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

FORM 10-KSB

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

For the Fiscal Year Ended December 31, 1998

Commission File Number: 0-27862

REALITY INTERACTIVE, INC.

MINNESOTA	41-1781991
State of Incorporation	I.R.S. Employer Identification Number

Suite 115
6121 Baker Road
Minnetonka, MN 55345
(612) 253-4700

Securities registered under Section 12(g) of the Exchange Act:
COMMON STOCK, $.01 PAR VALUE

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such 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

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulations S-B contained herein, and no disclosure will be contained, to the best of registrants knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB.

/X/

The Company's revenues for the Fiscal Year Ended December 31, 1998 totaled $744,221.

As of February 26, 1999, the Company had 4,677,407 shares of Common Stock outstanding. The aggregate market value of the 2,826,282 shares of Common Stock held by non-affiliates of the Company was $310,891, based on the closing bid price on February 26, 1999 on the Over The Counter Bulletin Board.

Transitional small business disclosure format: Yes No X

DOCUMENTS INCORPORATED BY REFERENCE: Portions of the Company's Proxy Statement for the Annual Meeting of Shareholders for the year ended December 31, 1998 are incorporated by reference in Part III.

FORM 10-KSB INDEX

SAFE HARBOR STATEMENT UNDER THE
PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

This Annual Report on Form 10-KSB contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements involve risks and uncertainties that may cause the Company's actual results to differ materially from the results discussed in the forward-looking statements. Factors that might cause such differences include, but are not limited to, doubt as to the Company's ability to continue as a going concern, the uncertainty in growth of the Company's revenues; limited growth of the market for multimedia education and training products; lack of market acceptance of the Company's products; inability of the Company to expand its marketing capability; inability of the Company to diversify its product offerings; failure of the Company to respond to evolving industry standards and technological changes; inability of the Company to meet its future additional capital requirements; inability of the Company to compete in the business education and training industry; loss of key management personnel; inability to retain subject matter experts; failure of the Company to secure adequate protection for the Company's intellectual property rights; and the Company's exposure to product liability claims. The forward-looking statements are qualified in their entirety by the cautions and risk factors set forth in Exhibit 99.1, under the caption "Cautionary Statement," to this Annual Report on Form 10-KSB for the year ended December 31, 1998.

PART I

ITEM 1. DESCRIPTION OF BUSINESS

GENERAL

Reality Interactive, Inc. (the "Company") was incorporated on May 24, 1994 for the purpose of developing technology-based knowledge solutions for the industrial marketplace. Since inception, the Company has developed several off-the-shelf multimedia training products within the areas of international quality and environmental management standards. To better align with the needs of the marketplace, the Company recently began offering multimedia and web development services to help customers improve business performance through technology-assisted knowledge transfer. The Company consults with its customers to identify initiatives and corporate best practices that are key to improving productivity, quality, cost reduction and time to market. The Company then uses its expertise with interactive technologies, such as the Web and multimedia, to develop solutions that foster enterprise-wide learning and culture change. The main markets for the Company's products and services are the United States and Western Europe.

The Company has incurred operating losses in each period since inception, and has an accumulated deficit of $14,807,494. To continue as a going concern, the Company must significantly increase revenues and continue to control expenses. Future operating results will depend upon many factors, including the rate at which industry adopts interactive multimedia and Web technology for education, training and knowledge transfer, the level of product and price competition, the Company's success in maturing its direct and indirect sales channels and the ability of the Company to manage its expenses in relation to sales. There is no assurance that the Company will be profitable in the future or that the previously mentioned increase in revenues and expense control will materialize.

MARKET BACKGROUND

Historically, organizations have provided training products and services to their employees primarily through videos, audio tapes, books and instructor-led seminars. Such training often requires employees to be away from their jobs for extended periods of time, and in some cases, to travel off-site for their training. Advances in computer and communications technology have caused organizations to rethink the way that training products and services are delivered. Currently, many organizations are beginning to utilize interactive multimedia training, such as CD-ROM and distance learning media (e.g., corporate intranets and the Internet), to overcome many of the cost and time constraints associated with traditional training methods. The Company believes that organizations increasingly are using technology-based learning solutions to accomplish the following training objectives: (i) to allow employees to obtain training "on demand" without leaving their offices, thus lowering the costs associated with off-site training; (ii) to control the learning environment, thus ensuring that training content is consistently delivered; (iii) to improve memory retention of critical work skills, thus improving employee productivity and maximizing the return on training investment; and (iv) to improve the measurement and tracking of employee learning progress. Although technology-based learning solutions promise to improve organizational and employee performance, instructor-led training and consultants are currently the primary means of training delivery in the corporate marketplace. The Company believes, however, that technology-based delivery of training will be used to supplement, and in some cases, replace instructor-led training and consultants.

BUSINESS STRATEGY

The Company's business strategy is to provide its customers with custom and off-the-shelf technology-based knowledge solutions to improve organizational and employee performance. The Company seeks to provide its customers with a broad range of product and service solutions to improve organizational and employee performance.

Such solutions will address the following customer needs:

TECHNOLOGY-ASSISTED KNOWLEDGE TRANSFER: The Company works closely with its customers to perform a thorough needs analysis, and then creates Web and multimedia solutions that become delivery vehicles for education, training and knowledge transfer. The Company's approach is multifaceted, combining instruction, print materials, online documentation and applications, and web-based collaboration tools to harness expert knowledge.

IMPLEMENTATION SUPPORT FOR BEST PRACTICES: The Company offers several packaged solutions in Web and CD-ROM format that capture the knowledge of subject matter experts in topics such as quality management (ISO 9000, QS-9000) and environmental management (ISO 14000 and Pollution Prevention). These packages can be tailored to reflect specific customer needs, programs and practices, and are supported by skilled implementation consultants from the Company's Professional Services Partners Program.

PERFORMANCE IMPROVEMENT SOFTWARE TOOLS: The Company's solutions bridge the gap between learning and doing by including software tools that model best practices, generate project documents, and assist in process analysis and enhancement.

KNOWLEDGE MANAGEMENT SOFTWARE TOOLS: The Company offers tools for creating dynamic knowledge bases that allows information associated with projects, processes and best practices to be collected and retained in a set of linked databases, organized to support key corporate initiatives.

GLOBAL SOLUTIONS IN MULTIPLE LANGUAGES: A core competency of the Company is its ability to create solutions in multiple languages. The Company works with industry experts and context checkers within each country to ensure that the result reflects the cultural assumptions and business practices of that region. Several of the Company's products are available in international versions, including German, French and Spanish.

PRODUCTS

The Company has developed off-the-shelf product solutions for both intranet and CD-ROM delivery. These products can be tailored at multiple levels to reflect specific corporate policies and procedures.

WEB-BASED: These products use the corporate intranet as a platform for learning and culture change around corporate initiatives, with links from training to online policies, procedures and resources.

CD-ROM: These products combine interactive multimedia instruction with hundreds of pages of print materials, including sample manuals, presentation overheads, project leader guides and checklists. CD-ROMs provide performance support in the form of online software tools for generating key business documents, including draft budgets, project plans and documented procedures.

The Company has developed four products within the areas of international quality and environmental management standards, which are discussed below in more detail:

QUALITY MANAGEMENT SOLUTIONS

The Company's family of quality management products provide training, software tools and online documents, all of which have been designed to follow a business process approach to quality system implementation. Consulting implementation support can be provided to customers through the Company's Professional Services Partner Program.

ISO 9000 IN THE WORKPLACE (WEB)
Uses the corporate intranet as a platform for education and training on the ISO 9000 international quality management standards and their impact on an organization. Intended for general employee and management awareness to facilitate culture change.

ISO 9000 REGISTRATION SERIES (CD-ROM)
A five-part multimedia performance support system that provides expert knowledge and software tools on the ISO 9000 quality process. It includes training for management, the project team and internal auditors, as well as software tools for generating project documentation.

QS-9000 COMPLIANCE SERIES (CD-ROM)
A four-part multimedia performance support system that guides companies through each step of these automotive quality requirements. It includes training for management, the project team and internal auditors, as well as software tools for generating project documentation.

ENVIRONMENTAL MANAGEMENT SOLUTIONS

Around the globe, organizations are adopting a new approach to environmental issues--a shift from reactive, end-of-pipe approaches for controlling environmental impact to more proactive approaches that incorporate environmental management into the entire business system. The Company has developed both Web and CD-ROM products that support the implementation of the ISO 14000 international environmental management system standards and Pollution Prevention programs. These products can optionally be supported by expert consultants from the Company's Professional Services Partner Program.

ISO 14000 IN THE WORKPLACE (WEB)
This product uses the corporate intranet as a platform for education and training on the ISO 14000 international environmental management standards and their impact on an organization. Intended for general employee and management awareness to facilitate culture change.

ISO 14000 EMS CONFORMANCE SERIES (CD-ROM)
A five-part multimedia performance support system that guides companies through the development, implementation and management of an environmental management system in accordance with this international environmental management standard. It includes training for management, the project team and internal auditors, as well as software tools for generating project documentation.

POLLUTION PREVENTION (CD-ROM)
A CD-ROM/Internet hybrid product that provides performance support tools for analyzing pollution reduction options. It also includes executive-level education on the business rationale for proactive pollution prevention, with an emphasis on source reduction. Users can link directly from within the product to a Company-maintained website that references national and regional pollution prevention resources on the Internet.

Each individual CD-ROM title generally sells for a price of $795 to $995, with discounts being offered for increasing levels of purchase commitments. Each web-based product is generally priced to sell at a fixed price per company employee, with discounts being offered based on the number of employees who access the program.

INTERNATIONAL PRODUCT VERSIONS

Localizing multimedia content for non-U.S. markets is far more challenging than conventional software localization because of differences in culture and business practices, which affect images, audio, video and instructional approach. The Company's localized products are not merely translations, but completely new products that are reviewed and validated by industry experts within the target country.

Current localized products:

/ / ISO 14000 IN THE WORKPLACE Web-based training in Spanish, French and German

/ / QS-9000 REGISTRATION SERIES CD-ROMs in German

ENTERPRISE KNOWLEDGE MANAGEMENT PRODUCTS

The Company has developed a new line of products focused specifically on Enterprise Knowledge Management (EKM-TM-). This evolving family of products uses the corporate intranet to facilitate the capture, collection, amplification and dissemination of corporate information and knowledge. As each new EKM product module is conceptualized and developed, it will be linked with the other modules to create a common, multifaceted network of tools to affect knowledge transfer in support of business process improvement.

Initial EKM products include the following:

EKM:EXPERTLINK-TM-
This product creates an online knowledge base via question/answer exchange. Employees seeking answers to questions can search and query the existing Q&A knowledge base. If the answer is not found, a question can be submitted to one or more qualified experts. Experts edit and respond to question/answer pairs in a secure area of a corporate intranet, and can provide links to additional resources on the Web. Once the answer is added to the knowledge base, an email notification is pushed to the questioner automatically.

With respect to the development of additional off-the-shelf multimedia training and knowledge management products, the Company intends to let market demand determine the direction of its product development strategy. The Company believes that such product development strategy may mature in the area of web-based performance improvement tools that can be adapted to a broad range of corporate needs.

SERVICES

The Company consults with customers on key best practice initiatives that enable them to gain access to new markets, improve organizational performance, comply with customer and regulatory mandates or realize a significant competitive advantage. These initiatives require intensive process analysis and realignment of procedures. The Company's consulting staff performs an extensive analysis of the training and knowledge needs for each initiative, and then develops customized learning and performance support solutions that deliver the training and knowledge to employees across the enterprise. These solutions can be delivered via the Web or CD-ROM.

SALES AND MARKETING

As discussed below, the Company uses several channels of marketing and distribution.

DIRECT SALES. Direct sales focuses on selling to Fortune 2000 companies. Sales cycles for this channel generally range from six to twelve months.

INDEPENDENT SALES AGENTS. The Company's independent sales agent program is primarily comprised of small to medium-sized companies that specialize in selling multimedia training or technology business solutions, or have demonstrated competencies in the area of international management standards.

CHANNEL RESELLERS. Channel resellers warehouse, market and distribute the Company's products. The Company has an agreement with the American Society for Quality ("ASQ") to warehouse, market and distribute its ISO 9000 and QS-9000 products. In addition, the Company has established a relationship with the Automotive Industry Action Group ("AIAG") to distribute the Company's QS-9000 products.

INTERNATIONAL DISTRIBUTORS. Currently, the Company is primarily focusing its international sales efforts on the Western European market. The Company also is represented in Asia Pacific markets.

MARKETING PARTNERS. The Company has developed relationships with certain organizations to act as promoters of the Company's products. Currently, the Company has relationships with the American National Standards Institute ("ANSI") and the Global Environment & Technology Foundation ("GETF") to market and promote the Company's ISO 14000 product.

PROFESSIONAL SERVICES PARTNER PROGRAM. The Company has developed a network of independent consultants who are trained in using the Company's digital tools as part of their solution set for customers. These consulting partners provide gap analysis, management consulting, documentation generation, project support and internal auditor training.

CLIENTS

The Company seeks to establish long-term relationships with companies desiring technology-based training and knowledge solutions. The Company has developed sales relationships with numerous companies, primarily through sales of its off-the-shelf CD-ROM products. The Company will attempt to further develop these relationships to involve the delivery of custom development services. Following is a partial list of new or repeat customers during 1997:

Hasbro	General Motors Corporation +	Boeing Corporation
Sundstrand Corporation +	Synergie Gmbh + *	G & K Services

+ Represents customers who, on a combined basis, accounted for 58% of the Company's revenue during 1998.

* Synergie Gmbh is the Company's German distributor.

COMPETITION

The market for resources that prepare companies for compliance to international management standards, such as ISO 9000, QS-9000 and ISO 14000, is highly fragmented. No single company has a dominant market share, and the Company generally competes with a variety of competitors, depending on factors such as the size of the customer, specific business requirements, geographic location and the level of investment anticipated by the customer.

The international standards market has traditionally been served by consultants, instructor-led training and companies that market books, manuals, tapes and similar technology solutions. Companies providing consulting services, who may also provide training services, on ISO 9000, QS-9000 and ISO 14000, such as Andersen Consulting, Ernst & Young and Grant Thornton, enjoy a high level of customer loyalty with respect to the implementation of enterprise-wide business practices. Companies providing technology solutions similar to the Company's product offerings include Powerway, Inc. and SystemCorp. The Company can offer no assurance that it will be ultimately successful in competing with such companies.

With respect to custom multimedia development services, the technology training industry is highly competitive, and the Company expects the intensity of competition to increase. The Company competes with numerous privately-held companies that provide custom multimedia development services, many of which have stronger client relationships, a better established market presence and a greater capacity to provide custom development services than the Company. The Company can offer no assurance that it will be ultimately successful in competing with such companies.

INTELLECTUAL PROPERTY RIGHTS

The Company regards its multimedia products as proprietary and relies primarily on a combination of statutory and common law copyright, trademark and trade secret laws, customer licensing agreements, employee and third-party non-disclosure agreements and other methods to protect its proprietary rights.

The Company's products are licensed to end-users under a perpetual, non-transferable, non-exclusive license. The Company relies primarily on a "shrink-wrap" license for protection, which is included inside the product packaging. Such a license sets forth the terms and conditions under which the customer may use the product and binds the purchaser upon purchase and use of the product. The Company does not require its shrink wrap licenses to be signed by the licensee and therefore may be unenforceable under the laws of certain jurisdictions.

The Company has made applications for registration of certain trademarks in the United States and other parts of the world where its products are actively marketed. Currently, the Company has received registration for the mark "Reality Interactive (and Logo Design)" in the United States, Switzerland, Benelux, France and Germany. The Company also has received registration for the mark "Real Tools for Accelerated Learning" in the United States. The Company has applied for trademark registration for the marks "Enterprise Knowledge Management," "EKM" and "EKM:ExpertLink" related to its product strategy in the area of knowledge management.

RESEARCH AND DEVELOPMENT

The Company's research and development expenditures are primarily comprised of direct employee costs. The Company also incurs outside product development costs related to subject matter content expertise, video and audio production and specialized computer programs.

For 1998, 1997 and 1996, the Company incurred research and development expenditures of $545,192, $1,351,658 and $2,355,922, respectively.

EMPLOYEES

As of February 26, 1999, the Company had 11 full-time employees and 1 independent contractor, including 3 in sales and marketing, 3 in administration and finance and 6 in research and development. This represents a 50% decrease in personnel since February 28, 1998. The Company's employees are not represented by any collective bargaining organization and the Company has never experienced a work stoppage. The Company believes its employee relations are good.

ITEM 2. DESCRIPTION OF PROPERTY

The Company's executive office is located in Minnetonka, Minnesota, where it leases approximately 10,000 square feet under a sublease that expires in July 2003. Under the sublease, the Company is obligated to pay an annual rent of approximately $145,000.

The Company considers its leased real property adequate for its current and foreseeable future, and in the opinion of management, is adequately covered by insurance.

ITEM 3. LEGAL PROCEEDINGS

NONE

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

NONE

PART II

ITEM 5. MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

A. MARKET PRICE OF COMMON STOCK

The Company's common stock trades on the Over The Counter Bulletin Board (OTC BB) under the symbol RINT. The following table sets forth the high and low prices of the Company's Common Stock for each calendar quarter for the past two years.

YEAR ENDED DECEMBER 31, 1998			YEAR ENDED DECEMBER 31, 1997		
QUARTER	HIGH	LOW	QUARTER	HIGH	LOW
First	$0.69	$0.28	First	$1.50	$0.63
Second	$0.78	$0.09	Second	$1.25	$0.50
Third	$0.28	$0.06	Third	$1.14	$0.50
Fourth	$0.17	$0.04	Fourth	$0.86	$0.25

As of March 26, 1999, the Company had 96 shareholders of record of the Company's Common Stock. The Company has never paid cash dividends on its common stock and does not anticipate paying cash dividends in the foreseeable future.

B. CHANGES IN SECURITIES (USE OF PROCEEDS FROM PUBLIC OFFERING)

NONE

ITEM 6. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION.

The following presentation of management's discussion and analysis of the Company's financial condition and results of operation should be read in conjunction with the Company's financial statements and notes contained herein for the years ended December 31, 1998 and 1997.

RESULTS OF OPERATIONS

REVENUES. Revenues were $744,221 for 1998, compared to revenues of $1,220,023 for 1997, a 39% decrease. This decrease was due primarily to a decrease in sales of the Company's CD-ROM products from $906,918 for 1997 to $384,637 for 1998. This sales decrease was attributed to a decrease in the Company's emphasis on its CD-ROM products because the market for training on international management standards never materialized.

Product and service revenues from clients that individually exceeded 10% of the Company's total revenues included three clients at 26%, 20% and 12% for the year ended December 31, 1998. For 1997, the Company generated revenue of approximately $689,000 from certain affiliates and divisions of General Motors Corporation. This revenue was the result of sales from the Company's QS-9000 COMPLIANCE SERIES and custom intranet development services. No other customers of the Company accounted for more than 10% of its revenue.

COST OF REVENUES. Cost of revenues were $346,743 for 1998, compared to $399,144 for 1997. The decrease in cost of revenues was primarily due to the decrease in product sales, although the Company experienced an increase in costs related to the completion of service contracts.

OPERATING EXPENSES. The Company's operating expenses for 1998 were $2,229,350, a 47% decrease over operating expenses of $4,231,268 for 1997. This decrease in operating expenses between 1998 and 1997 was due primarily to expense control measures that were implemented in response to lower revenues, and is further detailed in the following discussion:

(a) SALES AND MARKETING. Sales and marketing expenses were $493,908 for 1998, compared to $1,112,846 for 1997, a 56% decrease. This decrease between periods was due primarily to lower staffing, travel and general selling expenses as the Company focused its resources on sales opportunities in its local market. The Company also continued its cutbacks in direct product marketing initiatives, such as tradeshow and literature expenses.

The Company expects that sales and marketing expenses for 1999 will decrease from 1998 levels.

(b) RESEARCH AND DEVELOPMENT. Research and development expenses were $545,192 for 1998, compared to $1,351,658 for 1997, a 60% decrease. This decrease is primarily attributable to a decrease in development staff and a shift towards developing customer-specific products. Such customer-specific development costs are classified as cost of revenues when related project revenues are recognized.

For 1999, the Company expects that research and development expenses will decrease from 1998 levels.

(c) GENERAL AND ADMINISTRATIVE. General and administrative expenses were $1,190,250 for 1998, compared to $1,766,764 for 1997, a 33% decrease. This decrease was due primarily to a decrease in office rent, operating leases and professional fees associated with being a smaller company.

The Company expects that its general and administrative expenses for 1999 will decrease over 1998 levels.

OTHER INCOME (EXPENSE). The Company's net other income was $54,444 for 1998, compared to net other income of $175,467 for 1997. For 1998 and 1997, net other income consisted entirely of interest earned on short-term investments, with the decrease between years being attributed to declining cash reserves.

NET LOSS. Net loss was $1,777,428 for 1998, compared to a net loss of $3,234,922 for 1997. The Company expects to continue to experience losses for the foreseeable future in 1999 as its projected revenues will fall below its base operating expenses.

LIQUIDITY AND CAPITAL RESOURCES

The Company's cash and cash equivalents, and short-term investments were $291,697 as of December 31, 1998, compared to $2,018,539 as of December 31, 1997. This decrease in cash, cash equivalents and short-term investments was due primarily to the net loss from operations for the year ended December 31, 1998.

The Company expects that its current cash balance, along with collections from its existing accounts receivable and future revenue sources, will allow the Company to meet its obligations at least through May 31, 1999. See "Doubt as to the Company's Ability to Continue as a Going Concern".

DOUBT AS TO THE COMPANY'S ABILITY TO CONTINUE AS A GOING CONCERN

The Company has incurred operating losses in each period since inception, and anticipates that it will continue to experience operating losses and negative cash flow from operations for the foreseeable future in 1999. The Company believes that its current cash and accounts receivable balance, along with expected revenues over the foreseeable future, will not be sufficient to meet its working capital and capital expenditure requirements for all of 1999. Therefore, if the Company is to remain in business through December 1999, or future years, the Company will need to raise additional funds to finance its operations. In the event the Company requires additional financing, there can be no assurance that debt or equity financing will be available to the Company on favorable terms or at all.

IMPACT OF THE YEAR 2000 ISSUE

The Year 2000 Issue is the result of computer programs being written using two digits rather than four to define the applicable year. Some computer programs that have date-sensitive software may recognize a date using "00" as the year 1900 rather than the year 2000. All of the software produced by the Company has been analyzed and the Company is not aware of any potential for date recognition problems in its products. The Company also uses off-the-shelf software ("Administrative Software") produced by third parties for use in administrative functions such as word processing, billing and record keeping. The vendors of the Company's Administrative Software products have indicated that such products are Year 2000 compliant. In the event that any of these programs are susceptible to date recognition problems, this could result in a system failure or miscalculations causing disruptions of operations, including, among other things, a temporary inability to process critical business transactions. In the event that the Company experiences Year 2000 problems, the Company believes the cost to remedy such problems will be immaterial.

ITEM 7. FINANCIAL STATEMENTS

INDEX TO FINANCIAL STATEMENTS

ITEM 8. CHANGES AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

A report dated January 11, 1999 on Form 8-K was filed regarding a change in the Company's auditor for the year ending December 31, 1998.

PART III

ITEM 9. DIRECTORS, EXECUTIVE OFFICERS, PROMOTERS AND CONTROL PERSONS; COMPLIANCE WITH SECTION 16(a) OF THE EXCHANGE ACT.

The information under the captions "Election of Directors," "Executive Officers" and "Section 16(a) Beneficial Ownership Reporting Compliance," are contained in the Company's Proxy Statement relating to the Annual Meeting of Shareholders for the year ended December 31, 1998, and is incorporated herein by reference.

ITEM 10. EXECUTIVE COMPENSATION

The information contained under the caption "Executive Compensation" in the Company's Proxy Statement relating to the Annual Meeting of Shareholders for the year ended December 31, 1998 is incorporated herein by reference.

ITEM 11. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The information contained under the caption "Principal Shareholders" in the Company's Proxy Statement relating to the Annual Meeting of Shareholders for the year ended December 31, 1998 is incorporated herein by reference.

ITEM 12. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The information contained under the caption "Certain Relationships and Related Transactions" in the Company's Proxy Statement relating to the Annual Meeting of Shareholders for the year ended December 31, 1998 is incorporated herein by reference.

ITEM 13. EXHIBITS AND REPORTS ON FORM 8-K

(a) Index of Exhibits

Exhibit Number	Description
3.1(1)	Articles of Incorporation of the Company
3.2(1)	Amended and Restated Articles of Incorporation of the Company
3.3(1)	Bylaws of the Company
3.4(1)	Amended Bylaws of the Company
4.1(1)	Specimen form of the Company's Common Stock Certificate
4.2(1)	Warrant Agreement (including Form of Redeemable Warrant)
4.3(1)	Form of Bridge Loan Agreement, dated January 19, 1996, between the Company and various investors (including form of Bridge Note and Bridge Warrant)
4.4(1)	Canceled Promissory Note in favor of Brightstone Fund VI in the amount of $200,000
4.5(1)	Canceled Promissory Note in favor of Wyncrest Capital, Inc. in the amount of $120,000
4.6(1)	Warrant in favor of Brightstone Fund VI for 43,109 shares

Exhibit Number	Description
4.7(1)	Warrant in favor of Wyncrest Capital, Inc. for 25,188 shares
10.1(1)	ISO 9000 Content Agreement between Reality Interactive, Inc. and Process Management International, dated August 4, 1994
10.2(1)	Joint Marketing and Distribution Agreement between Reality Interactive, Inc. and American Society for Quality Control, Inc., dated May 10, 1995
10.3(1)	Agreement for Consulting Services between Reality Interactive, Inc. and Steven W. McClernon, dated January 15, 1996
10.4(1)	Sublease Agreement between Reality Interactive, Inc. and Collopy Saunders Real Estate, Inc., dated December 15, 1994
10.5(1)	Subject Matter Expert Agreement between Reality Interactive, Inc. and The Third Generation, Inc., dated January 6, 1996
10.6(1)	Subject Matter Expert Agreement between Reality Interactive, Inc. and WRITAR, dated February 1, 1996
10.7(1)	Reality Systems, Inc. 1994 Stock Incentive Plan, as amended (including form of Stock Option Agreement)
10.8(1)	Form of Non-Statutory Directors' Option Agreement (issued to certain non-employee directors or affiliates of non-employee directors in 1994 and 1995)
10.9(1)	Reality Interactive, Inc. 1996 Directors Stock Option Plan (including form of Directors Stock Option Agreement)
10.10(1)	Form of Shrink-Wrap License Agreement
10.11(1)	Form of Enterprise License Agreement
10.12(1)	Form of Volume Discount Agreement
10.13(1)	ISO 9000/QS-9000 Addendum, dated March 13, 1996, between the Company and Process Management Institute, Inc., amending the agreement dated August 4, 1994
10.14(1)	Form of Lock-Up Agreement
10.15(1)	Independent Software Vendor Agreement between the Company and Hewlett Packard
10.16(1)	Master Equipment Lease Agreement, dated June 15, 1995, and Amendment No. 1 to Master Equipment Lease Agreement, dated July 1995, each between the Company and Carlton Financial Corporation 10.17(1) Lease Agreement, dated January 30, 1996, between the Company and Lease Finance Group, Inc.
10.18(1)	Irrevocable Letters of Credit, dated June 20, 1995 and August 1, 1995, from BankWindsor in favor of Carlton Financial Corp. and Irrevocable Letter of Credit, dated December 27, 1995, in favor of Lease Finance Group, Inc.
10.19(2)	First Amendment to Joint Marketing and Distribution Agreement between Reality Interactive, Inc. and American Society for Quality Control, Inc., dated May 1, 1996
10.20(2)	Joint Marketing and Distribution Agreement between Reality Interactive, Inc. and American Society for Quality Control, Inc., dated May 17, 1996
10.21(3)	Equipment Lease between Reality Interactive, Inc. and Dexxon Capital Corporation Dated June 3, 1996
10.22(4)	Copyright License Agreement between Reality Interactive, Inc. and the American National Standards Institute dated August 30, 1996, including Modifying Agreement
10.23(4)	ISO 14000 Marketing and Promotion Agreement between Reality Interactive, Inc. and the American National Standards Institute dated September 20, 1996
10.24(4)	ISO 14000 Marketing and Promotion Agreement between Reality Interactive, Inc. and the Global Environment and Technology Foundation dated September 6, 1996
10.25(4)	Distribution Agreement between Reality Interactive, Inc. and Futuremedia PLC dated July 12, 1996
10.26(5)	Sublease Agreement between Reality Interactive, Inc. and IVI Publishing, Inc., dated September 17, 1996

Exhibit Number	Description
10.27(5)	Distribution Agreement between Reality Interactive, Inc. and Lasermedia (Deutschland) GMBH, dated October 9, 1996
10.28(5)	Amendment No. 2, dated December 9, 1996, to Master Equipment Lease Agreement, dated July 1995, each between the Reality Interactive, Inc. and Carlton Financial Corporation
10.29(5)	Irrevocable Letter of Credit, dated December 9, 1996, from BankWindsor in favor of Carlton Financial Corp.
10.30(6)	Master Distribution Agreement between Reality Interactive, Inc. and Interactive Media Communications, dated February 24, 1997
10.31(6)	Multinational Copyright Exploitation Agreement between Reality Interactive, Inc. and the International Organization for Standardization, dated February 17, 1997
10.32(6)	Multinational Copyright Exploitation Agreement between Reality Interactive, Inc. and the International Organization for Standardization, dated February 17, 1997
23.1	Consent of Price Waterhouse LLP
23.2	Consent of Lund Koehler Cox & Arkema LLP
27.1	Financial Data Schedule for the Year Ended December 31, 1998
99.1	Cautionary Statement

(1) Incorporated by reference to Amendment No. 2 to the Company's Registration Statement on Form SB-2 (File No. 333-01508C), as filed with the Securities and Exchange Commission on April 9, 1996.

(2) Incorporated by reference to the Company's Form 10-QSB for the quarter ended March 31, 1996.

(3) Incorporated by reference to the Company's Form 10-QSB for the quarter ended June 30, 1996.

(4) Incorporated by reference to the Company's Form 10-QSB for the quarter ended September 30, 1996.

(5) Incorporated by reference to the Company's Form 10-KSB for the year ended December 31, 1996.

(6) Incorporated by reference to the Company's Form 10-QSB for the quarter ended March 31, 1997.

(b) Reports on Form 8-K

A report dated January 11, 1999 on Form 8-K was filed regarding a change in the Company's auditor for the year ended December 31, 1998.

SIGNATURES

In accordance with Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

REALITY INTERACTIVE, INC.

Dated: March 31, 1999

By /S/ Wesley W. Winnekins

Wesley W. Winnekins
Chief Financial Officer

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

Name	Title	Date
/S/ Paul J. Wendorff ------------------------ Paul J. Wendorff	Chairman, Chief Executive Officer, President and Director (Principal Executive Officer)	March 31, 1999
/S/ Wesley W. Winnekins ------------------------ Wesley W. Winnekins	Chief Financial Officer and Secretary (Principal Financial and Accounting Officer)	March 31, 1999

EXHIBIT INDEX

EXHIBIT 23.1

CONSENT OF PRICEWATERHOUSECOOPERS LLP

CONSENT OF INDEPENDENT ACCOUNTANTS

We hereby consent to the incorporation by reference in the Registration Statement on Form S-8 (No. 333-05027) of Reality Interactive, Inc. of our report dated February 16, 1998 appearing in this Form 10-KSB.

/S/ PricewaterhouseCoopers LLP
- -------------------------------
PricewaterhouseCoopers LLP
Minneapolis, Minnesota
March 31, 1999

EXHIBIT 23.2

CONSENT OF LUND KOEHLER COX & ARKEMA LLP

CONSENT OF INDEPENDENT ACCOUNTANTS

As independent public accountants, we hereby consent to the incorporation by reference in the Registration Statement on Form S-8 (No. 333-05027) of Reality Interactive, Inc. of our report dated February 24, 1999 appearing in this Form 10-KSB.

/S/ Lund Koehler Cox and Arkema LLP
- -----------------------------------
Lund Koehler Cox and Arkema LLP
Minneapolis, Minnesota
March 31, 1999

5

YEAR
DEC-31-1998
DEC-31-1998
291,697
0
231,525
0
0
563,521
453,003
389,170
747,710
121,738
0
0
0
46,774
579,198
747,710
744,221
798,665
346,743
346,743
2,229,350
0
0
(1,777,428)
0
(1,777,428)
0
0
0
(1,777,428)
(0.38)
(0.38)

EXHIBIT 99.1

CAUTIONARY STATEMENT

Reality Interactive, Inc. (the "Company"), or persons acting on behalf of the Company, or outside reviewers retained by the Company making statements on behalf of the Company, or underwriters, from time to time make, in writing or orally, "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. When used in conjunction with an identified forward-looking statement, this Cautionary Statement is for the purpose of qualifying for the "safe harbor" provisions of such sections and is intended to be a readily available written document that contains factors which could cause results to differ materially from such forward-looking statements. These factors are in addition to any other cautionary statements, written or oral, which may be made or referred to in connection with any such forward-looking statement.

The following matters, among others, may have a material adverse effect on the business, financial condition, liquidity, results of operations or prospects, financial or otherwise, of the Company. Reference to this Cautionary Statement in the context of a forward-looking statement or statements shall be deemed to be a statement that any or more of the following factors may cause actual results to differ materially from those in such forward-looking statement or statements:

DOUBT AS TO THE COMPANY'S ABILITY TO CONTINUE AS A GOING CONCERN. The Company has incurred operating losses in each period since inception, and anticipates that it will continue to experience operating losses and negative cash flow from operations for the foreseeable future in 1999. The Company believes that its current cash and accounts receivable balance, along with expected revenues over the foreseeable future, will not be sufficient to meet its working capital and capital expenditure requirements for all of 1999. Therefore, if the Company is to remain in business through December 1999, the Company will need to raise additional funds to finance its operations. In the event the Company requires additional financing, there can be no assurance that debt or equity financing will be available to the Company on favorable terms or at all.

FUTURE ADDITIONAL CAPITAL REQUIREMENTS; NO ASSURANCE FUTURE CAPITAL WILL BE AVAILABLE. If the Company is unable to generate substantial revenues from its operations or if the Company's expenses exceed expectations, the Company will likely require additional funds to meet its capital requirements. The Company does not currently have available bank financing. The Company may be required to raise additional funds through public or private financings, including equity financings, or through collaborative arrangements. There can be no assurance that additional financing would be available on favorable terms, or at all. If funding is not available when needed or on acceptable terms, the Company may be forced to curtail its operations significantly or cease operations and abandon its business entirely.

DEVELOPING MARKET; MARKET ACCEPTANCE. The market for educating and training businesses has historically been served by consultants, instructor-led training and training publications such as books, manuals and tapes. Currently, there is little use of multimedia and web-based education and training products and services by businesses, and many of the Company's potential customers do not own or have access to the necessary equipment. The Company's future success will depend upon, among other factors, the extent to which companies acquire equipment compatible with the Company's products and services, and adopt and use multimedia and web-based education and training programs. In addition, the Company's success will depend in part on its ability to market and sell multiple copies of its products, as well as sell its custom development services, to large corporate customers. In the event that adoption and use of equipment compatible with the Company's products and services do not become widespread, the number of potential customers of the Company will be limited. There can be no assurance that the Company's products, the prices the Company charges for its products or its development services will be acceptable to the market or that the Company will be able to sell multiple copies of its products to large corporate customers.

LIMITED MARKETING CAPABILITY. The Company currently has a small sales and marketing staff and limited number of strategic alliances relating to distribution of its products. There can be no assurance that the Company will be able to build a suitable sales force or enter into satisfactory marketing alliances with third parties, or that its sales and marketing efforts will be successful.

DEPENDENCE ON DIVERSIFICATION OF PRODUCT OFFERINGS. The Company currently has a limited number of product offerings, and purchasers of the Company's products are not required to purchase additional products. Accordingly, the Company's products represent non-recurring revenue sources, and the success of the Company is dependent, in part, on its ability to develop sustained demand for its current products and to develop and sell additional products. There can be no assurance that the Company will be successful in developing and maintaining such demand or in developing and selling additional products.

DEPENDENCE ON EVOLVING INDUSTRY STANDARDS. The Company's initial product offerings prepare businesses for adherence to worldwide management standards. The failure of the Company to enhance its products in a timely manner to changes in the standards, the lack of public acceptance of such standards or the delay in introduction of or enhancement to such standards would materially adversely affect the Company's operations.

TECHNOLOGICAL CHANGE. The industry in which the Company competes is characterized by rapid technological change. The introduction of products embodying new technology can render existing products and product formats obsolete and unmarketable. The Company's success will depend on its ability to anticipate changes in technology and to develop and introduce new and enhanced products in a timely manner in response to technological changes, or if products or product enhancements by the Company do not achieve market acceptance, the Company's business would be materially adversely affected.

COMPETITION. The business education and training industry is highly competitive. A large number of companies are currently developing multimedia and web-based training, educational and instructional aids. Competitors also include national, regional and local accounting firms engaged in industrial consulting and instructor-led training and companies which market training tools such as books, videos and audio tapes. Some of the Company's existing competitors, as well as a number of potential competitors, have larger technical staffs, more established marketing and sales organizations, and greater financial resources than the Company. There can be no assurance the Company will be able to compete successfully with such companies, or at all.

FLUCTUATIONS IN OPERATING RESULTS. The Company's future operating results may vary substantially from quarter to quarter. At its current stage of operations, the Company's quarterly revenues and results of operations may be materially affected by the timing of the development and market acceptance of the Company's products. Generally, operating expenses will be higher during periods in which product development costs are incurred and marketing efforts are commenced. Due to these and other factors, including the general economy, stock market conditions and announcements by the Company or its competitors, the market price of the securities offered hereby may be highly volatile.

DEPENDENCE ON KEY PERSONNEL; LACK OF EMPLOYMENT AND NONCOMPETITION AGREEMENTS. The success of the Company is dependent in large part upon the ability of the Company to attract and retain key management and operating personnel. Qualified individuals are in high demand and are often subject to competing offers. In the future, the Company will need to hire additional skilled personnel in the areas of research and development, and sales and marketing. There can be no assurance that the Company will be able to attract and retain the qualified personnel needed for its business. The Company has no employment or noncompetition agreements with any of its management or other personnel.

DEPENDENCE ON ABILITY TO RETAIN SUBJECT MATTER EXPERTS. The Company's product development strategy requires the Company to retain third-party subject matter experts to perform research and development functions by providing accurate and informative content for the Company's products. There can be no assurance that the Company will be able to continue to attract and retain qualified subject matter experts required to develop new products and enhance existing products. The inability of the Company to attract and retain such experts could have a material adverse effect on the Company and its prospects.

INTELLECTUAL PROPERTY. The Company regards its multimedia products as proprietary and relies primarily on a combination of statutory and common law copyright, trademark and trade secret laws, customer licensing agreements, employee and third-party nondisclosure agreements and other methods to protect its proprietary rights. Despite these precautions, it may be possible for a third party to copy or otherwise obtain or use the Company's products or technology without authorization, or to develop similar products or technology independently. If unauthorized use or copying of the Company's product were to occur to any substantial degree, the Company's business and results of operations could be materially adversely affected. There can be no assurance that the Company's means of protecting its proprietary rights will be adequate or that the Company's competitors will not independently develop similar products.

The Company believes that developers of multimedia and web-based products may increasingly be subject to such claims as the number of products and competitors in the industry grows and the functionality of such products in the industry overlaps. Any such claim, with or without merit, could result in costly litigation and could have a material adverse effect on the Company.

LACK OF PRODUCT LIABILITY INSURANCE. The Company may face a risk of exposure to product liability claims in the event that use of its products is alleged to have resulted in damage to its customers. The Company does not currently carry product liability insurance. There can be no assurance that such insurance will be available on commercially reasonable terms, or at all, or that such insurance, even if obtained, would adequately cover any product liability claim. A product liability or other claim with respect to uninsured liabilities or in excess of insured liabilities could have a material adverse effect on the business and prospects of the Company.

INDEX TO FINANCIAL STATEMENTS

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To Reality Interactive, Inc.:

We have audited the accompanying balance sheet of Reality Interactive, Inc. as of December 31, 1998, and the related statements of operations, stockholders' equity and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of Reality Interactive, Inc. as of December 31, 1997 were audited by other auditors whose report dated February 16, 1998 expressed an unqualified opinion on those statements.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Reality Interactive, Inc. as of December 31, 1998, and the results of its operations and its cash flows for the year then ended, in conformity with generally accepted accounting principles.

The accompanying financial statements have been prepared assuming that Reality Interactive, Inc. will continue as a going concern. As discussed in Note 1 to the financial statements, Reality Interactive, Inc. has suffered recurring losses from operations and has a significant accumulated deficit that raises substantial doubt about its ability to continue as a going concern. Management's plans in regard to these matters are also described in Note 1. The 1998 financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Minneapolis, Minnesota
February 24, 1999

/S/ LUND KOEHLER COX & ARKEMA LLP

REALITY INTERACTIVE, INC.
BALANCE SHEET

	DECEMBER 31, 1997	DECEMBER 31, 1998
ASSETS		
Current assets:		
Cash and cash equivalents	$ 487,994	$ 291,697
Short-term investments	1,530,545	0
Accounts receivable	410,916	231,525
Inventory	71,197	0
Prepaid expenses and other current assets	52,357	40,299
Total current assets	2,553,009	563,521
Fixed assets, net	121,971	63,833
Restricted cash	58,500	111,000
Other assets	19,850	9,356
Total assets	$ 2,753,330	$ 747,710
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 36,117	$ 38,733
Accrued liabilities	130,213	31,938
Deferred revenue	181,906	49,495
Other current liabilities	1,694	1,572
Total current liabilities	349,930	121,738
Commitments (Note 5)		
Stockholders' equity:		
Common stock, $.01 par value, 25,000,000 shares authorized 4,677,407 shares issued and outstanding at both dates	46,774	46,774
Additional paid-in capital	15,386,692	15,386,692
Accumulated deficit	(13,030,066)	(14,807,494)
Total stockholders' equity	2,403,400	625,972
Total liabilities and stockholders' equity	$ 2,753,330	$ 747,710

See accompanying notes to the financial statements.

REALITY INTERACTIVE, INC.
STATEMENT OF OPERATIONS

	YEAR ENDED DECEMBER 31, 1997	1998
Product revenues	$ 906,918	$ 384,637
Service revenues	313,105	359,584
Total revenues	1,220,023	744,221
Cost of product revenues	203,951	81,682
Cost of service revenues	195,193	265,061
Total cost of revenues	399,144	346,743
Gross profit	820,879	397,478
Operating expenses:		
Sales and marketing	1,112,846	493,908
Research and development	1,351,658	545,192
General and administrative	1,766,764	1,190,250
Total operating expenses	4,231,268	2,229,350
Operating loss	(3,410,389)	(1,831,872)
Other income (expense):		
Interest income	175,467	54,444
Net loss	$(3,234,922)	$(1,777,428)
Basic and Diluted Loss Per Share:	$ (0.69)	$ (0.38)
Weighted average common shares outstanding	4,677,407	4,677,407

See accompanying notes to the financial statements.

REALITY INTERACTIVE, INC.
STATEMENT OF STOCKHOLDERS' EQUITY

	NUMBER OF SHARES ISSUED	COMMON STOCK	ADDITIONAL PAID-IN CAPITAL	ACCUMULATED DEFICIT	TOTAL STOCKHOLDERS' EQUITY
Balance at December 31, 1996	4,677,407	46,774	15,386,692	(9,795,144)	5,638,322
Net loss	-	-	-	(3,234,922)	(3,234,922)
Balance at December 31, 1997	4,677,407	$ 46,774	$ 15,386,692	$ (13,030,066)	$ 2,403,400
Net loss	-	-	-	(1,777,428)	(1,777,428)
Balance at December 31, 1998	4,677,407	$ 46,774	$ 15,386,692	$ (14,807,494)	$ 625,972

See accompanying notes to the financial statements.

REALITY INTERACTIVE, INC.
STATEMENT OF CASH FLOWS

	YEAR ENDED DECEMBER 31, 1997	YEAR ENDED DECEMBER 31, 1998
Cash flows from operating activities:		
Net loss	$(3,234,922)	$(1,777,428)
Reconciliation of net loss to net cash used by operating activities:		
Depreciation and amortization	96,308	63,115
Changes in assets and liabilities:		
Accounts receivable	(313,520)	179,391
Inventory	63,656	71,197
Prepaid expenses and other assets	19,109	22,552
Accounts payable	(80,272)	2,618
Accrued liabilities	11,527	(98,275)
Deferred revenue	179,209	(132,411)
Other current liabilities	(7,954)	(122)
Net cash used by operating activities	(3,266,859)	(1,669,363)
Cash flows from investing activities:		
Purchases of fixed assets	(26,343)	(4,977)
Purchases of short-term investments	(180,832)	(32,979)
Sales of short-term investments	3,395,000	1,563,522
Cash restricted for operating leases	58,300	(52,500)
Net cash used by investing activities	3,246,125	1,473,066
Net cash provided (used) during period	(20,734)	(196,297)
Cash and cash equivalents:		
Beginning of period	508,728	487,994
End of period	$ 487,994	$ 291,697

See accompanying notes to the financial statements.

1. ORGANIZATION AND STATUS

Reality Interactive, Inc. (the Company) was incorporated on May 24, 1994 for the purpose of developing technology-based knowledge solutions for the corporate marketplace. Since inception, the Company has developed several off-the-shelf multimedia training products within the areas of international quality and environmental management standards. To better align with the needs of the marketplace, the Company recently began offering multimedia and web development services to help customers improve business performance through technology-assisted knowledge transfer. The Company consults with its customers to identify initiatives and corporate best practices that are key to improving productivity, quality, cost reduction and time to market. The Company then uses its expertise with interactive technologies, such as the Web and multimedia, to develop solutions that foster enterprise-wide learning and culture change. The main markets for the Company's products and services are the United States and Western Europe.

The accompanying financial statements have been prepared on the basis that the Company will continue as a going concern, which contemplates the realization of assets and satisfaction of liabilities in the normal course of business. The Company has incurred operating losses in each period since inception, and has an accumulated deficit of $14,807,494. The Company expects that its current cash balance, along with collections from its existing accounts receivable and future revenue sources, will allow the Company to meet its obligations at least through May 31, 1999. To continue as a going concern, the Company must significantly increase revenues and continue to control expenses. Future operating results will depend upon many factors, including the rate at which industry adopts interactive multimedia and Web technology for education, training and knowledge transfer, the level of product and price competition, the Company's success in maturing its sales capabilities and the ability of the Company to manage its expenses in relation to sales. There is no assurance that the Company will be profitable in the future or the previously mentioned revenue increase and expense control will materialize.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

USE OF ESTIMATES
The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

CASH AND CASH EQUIVALENTS
Cash and cash equivalents include highly liquid investments with original maturities of less than 90 days and are generally invested in money market funds and certificates of deposit. The Company maintains its cash in bank deposit accounts at various financial institutions with high credit quality. The balances, at times, may exceed federally insured limits.

SHORT-TERM INVESTMENTS
Short-term investments consisted of commercial paper held for periods generally less than 90 days. These investments are considered available for sale and are carried at fair value. The estimated fair value of the investments approximates the amortized cost, and therefore, there are no unrealized gains or losses.

REVENUE RECOGNITION
Revenue derived from product sales and licenses is recognized upon shipment of the products. The Company has no significant obligations after shipment. Revenue derived from multimedia and Web-based development services is recognized on the percentage of completion method over the life of each project, which may range from three to nine months. Project costs include all direct labor costs and other direct costs related to service performance, such as contract labor, supplies and equipment costs. The Company's use of the percentage of completion method of revenue recognition requires estimates of the degree of project completion. To the extent these estimates prove to be inaccurate, the revenues and gross profits, if any, reported during the periods where the project is ongoing may not accurately reflect the final results of the project. Provisions for any estimated losses on uncompleted contracts are made in the period in which such losses are determinable. Revenue is reported net of reimbursable expenses.

ACCOUNTS RECEIVABLE
The Company considers all accounts receivable to be fully collectible. Accordingly, no allowance for uncollectible accounts has been established. If accounts become uncollectible, they are charged to operations when that determination has been made. The Company extends unsecured credit to customers in the normal course of business.

INVENTORY
Inventory consisted primarily of software media, manuals and related packaging materials. Inventory is carried at the lower of cost or market using the first-in, first-out valuation method.

FIXED ASSETS
Fixed assets are stated at cost. Accelerated depreciation methods are used for both book and tax purposes over the estimated useful life of the equipment ranging from three to seven years. Leasehold improvements were amortized over the lease term using the straight-line method.

INCOME TAXES
Income taxes are accounted for using the liability method under the provisions of Statement of Financial Accounting Standards (SFAS) No. 109, "Accounting for Income Taxes."

NET LOSS PER SHARE
In February 1997, the Financial Accounting Standards Board issued Statement No. 128, "Earnings Per Share" (SFAS No. 128). SFAS No. 128 applies to entities with publicly held common stock and is effective for financial statements for both interim and annual periods ending after December 15, 1997. After the effective date, all prior-period earnings (loss) per share data presented were restated to conform to the provisions of this statement. Under SFAS No. 128, the presentation of primary earnings (loss) per share is replaced with a presentation of basic earnings (loss) per share. SFAS No. 128 requires dual presentation of basic and diluted earnings (loss) per share for entities with complex capital structures. Basic earnings (loss) per share includes no dilution and is computed by dividing net earnings (loss) available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted earnings (loss) per share reflects the potential dilution of securities that could share in the earnings of an entity and is

similar to the former fully diluted earnings (loss) per share calculation. The Company has adopted SFAS No. 128 and all net earnings (loss) per share data presented complies with this statement. For the years ended December 31, 1998, and for all prior periods presented, basic and diluted loss per share for the Company is the same because the inclusion of stock options and warrants as common stock equivalents would be antidilutive.

PRODUCT DEVELOPMENT AND RESEARCH

Expenditures for software development costs and research are expensed as incurred. Such costs are required to be expensed until the point that technological feasibility and proven marketability of the product is established. Costs otherwise capitalizable after technological feasibility is achieved are also generally expensed because they are insignificant.

DEFINED CONTRIBUTION PLAN

The Company has established a qualified 401(k) profit sharing plan which allows eligible employees to defer a portion of their salary. The Plan does not require any discretionary Company contributions.

3. FIXED ASSETS

Fixed assets consist of the following:

	DECEMBER 31, 1997	DECEMBER 31, 1998
Computer equipment	$ 318,821	$ 332,938
Office equipment and furniture	120,065	120,065
Leasehold improvements	9,140	0
	448,026	453,003
Less accumulated depreciation and amortization	(326,055)	(389,170)
	$ 121,971	$ 63,833

4. INCOME TAXES

Significant components of the Company's deferred tax assets are as follows:

	DECEMBER 31, 1997	DECEMBER 31, 1998
Deferred tax assets:		
Net operating loss carryforwards	$ 5,268,000	$ 5,978,000
Other	50,000	50,000
Total deferred tax assets	5,318,000	6,028,000
Less valuation allowance	(5,318,000)	(6,028,000)
Net deferred tax assets	$ -	$ -

At December 31, 1998, the Company had net operating loss carryforwards of approximately $14,605,000 for income tax purposes. The net operating loss carryforwards expire in 2009 through 2013 if not previously utilized.

The Company has determined, based on the weight of available evidence at December 31, 1998, that it is more likely than not the Company's deferred tax assets will not be realized. Accordingly, a valuation allowance has been established for the tax benefits of these items. Future utilization of the available net operating loss carryforwards may be limited under Internal Revenue Code Section 382 due to future significant changes in ownership.

5. COMMITMENTS

LEASES
The Company leases office space, equipment and furniture under various operating lease agreements, the last of which expires in 2003.

At December 31, 1998, future minimum lease payments under noncancelable operating leases were as follows:

YEAR ENDING DECEMBER 31,	OPERATING LEASES
1999	$ 182,859
2000	145,411
2001	144,756
2002	144,756
2003	84,441
Total future minimum lease payments	$ 702,223

Rent expense was approximately $341,164 and $440,070 for the years ended December 31, 1997 and 1998, respectively.

The Company has entered into agreements with third party content providers and marketing partners that require royalty payments to be made based upon the sales of the Company's products. The amount expensed under these agreements for 1997 and 1998 totaled approximately $153,396 and $48,402, respectively.

LETTERS OF CREDIT
The Company has outstanding a letter of credit from a bank as security for an operating lease of office space. The Company is required to maintain the cash as collateral at the bank which issued the letter of credit. This amount is reflected as restricted cash at December 31, 1998.

6. STOCKHOLDERS' EQUITY

COMMON STOCK ISSUED
The holders of Common Stock are entitled to one vote for each share on all matters submitted to a vote of stockholders. Holders of Common Stock have no preemptive, subscription or conversion rights and there are no redemption or sinking fund provisions applicable thereto. The outstanding shares of Common Stock are fully paid and nonassessable.

WARRANTS

A summary of the Company's warrant activity is as follows:

	NUMBER	EXERCISE PRICE	EXPIRATION
Outstanding at December 31, 1996	3,365,922	$2.40-$8.00	1998-2001
1997 - No activity	-		
Outstanding at December 31, 1997	3,365,922	$2.40-$8.00	1998-2001
Expired	(7,625)	$3.00	12/31/98
Outstanding at December 31, 1998	3,358,297	$2.40-$8.00	1999-2001

Such warrants were issued in connection with various financing transactions by the Company. The holders of these warrants are not entitled to vote, receive dividends or exercise any other rights until such warrants have been duly exercised and payment of the purchase price has been made.

STOCK OPTIONS

At December 31, 1998, the Company had 700,000 shares of common stock reserved under its 1994 Stock Incentive Plan. The plan provides for grants of incentive and nonqualified stock options to officers, employees and independent contractors. Furthermore, the Company may grant nonqualified options outside of this plan. These stock options generally vest evenly over a three to four year period and are exercisable over periods up to five years from date of grant. In addition, the Company had 400,000 shares of common stock reserved under its 1996 Directors' Stock Option Plan. This plan provides for annual grants of options to purchase 10,000 shares of Common Stock per director per year and vests six months from the date of grant.

The Board of Directors establishes all terms and conditions of each grant. Stock options are granted at or above fair market value as determined by the Board of Directors at each grant date.

Option transactions under these plans are summarized as follows:

STOCK INCENTIVE PLAN	OPTIONS OUTSTANDING	EXERCISE PRICE PER SHARE	WEIGHTED AVERAGE EXERCISE PRICE PER SHARE
Options outstanding at December 31, 1996	498,050	$1.00 - $5.25	$2.87
Granted	585,600	$0.45 - $1.00	$0.82
Canceled	(600,550)	$0.81 - $5.25	$2.45
Options outstanding at December 31, 1997	483,100	$0.45 - $4.44	$0.90
Granted	180,000	$0.75	$0.75
Canceled	(75,600)	$0.50 - $4.44	$0.81
Options outstanding at December 31, 1998	587,500	$0.45 - $1.80	$0.87
Exercisable at December 31, 1998	102,625	$0.45 - $1.80	$1.08

DIRECTOR'S STOCK OPTION PLAN	OPTIONS OUTSTANDING	EXERCISE PRICE PER SHARE	WEIGHTED AVERAGE EXERCISE PRICE PER SHARE
Options outstanding at December 31, 1996	-	-	-
Granted	20,000	$1.13	$1.13
Options outstanding at December 31, 1997	20,000	$1.13	$1.13
Granted	10,000	$0.25	$0.25
Canceled	(30,000)	$0.25 - $1.13	$0.83
Options outstanding at December 31, 1998	0		

The following tables summarize stock options outstanding and exercisable at December 31, 1998:

	OUTSTANDING			EXERCISABLE	
EXERCISE PRICE RANGE	OPTIONS	WEIGHTED AVERAGE CONTRACTUAL LIFE REMAINING	WEIGHTED AVERAGE EXERCISE PRICE	OPTIONS	WEIGHTED AVERAGE EXERCISE PRICE
$0.45 - $0.89	446,500	3.70	$ 0.73	44,875	$ 0.64
$1.00	111,000	3.69	1.00	27,750	1.00
$1.80	30,000	0.78	1.80	30,000	1.80
	587,500	3.61	$ 0.87	102,625	$ 1.08

The estimated weighted average grant-date fair value of stock options granted during 1998 was $0.75 per option and $0.32 per option in 1997.

The Company adopted SFAS No. 123, "Accounting for Stock-Based Compensation." As allowed by SFAS No. 123, the Company applies APB Opinion No. 25 and related interpretations in accounting for its stock option plans and, accordingly, does not recognize compensation expense related thereto. If the Company had elected to recognize compensation expense based on the fair value of the options granted at grant date as prescribed by SFAS No. 123, net loss and net loss per share would have been increased to the pro forma amounts indicated in the following table:

	1997	1998
Net loss - as reported	$ (3,234,922)	$ (1,777,428)
Net loss - pro forma	$ (3,323,557)	$ (1,821,136)
Basic and Diluted net loss per share - as reported	$ (0.69)	$ (0.38)
Basic and Diluted net loss per share - pro forma	$ (0.71)	$ (0.39)

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following assumptions:

	1997	1998
Expected dividend level	0%	0%
Expected stock price volatility	50%	50%
Risk-free interest rate	6%	5.4%
Expected life of options	4 years	4 years

7. SIGNIFICANT CUSTOMERS

Product and service revenues from clients that individually exceeded 10% of the Company's total revenues included three clients at 26%, 20% and 12% for the year ended December 31, 1998, and one client at 56% for the year ended December 31, 1997. Accounts receivable from two of these customers represented approximately 26% and 23% of total accounts receivable at December 31, 1998.