers and retain our paying subscribers. This in turn depends on our ability to deliver a high-quality online personals experience to these members and paying subscribers. As a result, we must continue to invest significant resources in order to enhance our existing products and services and introduce new high-quality products and services that people will use. If we are unable to predict user preferences or industry changes, or if we are unable to modify our products and services on a timely basis, we may lose existing members and paying subscribers and may fail to attract new members and paying subscribers. Our revenue and expenses will also be adversely affected if our innovations are not responsive to the needs of our members and paying subscribers or are not brought to market in an effective or timely manner.

Our subscriber acquisition costs vary depending upon prevailing market conditions and may increase significantly in the future.

Costs for us to acquire paying subscribers are dependent, in part, upon our ability to purchase advertising at a reasonable cost. Our advertising costs vary over time, depending upon a number of factors, many of which are beyond our control. Historically, we have used online and offline advertising as the primary means of marketing our services. During 2016, our cost of revenue substantially decreased, primarily as a result of lower direct marketing expenses related to our Christian Networks.

Despite a slow economy, costs of online and/or offline advertising may continue to increase. If we are not able to reduce our other operating costs, increase our paying subscriber base or increase revenue per paying subscriber to offset these increases, our profitability will be adversely affected.

In addition, our costs to acquire subscribers may increase if we raise prices on our websites or attempt to further monetize our mobile applications, as potential customers may be slower or more reluctant to purchase higher-priced services.

Competition presents an ongoing threat to the performance of our business.

The dating industry is intensively competitive, with a consistent stream of new products and entrants. Some of our competitors may enjoy better competitive positions in certain geographical regions or user demographics that we currently serve or may serve in the future. We expect competition in the online personals business to continue to increase because there are no substantial barriers to entry. We believe our ability to compete depends upon many factors both within and beyond our control, including the following:

- the size and diversity of our member and paying subscriber bases;
- the timing and market acceptance of our products and services, including the developments and enhancements to those products and services relative to those offered by our competitors;
- customer service and support efforts;
- selling and marketing efforts; and

our brand strength in the marketplace relative to our competitors.

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We compete with traditional personals services, as well as newspapers, magazines and other traditional media companies that provide personals services. We also compete with a number of large and small companies, including Internet portals and specialty-focused media companies that provide online and offline products and services to the markets we serve. Our principal online personals services competitors include Match Group, which operates the Match.com, OkCupid, Plenty of Fish, and Tinder properties, and eHarmony and Zoosk. In addition, we face competition from multiple mobile-based apps such as Bumble and Hinge, and social networking sites such as Facebook. Many of our current and potential competitors have longer operating histories, significantly greater financial, technical, marketing and other resources and larger customer bases than we do. These factors may allow our competitors to respond more quickly than we can to new or emerging technologies and changes in customer preferences. These competitors may engage in more extensive research and development efforts, undertake more far-reaching marketing campaigns and adopt more aggressive pricing policies that may allow them to build larger member and paying subscriber bases than ours. Our competitors may develop products or services that are equal or superior to our products and services or that achieve greater market acceptance than our products and services. These activities could attract members and paying subscribers away from our websites and reduce our market share.

In addition, current and potential competitors are making, and are expected to continue to make, strategic acquisitions or establishing cooperatives and, in some cases, establishing exclusive relationships with significant companies or competitors to expand their businesses or to offer more comprehensive products and services. To the extent these competitors or potential competitors establish exclusive relationships with major portals, search engines and Internet Service Providers, or ISPs, our ability to reach potential members through online advertising may be restricted. Any of these competitors could cause us difficulty in attracting and retaining members and converting members into paying subscribers and could jeopardize our existing affiliate program and relationships with portals, search engines, ISPs and other online properties.

Our efforts to capitalize upon opportunities to expand into new products and services may fail and could result in a loss of capital and other valuable resources.

We may decide to expand into new products and services to increase our revenue base. If we expand into such offerings, management's time and attention will be less focused on our existing businesses and will require us to invest significant capital resources. The results of any expansion efforts into new products and services are unpredictable, and there is no guarantee that our efforts will have a positive effect on our revenue base. We face many risks associated with our planned expansion into new products and services, including but not limited to the following:

- competition from pre-existing competitors with significantly stronger brand recognition in the markets we enter;
- improper evaluation of the potential of such products and services;

- diversion of capital and other valuable resources away from our core business; and
- forgoing opportunities that are potentially more profitable.

If we fail to keep pace with rapid technological change, our competitive position will suffer.

We operate in a market characterized by rapidly changing technologies, evolving industry standards, frequent new product and service announcements, enhancements and changing customer demands. Accordingly, our performance will depend on our ability to adapt to rapidly changing technologies and industry standards, and our ability to continually improve the speed, performance, features, ease of use and reliability of our services in response to both evolving demands of the marketplace and competitive service and product offerings. There have been occasions when we have not been as responsive as many of our competitors in adapting our services to changing industry standards and the needs of our members and paying subscribers. Our industry has been subject to constant innovation and competition. New features are introduced by one competitor, and if they are perceived as attractive to users, other competitors replicate such new features. Over the last few years, such new feature introductions in the industry have included instant messaging, message boards, E-cards, personality profiles and mobile content delivery. Introducing new technologies into our systems involves numerous technical challenges, substantial amounts of capital and personnel resources and often takes many months to complete. We intend to continue to devote efforts and funds toward the development of additional technologies and services. For example, in 2016 and 2015 we introduced a number of new features, and we anticipate the introduction of additional features in 2017 and beyond. We may not be able to effectively integrate new technologies into our websites on a timely basis or at all, which may degrade the responsiveness and speed of our websites. Such technologies, even if integrated, may not function as expected.

We secured a \$10.0 million revolving credit facility, which could restrict our ability to use our operating cash flow for the growth of our business.

In January 2016, we entered into an initial credit agreement with Western Alliance Bank. If we are unable to pay our debts as they become due, we will be required to pursue one or more alternative strategies, such as refinancing or restructuring our indebtedness, selling additional debt or equity securities or selling assets. We may not be able to refinance our debt or issue additional debt or equity securities on favorable terms, if at all, and if we must sell our assets, it may negatively affect our ability to generate future revenue. If we are unable to meet our obligations as they become due or to comply with various financial covenants contained in the revolving credit facility, this could constitute an event of default.

Our obligations under the credit facility are secured by a lien on substantially all of the assets of Spark Networks USA, LLC, which is the borrower under the credit facility. Additionally, the credit facility is guaranteed by Spark Networks, Inc. and a number of our subsidiaries. Any default under the credit facility, could result in an acceleration of payment of all outstanding debt owed at the time, which could materially and adversely affect our financial condition.

Our revolving credit facility has certain covenants that could restrict how we operate our business.

The terms of our revolving credit facility contain various provisions that limit our ability to, among other things:

- incur or guarantee additional debt;
- incur capital expenditures;
- receive dividends or distributions from our subsidiaries;
- make investments and other restricted payments;
- make dividend payments or redeem equity securities;
- grant liens;
- acquire other entities;

transfer or sell assets;
engage in different lines of business; and
consolidate, merge or transfer all or substantially all of our assets.

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These covenants may affect our ability to operate and finance our business as we deem appropriate. If we are unable to meet our obligations as they become due or to comply with various financial covenants contained in the revolving credit facility, this could constitute an event of default.

We may not obtain any benefits from the Management Services Agreement with PEAK6.

As described in Note 12 to our Consolidated Financial Statements included in this annual report, we entered into a Management Services Agreement with PEAK6 in August 2016. We believe that the receipt of services from PEAK6 as contemplated in the Management Services Agreement will benefit the Company and its business operations. However, there can be no assurances that any services from PEAK6 will actually provide the expected benefits and, as a result, our business and operations may not improve and could deteriorate.

If we are unable to attract, retain and motivate key personnel or hire qualified personnel, or such personnel do not work well together, our growth prospects and profitability will be harmed.

Our performance is largely dependent on the talents and efforts of highly skilled individuals. The loss of any of our management or key personnel could seriously harm our business.

We may also encounter difficulties in recruiting personnel as we become a more mature company in a competitive industry. Competition in our industry for personnel is intense, and we are aware that our competitors have directly targeted our employees. We do not have non-competition agreements with most employees and, even in cases where we do, these agreements are of limited enforceability in California. We also do not maintain any key-person life insurance policies on our executives. The incentives to attract, retain and motivate employees provided by our option or restricted stock grants or by future arrangements, such as cash bonuses, may not be as effective as they have been in the past. If we do not succeed in attracting necessary personnel or retaining and motivating existing personnel, we may be unable to grow effectively.

Our business depends on our server and network hardware and software and our ability to obtain network capacity; our current safeguard systems may be inadequate to prevent an interruption in the availability of our services.

The performance of our server and networking hardware and software infrastructure is critical to our business and reputation, to our ability to attract visitors and members to our websites, to convert them into paying subscribers and to retain paying subscribers. An unexpected and/or substantial increase in the use of our websites could strain the capacity of our systems, which could lead to a slower response time or system failures. Although we have not recently experienced any significant delays, any future slowdowns or system failures could adversely affect the speed and responsiveness of our websites and would diminish the experience for our visitors, members and paying subscribers. We face risks related to our ability to scale up to potential increased customer levels while maintaining superior performance. If the usage of our websites substantially increases, we may need to purchase additional servers and networking equipment and services to maintain adequate data transmission speeds, the availability of which may be limited or the cost of which may be significant. Any system failure that causes an interruption in service or a decrease in the responsiveness of our websites could reduce traffic on our websites and, if sustained or repeated, could impair our reputation and the attractiveness of our brands as well as reduce revenue and negatively impact our operating results.

We are also in the process of integrating our hardware systems and software applications between the JDate.com and ChristianMingle.com segments. There can be no assurance that such integration will not cause disruptions in our business, and any such disruption could have a material adverse effect on our results of operations and financial condition. Further, any delay in the timing could decrease and/or delay our expense savings expected in respect of such integration, and any such disruption could have a material adverse effect on our results of operations and

financial condition.

Furthermore, we rely on many different hardware systems and software applications, some of which have been developed internally. If these hardware systems or software applications fail, it would adversely affect our ability to provide our services. If we are unable to protect our data from loss or electronic or magnetic corruption, or if we receive a significant unexpected increase in usage and are not able to rapidly expand our transaction-processing systems and network infrastructure without any systems interruptions, it could seriously harm our business and reputation. We have experienced occasional systems interruptions in the past as a result of unexpected increases in usage, and we cannot assure you that we will not incur similar or more serious interruptions in the future. From time to time, our company and our websites may be subject to delays and interruptions due to software viruses, or variants thereof, such as internet worms.

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In addition, we do not have a “high availability” disaster recovery system, which means in the event of any catastrophic failure involving our websites, we may be unable to serve our web traffic for a significant period of time. Our websites primarily operate from a single site located in Southern California. Any system failure, including network, software or hardware failure, that causes an interruption in the delivery of our websites and services or a decrease in responsiveness of our services would result in reduced visitor traffic, reduced revenue and would adversely affect our reputation and brands.

We may not be able to protect our systems, infrastructures and technologies from cyber attacks. In addition, we may be adversely affected by cyber attacks experienced by third parties. Any disruption of our systems, infrastructures and technologies, or compromise of our user data or other information, due to cyber attacks could have an adverse effect on our business, reputation, brands, financial condition and results of operations.

Our reputation and ability to attract, retain and serve our members is dependent upon the reliable performance and security of our computer systems and those of third parties that we utilize in our operations and the protection of confidential information about the Company and sensitive information provided by our members. The incidence of malicious technology-related events, such as cyber attacks, computer hacking, computer viruses, worms or other destructive or disruptive software, distributed denial of service attacks or other malicious activities (or any combination of these events) is on the rise worldwide and constantly evolving. From time to time, we may become the victim of these types of attacks.

Our computer systems and those of third parties we use in our operations are vulnerable to cybersecurity risks, including cyber attacks such as computer viruses, denial of service attacks, physical or electronic break-ins and similar disruptions. These systems periodically experience directed attacks intended to lead to interruptions and delays in our service and operations as well as loss, misuse or theft of data. Any attempt by hackers to obtain our data, disrupt our service, or otherwise access our systems, or those of third parties we use, if successful, could harm our business, be expensive to remedy and damage our reputation. While we continuously develop and maintain systems to detect and prevent events of this nature from impacting our various businesses, these efforts are costly and require ongoing monitoring and updating as technologies change and efforts to overcome preventative security measures become more sophisticated. Despite our efforts, we cannot assure you that these events will not occur in the future and if they do occur, will not have an adverse effect on our business, financial condition and results of operations.

Furthermore, we may become the victim of security breaches, such as the misappropriation, misuse, leakage, falsification or accidental release or loss of user, customer or vendor data maintained in our information technology systems or those of third parties with whom we do business (or upon whom we otherwise rely in connection with our day to day operations).

Any cyber attack or security breach we experience could prevent us from providing our products and services, damage our reputation, erode our brands and/or be costly to remedy, as well as result in a degradation of our products and services and/or cause damage to our systems, infrastructures, technologies and data. Even if we do not experience such events, the impact of any such events experienced by third parties with whom we do business (or upon whom we otherwise rely in connection with our day to day operations) could have a similar effect. Moreover, even cyber attacks and security breaches that do not impact us directly may result in a loss of consumer confidence generally, which could result in decreased likelihood of the use of our products and services.

We depend, in part, upon arrangements with third parties to drive traffic to our various websites.

We engage in a variety of activities designed to attract traffic to our various websites and convert visitors into members and paying subscribers. How successful we are in these efforts depends, in part, upon our continued ability to enter into arrangements with third parties to drive traffic to our various websites and our oversight of such third parties to ensure that they are appropriately communicating with online users. Pursuant to these arrangements, third parties generally promote our services on their websites or through e-mail campaigns and we pay them based upon a variety of arrangements (cost per registration, cost per one thousand impressions, a percentage of sales, etc.) Depending on how a third party communicates with online users via email, third-party email service providers could treat such email campaign as spam, and ultimately limit our ability to communicate with our members and paying subscribers via email.

These arrangements are generally not exclusive, are short term in nature and are generally terminable by either party given notice. If existing arrangements with third parties are terminated (or are not renewed upon their expiration) and we fail to replace this traffic and related revenues, or if we are unable to enter into new arrangements with existing and/or new third parties in response to industry trends, or if such third parties improperly manage email campaigns, our business, financial condition and results of operations could be adversely affected.

We rely on a number of third-party providers and their failure or unwillingness to continue to perform could harm us.

We rely on third parties to provide important services and technologies to us, including third parties that manage and monitor our offsite data center located in Southern California, ISPs, search engine marketing providers and credit card processors. In addition, we license technologies from third parties to facilitate our ability to provide our services. Any failure on our part to comply with the terms of these licenses could result in the loss of our rights to continue using the licensed technology, and we could experience difficulties obtaining licenses for alternative technologies. Furthermore, any failure of these third parties to provide these and other services, or errors, failures, interruptions or delays associated with licensed technologies, could significantly harm our business. Any financial or other difficulties our providers face may have negative effects on our business, the nature and extent of which we cannot predict. Except to the extent of the terms of our contracts with such third party providers, we exercise little or no control over them, which increases our vulnerability to problems with the services and technologies they provide and license to us. In addition, if any fees charged by third-party providers were to substantially increase, such as if ISPs began charging us for emails sent by our paying subscribers to other members or paying subscribers, we could incur significant additional losses.

We may not be effective in protecting our Internet domain names or proprietary rights upon which our business relies or in avoiding intellectual property infringement claims.

We regard substantial elements of our websites and the underlying technology as proprietary, and attempt to protect them by relying on trademark, service mark, copyright, patent and trade secret laws and restrictions on disclosure and transferring title and other methods. We also generally enter into confidentiality agreements with our employees and consultants, and generally seek to control access to and distribution of our technology, documentation and other proprietary information. Despite these precautions, it may be possible for a third party to copy or otherwise obtain and use our proprietary information without authorization or to develop similar or superior technology independently. Effective trademark, service mark, copyright, patent and trade secret protection may not be available in every country in which our services are distributed or made available through the Internet, and policing unauthorized use of our proprietary information is difficult. Any such misappropriation or development of similar or superior technology by third parties could adversely impact our profitability and our future financial results.

We believe that our websites, services, trademarks, patent and other proprietary technologies do not infringe upon the rights of third parties. However, there can be no assurance that our business activities do not and will not infringe upon the proprietary rights of others, or that other parties will not assert infringement claims against us. We are aware that other parties utilize the “Spark” name, or other marks that incorporate it, and those parties may have rights to such marks that are superior to ours. From time to time, we have been, and expect to continue to be, subject to claims in the ordinary course of business including claims of alleged infringement of the trademarks, service marks and other intellectual property rights of third parties by us. Although such claims have not resulted in any significant litigation or had a material adverse effect on our business to date, any such claims and resultant litigation might subject us to temporary injunctive restrictions on the use of our products, services or brand names and could result in significant liability for damages for intellectual property infringement, require us to enter into royalty agreements, or restrict us from using infringing software, services, trademarks, patents or technologies in the future. Even if not meritorious, such litigation could be time-consuming and expensive and could result in the diversion of management’s time and attention away from our day-to-day business.

We currently hold various web domain names related to our brands and in the future may acquire new web domain names. The regulation of domain names in the United States and in foreign countries is subject to change. Governing bodies may establish additional top level domains, appoint additional domain name registrars or modify the requirements for holding domain names. As a result, we may be unable to acquire or maintain relevant domain names in all countries in which we conduct business. Furthermore, the relationship between regulations governing domain

names and laws protecting trademarks and similar proprietary rights is unclear. We may be unable to prevent third parties from acquiring domain names that are similar to, infringe upon or otherwise decrease the value of our existing trademarks and other proprietary rights or those we may seek to acquire. Any such inability to protect ourselves could cause us to lose a significant portion of our members and paying subscribers to our competitors.

We may face potential liability, loss of users and damage to our reputation for violation of our privacy policy or privacy laws and regulations or be required to change our business practices in an adverse manner.

Our privacy policy prohibits the sale or disclosure to any third party of any member's personal identifying information, except to the extent expressly set forth in the policy. Growing public concern about privacy and the collection, distribution and use of information about individuals may subject us to increased regulatory scrutiny and/or litigation. In the past, the Federal Trade Commission has investigated companies that have used personally identifiable information without permission or in violation of a stated privacy policy. If we are accused of violating the stated terms of our privacy policy, we may be forced to expend significant amounts of financial and managerial resources to defend against these accusations and we may face potential liability. Our membership database holds confidential information concerning our members, and we could be sued if any of that information is misappropriated or if a court determines that we have failed to protect that information.

In addition, our affiliates handle personally identifiable information pertaining to our members and paying subscribers. Both we and our affiliates are subject to laws and regulations related to Internet communications, consumer protection, advertising, privacy, security and data protection. For example, we are subject to the CAN-SPAM Act of 2003, California's Information Practice Act, which requires notification to users when there is a security breach of personal data, and other state regulations that impose additional requirements on data protection, such as the requirement to encrypt data sent over the internet. If we or our affiliates are found to be in violation of these laws and regulations, we may become subject to administrative fines or litigation or be required to change our data practices, which could materially increase our expenses, adversely affect our results of operations and cause the value of our securities to decline.

Proposed legislation concerning data protection is currently pending at the U.S. federal and state level as well as in certain foreign jurisdiction. In addition, the interpretation and application of data protection laws in Europe, the United States and elsewhere are still uncertain. It is possible that these laws may be interpreted and applied in a manner that is inconsistent with our data practices. If so, in addition to the possibility of fines, this could result in an order requiring that we change our data practices, which could have an adverse effect on our business. Complying with these laws as they evolve could cause us to incur substantial costs or require us to change our business practices in a manner adverse to our business.

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

We may be sued for defamation, civil rights infringement, negligence, copyright or trademark infringement, invasion of privacy, personal injury, product liability or under other legal theories relating to information that is published or made available on our websites and the other sites linked to it. These types of claims have been brought, sometimes successfully, against online services in the past. We also offer messaging services on our websites and send emails directly and through third parties, which may subject us to potential risks, such as liabilities or claims resulting from unsolicited email or spamming, lost or misdirected messages, security breaches, illegal or fraudulent use of email or personal information or interruptions or delays in email service. Our insurance does not specifically provide for coverage of these types of claims and, therefore, may be inadequate to protect us against them. In addition, we could incur significant costs in investigating and defending such claims, even if we ultimately are not held liable. If any of these events occurs, our revenue could be materially adversely affected or we could incur significant additional expense, and the market price of our securities may decline.

Our quarterly results may fluctuate because of many factors and, as a result, investors should not rely on quarterly operating results as indicative of future results.

Fluctuations in operating results or the failure of operating results to meet the expectations of public market analysts and investors may negatively impact the value of our common stock. Quarterly operating results may fluctuate in the future due to a variety of factors that could affect revenue or expenses in any particular quarter. Fluctuations in quarterly operating results could cause the value of our securities to decline. Investors should not rely on quarter-to-quarter comparisons of results of operations as an indication of future performance. Factors that may affect our quarterly results include:

- the demand for, and acceptance of, our online personals services and enhancements to these services;
- the timing and amount of our subscription revenue;
- the introduction, development, timing, competitive pricing and market acceptance of our websites and services and those of our competitors;
- the magnitude and timing of marketing initiatives and capital expenditures relating to expansion of our operations;
- the cost and timing of online and offline advertising and other marketing efforts;

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the maintenance and development of relationships with portals, search engines, ISPs and other web properties and other entities capable of attracting potential members and paying subscribers to our websites;

- technical difficulties, system failures, system security breaches, or downtime of the Internet, in general, or of our products and services, in particular;
- costs related to any acquisitions or dispositions of technologies or businesses;
- fluctuations in foreign exchange rates; and
- general economic conditions, as well as those specific to the Internet, online personals and related industries.

As a result of the factors listed above and because the online personals business is still immature, making it difficult to predict consumer demand, it is possible that in future periods results of operations may be below the expectations of public market analysts and investors. This could cause the market price of our securities to decline.

Adverse capital and credit market conditions could limit our access to capital and increase our cost of capital, which may significantly affect our ability to meet liquidity needs.

The capital and credit markets have been experiencing extreme volatility over the last few years. In some cases, the markets have exerted downward pressure on availability of liquidity and credit capacity for certain issuers. Without sufficient liquidity, we may be forced to curtail certain operations and may be unable to operate our business as we deem appropriate. Disruptions, uncertainty or volatility in the capital and credit markets may also limit our access to capital required to operate our business. Such market conditions may limit our ability to replace, in a timely manner, maturing liabilities and access the capital necessary to operate and grow our business. As such, we may be forced to delay raising capital or bear an unattractive cost of capital which could decrease our profitability and significantly reduce our financial flexibility. Our results of operations, financial condition, cash flows and capital position could be materially adversely affected by disruptions in the financial markets.

Goodwill, intangible assets and other long-lived assets are subject to impairment risk.

We review the potential impairment of goodwill and indefinite-lived intangible assets at least annually, or more frequently if events or changes in circumstances indicate that the carrying value may not be recoverable and test property, plant and equipment and other intangible assets for impairment whenever changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

Indicators that may signal that an asset has become impaired include a significant decline in actual or projected revenue, a significant decline in the market value of our common stock, a significant decline in performance of certain acquired companies relative to our original projections, an excess of our net book value over our market value, a significant decline in our operating results relative to our operating forecasts, a significant change in the manner of our use of acquired assets or the strategy for our overall business, a significant decrease in the fair value of an asset, a shift in technology demands and development, or a significant turnover in key management or other personnel.

The assessment for potential impairment of the Company's goodwill, intangible assets or other long-term assets requires management to make judgments on a number of significant estimates and assumptions, including projected cash flows, discount rates, projected long-term growth rates and terminal values. The Company may be required to record a significant charge in its consolidated financial statements during the period in which any impairment of its goodwill, intangible assets or other long-term assets is identified and this could negatively impact the Company's financial condition and results of operations. Changes in management estimates and assumptions as they relate to valuation of goodwill, intangible assets or other long-lived assets could affect the Company's financial condition or results of operations in the future.

We may need additional capital to finance our growth or to compete, which may cause dilution to existing stockholders or limit our flexibility in conducting our business activities.

We currently anticipate that existing cash and cash equivalents and cash flow from operations will be sufficient to meet our anticipated needs for working capital, operating expenses and capital expenditures for at least the next twelve months. However, we may need to raise additional capital in the future to fund expansion, whether in new vertical affinity or geographic markets, develop newer or enhanced services, respond to competitive pressures or acquire complementary businesses, technologies or services. Such additional financing may not be available on terms acceptable to us or at all. To the extent that we raise additional capital by issuing equity securities, our stockholders may experience substantial dilution, and to the extent we engage in additional debt financing, if available, we may become subject to additional restrictive covenants that could limit our flexibility in conducting future business activities. If additional financing is not available or not available on acceptable terms, we may not be able to fund our expansion, promote our brands, take advantage of acquisition opportunities, develop or enhance services or respond to

competitive pressures.

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If we fail to maintain an effective system of internal control over financial reporting, we may not be able to accurately report our financial results or prevent fraud. As a result, current and potential stockholders could lose confidence in our financial reporting, which would harm the value of our stock.

Effective internal controls over financial reporting are necessary for us to provide reliable financial reports, effectively prevent fraud and operate as a public company. We are required to report on an annual basis on the effectiveness of our internal controls over financial reporting. We have, in the past, discovered and may, in the future, discover areas of our internal controls over financial reporting that need improvement. If we are unable to adequately maintain or improve our internal controls over financial reporting, we may report that our internal controls are ineffective. If we cannot provide reliable financial reports or prevent fraud, our reputation and operating results would be harmed. Ineffective internal controls over financial reporting could also cause investors to lose confidence in our reported financial information which would likely have a negative effect on the trading price of our securities or could affect our ability to access the capital markets and which could result in regulatory proceedings against us by, among others, the U.S. Securities Exchange Commission.

Acquisitions could result in operating difficulties, dilution and other harmful consequences.

We have historically and may in the future further extend and develop our presence, both within the United States and internationally, partially through acquisitions of entities offering online personals services and related businesses. We have relatively limited experience acquiring companies and the companies we have acquired have been small. We have evaluated, and continue to evaluate, a wide array of potential strategic transactions. From time to time, we may engage in discussions regarding potential acquisitions, some of which may divert significant resources away from our daily operations. In addition, the process of integrating an acquired company, business or technology is risky and may create unforeseen operating difficulties and expenditures. Some areas where we may face risks include:

- the need to implement or remediate controls, procedures and policies of acquired companies that lacked appropriate controls, procedures and policies prior to the acquisition;
- diversion of management time and focus from operating our business to acquisition integration challenges;
- cultural challenges associated with integrating employees from an acquired company into our organization;
- retaining employees from the businesses we acquire; and
- the need to integrate each company's accounting, management information, human resources and other administrative systems to permit effective management.

The anticipated benefit of many of our acquisitions may not materialize. Future acquisitions could result in potentially dilutive issuances of our equity securities, the incurrence of debt, contingent liabilities or amortization expenses, or write-offs, any of which could harm our financial condition. Future acquisitions may require us to obtain additional equity or debt financing, which may not be available on favorable terms or at all.

Our limited experience outside the United States increases the risk that any international expansion efforts and operations will not be effective.

One of our strategies is to maintain and expand our presence in international markets. Although we currently have websites that directly serve the French, Israeli and United Kingdom markets, we have only limited experience with operations outside the United States. Expansion into international markets requires management time and capital resources. In addition, we face the following additional risks associated with our expansion outside the United States:

- challenges caused by distance, language and cultural differences;
- local competitors with substantially greater brand recognition, more users and more traffic than we have;
- our need to create and increase our brand recognition and improve our marketing efforts internationally and build strong relationships with local affiliates;

longer payment cycles in some countries;
credit risk and higher levels of payment fraud in some countries;
different legal and regulatory restrictions among jurisdictions;
political, social and economic instability;
potentially adverse tax consequences; and
higher costs associated with doing business internationally.

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Our international operations subject us to risks associated with currency fluctuations.

Our foreign operations may subject us to currency fluctuations and such fluctuations may adversely affect our financial position and results. However, sales and expenses to date have occurred primarily in the United States. For this reason, we have not engaged in foreign exchange hedging. Currency risk positions could change correspondingly and the use of foreign exchange hedging instruments could become necessary. Effects of exchange rate fluctuations on our financial condition, operations and profitability may depend on our ability to manage our foreign currency risks. There can be no assurance that steps taken by management to address foreign currency fluctuations will eliminate all adverse effects and, accordingly, we may suffer losses due to adverse foreign currency fluctuation.

Our business could be significantly impacted by the occurrence of natural disasters and other catastrophic events.

Our operations depend upon our ability to maintain and protect our network infrastructure, hardware systems and software applications, which are housed primarily at data centers located in Southern California that are managed by a third party. Our business is therefore susceptible to earthquakes, tsunamis and other catastrophic events, including acts of terrorism. We currently do not possess a “high availability” disaster recovery system. As a result, outages and downtime caused by natural disasters and other events out of our control, which affect our systems or data centers, could adversely affect our reputation, brands and business.

We hold a fixed amount of insurance coverage, and if we were found liable for an uninsured claim, or claim in excess of our insurance limits, we may be forced to expend significant capital to resolve the uninsured claim.

We contract for a fixed amount of insurance to cover potential risks and liabilities, including, but not limited to, cyber liability, property and casualty insurance, general liability insurance and errors and omissions liability insurance. If we decide to pursue obtaining additional insurance coverage in the future, it is possible that (1) we may not be able to get enough insurance to meet our needs; (2) we may have to pay very high premiums for the additional coverage; (3) we may not be able to acquire any insurance for certain types of business risk; or (4) we may have gaps in coverage for certain risks. This could leave us exposed to potential uninsured claims for which we could have to expend significant amounts of capital resources. Consequently, if we were found liable for a significant uninsured claim in the future, we may be forced to expend a significant amount of our operating capital to resolve the uninsured claim.

Our services may not be well-suited to many alternate web access devices, and as a result the growth of our business could be negatively affected.

The number of people who access the Internet through devices other than desktop and laptop computers, including mobile telephones, tablets, and other handheld computing devices, has increased dramatically in the past several years, and we expect this growth to continue. The smaller screen and keyboard sizes and reduced functionality currently associated with such devices may make the use of our services through such devices more difficult and generally impairs the member experience relative to access via desktop and laptop computers. If we are unable to attract and retain a substantial number of such device users to our online personals services or if we are unable to develop services that are more compatible with such devices in a timely fashion, our growth could be adversely affected.

Risks Related to Our Industry

Our network is vulnerable to security breaches and inappropriate use by Internet users, which could disrupt or deter future use of our services.

Concerns over the security of transactions conducted on the Internet and the privacy of users may inhibit the growth of the Internet and other online services generally, and online commerce services, like ours, in particular. To date, we have not experienced any material breach of our security systems; however, a failure on our part to effectively prevent security breaches could significantly harm our business, reputation and results of operations and could expose us to lawsuits by state and federal consumer protection agencies, by governmental authorities in the jurisdictions in which we operate, and by consumers. Anyone who is able to circumvent our security measures could misappropriate proprietary information, including customer credit card and personal data, cause interruptions in our operations or damage our brand and reputation. Such breach of our security measures could involve the disclosure of personally identifiable information and could expose us to a material risk of litigation, liability or governmental enforcement proceeding. We cannot assure you that our financial systems and other technology resources are completely secure from security breaches or sabotage, and we have occasionally experienced security breaches and attempts at “hacking.” We may be required to incur significant additional costs to protect against security breaches or to alleviate problems caused by such breaches. Any well-publicized compromise of our security or the security of any other Internet provider could deter people from using our services or the Internet to conduct transactions that involve transmitting confidential information or downloading sensitive materials, which could have a detrimental impact on our existing and potential customer base.

Computer viruses may cause delays or other service interruptions and could damage our reputation, affect our ability to provide our services and adversely affect our revenue. The inadvertent transmission of computer viruses could also expose us to a material risk of loss or litigation and possible liability. Moreover, if a computer virus affecting our system were highly publicized, our reputation could be significantly damaged, resulting in the loss of current and future members and paying subscribers.

We face certain risks related to the physical and emotional safety of our members and paying subscribers.

The nature of online personals services is such that we cannot control the actions of our members and paying subscribers in their communication or physical actions. There is a possibility that one or more of our members or paying subscribers could be physically or emotionally harmed following interaction with another one of our members or paying subscribers. We warn our members and paying subscribers that we do not conduct background checks on other members and paying subscribers and, given our lack of physical presence, we do not take any action to ensure personal safety on a meeting between members or paying subscribers arranged following contact initiated via our websites. If an unfortunate incident of this nature occurred in a meeting of two people following contact initiated on one of our websites or a website of one of our competitors, any resulting negative publicity could materially and adversely affect us or the online personals industry in general. Any such incident involving one of our websites or mobile applications could damage our reputation and our brands. This, in turn, could adversely affect our revenue and could cause the value of our common stock to decline. In addition, the affected members or paying subscribers could initiate legal action against us, which could cause us to incur significant expense, whether we were successful or not, and damage our reputation.

We are or may be subject to litigation and regulatory actions that may distract management and could have a material adverse effect on our financial condition and results of operations.

We are or have been a party to various litigation claims and legal proceedings, including purported class action lawsuits and litigation involving our business operations and intellectual property. We may also be subject to

regulatory actions and litigation based on our business operations. For example, we supply online personals services and in many jurisdictions, companies deemed dating service providers are subject to additional regulation, while companies that provide personals services are not generally subject to similar regulation. Because personals services and dating services can seem similar, we are exposed to potential litigation, including class action lawsuits, associated with providing our personals services. In the past, a small percentage of our members have alleged that we are a dating service provider, and, as a result, they claim that we are required to comply with regulations that include, but are not limited to, providing language in our contracts that may allow members to (1) rescind their contracts within a certain period of time, (2) demand reimbursement of a portion of the contract price if the member dies during the term of the contract and/or (3) cancel their contracts in the event of disability or relocation. If a court holds that we have provided and are providing dating services of the type the dating services regulations are intended to regulate, we may be required to comply with regulations associated with the dating services industry and be liable for any damages as a result of our past non-compliance.

Previously, we were subject to three separate yet similar class action complaints filed against us in state court alleging violations of dating service statutes—one in each of Illinois, New York and California. Although all of the complaints were dismissed and are no longer subject to appeal, the opinion in the Illinois case provided that we are subject to the Illinois Dating Services Act and, as such, our subscription agreements violate the act and are void and unenforceable. This ruling may subject us to potential liability for claims brought by the Illinois Attorney General or customers that have been injured by such violation of the statute.

We review the litigation and accrue appropriate amounts where necessary. These assessments and estimates are based on information available to management at the time and involve a significant amount of management judgment. As a result, actual outcomes or losses may differ materially from those envisioned by our current assessments and estimates. We intend to defend vigorously against any litigation claims. However, no assurance can be given that these matters will be resolved in our favor and, depending on the outcome of these disputes, we may choose to alter our business practices. Our failure to successfully defend or settle litigation claims could result in liability that, to the extent not covered by our insurance, could have a material adverse effect on our financial condition and results of operations. Furthermore, the defense of litigation claims may also be both time consuming and expensive.

We are exposed to risks associated with credit card fraud and credit payment, which, if not properly addressed, could increase our operating expenses.

We depend on the continuing availability of credit card usage to process subscriptions and this availability, in turn, depends on acceptable levels of chargebacks and fraud performance. We have suffered losses and may continue to suffer losses as a result of subscription orders placed with fraudulent credit card data, even though the associated financial institution approved payment. Under current credit card practices, a merchant is liable for fraudulent credit card transactions when, as is the case with the transactions we process, that merchant does not obtain a cardholder's signature. Our failure to adequately control fraudulent credit card transactions would result in significantly higher credit card-related costs and, therefore, increase our operating expenses and may preclude us from accepting credit cards as a means of payment.

We face risks associated with our dependence on computer and telecommunications infrastructure.

Our services are dependent upon the use of the Internet and telephone and broadband communications to provide high-capacity data transmission without system downtime. There have been instances where regional and national telecommunications outages have caused us, and other Internet businesses, to experience systems interruptions. Any additional interruptions, delays or capacity problems experienced with telephone or broadband connections could adversely affect our ability to provide services to our customers. The temporary or permanent loss of all, or a portion, of the telecommunications system could cause disruption to our business activities and result in a loss of revenue. Additionally, the telecommunications industry is subject to regulatory control. Amendments to current regulations, which could affect our telecommunications providers, could disrupt or adversely affect the profitability of our business.

In addition, if any of our current agreements with telecommunications providers were terminated, we may not be able to replace any terminated agreements with equally beneficial ones. There can be no assurance that we will be able to renew any of our current agreements when they expire or, if we are able to do so, that such renewals will be available on acceptable terms. We also do not know whether we will be able to enter into additional agreements or that any relationships, if entered into, will be on terms favorable to us.

Our business depends, in part, on the growth and maintenance of the Internet, and our ability to provide services to our members and paying subscribers may be limited by outages, interruptions and diminished capacity of the Internet.

Our performance will depend, in part, on the continued growth and maintenance of the Internet. This includes maintenance of a reliable network backbone with the necessary speed, data capacity and security for providing reliable Internet services. Internet infrastructure may be unable to support the demands placed on it if the number of Internet users continues to increase, or if existing or future Internet users access the Internet more often or increase their bandwidth requirements. In addition, viruses, worms and similar programs may harm the performance of the Internet. We have no control over the third-party telecommunications, cable or other providers of access services to the Internet that our members and paying subscribers rely upon. There have been instances where regional and

national telecommunications outages have caused us to experience service interruptions during which our members and paying subscribers could not access our services. Any additional interruptions, delays or capacity problems experienced with any points of access between the Internet and our members could adversely affect our ability to provide services reliably to our members and paying subscribers. The temporary or permanent loss of all, or a portion, of our services on the Internet, the Internet infrastructure generally, or our members' and paying subscribers' ability to access the Internet could disrupt our business activities, harm our business reputation, and result in a loss of revenue. Additionally, the Internet, electronic communications and telecommunications industries are subject to federal, state and foreign governmental regulation. New laws and regulations governing such matters could be enacted or amendments may be made to existing regulations at any time that could adversely impact our services. Any such new laws, regulations or amendments to existing regulations could disrupt or adversely affect the profitability of our business.

We rely on third-party platforms such as the Apple App Store and the Google Play Store to distribute our mobile applications and collect revenue. If we are unable to maintain a good relationship with such platform providers, if their terms and conditions or pricing changed to our detriment, if we violate, or if a platform provider believes that we have violated, the terms and conditions of its platform, or if any of these platforms were unavailable for a prolonged period of time, our business will suffer.

With the launch of our portfolio of mobile applications, we have recognized an increasing amount of revenue from distribution of our subscriptions on the Apple App Store and the Google Play Store, where we rely on the payments processing systems of these platform providers. We are subject to their standard terms and conditions for application developers, which govern the promotion, distribution and operation of applications on their platforms. In addition, if we violate, or if a platform provider believes that we have violated, its terms and conditions, the particular platform provider may discontinue or limit our access to that platform, which would harm our business. Our business would be harmed if they discontinue or limit our access to their platforms, if their platforms decline in popularity, if they modify their current discovery mechanisms, communication channels available to developers, respective terms of service or other policies, including fees, or change how the personal information of subscribers is made available to developers or develop their own competitive offerings.

We are subject to burdensome government regulations and legal uncertainties affecting the Internet that could adversely affect our business.

Our business is regulated by diverse and evolving laws and governmental authorities in the United States and other countries in which we operate. Legal uncertainties surrounding domestic and foreign government regulations could increase our costs of doing business, require us to revise our services, prevent us from delivering our services over the Internet or slow the growth of the Internet, any of which could increase our expenses, reduce our revenue or cause our revenue to grow at a slower rate than expected and materially adversely affect our business, financial condition and results of operations. Laws and regulations related to Internet communications, security, privacy, intellectual property rights, commerce, taxation, entertainment, recruiting and advertising are becoming more prevalent, and new laws and regulations are under consideration by the United States Congress, state legislatures and foreign governments. For example, in recent years, legislation related to the use of background checks for users of online personals services was proposed in Ohio, Texas, California, Michigan, New Jersey, Florida and Virginia. The New Jersey legislature enacted such a law in 2008 and other state legislatures may still be considering the implementation of such legislation. The interpretation of the New Jersey statute as well as the enactment of any of these proposed laws could require us to alter our service offerings and could negatively impact our performance by making it more difficult and costly to obtain new subscribers and may also subject us to additional liability for failure to properly screen our subscribers. Additionally, statutes have been enacted in at least sixteen states regulating automatic renewals to varying degrees. Generally, these statutes require companies to disclose automatic renewal policies in a clear and conspicuous manner. In California, under California Business and Professions Code Section 17600, et seq., the statute prohibits retailers from charging a consumer's debit card, credit card, or bank account for ongoing orders without his/her explicit consent. Similar to our interpretation of the New Jersey statute, the interpretation of this statute could require us to alter our service offerings and could impact our service. Promulgation of new laws, changes in current laws, the existence of ambiguous laws that are difficult to implement, changes in interpretations by courts and other governments officials of existing laws, our inability or failure to comply with current or future laws or strict enforcement by current or future government officers of current or future laws could adversely affect us by reducing our revenue, increasing our operating expenses and exposing us to significant potential liabilities.

Furthermore, in part as a result of current economic conditions, some states have begun to, and others may in the future, impose state taxes on services provided through the Internet, such as online personals, which will increase the cost of our services and could adversely affect our business. Any legislation and regulations enacted or newly enforced or restrictions arising from current or future government investigations or policy could dampen the growth in use of the Internet, generally, decrease the profitability of Internet related businesses and diminish the acceptance of the Internet as a communications, commercial, entertainment, recruiting and advertising medium. In addition to new laws and regulations being adopted, existing laws that are not currently being applied to the Internet may subsequently be applied to it, in some cases with a retroactive effect or penalty, and, in several jurisdictions, legislatures are considering laws and regulations that would apply to the online personals industry in particular. Many areas of law affecting the Internet and online personals remain unsettled, even in areas where there has been some legislative action. It may take years to determine whether and how existing laws such as those governing consumer protection, intellectual property, libel and taxation apply to the Internet or to our services. In the normal course of our business, we handle personally identifiable information pertaining to our members and paying subscribers residing in the United States and other countries. In recent years, many of these countries have adopted privacy, security and data protection laws and regulations intended to prevent improper uses and disclosures of personally identifiable information. In addition, some jurisdictions impose database registration requirements for which significant monetary and other penalties may be imposed for noncompliance. These laws may impose costly administrative requirements, limit our handling of information, and subject us to increased government oversight and financial liabilities. Privacy laws and regulations in the United States and foreign countries are subject to change and may be inconsistent, and additional requirements may be imposed at any time. These laws and regulations, the costs of complying with them, administrative fines for noncompliance and the possible need to adopt different compliance measures in different jurisdictions could materially increase our expenses and cause the value of our securities to decline.

Risks Related to Owning Our Securities

If an active trading market for our stock is not maintained or if securities analysts downgrade our stock or cease coverage of us, the price of our stock could decline.

We cannot assure you that an active trading market will be sustained or that the market price of our common stock will not decline. The price at which our common stock trades is likely to be highly volatile and may fluctuate substantially due to many factors, some of which are outside of our control. In addition, the stock market has experienced significant price and volume fluctuations that have affected the market price for the stock of many technology, communications and entertainment and media companies. Those market fluctuations were sometimes unrelated or disproportionate to the operating performance of these companies. Any significant stock market fluctuations in the future, whether due to our actual performance or prospects or not, could result in a significant decline in the market price of our securities. Furthermore, the trading market for our common stock relies in part on the research and reports that industry or financial analysts publish about us or our business. Currently, two financial analysts publish reports about us and our business. We do not control these or any other analysts. Furthermore, there are many large, well-established, publicly traded companies active in our industry and market, which may mean that it is less likely that we will receive widespread analyst coverage. If any of the analysts who cover us downgrade our stock, our stock price would likely decline rapidly. If these analysts cease coverage of our Company, we could lose visibility in the market, which in turn could cause our stock price to decline.

Five of our stockholders own approximately 60% of our stock and could exercise significant influence over the Company.

As of December 31, 2016, PEAK6, Spruce House Capital LLC, 402 Capital, Osmium Partners, and entities controlled by Lloyd I. Miller, III (“Mr. Miller”) and their respective affiliates beneficially owned approximately, in the aggregate, 60% of the Company’s outstanding common stock. While we believe such stockholders are unaffiliated and do not constitute a “group” as defined in the Exchange Act, as amended, these stockholders individually possess influence over our company, and the managing members of Osmium Partners and 402 Capital each serve on our Board of Directors along with designees from PEAK6 and Mr. Miller. Concentrated ownership may influence matters requiring stockholder approval, including the election of directors.

We may implement stock repurchase plans, which may restrict our funds available for other actions and negatively affect the market price of our securities.

In December 2013, we implemented a stock repurchase plan and may implement additional stock repurchase plans in the future. A stock repurchase plan may not have the effects anticipated by our Board of Directors and may instead harm the market price and liquidity of our securities. The full implementation of any repurchase plan could use a significant portion of our cash reserves, and this use of cash could limit our future flexibility to complete acquisitions of businesses or technology or other transactions. Implementation of a repurchase plan would also result in an increase in the percentage of common stock owned by our existing stockholders, and such increase may trigger disclosure or other regulatory requirements for our larger stockholders. As a result, certain stockholders may liquidate a portion of their holdings, which may have a negative impact on the market price of our securities. Furthermore, repurchases of stock may affect the trading of our common stock to the extent we fail to satisfy continued-listing requirements of the exchange on which our stock trades, including those based on numbers of holders or public float of our common stock. A repurchase plan will also reduce the number of shares of our common stock in the market, which may impact the development of an active trading market in our stock, causing a negative impact on the market price of our stock.

We have never paid any dividend and we may or may not pay dividends in the foreseeable future.

To date, we have not declared or paid any cash dividends on our common stock and currently intend to retain any future earnings for funding growth. We do not anticipate paying any dividends in the foreseeable future. As a result, you should not rely on an investment in our stock if you require dividend income. Capital appreciation, if any, of our stock may be your sole source of gain for the foreseeable future.

Our charter documents, our stockholder rights plan and our bylaws may have anti-takeover effects that could prevent a change in control, which may cause our stock price to decline.

Our certificate of incorporation or our bylaws could make it more difficult for a third party to acquire us, even if closing such a transaction would be beneficial to our stockholders. We are authorized to issue up to 10,000,000 shares of preferred stock. This preferred stock may be issued in one or more series, the terms of which may be determined at the time of issuance by our Board of Directors without further action by stockholders. The terms of any series of preferred stock may include voting rights (including the right to vote as a series on particular matters), preferences as to dividend, liquidation, conversion and redemption rights and sinking fund provisions. No preferred stock is currently outstanding. The issuance of any preferred stock could materially adversely affect the rights of the holders of our common stock, and therefore, reduce the value of our common stock. In particular, specific rights granted to future holders of preferred stock could be used to restrict our ability to merge with, or sell our assets to, a third party and thereby preserve control by the present Board of Directors.

There are no cumulative voting rights provided for in our bylaws or certificate of incorporation. While we have recently amended our bylaws to enable stockholders to call special meetings, our certificate of incorporation and bylaws still contain provisions that could have the effect of discouraging potential acquisition proposals or making a tender offer or delaying or preventing a change in control, including changes a stockholder might consider favorable. In particular, the certificate of incorporation and bylaws, as applicable, among other things:

- provide the Board of Directors with the ability to alter the bylaws without stockholder approval;
- provide for an advance notice procedure with regard to the nomination of candidates for election as Directors and with regard to business to be brought before a meeting of stockholders; and
- provide that vacancies on the Board of Directors may be filled by a majority of directors in office, although less than a quorum.

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We have also adopted a stockholder rights plan pursuant to which each share of common stock also has a “right” attached to it. The rights are not exercisable except upon the occurrence of certain takeover-related events – most importantly, the acquisition by a third party (the “Acquiring Person”) of more than 30% of our outstanding voting shares if the Acquiring Person has not concurrently made a tender offer to acquire all outstanding shares of common stock. Once triggered, the rights entitle the stockholders, other than the Acquiring Person, to purchase additional shares of common stock at a 50% discount to their fair market value. The effect of triggering the rights is to expose the Acquiring Person to severe dilution of its ownership interest, as the shares of common stock of our company (or any surviving corporation) are offered to all of the stockholders other than the Acquiring Person at a steep discount to their market value.

On September 23, 2016, the Board of Directors approved the amended and restated bylaws of the Company (the “Amended and Restated Bylaws”), in order to preserve certain tax benefits of the Company. The Company’s Amended and Restated Bylaws add Article VII, which imposes certain restrictions on the transfer of the Company’s securities. In particular, until the expiration of the transfer restrictions, any attempted transfer of the Company’s common stock shall be prohibited and void to the extent that, as a result of the transfer (or any series of transfers of which such transfer is a part), either (i) any person or group of persons would own 4.9% or more of the Company’s Common Stock directly or indirectly, as deemed to constructively own or otherwise aggregated pursuant to Section 382 of the Internal Revenue Code; (ii) the ownership interest in the Company of any person or group of persons owning 4.9% or more of the Company’s Common Stock would be increased; or (iii) any shareholder holding 5% or more of the total market value of the Company’s securities transfers, or agrees to transfer, any securities of the Company.

All of the foregoing provisions may have the effect of discouraging a third-party from acquiring Spark Networks, Inc. even if doing so would be beneficial to its stockholders. These provisions are expected to discourage certain types of coercive takeover practices and inadequate takeover bids and to encourage persons seeking to acquire control of Spark Networks, Inc. to first negotiate with its Board. These provisions of Delaware law also may discourage, delay or prevent someone from acquiring or merging with us, which may cause the market price of our common stock to decline.

Conflicts involving Israel could have a material adverse impact upon our business and operating results.

Our Hebrew language sites, JDate.co.il and Cupid.co.il, represent approximately 10% of our Jewish Networks revenue. As a result, any conflicts involving or attacks against Israel could impact our members’ and potential members’ interest in our services, and may have a material impact upon our subscriber and revenue bases as conflict occurs.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

We do not own any real property that is materially important to our business. Our headquarters are currently located in Los Angeles, California, where we occupy approximately 16,000 square feet of office space, housing our technology department and most of our corporate and administrative personnel. Our current lease for this space expires on October 31, 2018 with monthly basic rent ranging from approximately \$43,000 to \$51,000 with six months of rent abatement, as well as scheduled rent increases and rent credits. We also lease office space in Utah and datacenter space in California. We believe that our facilities are adequate for our current needs and suitable additional or substitute space will be available in the future to replace our existing facilities, if necessary, or accommodate expansion of our operations.

ITEM 3. LEGAL PROCEEDINGS

Overview

We are, and from time to time may become, involved in various legal proceedings arising in the normal course of business activities, such as patent infringement claims, trademark oppositions and consumer or advertising complaints, as well as stockholder derivative actions, class action lawsuits and other matters. The amounts that may be recovered in such matters may be subject to insurance coverage. Rules of the Securities and Exchange Commission require the description of material pending legal proceedings (other than ordinary, routine litigation incident to the registrant's business) and advise that proceedings ordinarily need not be described if they primarily involve damages claims for amounts (exclusive of interest and costs) not exceeding 10% of the current assets of the registrant and its subsidiaries on a consolidated basis. In the listing of litigation matters below, we have included matters that we do not believe rise to this level but rather involve issues or claims that may be of particular interest to our stockholders, regardless of whether any of these matters may be material to our financial position or operations based upon the standard set forth in the SEC's rules.

California Unruh Act Litigation – Werner, et al. v. Spark Networks, Inc. and Spark Networks USA, LLC and Wright, et al. v. Spark Networks, Inc., Spark Networks USA, LLC, et al.

On July 19, 2013, Aaron Werner, on behalf of himself and all other similarly situated individuals, filed a putative Class Action Complaint (the “Werner Complaint”) in the Superior Court for the State of California, County of Los Angeles against Spark Networks, Inc. and Spark Networks USA, LLC (collectively “Spark Networks”). The Werner Complaint alleges that Spark Networks’ website ChristianMingle.com violates California’s Unruh Civil Rights Act (the “Unruh Act”) by allegedly discriminating on the basis of sexual orientation. The Werner Complaint requests the following relief: an injunction, statutory, general, compensatory, treble and punitive damages, attorneys’ fees and costs, pre-judgment interest, and an award for any other relief the Court deems just and appropriate. On December 23, 2013, Richard Wright, on behalf of himself and all other similarly situated individuals, filed a putative Class Action Complaint (the “Wright Complaint”) in the Superior Court for the State of California, County of San Francisco against Spark Networks, Inc. The Wright Complaint alleges that Spark Networks, Inc.’s commercial dating services including ChristianMingle.com, LDSSingles.com, CatholicMingle.com, BlackSingles.com, MilitarySinglesConnection.com and AdventistSinglesConnection.com violate the Unruh Act by allegedly intentionally and arbitrarily discriminating on the basis of sexual orientation. The Wright Complaint requests the following relief: a declaratory judgment, a preliminary and permanent injunction, statutory penalties, reasonable attorneys’ fees and costs, pre-judgment interest, and an award for any other relief the Court deems just and appropriate. A motion filed by Spark Networks to consolidate the two matters in Los Angeles Superior Court was granted. On February 25, 2016, the parties reached a settlement which included the following terms: (1) individual settlement payments of \$4,000 each in statutory damages and \$5,000 each in service awards to plaintiffs Werner and Wright, and (2) \$450,000 in attorneys’ fees and costs to compensate Werner and Wright’s counsel for their time and out-of-pocket expenses. On April 19, 2016, the plaintiffs’ counsel filed a motion for an order granting approval of the settlement. On June 27, 2016, the judge approved the settlement during the hearing on the Motion for Preliminary Approval of Class Action Settlement. All amounts have been paid as of December 31, 2016.

Israeli Consumer Actions Ben-Jacob vs. Spark Networks (Israel) Ltd., Gever vs. Spark Networks (Israel) Ltd. and Korland vs. Spark Networks (Israel) Ltd.

Three class action law suits have been filed in Israel alleging inter alia violations of the Israel Consumer Protection Law of 1981. Spark Networks (Israel) Ltd. (“Spark Israel”) was served with a Statement of Claim and a Motion to Certify it as a Class Action in the Ben-Jacob action on January 14, 2014. The plaintiff alleges that Spark Israel refused to cancel her subscription and provide a refund for unused periods and claims that such a refusal is in violation of the Consumer Protection Law. Spark Israel was served with a Statement of Claim and a motion to Certify it as a Class Action in the Gever action on January 21, 2014. The plaintiff alleges that Spark Israel renewed his one month subscription without receiving his positive agreement in advance and claims that such renewal is prohibited under the Consumer Protection Law and its regulations. Spark Israel was served with a Statement of Claim and a Motion to Certify it as a Class Action in the Korland action on February 12, 2014. The plaintiff alleges that Spark Israel refused to give her a full refund and charged her the price of a one month subscription to the JDate website in violation of the Consumer Protection Law. In each of these three cases, the plaintiff is seeking personal damages and damages on behalf of a defined group. On May 8, 2014, the Court granted Spark Israel’s motion to consolidate all three cases. All three cases are now consolidated and will be litigated jointly. Spark Israel’s combined response to these motions to certify the class actions was filed November 1, 2014, and the plaintiffs responded to the combined response. The parties had a hearing before the judge on December 24, 2014. Following the hearing the judge ordered that the pleadings filed by the parties be transferred to the Israel Consumer Council (“ICC”) so that the ICC can provide its position as to the parties’ allegations within 90 days. The ICC issued its opinion on April 1, 2015. Following the filing of the ICC opinion, the parties filed briefs addressing the ICC opinion. On January 7, 2016, the parties advised the Court that they have agreed on the terms of a settlement agreement, and jointly moved to approve the agreement and give it the effect of a judgment. According to the terms of the settlement agreement, clients who bought a subscription to JDate.co.il on October 12, 2008 or later will be entitled to receive certain benefits. The settlement agreement, which provides for compensation and legal fees, will only come into effect if the court approves it. On January 14, 2016 the Court ordered the parties to publish the terms of the proposed settlement agreement. The Court allowed for the Attorney General or any person who wishes to object to the settlement or exclude himself from the class to file their position with the Court through March 10, 2016. On March 10, 2016, the ICC filed an objection to the settlement agreement, arguing inter alia that the benefits offered to the clients are insufficient, and that the Company's new business model does not comply with certain legal requirements. The Company and the plaintiffs filed their responses on March 24, 2016. On April 14, 2016, the Attorney General notified the Court that it has no objection to the settlement agreement. On February 8, 2017, a hearing was held during which the judge asked questions about the settlement agreement. The Company and the plaintiffs filed a revised settlement agreement on February 18, 2017, for the judge’s final approval. On February 28, 2017, the judge approved the settlement agreement, which provided for compensation and legal fees under terms from the original settlement agreement. The Company has recorded an accrual of \$52,000 for the probable cost related to resolving this matter as of December 31, 2016.

Scottsdale Insurance Co. v. Spark Networks, Inc., et al.

On January 13, 2016, Scottsdale Insurance Company (“Scottsdale”) filed a complaint for declaratory relief and reimbursement/unjust enrichment against Spark Networks, Inc. in the United States District Court for the Central District of California. In its complaint, Scottsdale alleges that, after the Company was sued in the Werner Complaint, the Company tendered its defense and indemnity to Scottsdale pursuant to the terms of the business and management indemnity insurance policy that Scottsdale had issued to the Company on November 1, 2012. The complaint alleges that, after receiving the demand, Scottsdale accepted the defense of the Company in the Werner Complaint under a reservation of rights, including Scottsdale’s right to seek reimbursement of any amounts paid to defend against non-covered claims. The Company filed its answer and counterclaims against Scottsdale on March 7, 2016, seeking damages for Scottsdale’s breach of policy and breach of the implied covenant of good faith and fair dealing. The parties executed a settlement agreement on July 6, 2016, whereby Scottsdale reimbursed the Company \$238,000 for

all reasonable and necessary attorney's fees and costs in defense against the Werner Complaint as of December 31, 2016.

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City of Santa Monica, California – City Attorney General Investigation

On May 16, 2016, representatives from Spark Networks met with representatives from a cross-jurisdictional working group consisting of consumer fraud attorneys from the City of Santa Monica and offices of the District Attorney from the counties of Los Angeles, Santa Cruz, Santa Clara and San Diego (“Cross Jurisdictional Group”). This meeting was held at the request of the Cross Jurisdictional Group, as a “pre-filing” meeting to explain and potentially resolve issues over auto-renewal disclosures by the Spark Network websites. The Cross Jurisdictional Group alleges that the Spark Networks websites violate California law on disclosure of auto-renewal terms and ability to cancel auto-renewal. They also claim that the Spark Networks websites violate California dating contract statutes, which (where applicable) require a three day right to cancel. The Cross Jurisdictional Group sent a voluntary document request (not a subpoena) to the Company on June 2, 2016. The Company cooperated with the Cross Jurisdictional Group and provided information in response to the voluntary request. The Cross Jurisdictional Group has indicated that it would like the Company to change its disclosures in certain respects, and that it intends to seek the payment of a penalty in an unspecified amount. In response to these disclosure requests, the Company has made changes. On March 8, 2017, the Company received a settlement communication from the City of Santa Monica and offices of the District Attorney, proposing settlement terms including payment of civil penalties, restitution to consumers, investigative costs and legal fees ranging from \$1.5 million to \$2.2 million. The Company has not responded to the settlement communication and intends to vigorously defend against the claims by the City of Santa Monica. As of December 31, 2016, the Company is unable to reasonably estimate the possibility of an unfavorable outcome, or the amount of any liability that may result from this matter.

Banertek LLC vs. Spark Networks, Inc.

On August 1, 2016, Banertek LLC filed a complaint for patent infringement with a demand for jury trial against Spark Networks, Inc. The Company was served with the complaint and summons as of October 10, 2016. The parties executed a confidential settlement agreement on December 5, 2016.

Jedi Technologies, Inc. vs. Spark Networks, Inc., Spark Networks USA, LLC and Smooch Labs, Inc.

On November 15, 2016, Jedi Technologies, Inc. filed a complaint for patent infringement with a demand for jury trial against Spark Networks, Inc, Spark Networks USA, LLC and Smooch Labs, Inc. The Company was served with the complaint and summons as of November 21, 2016. The Company filed a motion to dismiss on January 12, 2017 in the District of Delaware, and received Jedi Technologies, Inc.’s opposition to the motion to dismiss. The Company filed its reply to the opposition on February 2, 2017. As of December 31, 2016, the Company is unable to reasonably estimate the possibility of an unfavorable outcome, or the amount of any liability that may result from this matter.

We intend to defend vigorously against each of the above matters. At this time, management does not believe the above matters, either individually or in the aggregate, will have a material adverse effect on the Company’s results of operations or financial condition and believes the recorded legal accruals as of December 31, 2016 are adequate in light of the probable and estimable liabilities. However, no assurance can be given that these matters will be resolved in our favor.

We have additional existing legal claims and may encounter future legal claims in the normal course of business. In our opinion, the resolutions of the existing legal claims are not expected to have a material impact on our financial position or results of operations.

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable.

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PART II.

ITEM MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED SHAREHOLDER MATTERS AND
5. ISSUER PURCHASES OF EQUITY SECURITIES

Market Information

Spark Networks, Inc.'s common stock is traded on the NYSE MKT under the trading symbol "LOV." The following table summarizes the high and low closing sales prices of our common stock as reported by the NYSE MKT.

Year ended December 31, 2015	High	Low
First Quarter	\$4.04	\$3.31
Second Quarter	\$4.07	\$2.85
Third Quarter	\$3.26	\$2.83
Fourth Quarter	\$4.00	\$3.00

Year ended December 31, 2016	High	Low
First Quarter	\$3.82	\$2.22
Second Quarter	\$2.42	\$1.41
Third Quarter	\$1.97	\$1.42
Fourth Quarter	\$1.67	\$0.84

Holders

As of March 16, 2017 there were 62 holders of record of our common stock and the closing price of our common stock on NYSE MKT was \$0.99. Because a large portion of the outstanding shares of our common stock are held by brokers and other institutions on behalf of shareholders, we are not able to estimate the total number of beneficial shareholders represented by these record holders.

Dividends

We have not declared or paid any cash dividends on our common stock. We presently intend to retain our future earnings, if any, to fund the development and growth of our business and, therefore, do not have plans to pay any cash dividends in the near future.

Pursuant to the Company's credit agreement, as further described in "Management Discussion and Analysis of Financial Condition and Results of Operations", the Company is permitted to repurchase or redeem equity interests or issue dividends of up to \$1.0 million during the term of the credit agreement.

Securities Authorized for Issuance Under Equity Compensation Plans

Our equity compensation plan information is provided as set forth in Part III, Item 11 herein.