EASYLINK SERVICES CORP
Form 10-Q
November 15, 2004

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

|X| QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2004

OR

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

Commission File Number 0-26371

EASYLINK SERVICES CORPORATION
(Exact Name of Registrant as Specified in Charter)

Delaware (State or other Jurisdiction of) Incorporation or Organization)	13-3787073 (I.R.S. Employer Identification No.)
33 Knightsbridge Road, Piscataway, NJ (Address of Principal Executive Office)	08854 (Zip Code)

(732) 652-3500
(Registrant's Telephone Number Including Area Code)

Indicate by check 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 |X| No |_|

Indicate by check mark whether the registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2).
Yes [ ] No [X]

Common stock outstanding at November 1, 2004: Class A common stock $0.01 par value 43,213,079 shares, and Class B common stock $0.01 par value 1,000,000 shares.

EASYLINK SERVICES CORPORATION
SEPTEMBER 30, 2004

FORM 10-Q
INDEX

ITEM 1 CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Easylink Services Corporation
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share and per share data)

September

	2004
	(Unaudit
ASSETS	
Current assets:	
Cash and cash equivalents	$ 11,06
Accounts receivable, net of allowance for doubtful accounts of $4,280 and $4,824 as of September 30, 2004 and December 31, 2003, respectively	9,81
Prepaid expenses and other current assets	4,25
Total current assets	25,13
Property and equipment, net	8,48
Goodwill, net	6,26
Other intangible assets, net	9,61
Other assets	1,21
Total assets	$50,72
LIABILITIES AND STOCKHOLDERS' EQUITY	
Current liabilities:	
Accounts payable	$7,98
Accrued expenses	13,76
Restructuring reserves payable	78
Current portion of notes payable	4,48
Current portion of capitalized interest on notes payable	85
Other current liabilities	1,56
Net liabilities of discontinued operations	52
Total current liabilities	29,96
Notes payable, less current portion	7,13
Capitalized interest on notes payable, less current portion	38
Other long term liabilities	1,24
Total liabilities	38,72
Stockholders' equity:	
Common stock, $0.01 par value; 510,000,000 shares authorized at September 30, 2004 and December 31, 2003, respectively:	
Class A--500,000,000 shares authorized at September 30, 2004 and December 31, 2003; 43,173,967 and 42,821,500 shares issued and outstanding at September 30, 2004 and December 31, 2003, respectively	43
Class B--10,000,000 shares authorized at September 30, 2004 and December 31, 2003; 1,000,000 issued and outstanding at September 30, 2004 and December 31, 2003	1
Additional paid-in capital	553,28
Accumulated other comprehensive loss	(3
Accumulated deficit	(541,69
Total stockholders' equity	11,99

Total liabilities and stockholders' equity	$50,72

See accompanying notes to unaudited condensed consolidated financial statements.

EasyLink Services Corporation
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except share and per share data)
(unaudited)

	Three Months Ended September 30, 2004	Three Months Ended September 30, 2003
Revenues	$ 22,509	$ 25,065
Cost of revenues	8,428	10,863
Gross profit	14,081	14,202
Sales and marketing	4,349	4,392
General and administrative	5,959	5,686
Product development	1,675	1,377
Amortization of intangible assets	517	517
Restructuring charges	(350)	788
Gain on sale of MailWatch service line	(4,126)	--
Total operating expenses	8,024	12,760
Income from operations	6,057	1,442
Other income (expense), net:		
Interest income	11	5
Interest expense	(116)	(134)
Other, net	89	54
Total other income (expense), net	(16)	(75)
Income from continuing operations before income taxes	6,041	1,367
Provision for Federal and State income taxes	1,550	--
Income from continuing operations	4,491	1,367

Loss from discontinued operations	--	(838)
Net income	$ 4,491	$ 529
Basic and diluted net income (loss) per share:		
Income from continuing operations	$0.10	$0.03
Loss from discontinued operations	--	$ (0.02)
Net income per share	$ 0.10	$ 0.01
Weighted-average basic shares outstanding	44,163,230	43,534,594
Weighted-average diluted shares outstanding	44,670,335	44,479,302

See accompanying notes to unaudited condensed consolidated financial statements.

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EasyLink Services Corporation
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except share and per share data)
(unaudited)

	Nine Months Ended September 30,	
	2004	2003
Revenues	$ 70,899	$ 76,608
Cost of revenues	28,518	37,931
Gross profit	42,381	38,677
Sales and marketing	13,628	14,064
General and administrative	18,024	18,700
Product development	5,032	5,039
Amortization of intangible assets	1,550	1,550
Restructuring charges	(350)	788
Gain on sale of MailWatch service line	(4,126)	--
Total operating expenses	33,758	40,141

Income (loss) from operations	8,623	(1,464)
Other income (expense), net:		
Interest income	29	30
Interest expense	(368)	(1,231)
Gain on debt restructurings and settlements	--	53,666
Other, net	105	44
Total other income (expense), net	(234)	52,509
Income from continuing operations before income taxes	8,389	51,045
Provision for Federal and State income taxes	1,750	--
Income from continuing operations	6,639	51,045
Loss from discontinued operations	--	(838)
Net income	$6,639	$50,207
Basic net income (loss) per share:		
Income from continuing operations	$0.15	$1.57
Loss from discontinued operations	--	$(0.03)
Net income per share	$0.15	$1.54
Diluted net income (loss) per share:		
Income from continuing operations	$0.15	$1.56
Loss from discontinued operations	--	$ (0.03)
Net income per share	$0.15	$1.53
Weighted-average basic shares outstanding	44,030,611	32,505,571
Weighted-average diluted shares outstanding	44,915,837	32,620,014

See accompanying notes to unaudited condensed consolidated financial statements.

EasyLink Services Corporation

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(unaudited)

	Nine Mont
	2004
Cash flows from operating activities:	
Net income	$ 6,639
Adjustments to reconcile net income to net cash provided by operating activities:	
Loss from discontinued operations	--
Depreciation and amortization	3,975
Amortization of intangible assets	2,010
Provision for doubtful accounts	441
Provision for restructuring and impairments	(350
Gain on debt restructuring and settlements	--
Gain on sale of MailWatch service line	(4,126
Non-cash interest	36
Issuance of shares to employee benefit plans	286
Other non-cash charges	167
Changes in operating assets and liabilities:	
Accounts receivable, net	1,170
Prepaid expenses and other current assets	(740
Other assets	43
Accounts payable, accrued expenses and other current liabilities	(3,371
Net cash provided by operating activities	6,180
Cash flows from investing activities:	
Purchases of property and equipment, including capitalized software	(1,918
Cash proceeds from sale of MailWatch service line	3,500
Net cash provided by (used in) investing activities	1,582
Cash flows used in financing activities:	
Payments under capital lease obligations	(283
Payments of capitalized interest	(752
Payments of notes payable	(1,860
Proceeds from exercise of employee stock options	24
Proceeds from issuance of Class A common stock	--
Net cash used in financing activities	(2,871
Effect of foreign exchange rate changes on cash and cash equivalents	(153
Net increase (decrease) in cash and cash equivalents	4,738
Cash used in discontinued operations	(300
Cash and cash equivalents at beginning of the period	6,623

Cash and cash equivalents at the end of the period..................................	$11,061
	=======

Supplemental disclosure of interest paid and non-cash information:

During the nine months ended September 30, 2004 and 2003, the Company paid approximately $0.4 and $0.6 million, respectively, for interest.

During the nine months ended September 30, 2004, the Company issued shares of Class A common stock as follows:

The Company issued 28,022 shares of Class A common stock valued at approximately $37,000 as payment for interest in lieu of cash.

The Company issued 189,445 shares of Class A common stock valued at approximately $284,000 in connection with matching contributions to its 401(k) plan.

The Company issued 99,500 shares of Class A common stock valued at approximately $149,000 to a former employee of the Company pursuant to the settlement of a commitment to the employee to issue such shares originally entered into in 2001.

The Company issued 35,500 shares of Class A common stock valued at approximately $24,000 in connection with the exercise of employee stock options.

During the nine months ended September 30, 2003, the Company issued shares of Class A common stock as follows:

The Company issued 274,629 shares of Class A common stock valued at approximately $200,000 as payment for interest in lieu of cash.

The Company issued 23,585,037 shares of Class A common stock in connection with the cancellation of debt. These shares were valued at approximately $13.0 million (See Note 3).

The Company issued 455,173 shares of Class A common stock valued at approximately $375 thousand in connection with matching contributions to its 401(k) plan.

The Company issued 71,550 shares of Class A common stock valued at approximately $70 thousand in connection with the exercise of employee stock options.

Non-cash investing activities:

During the three and nine months ended September 30, 2004, the Company received 123,193 shares valued at approximately $1.5 million of Infocrossing, as part of the consideration for the sale of Mailwatch service line.

See accompanying notes to unaudited condensed consolidated financial statements.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(1) SUMMARY OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES

(a) Summary of Operations

The Company offers a broad range of information exchange services to businesses and service providers, including Transaction Management Services consisting of integrated desktop messaging services and document capture and management services such as fax to database, fax to data and data conversion services; Transaction Delivery Services consisting of electronic data interchange or "EDI," and production messaging services utilizing email, fax and telex: and, through July 31, 2004, services that protect corporate e-mail systems such as virus protection, spam control and content filtering services (the Mailwatch service line).

The Company operates in a single industry segment, business communication services. Although the Company provides various major service offerings, many customers employ multiple services using the same access and network facilities. Similarly, network operations and customer support services are provided across various services. Accordingly, allocation of expenses and reporting of operating results by individual services would be impractical and arbitrary. Services are provided in the United States and certain other regions in the world (predominantly in the United Kingdom).

(b) Unaudited Interim Condensed Consolidated Financial Information

The accompanying interim condensed consolidated financial statements as of September 30, 2004 and for the three and nine months ended September 30, 2004 and 2003 have been prepared by the Company and are unaudited. In the opinion of management, the unaudited interim condensed consolidated financial statements have been prepared on the same basis as the annual consolidated financial statements and reflect all adjustments, which include only normal recurring adjustments, necessary to present fairly the consolidated financial position of EasyLink Services as of September 30, 2004 and the consolidated results of operations and cash flows for the interim periods ended September 30, 2004 and 2003. The results of operations for any interim period are not necessarily indicative of the results of operations for any other future interim period or for a full fiscal year. The condensed consolidated balance sheet at December 31, 2003 has been derived from audited consolidated financial statements at that date.

For each of the years ended December 31, 2003 and 2002, the Company received a report from its independent accountants containing an explanatory paragraph stating that the Company suffered recurring losses from operations since inception and has a working capital deficiency that raises substantial doubt about the Company's ability to continue as a going concern. The unaudited condensed consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amounts and classification of liabilities that might be necessary should the Company be unable to continue as a going concern. Management believes the Company's ability to continue as a going concern is dependent upon its ability to generate sufficient cash flow to meet its obligations on a timely basis, to obtain additional financing or refinancing as may be required and ultimately to achieve continued profitable operations.

Certain information and note disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to the Securities and Exchange Commission's rules and regulations. It is suggested that these unaudited interim condensed consolidated financial statements be read in conjunction with the Company's audited consolidated financial statements and notes thereto for the year ended December 31, 2003 as included in the Company's Form 10-K filed with the Securities and Exchange Commission on March 30, 2004.

(c) Principles of Consolidation and Basis of Presentation

The consolidated financial statements include the accounts of the Company and its wholly-owned or majority-owned subsidiaries. All other investments that the Company does not have the ability to control or over which it does not exercise significant influence are accounted for under the cost method. The interest of shareholders other than those of EasyLink is recorded as minority interest in the accompanying consolidated statements of operations and consolidated balance sheets. When losses applicable to minority interest holders in a subsidiary exceed the minority interest in the equity capital of the subsidiary, these losses are included in the Company's results, as the minority interest holder has no obligation to provide further financing to the subsidiary. All significant intercompany accounts and transactions have been eliminated in consolidation.

The net liabilities of WORLD.com, a wholly owned subsidiary, and its majority owned subsidiaries, are reported as discontinued operations in the consolidated balance sheets as of September 30, 2004 and December 31, 2003 as a result of the sale or discontinuance of the operations of this business in 2001.

(d) Use of Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities and the reported amounts of revenues and expenses. These estimates and assumptions relate to the estimates of collectibility of accounts receivable, the realization of goodwill and other intangibles, accruals and other factors. Actual results could differ from those estimates.

(e) Revenue Recognition

The Company's services include Transaction Management Services consisting of integrated desktop messaging services and document capture and management services such as fax to database, fax to data and data conversion services; Transaction Delivery Services consisting of electronic data interchange or "EDI," and production messaging services utilizing email, fax and telex; and, through July 31, 2004, services that protect corporate e-mail systems such as virus protection, spam control and content filtering services (the Mailwatch service line). The Company derives revenues from monthly fees and usage-based charges for its transaction delivery and management services; from monthly per-user or per-message fees for its virus protection, spam control and content filtering services, and from license fees. Revenue from services is recognized as the services are performed. Facsimile license revenue is recognized over the average estimated customer life of 3 years.

Other revenues include revenues from (i) the sale of domain names, which are recognized at the time when the ownership of the domain name is transferred provided that no significant Company obligation remains and collection of the resulting receivable is probable and (ii) the licensing of domain names wherein revenue is recognized ratably over the license period. To date, such revenues have not been material.

(f) Financial Instruments and Concentration of Credit Risk

Financial instruments that potentially subject the Company to significant concentrations of credit risk consist of cash, cash equivalents, restricted investments, accounts receivable, notes payable and convertible notes payable. At September 30, 2004 and December 31, 2003, the fair value of cash, cash equivalents, restricted investments and accounts receivable approximated their financial statement carrying amount because of the short-term maturity of these instruments. The recorded values of notes payable and convertible notes payable approximate their fair values, as interest approximates market rates with the exception of the Convertible Subordinated Notes payable with a carrying value of $1.4 million at September 30, 2004 and December 31, 2003. However, as these notes are payable in February 2005, management estimates that their fair value approximates their carrying value.

Credit is extended to customers based on the evaluation of their financial condition and collateral is not required. The Company performs ongoing credit assessments of its customers and maintains an allowance for doubtful accounts. No single customer exceeded 10% of either total revenues or accounts receivable as of and for the three and nine months periods ended September 30, 2004 and 2003. Revenues from the Company's five largest customers accounted for an aggregate12% and 6% of the Company's total revenues for the nine months ended September 30, 2004 and 2003, respectively.

(g) Basic and Diluted Net Income Per Share

Net income per share is presented in accordance with the provisions of SFAS No. 128, "Earnings Per Share", and the Securities and Exchange Commission Staff Accounting Bulletin No. 98. Under SFAS No. 128, basic Earnings per Share ("EPS") excludes dilution for common stock equivalents and is computed by dividing income or loss available to common shareholders by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock and resulted in the issuance of common stock. Although diluted net income per share for the three and nine months ended September 30, 2004 is equal to basic net income per share, the amounts for the three month and nine month periods include the effect of employee options to purchase 1.6 million shares of common stock

(h) Stock-Based Compensation Plans

As allowed by SFAS No. 123, Accounting for Stock-Based Compensation, as amended by SFAS No. 148, we have retained the compensation measurement principles of Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees, and its related interpretations for stock options. SFAS No. 148 also requires more prominent and more frequent disclosures in both interim and annual financial statements about the method of accounting for stock-based compensation and the effect of the method used on reporting results. We adopted the disclosure provisions of SFAS No. 148 as of December 31, 2002 and continue to apply the measurement provisions of APB 25. Under APB Opinion No. 25, compensation expense is recognized based upon the difference, if any, at the measurement date between the market value of the stock and the option exercise price. The measurement date is the date at which both the number of options and the exercise price for each option are known. The following table illustrates the effect on net income and net income per share if we had applied the fair value recognition provisions of SFAS No. 123 to stock-based employee compensation.

($ in thousands, except per share amounts)	For the three months ended September 30, 2004	2003
Net income as reported	$ 4,491	$ 1,367
Deduct: total stock based employee compensation determined under the fair value method for all awards, net of tax	(367)	(1,968)
Pro forma income (loss) from continuing operations	$ 4,124	$ (601)
Loss from discontinued operations	$ --	$ (838)
Pro forma net income (loss)	$ 4,124	$ (1,439)
Basic net income (loss) per share:		
As reported	$0.10	$ 0.03
Deduct: total stock based employee compensation determined under the fair value method for all awards, net of tax	$ (0.01)	$ (0.04)
Pro forma income (loss) from continuing operations	$ 0.09	$ (0.01)
Loss from discontinued operations	$ --	$ (0.02)
Pro forma	$ 0.09	$ (0.03)
Diluted net income (loss) per share:		
As reported	$0.10	$ 0.03
Deduct: total stock based employee compensation determined under the fair value method for all awards, net of tax	$ (0.01)	$ (0.04)
Pro forma income (loss) from continuing operations	$ 0.09	$ (0.01)
Loss from discontinued operations	$ --	$ (0.02)
Pro forma	$ 0.09	$ (0.03)

The resulting effect on the pro forma net income (loss) disclosed for the three and nine month periods ended September 30, 2004 and 2003 is not likely to be representative of the effects on the net income (loss) on a pro forma basis in future years, because the pro forma results include only the impact of grants issued to date and related vesting, while subsequent years will include additional grants and vesting. For purposes of pro-forma disclosure, the estimated fair value of the options is amortized to expense over the options' vesting period.

(i) Recent Accounting Pronouncements

In January 2003, the FASB issued Interpretation No. 46 ("FIN46"), Consolidation of Variable Interest Entities", and replaced this interpretation with FIN 46(R) in December 2003. FIN 46 and FIN 46(R) address how a business enterprise should evaluate whether it has a controlling financial interest in an entity through means other than voting rights and accordingly should consolidate the entity. The provisions of FIN46 were effective immediately for all arrangements entered into with new variable interest entities ("VIEs") after January 31, 2003. However, the Company had not entered into any arrangements with VIEs after January 31, 2003. The Company is required to apply FIN46R to variable interests in VIEs created after December 31, 2003. For any VIEs created on or before December 31, 2003, the assets, liabilities and non-controlling interests of VIEs initially would be measured at their carrying amounts with any difference between the net amount added to the balance sheet and any previously recognized interest being recognized as the cumulative effect of an accounting change. The adoption of FIN46R on January 1, 2004 did not have any impact on the Company's financial position or results of operations.

(2) SALE OF MAILWATCH SERVICE LINE

On July 31, 2004, the Company sold its MailWatch service line to Infocrossing, Inc. for a total of approximately $5.0 million, including $3.5 million in cash and 123,193 shares of Infocrossing's common stock valued at approximately $1.5 million. The sale resulted in a gain of $4.1 million before income taxes and approximately $ 2.5 million after income taxes. The Infocrossing stock is reported at market value in the September 30, 2004 balance sheet in prepaid expenses and other current assets and the unrealized gain related thereto of $387,000 is included in the accumulated other comprehensive loss account in stockholders' equity.

(3) NOTES PAYABLE

During the nine months ended September 30, 2003, the Company entered into a series of transactions with debt holders to eliminate a total of $63.0 million of indebtedness in exchange for cash payments of $3.1 million and, the issuance of 23.6 million shares of Class A common stock valued at $13.0 million. The eliminated debt included $21.8 million of 7% Convertible Subordinated Notes, due February 2005, $31.1 million of 10% Senior Convertible Notes, due January 2006, $2.7 million note payable to the former shareholder of STI (who is an officer and director of the Company), $6.0 million of Restructure Notes and $0.5 million in other indebtedness. The Company also entered into agreements to repay an outstanding note in the principal amount of $115,000 and accrued interest obligations in the aggregate amount of $959,000 over the next three years. This accrued interest includes $284,000 due to the former shareholder of STI. In addition, after eliminating $6.5 million of previously capitalized interest, $2.7 million of accrued interest, and $0.3 million of debt issuance costs on the eliminated notes, these transactions resulted in a gain of $53.7 million, or $1.52 per share on a basic and diluted basis. Also the transaction relating to the previous $115,000 note and $959,000 of accrued interest have been accounted for in accordance with Financial Accounting Standards Board Statement No. 15, "Accounting by Debtors and Creditors for Troubled Debt Restructurings."

Notes payable and capitalized interest on notes payable include the following, in thousands:

	September 30, 2004	
	Capitalized Interest	Principal
2000 7% Convertible Subordinated Notes due February 2005	$ --	$ 1,425
2001 12% Restructure note: as amended and restated effective September 2003	1,188	9,006
2001 12% Note payable to former shareholder of STI	--	--
2001 12% Restructure notes due in 13 quarterly payments beginning June 2003	55	757
2001 Restructuring balloon payments due October 2004	--	427
Total notes payable and capitalized interest	1,243	11,615
Less current portion	855	4,480
Non current portion	$ 389	$ 7,135

(4) RESTRUCTURING CHARGES

During the three months ended September 30, 2003, the Company recorded restructuring charges of $788,000, representing revised estimates of previously established charges for net abandonment costs on leases. In the three months ended September 30, 2004, the estimates were revised again, largely due to a negotiated settlement of liability on one lease, resulting in the reversal of restructuring charges of $350,000.

(5) INCOME TAXES

The Company recorded a provision for Federal and state income taxes in the three and nine months ended September 30, 2004 based on its anticipated effective tax rates for the full year 2004. The effective rate varies from standard tax rates primarily due to the utilization of available net operating loss carry forwards for Federal and certain state income tax purposes.

The availability of the Company's existing net operating loss carryforwards to offset income in the current periods and in the future has been determined to be significantly limited. As a result of numerous historical equity transactions, the Company has experienced "ownership changes" as defined by Section 382 of the Internal Revenue Code of 1986, as amended (the "Code") and, accordingly, the utilization of net operating loss carryforwards is limited under the change in stock ownership rules of the Code.

The elimination of outstanding debt in the nine months ended September 30, 2003 resulted in substantial income from cancellation of debt for income tax purposes. The Company reduced its income tax payable as a result of the restructuring by, among other things, offsetting the income with its historical net operating losses and otherwise reducing the income in accordance with applicable income tax rules. As a result, the Company does not expect to incur any material current income tax liability from the elimination of this debt. However, the relevant tax authorities may challenge the Company's income tax positions.

(6) COMMITMENTS AND CONTINGENCIES

Master Carrier Agreement

In April 2004, the Company entered into a Data Service Terms and Pricing attachment ("MCA Attachment") to its Master Carrier Agreement with AT & T for the purchase of private line and satellite services. Under the MCA Attachment, the term is for a minimum of 18 months with an option by the Company to extend the term for an additional 12 months. Under the MCA Attachment, the Company has a minimum purchase commitment for services equal to $3.6 million during the initial 18 month period. Similar to the original agreement, if the Company terminates the MCA Attachment prior to the end of the term or AT&T terminates the services for the Company's breach, the Company must pay to AT&T a termination charge equal to 50% of the unsatisfied minimum purchase commitment for the remaining portion of the term.

Tax assessment

In September 2004, the Company received a notice of a proposed New York state tax assessment amounting to $388,000 plus interest and penalties of $107,000 for sales and use taxes principally related to the taxability of its services. The Company intends to dispute the proposed assessment in general as it believes it is not liable for such taxes. Accordingly, the Company does not believe that this proposed tax adjustment will have a material affect on its financial statements although it can not give any assurance as to the likelihood of success or its ultimate liability.

ITEM 2 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

We make forward-looking statements within the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995 throughout this report. These statements relate to our future plans, objectives, expectations and intentions. These statements may be identified by the use of words such as "expects," "anticipates," "intends," "believes," "estimates," "plans" and similar expressions. Our actual results could differ materially from those discussed in these statements. Factors that could contribute to such differences include, but are not limited to, those discussed in the "Risk Factors" section of this report. EasyLink Services Corporation undertakes no obligation to update publicly any forward-looking statements for any reason even if new information becomes available or other events occur in the future.

Unless otherwise indicated or the context otherwise requires, all references to "we," "us," "our" and similar terms refer to EasyLink Services Corporation and its direct and indirect subsidiaries.

OVERVIEW

We are a provider of services that facilitate the electronic exchange of information between enterprises, their trading communities and their customers. On an average business day, we handle approximately one million transactions that are integral to the movement of money, materials, products and people in the global economy such as insurance claims, trade and travel confirmations, purchase orders, invoices, shipping notices and funds transfers, among many others. We offer a broad range of information exchange services to businesses and service providers, including Transaction Management Services consisting of integrated desktop messaging services and document capture and management services such as fax to database, fax to data and data conversion services; Transaction Delivery Services consisting of electronic data interchange or "EDI," and production messaging services utilizing email, fax and telex; and, through July 31, 2004, services that protect corporate e-mail systems such as virus protection, spam control and content filtering services (the Mailwatch service line).

REVENUES

For the nine months ended September 30, 2004, revenues were $70.9 million in comparison to revenues of $76.6 million for the nine months ended September 30, 2003. The decline in revenue is primarily the net result of (1) a $7.6 million (11%) decrease in production messaging services in the Transaction Delivery Services group as a result of lower volumes, negotiated customer price reductions at the time of service contract renewals and the loss of certain customers (2) a $1.1 million decrease in MailWatch revenues as a result of the sale of this service line as of July 31, 2004; and (3) an increase in Transaction Management Services of $3.1 million (52%). Production messaging services have been impacted by continuing pricing pressures in the telecommunications market and by technological factors that replace or reduce the deployment of such services by our customers. We have offset, and we intend to continue to offset, this revenue erosion by expanding the use of our services within our large base of existing customers, by selling our services to new customers and by expanding our new Transaction Management Services including Document Capture and Management services. However, the overall declines may continue.

Our revenues by quarter for 2004 year-to-date and 2003 were as follows (in thousands):

	3rd Qtr 2004	2nd Qtr 2004	1st Qtr 2004	4th Qtr 2003	3r 2
Transaction Management Services	$3,093	$ 3,077	$ 2,771	$ 2,467	$ 2,
Transaction Delivery Services	18,986	19,948	20,552	21,219	21,
MailWatch	430	1,028	1,014	1,052	1,
	$22,509	$24,053	$24,337	$24,738	$25,

OPERATING RESULTS

Our operating results have improved in the nine months ended September 30, 2004 even though revenues declined in comparison to the same period in 2003. Our income from operations amounted to $8.6 million in 2004 (inclusive of the $4.1 million gain on the MailWatch sale) in comparison to a loss from operations of $1.5 million in the 2003 period. The improved operations were as a result of reduced costs of revenues, in total and as a percentage of revenues, and, to a lesser extent, as a result of reduced operating expenses including the impact of the reversal of $350,000 of restructuring charges in 2004 as compared to a $788,000 provision recorded in 2003. Net income for the nine months ended September 30, 2004 was $6.6 million as compared to income from continuing operations for the nine months ended September 30, 2003 of $51.0 million. However, the results for 2003 included a gain on debt restructuring and settlements of $53.7 million while the 2004 period included a gain on the sale of the MailWatch service line, net of income taxes, of $2.5 million.

CRITICAL ACCOUNTING POLICIES

In response to the Securities & Exchange Commission's (SEC) Release No. 33-8040, "Cautionary Advice Regarding Disclosure About Critical Accounting Policies," we have identified the most critical accounting principles upon which our financial status depends. Critical principles were determined by considering accounting policies that involve the most complex or subjective decisions or assessments. The most critical accounting policies were identified to be those related to revenue recognition, accounts receivable, impairment of long-lived assets, contingencies and litigation and restructuring activities. Refer to the Company's Form 10K for the year ended December 31, 2003 as filed with the SEC on March 30, 2004 for a description of these critical accounting policies.

RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2004 AND 2003

Revenues

Revenues for the three months ended September 30, 2004 were $22.5 million, as compared to $25.1 million for the comparable period in 2003. The decrease of $2.6 million was due to (1) a $2.7 million decrease in our production messaging services, which include fax, telex and email services, as a result of lower volumes, negotiated individual customer price reductions at the time of service contract renewals and loss of certain customers; and (2) $0.8 million in lower MailWatch revenues as a result of the sale of this service line; offset by $1.0 million in higher Transaction Management Services revenues.

Cost of Revenues

Cost of revenues for the three months ended September 30, 2004 decreased to $8.4 million as compared to $10.9 million for the comparable period in 2003 and, as a percentage of revenues, these costs decreased to 37.4% in the 2004 quarter as compared to 43.3% of revenues in the comparable 2003 quarter. The decrease in costs as a percentage of revenue reflects a 2.9% decrease related to depreciation charges and a total of 3.0% decrease related to all other costs, primarily in variable telecommunications charges and fixed network facilities as a result of our cost reduction and network efficiency efforts. We anticipate that the cost of revenues will approximate the current quarter's level through the end of 2004.

Cost of revenues consists primarily of costs incurred in the delivery and support of our services, including depreciation of equipment used in our computer systems, the cost of telecommunications services including local access charges, leased network backbone circuit costs and long distance domestic and international termination charges, and personnel costs associated with our systems and databases.

Sales and Marketing Expenses

Sales and marketing expenses were $4.3 million and $4.4 million for the three months ended September 30, 2004 and 2003, respectively. Included in this category are costs related to salaries and commissions for sales, marketing, and business development personnel. Also included are costs for promotional programs, trade shows and marketing materials. We anticipate that sales and marketing expenses will increase in the fourth quarter of 2004 and during subsequent periods in 2005 due to increased personnel added in the 4th quarter and anticipated for the 1st quarter of 2005.

General and Administrative Expenses

General and administrative expenses were $6.0 million during the three months ended September 30, 2004 as compared to $5.7 million during the comparable period of 2003. While certain of these costs will vary from period to period, we anticipate general and administrative expenses in the fourth quarter of 2004 and in 2005 will be comparable to the third quarter 2004 amount.

Product Development Expenses

Product development costs, which consist primarily of personnel and consultants' time and expense to research, conceptualize, and test product launches and enhancements to our products, were relatively comparable in the three months ended September 30, 2004 and 2003, amounting to $1.7 million and $1.4 million respectively.

Restructuring Charges

During the three months ended September 30, 2003, the Company recorded restructuring charges of $788,000, representing revised estimates of previously established charges for net abandonment costs on leases. In the three months ended September 30, 2004, the estimates were revised again, largely due to a negotiated settlement of liability on one lease, resulting in the reversal of restructuring charges of $350,000.

RESULTS OF OPERATIONS FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2004 AND 2003

Revenues

Revenues for the nine months ended September 30, 2004 were $70.9 million, as compared to $76.6 million for the comparable period in 2003. The decrease of $5.7 million was due primarily to reduced revenues in our production messaging services, which include fax, telex and email services, as a result of lower volumes, negotiated individual customer price reductions at the time of service contract renewals and loss of certain customers. Revenues in the 2004 and 2003 periods consist almost entirely of revenues from providing information exchange services to businesses and are derived from electronic data interchange services or "EDI;" production messaging services; integrated desktop messaging services; document capture and management services(in 2004 only) and other services.

Cost of Revenues

Cost of revenues for the nine months ended September 30, 2004 decreased to $28.5 million as compared to $37.9 million for the comparable period in 2003 and, as a percentage of revenues, these costs decreased to 40.2% in the 2004 period as compared to 49.5% of revenues in the comparable 2003 period. The decrease in costs as a percentage of revenue reflects a 3.1% decrease related to depreciation charges and a total of 7.9% related to all other costs, primarily in variable telecommunications charges and fixed network facilities as a result of our cost reduction and network efficiency efforts.

Cost of revenues consists primarily of costs incurred in the delivery and support of our services, including depreciation of equipment used in our computer systems, the cost of telecommunications services including local access charges, leased network backbone circuit costs and long distance domestic and international termination charges, and personnel costs associated with our systems and databases.

Sales and Marketing Expenses

Sales and marketing expenses were $13.6 million and $14.1 million for the nine months ended September 30, 2004 and 2003, respectively. Included in this category are costs related to salaries and commissions for sales, marketing, and business development personnel. Also included are costs for promotional programs, trade shows and marketing materials. The lower costs in the 2004 period were the result of reduced staffing but we anticipate that sales and marketing expenses will increase in the remainder of 2004.

General and Administrative Expenses

General and administrative expenses were $18.0 million during the nine months ended September 30, 2004 as compared to $18.7 million during the comparable period of 2003. The decrease in these costs is the net impact of various cost components including $277,000 in reduced office facilities expense as a result of the restructuring activities completed in 2003 and $425,000 in reduced customer billing costs.

Product Development Expenses

Product development costs, which consist primarily of personnel and consultants' time and expense to research, conceptualize, and test product launches and enhancements to our products, were $5.0 million for the nine months ended September 30, 2004 and 2003.

Restructuring Charges

During the nine months ended September 30, 2003, the Company recorded restructuring charges of $788,000, representing revised estimates of previously established charges for net abandonment costs on leases. In the nine months ended September 30, 2004, the estimates were revised again, largely due to a negotiated settlement of liability on one lease, resulting in the reversal of restructuring charges of $350,000.

Other Income (Expense), Net

Interest expense: Interest expense was $368,000 for the nine months ended September 30, 2004 as compared to $1.2 million for the same period in 2003. The decrease was due to the elimination of indebtedness as a result of the debt restructuring and settlements completed during 2003.

Gain on debt restructuring and settlements: In the nine months ended September 30, 2003, we eliminated $63.0 million of indebtedness in exchange for the payment of $3.1 million in cash and the issuance of 23.6 million shares of Class A common stock valued at $13.0 million pursuant to our announced efforts to eliminate substantially all of our outstanding indebtedness. After reversing $6.5 million of previously capitalized interest and $2.4 million of accrued interest net of debt issuance costs, we recorded total gains of $53.7 million on these transactions.

LIQUIDITY AND CAPITAL RESOURCES

Net cash provided by operating activities was $6.2 million for the nine months ended September 30, 2004 in comparison to $3.8 million in cash provided from operating activities for the same period in 2003.

Net cash used in investing activities, consisting of purchases of property and equipment, amounted to $1.9 million and $4.1 million for the nine months ended September 30, 2004 and 2003, respectively. The higher expenditures in the 2003 period included $1.9 million related to the consolidation of our New Jersey office facilities into a single location. Cash proceeds from the MailWatch sale also added $3.5 million in 2004.

Net cash used in financing activities was $2.9 million and $4.9 million for the nine months ended September 30, 2004 and 2003, respectively. In 2004 these activities were comprised of scheduled payments of debt principal and interest and payments under capital lease obligations as compared to $5.9 million in debt service and capital lease payments in 2003 net of the proceeds of $1.0 million from the issuance of 1.9 million shares of class A common stock in a private placement. The 2003 amount includes approximately $3.1 million paid as part of the debt restructurings and settlements completed in that period.

At September 30, 2004, we had $11.1 million of cash and cash equivalents which represents an increase of $4.4 million from December 31, 2003. The current amount includes the $3.5 million received from the sale of the MailWatch service line.

At September 30, 2004 we had a working capital deficit of $4.8 million which is $7.0 million less than the deficit of $11.8 million at December 31, 2003 and $14.8 million less than the deficit of $19.6 million at December 31, 2002. We intend to continue our efforts to reduce the working capital deficit through payment of liabilities with funds generated from operations; through reductions in certain liabilities by agreeing to settlements and delayed payment arrangements with vendors and payees; by refinancing our debt obligations to defer payments of principal, if possible; and by raising funds through the sale of certain assets.

ITEM 3 QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company is exposed to market risk, primarily from changes in interest rates, foreign exchange rates and credit risk. The Company maintains continuing operations in Europe (mostly in England) and, to a lesser extent, in Singapore and Malaysia. Fluctuations in exchange rates may have an adverse effect on the Company's results of operations and could also result in exchange losses. The impact of future rate fluctuations cannot be predicted adequately. To date the Company has not sought to hedge the risks associated with fluctuations in exchange rates.

Market Risk - Our accounts receivable are subject, in the normal course of business, to collection risks. We regularly assess these risks and have established policies and business practices to protect against the adverse effects of collection risks. As a result we do not anticipate any material losses in excess of the allowance for doubtful accounts.

Interest Rate Risk - Interest rate risk refers to fluctuations in the value of a security resulting from changes in the general level of interest rates. Investments that are classified as cash and cash and equivalents have original maturities of three months or less. Changes in the market's interest rates do not affect the value of these investments. Marketable securities are comprised of U.S. Treasury Notes and are classified as available-for-sale and subject to interest rate fluctuations.

RISK FACTORS THAT MAY AFFECT FUTURE RESULTS

WE HAVE ONLY A LIMITED OPERATING HISTORY AND SOME OF OUR SERVICES ARE IN A NEW AND UNPROVEN INDUSTRY.

We have only a limited operating history upon which you can evaluate our business and our prospects. EasyLink was incorporated under the name Globecomm, Inc. in 1994 in the State of Delaware. We launched our business by offering a commercial email service in November 1996 under the name iName. We changed our company name to Mail.com, Inc. in January 1999. In February 2000, we acquired NetMoves Corporation, a provider of a variety of transaction delivery services to businesses. In March 2000, we formed WORLD.com to develop and operate our domain name properties as independent Web sites. In the fourth quarter of 2000, we announced our intention to focus exclusively on the business market and to sell all assets not related to this business. In February 2001, we acquired Swift Telecommunications, Inc., which had contemporaneously acquired the EasyLink Services business from AT&T Corp. The EasyLink Services business is a provider of transaction delivery services such as electronic data interchange or EDI and production messaging services. Swift was a provider of production messaging services, principally telex services. On March 30, 2001, we announced that we had sold our advertising network business to Net2Phone, Inc., and on May 3, 2001 our Asia.com, Inc. subsidiary completed the sale of its business. In October 2001, we sold a subsidiary of India.com, Inc. and have since ceased the conduct of the portal operations of India.com, Inc. In January 2002, we announced our strategy to expand our position in the transaction delivery segment of the electronic commerce market and to begin to offer to our large customer base related transaction management services that automate more components of our customers' business processes. In 2002, we commercially introduced our Document Capture and Management Services which began to generate revenues in 2003. Our success will depend in part upon our ability to maintain or expand our sales of transaction delivery services , our ability to successfully develop transaction management services, the development of a viable market for fee-based transaction management services on an outsourced basis and our ability to compete successfully in those markets. For the reasons discussed in more detail below, there are substantial obstacles to our achieving and sustaining profitability.

WE HAVE INCURRED LOSSES FROM OPERATIONS SINCE INCEPTION.

We have not achieved income from operations in any fiscal year, and we may not be able to achieve or sustain profitability. We incurred a net loss of $85.8 million for the year ended December 31, 2002. We had net income of $50.9 million for the year ended December 31, 2003; however, the net income for 2003 included $54.1 million of gains on debt restructuring and settlements. We had an accumulated deficit of $541.7 million as of September 30, 2004. We intend to upgrade and enhance our technology and networks, continue our international expansion, increase our sales and marketing expenditures and improve and expand our management information and other internal systems. We intend to continue to make strategic acquisitions and investments where resources permit, which may result in significant amortization of intangibles and other expenses or a later impairment charge arising out of the write-off of goodwill booked as a result of such acquisitions or investments. We intend to make these expenditures in anticipation of higher revenues, but there will be a delay in realizing higher revenues even if we are successful. We have experienced declining revenues in each of the years ended December 31, 2003 and 2002 as compared to the prior year. See Part II, Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations contained in our Form 10-K for the year ended December 31, 2003. No assurance can be given that we will be able to offset or otherwise reduce all or any of the cancellation of debt income resulting from the elimination of debt pursuant to our debt restructuring. If we do not succeed in substantially increasing our revenues, our losses may recur.

WE MAY NEED TO RAISE CAPITAL IN THE FUTURE TO INVEST IN THE GROWTH OF OUR BUSINESS AND TO FUND NECESSARY EXPENDITURES.

We may need to raise additional capital in the future. See Part II. Item 7 - Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity and Capital Resources contained in our Form 10-K filed March 30, 2004. At September 30, 2004, we had $11.1 million of cash and cash equivalents. Our principal fixed commitments consist of subordinated convertible notes, senior convertible notes, notes payable, obligations under capital leases, obligations under office space leases, accounts payable and other current obligations, commitments for capital expenditures and commitments for telecommunications services. For each of the four years ended December 31, 2003, 2002, 2001 and 2000, we received a report from our independent accountants containing an explanatory paragraph stating that we suffered recurring losses from operations since inception and have a working capital deficiency that raise substantial doubt about our ability to continue as a going concern. We may need additional financing to invest in the growth of our business and to pay other obligations, and the availability of such financing when needed, on terms acceptable to us, or at all, is uncertain. See "Risk Factors - We have incurred significant indebtedness for money borrowed, and we may be unable to pay debt service on this indebtedness." If we are unable to raise additional financing, generate sufficient cash flow, or restructure our debt obligations before they become due and payable, we may be unable to continue as a going concern.

If we raise additional funds by issuing equity securities or debt convertible into equity securities, stockholders may experience significant dilution of their ownership interest. The amount of dilution resulting from issuance of additional shares of Class A common stock and securities convertible into Class A common stock and the potential dilution that may result from future issuances has significantly increased in light of the decline in our stock price. Moreover, we could issue preferred stock that has rights senior to those of the Class A common stock. Some of our stockholders have registration rights that could interfere with our ability to raise needed capital. If we raise funds by issuing debt, our lenders may place limitations on our operations, including our ability to pay dividends, although we do not anticipate paying any cash dividends on our stock in the foreseeable future.

WE HAVE INCURRED SIGNIFICANT INDEBTEDNESS FOR MONEY BORROWED, AND WE MAY BE UNABLE TO PAY DEBT SERVICE ON THIS INDEBTEDNESS.

As of September 30, 2004, we had outstanding $1.4 million in subordinated convertible notes due in 2005; $10.2 million in principal amount of notes and other obligations due in installments through June, 2006; obligations under office space leases; and commitments for telecommunications services. We currently have $5.6 million in principal and interest payments due during the twelve month period after September 30, 2004. We had an operating loss and negative cash flow for each of the years ended December 31, 2003 and 2002. In addition, we have a substantial amount of outstanding accounts payable and other obligations. Accordingly, cash generated by our operations would have been insufficient to pay the amount of principal and interest payable annually on our outstanding indebtedness and to pay all of our other obligations.

We cannot assure you that we will be able to pay interest and other amounts due on our outstanding indebtedness, or our other obligations, on the scheduled dates or at all. If our cash flow and cash balances are inadequate to meet our obligations, we could face substantial liquidity problems. If we are unable to generate sufficient cash flow or otherwise obtain funds necessary to make required payments, or if we otherwise fail to comply with any covenants in our indebtedness, we would be in default under these obligations, which would permit these lenders to accelerate the maturity of the obligations and could cause defaults under our indebtedness. Any such default could have a material adverse effect on our business, results of operations and financial condition. We cannot assure you that we would be able to repay amounts due on our indebtedness if payment of the indebtedness were accelerated following the occurrence of an event of default under, or certain other events specified in, the agreements governing our outstanding indebtedness and capital leases.

The elimination of outstanding debt pursuant to our debt restructuring completed in 2003 and prior years resulted in substantial cancellation of debt income for income tax purposes. We intend to minimize income tax payable as a result of the restructuring by, among other things, offsetting the income with our historical net operating losses and otherwise reducing the income in accordance with applicable income tax rules. As a result, we do not expect to incur any material current income tax liability as a result of the elimination of this debt. However, the relevant tax authorities may challenge our income tax positions, including the use of our historical net operating losses to offset some or all of the cancellation of debt income and the application of the income tax rules reducing the cancellation of debt income. If we are not able to offset or otherwise reduce the cancellation of debt income, we may incur material income tax liabilities as a result of the elimination of debt and we may be unable to pay these liabilities.

We may incur substantial additional indebtedness in the future. The level of our indebtedness, among other things, could (1) make it difficult for us to make payments on our indebtedness, (2) make it difficult to obtain any necessary financing in the future for working capital, capital expenditures, debt service requirements or other purposes, (3) limit our flexibility in planning for, or reacting to changes in, our business, and (4) make us more vulnerable in the event of a downturn in our business.

WHERE RESOURCES PERMIT, WE INTEND TO CONTINUE TO ACQUIRE, OR MAKE STRATEGIC INVESTMENTS IN, OTHER BUSINESSES AND ACQUIRE OR LICENSE TECHNOLOGY AND OTHER ASSETS AND WE MAY HAVE DIFFICULTY INTEGRATING THESE BUSINESSES OR GENERATING AN ACCEPTABLE RETURN.

We have completed a number of acquisitions and strategic investments since our initial public offering in 1999. For example, we acquired NetMoves Corporation, a provider of production messaging services and integrated desktop messaging services to businesses. We also acquired Swift Telecommunications, Inc. and the EasyLink Services business that it had contemporaneously acquired from AT&T Corp. Where resources permit, we will continue our efforts to acquire or make strategic investments in businesses and to acquire or license technology and other assets, and any of these acquisitions may be material to us. We cannot assure you that acquisition or licensing opportunities will continue to be available on terms acceptable to us or at all. Such acquisitions involve risks, including:

- inability to raise the required capital;

- difficulty in assimilating the acquired operations and personnel;

- inability to retain any acquired member or customer accounts;

- disruption of our ongoing business;

- the need for additional capital to fund losses of acquired businesses;

- inability to successfully incorporate acquired technology into our service offerings and maintain uniform standards, controls, procedures and policies; and

- lack of the necessary experience to enter new markets.

We may not successfully overcome problems encountered in connection with potential acquisitions. In addition, an acquisition could materially impair our operating results by diluting our stockholders' equity, causing us to incur additional debt or requiring us to incur acquisition expenses or amortize or depreciate acquired intangible and tangible assets or to incur impairment charges as a result of the write-off of goodwill recorded as a result of such acquisition.

WE MAY BE UNABLE TO SUCCESSFULLY COMPLETE THE MIGRATION OF THE NETWORK RELATING TO OUR BUSINESS ACQUIRED FROM AT&T OFF OF AT&T PREMISES.

On February 23, 2001, we completed the acquisition of Swift Telecommunications, Inc. which had contemporaneously acquired the EasyLink Services business of AT&T Corp. The EasyLink Services business acquired from AT&T provides a variety of transaction delivery services. This business was a division of AT&T and was not a separate independent operating entity. We hired only a portion of the employees of the business.

Under a Transition Services Agreement entered into in connection with the acquisition, AT&T agreed to provide us with a variety of services to enable us to continue to operate the business pending the transition to EasyLink. We have successfully transitioned virtually all of these services provided by AT&T under the Transition Services Agreement to ourselves, including customer service, network operations center, telex switching equipment and services and office space in a variety of locations. The Transition Services Agreement expired on January 31, 2003. However, the network for the portion of this business relating to EDI, fax and email services continues to reside on AT&T's premises under an agreement with AT&T, but is being operated and maintained by EasyLink. This agreement expires on January 31, 2006, and AT&T has informed us that they will not extend the agreement beyond this date. If we are unable to extend the agreement, we will need to either migrate the network off of the AT&T premises to EasyLink's premises or migrate the customers to a replacement network.

We cannot assure you that we will be able to successfully migrate the remaining EasyLink Services customers or network from AT&T's premises to our own premises, or successfully integrate them into our operations, in a timely manner or without incurring substantial unforeseen expense or without service interruption to our customers. Even if successfully migrated, we may be unable to operate the business at expense levels that are ultimately profitable for us. We cannot assure you that we will be able to retain all of the customers of the EasyLink Services business. Our inability to successfully migrate, integrate or operate the network and operations, or to retain customers, of the EasyLink Services business will result in a material adverse effect on our business, results of operations and financial condition.

OUTSOURCING OF TRANSACTION MANAGEMENT SERVICES MAY NOT PROVE TO BE VIABLE BUSINESS.

An important part of our business strategy is to leverage our existing global customer base and global network by continuing to provide our existing transaction delivery services and by offering these customers additional transaction delivery and new transaction management services in the future. The market for transaction management services is only beginning to develop. Our success will depend on the development of viable markets for the outsourcing of new transaction management services which is somewhat speculative.

There are significant obstacles to the full development of a sizable market for the outsourcing of transaction management services. Outsourcing is one of the principal methods by which we will attempt to reach the size we believe is necessary to be successful. Security and the reliability of the Internet, however, are likely to be of concern to enterprises and service providers deciding whether to outsource their transaction management or to continue to provide it themselves. These concerns are likely to be particularly strong at larger businesses and service providers, which are better able to afford the costs of maintaining their own systems. While we intend to focus exclusively on our outsourced transaction delivery and transaction management services, we cannot be sure that we will be able to maintain or expand our business customer base. In addition, the sales cycle for many of these services is lengthy and could delay our ability to generate revenues in this market.

OUR STRATEGY OF DEVELOPING AND OFFERING TO EXISTING CUSTOMERS ADDITIONAL TRANSACTION DELIVERY AND TRANSACTION MANAGEMENT SERVICES MAY BE UNSUCCESSFUL.

As part of our business strategy, we plan to develop and offer to existing customers additional transaction delivery and transaction management services that will automate more of our customers' business processes. We cannot assure you that we will be able to successfully develop these additional services in a timely manner or at all or, if developed, that our customers will purchase these services or will purchase them at prices that we wish to charge. Standards for pricing in the market for new transaction delivery and transaction management services are not yet well defined and some businesses and service providers may not be willing to pay the fees we wish to charge. We cannot assure you that the fees we intend to charge will be sufficient to offset the related costs of providing these services.

WE MAY FAIL TO MEET MARKET EXPECTATIONS BECAUSE OF FLUCTUATIONS IN OUR QUARTERLY OPERATING RESULTS, WHICH WOULD CAUSE OUR STOCK PRICE TO DECLINE.

We may experience significant fluctuations in our quarterly results. It is likely that our operating results in some quarters will be below market expectations. In this event, the price of our Class A common stock is likely to decline. The following are among the factors that could cause significant fluctuations in our operating results:

- incurrence of other cash and non-cash accounting charges, including charges resulting from acquisitions or dispositions of assets, including from the disposition of our remaining non-core assets, and write-downs of impaired assets;

- increases or decreases in the number of transactions generated by our customers (such as insurance claims, trade and travel confirmations, purchase orders, invoices, shipping notices, funds transfers, among others), which is affected by factors that affect specific customers, the respective industries in which our customers conduct business and the economy generally;

- gains from the restructuring or settlement of debt and other obligations;

- non-cash charges associated with repriced stock options, if our stock price rises above $16.90;

- system outages, delays in obtaining new equipment or problems with planned upgrades;

- disruption or impairment of the Internet;

- demand for outsourced transaction delivery and transaction management services;

- attracting and retaining customers and maintaining customer satisfaction;

- introduction of new or enhanced services by us or our competitors;

- changes in our pricing policy or that of our competitors;

- changes in governmental regulation of the Internet and transaction delivery and transaction management services in particular; and

- general economic and market conditions and global political factors.

Other such factors in our non-core assets include:

- incurrence of additional expenditures without receipt of offsetting revenues pending the sale of these assets.

WE MAY INCUR SIGNIFICANT STOCK BASED COMPENSATION CHARGES RELATED TO REPRICED OPTIONS IF OUR STOCK PRICE RISES ABOVE $16.90.

In light of the decline in our stock price and in an effort to retain our employee base, on November 14, 2000, the Company offered to certain of its employees, officers and directors, other than Gerald Gorman, the right to reprice certain outstanding stock options to an exercise price equal to $16.90 per share, the closing price of the Company's Class A common stock on Nasdaq on November 14, 2000 as adjusted for our reverse stock split effected on January 23, 2002. Options to purchase 632,799 shares were repriced. The repriced options vest at the same rate that they would have vested under their original terms. In March 2000, Financial Accounting Standards Board ("FASB") issued FASB Interpretation No. 44, "Accounting for Certain Transactions Involving Stock

Compensation, an interpretation of APB Opinion No. 25" ("Interpretation"). Among other issues, this Interpretation clarifies (a) the definition of employee for purposes of applying Opinion 25, (b) the criteria for determining whether a plan qualifies as a noncompensatory plan, (c) the accounting consequence of various modifications to the terms of a previously fixed stock option or award, and (d) the accounting for an exchange of stock compensation awards in a business combination. As a result, under the Interpretation, stock options repriced after December 15, 1998 are subject to variable plan accounting treatment. This guidance requires the Company to remeasure compensation cost for outstanding repriced options each reporting period based on changes in the market value of the underlying common stock. If our stock price rises above the $16.90 exercise price of the repriced options, this accounting treatment may result in significant non-cash compensation charges in future periods.

SEVERAL OF OUR COMPETITORS HAVE SUBSTANTIALLY GREATER RESOURCES, LONGER OPERATING HISTORIES, LARGER CUSTOMER BASES AND BROADER PRODUCT OFFERINGS.

Our business is, and we believe will continue to be, intensely competitive. See "Part I Item 1 - Business - Competition" contained in our Form 10-K for the year ended December 31, 2003 and subsequent reports filed with the Securities and Exchange Commission.

Many of our competitors have greater market presence, engineering and marketing capabilities, and financial, technological and personnel resources than those available to us. As a result, they may be able to develop and expand their communications and network infrastructures more quickly, adapt more swiftly to new or emerging technologies and changes in customer requirements, take advantage of acquisition and other opportunities more readily, and devote greater resources to the marketing and sale of their products and services. In addition, current and potential competitors have established or may establish cooperative relationships among themselves or with third parties to increase the ability of their services to address the needs of our current and prospective customers. Accordingly, it is possible that new competitors or alliances among competitors may emerge and rapidly acquire significant market share. In addition to direct competitors, many of our larger potential customers may seek to internally fulfill their messaging needs through the deployment of their own on premises messaging systems.

Some of our competitors provide a variety of telecommunications services and other business services, as well as software and hardware solutions, in addition to transaction delivery or transaction management services. The ability of these competitors to offer a broader suite of complementary services and software or hardware may give them a considerable advantage over us.

The level of competition is likely to increase as current competitors increase the sophistication of their offerings and as new participants enter the market. In the future, as we expand our service offerings, we expect to encounter increased competition in the development and delivery of these services. We may not be able to compete successfully against our current or future competitors.

IT IS DIFFICULT TO RETAIN KEY PERSONNEL AND ATTRACT ADDITIONAL QUALIFIED EMPLOYEES IN OUR BUSINESS AND THE LOSS OF KEY PERSONNEL AND THE BURDEN OF ATTRACTING ADDITIONAL QUALIFIED EMPLOYEES MAY IMPEDE THE OPERATION AND GROWTH OF OUR BUSINESS AND CAUSE OUR REVENUES TO DECLINE.

Our future success depends to a significant extent on the continued service of our key technical, sales and senior management personnel, but they have no contractual obligation to remain with us. In particular, our success depends on the continued service of Gerald Gorman, our Chairman, Thomas F. Murawski, our President and Chief Executive Officer, George Abi Zeid, our President-International Operations, and Michael A. Doyle, our Vice President and Chief Financial Officer. The loss of the services of Messrs. Gorman, Murawski or Abi Zeid or of Mr. Doyle, or several other key employees, would impede the operation and growth of our business.

To manage our existing business and handle any future growth, we will have to attract, retain and motivate additional highly skilled employees. In particular, we will need to hire and retain qualified sales people if we are to meet our sales goals. We will also need to hire and retain additional experienced and skilled technical personnel in order to meet the increasing technical demands of our expanding business. Competition for employees in messaging-related businesses is intense. We have in the past experienced, and expect to continue to experience, difficulty in hiring and retaining employees with appropriate qualifications. If we are unable to do so, our management may not be able to effectively manage our business, exploit opportunities and respond to competitive challenges.

OUR BUSINESS IS HEAVILY DEPENDENT ON TECHNOLOGY, INCLUDING TECHNOLOGY THAT HAS NOT YET BEEN PROVEN RELIABLE AT HIGH TRAFFIC LEVELS AND TECHNOLOGY THAT WE DO NOT CONTROL.

The performance of our computer systems is critical to the quality of service we are able to provide to our customers. If our services are unavailable or fail to perform to their satisfaction, customers may cease using our service. In addition, our agreements with several of our customers establish minimum performance standards. If we fail to meet these standards, our customers could terminate their relationships with us and assert claims for service fee rebates or monetary damages.

WE MAY NEED TO UPGRADE SOME OF OUR COMPUTER SYSTEMS TO ACCOMMODATE INCREASES IN TRAFFIC AND TO ACCOMMODATE INCREASES IN THE USAGE OF OUR SERVICES, BUT WE MAY NOT BE ABLE TO DO SO WHILE MAINTAINING OUR CURRENT LEVEL OF SERVICE, OR AT ALL.

We must continue to expand and adapt our computer systems as the number of customers and the amount of information they wish to transmit increases and as their requirements change, and as we further develop our services. Because we have only been providing some of our services for a limited time, and because our computer systems for these services have not been tested at greater capacities, we cannot guarantee the ability of our computer systems to connect and manage a substantially larger number of customers or meet the needs of business customers at high transmission speeds. If we cannot provide the necessary service while maintaining expected performance, our business would suffer and our ability to generate revenues through our services would be impaired.

The expansion and adaptation of our computer systems will require substantial financial, operational and managerial resources. We may not be able to accurately project the timing of increases in traffic or other customer requirements. In addition, the very process of upgrading our computer systems could cause service disruptions. For example, we may need to take various elements of the network out of service in order to install some upgrades.

OUR COMPUTER SYSTEMS MAY FAIL AND INTERRUPT OUR SERVICE.

Our customers have in the past experienced interruptions in our services. We believe that these interruptions will continue to occur from time to time. These interruptions are due to hardware failures, failures in telecommunications and other services provided to us by third parties and other computer system failures. These failures have resulted and may continue to result in significant disruptions to our service. Some of our operations have redundant switch-over capability. Although we plan to install backup computers and implement procedures on other parts of our operations to reduce the impact of future malfunctions in these systems, the presence of single points of failure in our network increases the risk of service interruptions. In addition, substantially all of our computer and communications systems relating to our services are currently located in Glen Head, New York; Jersey City, New Jersey; Piscataway, New Jersey; Washington, DC; Bridgeton, Missouri; Dayton, Ohio, and London, England. We currently do not have alternate sites from which we could conduct these operations in the event of a disaster. Our computer and communications hardware is vulnerable to damage or interruption from fire, flood, earthquake, power loss, telecommunications failure and similar events. Our services would be suspended for a significant period of time if any of our primary data centers was severely damaged or destroyed. We might also lose customer transaction documents and other customer files, causing significant customer dissatisfaction and possibly giving rise to claims for monetary damages. As a result of the recent relocation of our corporate headquarters during the first quarter of 2003, we plan to consolidate over time an increasing portion of our computer systems and networks at the new location. This consolidation may result in interruptions in our services to some of our customers.

OUR SERVICES WILL BECOME LESS DESIRABLE OR OBSOLETE IF WE ARE UNABLE TO KEEP UP WITH THE RAPID CHANGES CHARACTERISTIC OF OUR BUSINESS.

Our success will depend on our ability to enhance our existing services and to introduce new services in order to adapt to rapidly changing technologies, industry standards and customer demands. To compete successfully, we will have to accurately anticipate changes in business demand and add new features to our services very rapidly. We may not be able to integrate the necessary technology into our computer systems on a timely basis or without degrading the performance of our existing services. We cannot be sure that, once integrated, new technology will function as expected. Delays in introducing effective new services could cause existing and potential customers to forego use of our services.

OUR BUSINESS WILL SUFFER IF WE ARE UNABLE TO PROVIDE ADEQUATE SECURITY FOR OUR SERVICE, OR IF OUR SERVICE IS IMPAIRED BY SECURITY MEASURES IMPOSED BY THIRD PARTIES.

Security is a critical issue for any outsourced transaction delivery or transaction management service, and presents a number of challenges for us. If we are unable to maintain the security of our service, our reputation and our ability to attract and retain customers may suffer, and we may be exposed to liability. Third parties may attempt to breach our security or that of our customers whose networks we may maintain or for whom we provide services. If they are successful, they could obtain information that is sensitive or confidential to a customer or otherwise disrupt a customer's operations or obtain confidential information, including our customer's profiles, passwords, financial account information, credit card numbers, message content, stored email or other personal or business information or similar information relating to our customer's customers. Our customers or their employees or customers may assert claims for money damages for any breach in our security and any breach could harm our reputation.

Our computers are vulnerable to computer viruses, physical or electronic break-ins and similar incursions, which could lead to interruptions, delays or loss of data. We expect to expend significant capital and other resources to license or create encryption and other technologies to protect against security breaches or to alleviate problems caused by any breach. Nevertheless, these measures may prove ineffective. Our failure to prevent security breaches may expose us to liability and may adversely affect our ability to attract and retain customers and develop our business market. Security measures taken by others may interfere with the efficient operation of our service, which may harm our reputation and adversely impact our ability to attract and retain customers. "Firewalls" and similar network security software employed by third parties can interfere with the operation of our services.

Our customers are subject to, and in turn require that their service providers meet, increasingly strict guidelines for network and operational security. If we are unable to meet the security requirements of a customer, we may be unable to obtain or keep their business. This is particularly the case for customers in the health insurance and financial services industries, which are subject to legal requirements governing the security and confidentiality of customer information.

WE ARE DEPENDENT ON LICENSED TECHNOLOGY AND THIRD PARTY COMMERCIAL PARTNERS.

We license a significant amount of technology from third parties, including technology related to our Internet fax services, billing processes and databases. We also rely on third party commercial partners to provide services for our trading community enablement services, document capture and management services and some of our other services. We anticipate that we will need to license additional technology or to enter into additional commercial relationships to remain competitive. We may not be able to license these technologies or to enter into arrangements with prospective commercial partners on commercially reasonable terms or at all. Third-party licenses and strategic commercial relationships expose us to increased risks, including risks relating to the integration of new technology, the diversion of resources from the development of our own proprietary technology, a greater need to generate revenues sufficient to offset associated license or service fee costs, and the possible termination of or failure to renew an important license or other agreement by the third-party licensor or commercial partner.

IF THE INTERNET AND OTHER THIRD-PARTY NETWORKS ON WHICH WE DEPEND TO DELIVER OUR SERVICES BECOME INEFFECTIVE AS A MEANS OF TRANSMITTING DATA, THE BENEFITS OF OUR SERVICE MAY BE SEVERELY UNDERMINED.

Our business depends on the effectiveness of the Internet as a means of transmitting data. The recent growth in the use of the Internet has caused frequent interruptions and delays in accessing and transmitting data over the Internet. Any deterioration in the performance of the Internet as a whole could undermine the benefits of our services. Therefore, our success depends on improvements being made to the entire Internet infrastructure to alleviate overloading and congestion. We also depend on telecommunications network suppliers such as AT&T Corp., MCI and XO Communications for a variety of telecommunications and Internet services. The network for the EasyLink Services business acquired from AT&T continues to reside on AT&T's premises. See "Risk Factors - We may be unable to successfully complete the migration of the network relating to our business acquired from AT&T off of AT&T premises" above, "Item 1. Business - Technology" contained in our Form 10-K for the year ended December 31, 2003 and subsequent filings with the Securities and Exchange Commission.

GERALD GORMAN AND GEORGE ABI ZEID COLLECTIVELY BENEFICIALLY OWNED AS OF OCTOBER 31, 2004 APPROXIMATELY 26.9% OF THE TOTAL OUTSTANDING VOTING POWER OF EASYLINK AND WILL BE ABLE TO EXERT SIGNIFICANT INFLUENCE OVER ANY VOTE OF STOCKHOLDERS.

Gerald Gorman, our Chairman, beneficially owned as of October 31, 2004 Class A and Class B common stock representing approximately 19.5% of the voting power of our outstanding common stock. Each share of Class B common stock entitles the holder to 10 votes on any matter submitted to the stockholders. George Abi Zeid, our President-International Operations and Director, beneficially owned as of October 31, 2004 Class A common stock representing approximately 7.4% of the voting power of our outstanding common stock. Based on their voting power as of October 31, 2004, Mr. Gorman and Mr. Abi Zeid will likely be able to exert significant influence over the outcome of all matters requiring stockholder approval, including the election of directors, amendment of our charter and approval of significant corporate transactions. Mr. Gorman and Mr. Abi Zeid may be in a position to prevent a change in control of EasyLink even if other stockholders holding a majority of the voting power of the shares not held by Mr. Gorman and Mr. Abi Zeid were in favor of the transaction. In addition, our charter contains provisions that could deter or make more expensive a takeover of EasyLink. These provisions include the ability to issue "blank check" preferred stock without stockholder approval.

OUR EXPANSION INTO INTERNATIONAL MARKETS IS SUBJECT TO SIGNIFICANT RISKS AND OUR LOSSES MAY INCREASE AND OUR OPERATING RESULTS MAY SUFFER IF OUR REVENUES FROM INTERNATIONAL OPERATIONS DO NOT EXCEED THE COSTS OF THOSE OPERATIONS.

We intend to continue to expand into international markets and to expend significant financial and managerial resources to do so. We may not be able to compete effectively in international markets. If our revenues from international operations do not exceed the expense of establishing and maintaining these operations, our losses will increase and our operating results will suffer. We face significant risks inherent in conducting business internationally, such as:

- uncertain demand in foreign markets for transaction delivery and transaction management services;

- difficulties and costs of staffing and managing international operations;

- differing technology standards;

- difficulties in collecting accounts receivable and longer collection periods;

- economic instability and fluctuations in currency exchange rates and imposition of currency exchange controls;

- potentially adverse tax consequences;

- regulatory limitations on the activities in which we can engage and foreign ownership limitations on our ability to hold an interest in entities through which we wish to conduct business;

- political instability, unexpected changes in regulatory requirements, and reduced protection for intellectual property rights in some countries;

- export restrictions;

- terrorism; and

- difficulties in enforcing contracts and potentially adverse consequences.

REGULATION OF TRANSACTION DELIVERY AND TRANSACTION MANAGEMENT SERVICES AND INTERNET USE IS EVOLVING AND MAY ADVERSELY IMPACT OUR BUSINESS.

There are currently few laws or regulations that specifically regulate activity on the Internet. However, laws and regulations may be adopted in the future that address issues such as user privacy, pricing, and the characteristics and quality of products and services. For example, the Telecommunications Act of 1996 restricts the types of information and content transmitted over the Internet. Several telecommunications companies have petitioned the FCC to regulate ISPs and online service providers in a manner similar to long distance telephone carriers and to impose access fees on these companies. This could increase the cost of transmitting data over the Internet. Any new laws or regulations relating to the Internet could adversely affect our business.

Moreover, the extent to which existing laws relating to issues such as property ownership, pornography, libel and personal privacy are applicable to the Internet is uncertain. We could face liability for defamation, copyright, patent or trademark infringement and other claims based on the content of messages transmitted over our system. We may also face liability for unsolicited commercial and other email and fax messages sent by users of our services. We do not and cannot screen all the content generated and received by users of our services or the recipients of messages delivered through our services. Some foreign governments, such as Germany, have enforced laws and regulations related to content distributed over the Internet that are more strict than those currently in place in the United States.

A majority of our services are currently classified by the FCC as "information services," and therefore are currently exempt from telecommunication services regulation. While the FCC has until now exercised forbearance in regulating IP communications, it has indicated that it might regulate certain IP communications as "telecommunications services" in the future. There can be no assurance that the FCC will not change its regulatory classification system and thereby subject us to unexpected and burdensome additional regulation. In addition, a variety of states regulate certain telecommunications services when provided on an intrastate basis.

We obtained authorizations from the FCC to provide such telecommunications services in conjunction with our acquisition of these telecommunications services from NetMoves, and are classified as a "non-dominant interexchange carrier." While the FCC has generally chosen not to exercise its statutory power to closely regulate the charges or practices of non-dominant carriers, it will act upon complaints against such carriers for failure to comply with statutory obligations or with the FCC's rules, regulations and policies - to the extent that such services are, in the FCC's view, subject to regulation.

Continued changes in telecommunications regulations may significantly reduce the cost of domestic and international calls. To the extent that the cost of domestic and international calls decreases, we will face increased competition for our fax services which may have a material adverse effect on our business, financial condition or results in operations.

In connection with the deployment of Internet-capable nodes in countries throughout the world, we are required to satisfy a variety of foreign regulatory requirements. We intend to explore and seek to comply with these requirements on a country-by-country basis as the deployment of Internet-capable fax nodes continues. There can be no assurance that we will be able to satisfy the regulatory requirements in each of the countries currently targeted for node deployment, and the failure to satisfy such requirements may prevent us from installing Internet-capable fax nodes in such countries. The failure to deploy a number of such nodes could have a material adverse effect on our business, operating results and financial condition.

Our fax nodes and our faxLauncher service utilize encryption technology in connection with the routing of customer documents through the Internet. The export of such encryption technology is regulated by the United States government. We have authority for the export of such encryption technology other than to countries such as Cuba, Iran, Iraq, Libya, and North Korea. Nevertheless, there can be no assurance that such authority will not be revoked or modified at any time for any particular jurisdiction or in general. In addition, there can be no assurance that such export controls, either in their current form or as may be subsequently enacted, will not limit our ability to distribute our services outside of the United States or electronically. While we take precautions against unlawful exportation of our software, the global nature of the Internet makes it virtually impossible to effectively control the distribution of our services. Moreover, future Federal or state legislation or regulation may further limit levels of encryption or authentication technology. Any such export restrictions, the unlawful exportation of our services, or new legislation or regulation could have a material adverse effect on our business, financial condition and results of operations.

The legal structure and scope of operations of our subsidiaries in some foreign countries may be subject to restrictions which could result in severe limits to our ability to conduct business in these countries. To the extent that we develop or offer messaging services in foreign countries, we will be subject to the laws and regulations of these countries. The laws and regulations relating to the Internet and telecommunications services in many countries are evolving and in many cases are unclear as to their application. For example, in India, the PRC and other countries we may be subject to licensing requirements with respect to the activities in which we propose to engage and we may also be subject to foreign ownership limitations or other approval requirements that preclude our ownership interests or limit our ownership interests to up to 49% of the entities through which we propose to conduct any regulated activities. If these limitations apply to our activities, including our activities conducted through our subsidiaries, our opportunities to generate revenue will be reduced, our ability to compete successfully in these markets will be adversely affected, our ability to raise capital in the private and public markets may be adversely affected and the value of our investments and acquisitions in these markets may decline. Moreover, to the extent we are limited in our ability to engage in certain activities or are required to contract for these services from a licensed or authorized third party, our costs of providing our services will increase and our ability to generate profits may be adversely affected.

OUR INTELLECTUAL PROPERTY RIGHTS ARE CRITICAL TO OUR SUCCESS, BUT MAY BE DIFFICULT TO PROTECT.

We regard our copyrights, service marks, trademarks, trade secrets, domain names and similar intellectual property as critical to our success. We rely on trademark and copyright law, trade secret protection and confidentiality and/or license agreements with our employees, customers, strategic partners and others to protect our proprietary rights. Despite our precautions, unauthorized third parties may improperly obtain and use information that we regard as proprietary. Third parties may submit false registration data attempting to transfer key domain names to their control. Our failure to pay annual registration fees for domain names may result in the loss of these domains to third parties. Third parties have challenged our rights to use some of our domain names, and we expect that they will continue to do so, which may affect the value that we can derive from the planned disposition of the domain names included among our non-core assets.

The status of United States patent protection for software products and services is not well defined and will evolve as additional patents are granted. We have applied for a patent for some of our services, and we do not know if our application will be issued with the scope of the claims we seek or at all. The laws of some foreign countries do not protect proprietary rights to the same extent as do the laws of the United States. Our means of protecting our proprietary rights in the United States or abroad may not be adequate and competitors may independently develop similar technology.

Third parties may infringe or misappropriate our copyrights, trademarks and similar proprietary rights. In addition, other parties have asserted and may in the future assert infringement claims against us. We cannot be certain that our services do not infringe issued patents. Because patent applications in the United States are not publicly disclosed until the patent is issued, applications may have been filed which relate to our services.

We have been and may continue to be subject to legal proceedings and claims from time to time in the ordinary course of our business, including claims related to the use of our domain names and claims of alleged infringement of the trademarks and other intellectual property rights of third parties. Third parties have challenged our rights to register and use some of our domain names based on trademark principles and on the Anticybersquatting Consumer Protection Act. If domain names become more valuable to businesses and other persons, we expect that third parties will continue to challenge some of our domain names and that the number of these challenges may increase. In addition, the existing or future laws of some countries, in particular countries in Europe, may limit or prohibit the use in those countries or elsewhere of some of our geographic names that contain the names of a city in those countries or the name of those countries. Intellectual property litigation is expensive and time-consuming and could divert management's attention away from running our business. These claims and the potential for such claims may reduce the value that we can expect to receive from the disposition of our domain names.

In connection with the sale of our consumer-based email and advertising network business, we transferred to the buyer the rights to direct the "MX" record, or the right to direct email messages addressed to domain names owned by us and used in this business. Although we do not operate the service or have any role in the delivery of messages sent by users of the service, our position as the registrant of the domain names used as addresses for email accounts maintained by such service may subject us to claims from time to time. We could face liability for defamation, copyright, patent or trademark infringement, harassment, unsolicited commercial e-mail and other claims based on the content of the messages transmitted over the service of this business. These claims, even if without merit, can cause us to incur legal expenses and may divert management time and resources.

WE MAY INCUR EXPENSES AND LIABILITIES AS A RESULT OF PENDING LEGAL PROCEEDINGS.

The Company is involved in legal proceedings that may result in additional expenses or liability. See "Legal Proceedings" contained in Part I, Item 3 of our Form 10-K for the year ended December 31, 2003 and "Legal Proceedings" contained in Part II, Item 1 of this Form 10-Q. These proceedings include a broker's fee dispute in which the Company is appealing a $931,000 judgment imposed on it and tax assessments relating to our discontinued India.com business in the amount of approximately $650,000. Although the Company intends to pursue its defense of these matters vigorously, no assurance can be given that the Company's efforts will be successful. To the extent that the Company is not successful in appealing the judgment or defending the tax assessment, it will be required to pay the judgment in the broker's fee dispute or to pay the tax assessment that may be found to apply in the India tax proceedings. The Company has already paid $400,000 into a trust account to secure the payment of the judgment relating to the broker fee if the judgment is upheld on appeal. Although we intend to defend vigorously these matters, we cannot assure you that our ultimate liability, if any, in connection with these matters will not have a material adverse effect on our results of operations, financial condition or cash flows.

A SUBSTANTIAL AMOUNT OF OUR COMMON STOCK MAY COME ONTO THE MARKET IN THE FUTURE, WHICH COULD DEPRESS OUR STOCK PRICE.

Sales of a substantial number of shares of our common stock in the public market could cause the market price of our Class A common stock to decline. As of October 31, 2004, we had an aggregate of 44,213,079 shares of Class A and Class B common stock outstanding. As of October 31, 2004, we had options to purchase approximately 5.2 million shares of Class A common stock outstanding. As of October 31, 2004, we had warrants to purchase 798,523 shares of Class A common stock outstanding. As of October 31, 2004, we had approximately 37,177 shares of Class A common stock issuable upon conversion of outstanding convertible notes and an indeterminate number of additional shares of Class A common stock issuable over three years in payment of interest on $297,000 principal amount of notes.

As of the date of this filing on Form 10-Q, substantially all of the shares of our outstanding Class A common stock and Class B common stock were freely tradable, in some cases subject to the volume and manner of sale limitations contained in Rule 144. We may issue large amounts of additional Class A common stock, which may also be sold and which could adversely affect the price of our stock. Approximately 23.6 million of our outstanding shares were issued in connection with the elimination of debt during the nine months ended September 30, 2003. If the holders of these shares sell large numbers of shares, these holders could cause the price of our Class A common stock to fall.

As of the date of this filing on Form 10-Q, the holders of approximately 8.2 million shares of outstanding Class A common stock, the holders of 0.8 million shares of Class A common stock issuable upon exercise of our outstanding warrants and the holders of approximately 29,657 shares of Class A common stock issuable upon conversion of our outstanding senior convertible notes had the right, subject to various conditions, to require us to file registration statements covering their shares, or to include their shares in registration statements that we may file for ourselves or for other stockholders. By exercising their registration rights and selling a large number of shares, these holders could cause the price of the Class A common stock to fall. An undetermined number of these shares have been sold publicly pursuant to Rule 144.

OUR CLASS A COMMON STOCK MAY BE SUBJECT TO DELISTING FROM THE NASDAQ NATIONAL MARKET.

Our Class A common stock may face potential delisting from the Nasdaq National Market which could hurt the liquidity of our Class A common stock. We may be unable to comply with the standards for continued listing on the Nasdaq National Market. These standards require, among other things, that our Class A common stock have a minimum bid price of $1. Specifically, an issuer will be considered non-compliant with the minimum bid price requirement only if it fails to satisfy the applicable requirement for any 30 consecutive trading day period. It would then be afforded a 90-calendar day grace period in which to regain compliance. In addition, the listing standards require that we maintain compliance with various other standards, including market capitalization or total assets and total revenue, number of publicly held shares, which are shares held by persons who are not officers, directors or beneficial owners of 10% of our outstanding shares, and market value of publicly held shares. Alternatively, we can comply with certain other standards, including a $10 million minimum stockholders' equity requirement. The minimum bid price of our stock was below $1 during various periods in the fourth quarter of 2000 and the first quarter of 2001 and was below $1 during the period from March 14, 2001 through January 22, 2002.

On January 23, 2002, we effected a ten-for-one reverse stock split. Although our stock price exceeded the $1 minimum bid price requirement for a period of time after our reverse stock split, our stock price was also below $1.00 during the period from July 10, 2002 through July 26, 2002 and from July 30, 2002 through August 16, 2002 and from November 18, 2002 until July 11, 2003. Although the Company regained compliance with the minimum bid price requirement on August 4, 2003 after a hearing before a Nasdaq Listing Qualifications Panel, no assurance can be given that we will maintain compliance with the minimum bid price requirement. If we are unable to maintain compliance, we may be subject to delisting.

We had a total stockholders' equity in the amount of $12.0 million as of September 30, 2004 in comparison to the $10 million minimum total stockholders' equity requirement. An alternative listing standard to the minimum total stockholders equity standard requires that we maintain a minimum market value of our publicly held shares of not less than $15 million. As of the filing of this Form 10-Q, we were in compliance with the $15 million minimum market value of publicly held shares alternative standard.

There can be no assurance that EasyLink will maintain compliance with the minimum bid price requirement or that it will maintain compliance with the other listing standards, including the $15 million minimum market value of publicly held shares requirement.

EasyLink notified Nasdaq on October 13, 2004 that, if EasyLink does not appoint another independent director to its board on or before November 12, 2004, EasyLink will no longer be in compliance with Nasdaq Marketplace Rule 4350(c), which requires that a majority of the board of directors be comprised of independent directors as defined in Nasdaq Marketplace Rule 4200. Three of EasyLink's six other members of the board are independent under Nasdaq's rules. Mr. Duff's resignation became effective on November 12, 2004 and EasyLink has not appointed another independent director as of such date. EasyLink is required under Nasdaq Marketplace Rule 4350(c) to regain compliance with the majority independent director requirement by the earlier of its 2005 annual shareholders meeting and one year after the November 12, 2004 effective date of Mr. Duff's resignation. In response to Mr. Duff's departure and the resulting non-compliance with Nasdaq's majority independent director requirement, EasyLink's independent directors have commenced a search for independent director candidates with a view to filling the vacancy created by Mr. Duff's resignation.

If our common stock were to be delisted from trading on the Nasdaq National Market and were neither re-listed thereon nor listed for trading on the Nasdaq Small Cap Market or other recognized securities exchange, trading, if any, in the Class A common stock may continue to be conducted on the OTC Bulletin Board or in the non-Nasdaq over-the-counter market. Delisting would result in limited release of the market price of the Class A common stock and limited news coverage of EasyLink and could restrict investors' interest in our Class A common stock and materially adversely affect the trading market and prices for our Class A common stock and our ability to issue additional securities or to secure additional financing.

OUR STOCK PRICE HAS BEEN VOLATILE AND WE EXPECT THAT IT WILL CONTINUE TO BE VOLATILE.

Our stock price has been volatile since our initial public offering and we expect that it will continue to be volatile. As discussed above, our financial results are difficult to predict and could fluctuate significantly. In addition, the market prices of securities of electronic services companies have been highly volatile. A stock's price is often influenced by rapidly changing perceptions about the future of electronic services or the results of other Internet or technology companies, rather than specific developments relating to the issuer of that particular stock. As a result of volatility in our stock price, a securities class action may be brought against us. Class-action litigation could result in substantial costs and divert our management's attention and resources.

ITEM 4 CONTROLS AND PROCEDURES

As of the end of the period covered by this Quarterly Report on Form 10-Q, our management, including our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of EasyLink's "disclosure controls and procedures," as that term is defined in Rule 13a-15(e) and 15d-15(e) promulgated under the Securities and Exchange Act of 1934, as amended (the "Exchange Act"). Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures are effective to ensure that information required to be disclosed by EasyLink in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms, and to ensure that such information is made known to the Chief Executive Officer and Chief Financial Officer as appropriate to allow timely decisions regarding required disclosure. During the period covered by this Quarterly Report on Form 10-Q, there were no changes in our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II OTHER INFORMATION

ITEM 1: LEGAL PROCEEDINGS

In connection with the Company's appeal of a $931,000 judgment entered by the court in a favor of a broker, the Court permitted the Company, in lieu of posting an appeal bond, to place $50,000 per month for eight months commencing November 7, 2003, for a total of $400,000, into a trust account to provide funds for the payment of the judgment if upheld on appeal. The broker appealed the Court's order permitting the Company to place funds in the trust account in lieu of posting an appeal bond. On April 14, 2004, the United States Court of Appeals for the Second Circuit denied the broker's motion. The Company has paid in full the $400,000 into the trust account. Oral arguments on the appeal occurred on September 22, 2004, and the parties wait the decision of the Court of Appeals.

The Company and DTC have settled the lawsuit by DTC against the Company relating to the termination of a sublease. Under the settlement, the Company paid DTC $30,000 in partial reimbursement for DTC's legal expenses and the parties agreed to exchange mutual releases with respect to all claims under the lease and the lawsuit. The settlement and the release of the signed settlement documents now held in escrow by the attorneys for both sides is subject to the clearance of a check issued by EasyLink to DTC in payment of the $30,000. The court has entered an order dismissing the case with prejudice subject to reinstitution by either party if the settlement is not completed.

The Company previously reported that the staff of the US Securities and Exchange Commission is reviewing certain transactions accounting for approximately $3 million of revenue generated by its former advertising network business in 2000, a year in which the Company reported $61.2 million in total revenue. The staff has informed the Company that it is also reviewing an additional amount of approximately $1.8 million of revenue from the former advertising network business. The Company understands that the staff is in part reviewing whether and to what extent the revenue under review may be recognized under EITF 99-17, relating to accounting for advertising barter transactions, which became effective in January 2000. A substantial majority of the revenue being reviewed was reported after the Company announced its intention to sell its advertising network business, which the Company ultimately sold in March 2001. The Company is engaged in ongoing discussions with the staff regarding the foregoing and has taken the position that the transactions at issue are not material to the Company's 2000 financial statements.

See Part I, Item 3 Legal Proceedings contained in our Form 10-K filing for the year ended December 31, 2003 for a description of the foregoing legal proceedings and other matters.

ITEM 2: CHANGES IN SECURITIES AND USE OF PROCEEDS

Recent Sales of Unregistered Securities

During the three months ended September 30, 2004, the Company issued shares of Class A common stock as follows:

The Company issued 8,964 shares of Class A common stock valued at approximately $11,000 as payment for interest in lieu of cash. The issuance of the shares was made pursuant to the terms of the underlying notes on which the interest accrued and not at the election of the holders of the notes. The issuance of the notes and, therefore, the issuance of the shares in payment of interest were exempt from registration pursuant to the private placement exemption contained in Section 4(2) of the Securities Act because the shares were issued in a transaction not involving a public offering to investors capable of evaluating the merits and risks of the investment and not in need of the protections afforded by registration under the Act.

The Company issued 28,202 shares of Class A common stock valued at approximately $39,000 in connection with matching contributions to its 401(k) plan. These issuances were not subject to the registration requirements of the Securities Act because the issuance of the shares was not voluntary and contributory on the part of employees.

ITEM 4: SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None

ITEM 6 EXHIBITS AND REPORTS ON FORM 8-K

The following exhibits are filed as part of this report:

Exhibit 31.1	Rule 13a-14(a)/15d-14(a) Certification of the Chief Executive Officer
Exhibit 31.2	Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer
Exhibit 32.1	Section 1350 Certification of the Chief Executive Officer
Exhibit 32.2	Section 1350 Certification of the Chief Financial Officer

Reports on Form 8-K - EasyLink Services Corporation filed the following reports on Form 8-K during the three months ended September 30, 2004:

On July 1, 2004, the Company submitted a Form 8-K to report that the staff of the US Securities and Exchange Commission is reviewing certain transactions of its former advertising network business in 2000.

On August 5, 2004, the Company submitted a Form 8-K to furnish its second quarter 2004 earnings announcement pursuant to Item 12 of Form 8-K.

On August 16, 2004, the Company submitted a Form 8-K relating to the sale of its MailWatch service line and certain assets related thereto (the "MailWatch business") to Infocrossing, Inc.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report on Form 10-Q to be signed on its behalf by the undersigned thereto duly authorized.

EasyLink Services Corporation

/s/ MICHAEL A. DOYLE

Vice President and
Chief Financial Officer

November 15, 2004

Exhibit Index

Exhibit 31.1	Rule 13a-14(a)/15d-14(a) Certification of the Chief Executive Officer
Exhibit 31.2	Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer
Exhibit 32.1	Section 1350 Certification of the Chief Executive Officer
Exhibit 32.2	Section 1350 Certification of the Chief Financial Officer