PRIVATE MEDIA GROUP INC
Form 10-Q
August 14, 2009

U.S. SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended June 30, 2009

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from______ to______.

Commission file number 000-25067

PRIVATE MEDIA GROUP, INC.

(Exact Name of Registrant as Specified in its Charter)

Nevada	**87-0365673**
(State or other jurisdiction of	**(I.R.S. Employer Identification Number)**

incorporation or organization)

537 Stevenson Street, San Francisco, California 94103

(Address of U.S. principal executive offices)

Calle de la Marina 16-18, Floor 18, Suite D, 08005 Barcelona, Spain

(Address of European principal executive offices)

U.S. (415) 575-9700, Europe 34-93-620-8090

(Issuer s telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the past 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 þ No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes ¨ No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated file, a non-accelerated filer, or a smaller reporting company (as defined in Rule 12b-2 of the Act).

Large Accelerated Filer ¨ Accelerated Filer ¨ Non-accelerated filer ¨ Smaller Reporting Company þ

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ¨ No þ

State the number of shares outstanding of each of the issuer s classes of common equity, as of the latest practicable date

Class	**Outstanding at August 11, 2009**
Common Stock, par value $.001	62,114,803

PART I FINANCIAL INFORMATION

Item 1. Financial Statements

PRIVATE MEDIA GROUP, INC.

CONSOLIDATED BALANCE SHEETS

	December 31, 2008 EUR	June 30, (Unaudited) 2009 EUR	2009 USD
	(in thousands)		
ASSETS			
Cash and cash equivalents	552	484	681
Trade accounts receivable	6,066	5,501	7,747
Related party receivable	7,038	7,244	10,203
Inventories - net (Note 3)	5,038	4,394	6,189
Deferred income tax asset	6,188	6,188	8,716
Prepaid expenses and other current assets	1,238	865	1,219
TOTAL CURRENT ASSETS	26,120	24,676	34,755
Library of photographs and videos	15,138	13,539	19,069
Property, plant and equipment	3,154	6,122	8,623
Other intangible assets	2,971	4,813	6,779
Goodwill (Note 2)	2,132	10,107	14,235
Other investments	1,022	1,022	1,439
Other assets	321	307	432
TOTAL ASSETS	50,859	60,585	85,331
LIABILITIES AND SHAREHOLDERS EQUITY			
Short-term borrowings	4,401	4,297	6,053
Current portion of long-term borrowings		141	199
Accounts payable trade	3,816	5,645	7,951
Income taxes payable	1,087		
Deferred income taxes	24	24	34
Accrued other liabilities	920	1,802	2,539
TOTAL CURRENT LIABILITIES	10,249	11,910	16,775
Contingent consideration payable (Note 2)		3,575	5,035
Related party payable		203	285
Other long-term liabilities		218	307
TOTAL LIABILITIES	10,249	15,906	22,402
SHAREHOLDERS EQUITY			
$4.00 Series A Convertible Preferred Stock 10,000,000 shares authorized, none issued and outstanding at December 31, 2008 and June 30, 2009, respectively			
Common Stock, $.001 par value, 100,000,000 shares authorized 53,580,494 and 62,114,803 issued and outstanding at December 31, 2008 and June 30, 2009, respectively	885	892	1,256
Additional paid-in capital	21,728	28,366	39,952
Retained earnings	22,074	19,686	27,726
Accumulated other comprehensive income	(4,077)	(4,264)	(6,005)
TOTAL SHAREHOLDERS EQUITY	40,610	44,680	62,929

TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	50,859	60,586	85,332

See accompanying notes to consolidated statements.

PRIVATE MEDIA GROUP, INC.

CONSOLIDATED STATEMENTS OF INCOME (LOSS)

AND COMPREHENSIVE INCOME (LOSS)

	Three-months ended June 30, (unaudited)			Six-months ended June 30, (unaudited)	
	2008 EUR	2009 EUR	2008 EUR	2009 EUR	2009 USD
			(in thousands)		
Net sales	5,200	6,175	10,452	11,979	16,872
Cost of sales	3,562	4,030	6,959	7,595	10,698
Gross profit	1,638	2,145	3,493	4,384	6,175
Selling, general and administrative expenses	2,858	4,371	6,114	7,979	11,238
Operating income (loss)	(1,220)	(2,226)	(2,621)	(3,595)	(5,064)
Interest expense	70	94	148	191	270
Interest income	40	54	116	110	155
Income (loss) before income taxes	(1,250)	(2,266)	(2,653)	(3,677)	(5,178)
Income tax (benefit)	(424)	713	(987)	(1,288)	(1,815)
Net income (loss)	(826)	(1,553)	(1,666)	(2,388)	(3,364)
Other comprehensive income:					
Foreign currency translation adjustments	(4)	34	(764)	(186)	(263)
Comprehensive income	(830)	(1,519)	(2,430)	(2,575)	(3,626)
Net income (loss) per share:					
Basic	(0.02)	(0.03)	(0.03)	(0.04)	(0.06)
Diluted	(0.02)	(0.03)	(0.03)	(0.04)	(0.06)

See accompanying notes to consolidated statements.

PRIVATE MEDIA GROUP, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Six-months ended June 30, (unaudited)		
	2008 EUR	2009 EUR	2009 USD
	(in thousands)		
Cash flows from operating activities:			
Net income (loss)	(1,666)	(2,388)	(3,364)
Adjustment to reconcile net income to net cash flows from operating activities:			
Depreciation	582	457	644
Stock based compensation	7	2	3
Bad debt provision	55	222	313
Amortization of other intangible assets	62	62	87
Amortization of web pages		809	1,140
Amortization of photographs and videos	3,162	2,979	4,196
Effects of changes in operating assets and liabilities:			
Trade accounts receivable	1,617	420	592
Related party receivable	(116)	(192)	(270)
Inventories	470	861	1,212
Prepaid expenses and other current assets	1,008	481	677
Accounts payable trade	(442)	(54)	(76)
Income taxes payable	(976)	(1,087)	(1,531)
Accrued other liabilities	(100)	48	68
Net cash provided by operating activities	3,664	2,620	3,690
Cash flows used in investing activities:			
Investment in library of photographs and videos	(2,618)	(1,380)	(1,944)
Capital expenditures	(870)	(956)	(1,346)
Cash received in acquisition		35	50
Investments in (sale of) other assets	35	15	21
Net cash (used in) investing activities	(3,454)	(2,286)	(3,220)
Cash flows from financing activities:			
Short-term borrowings repayments	(230)	(294)	(414)
Short-term borrowings additions	250	66	93
Long-term borrowings repayments	(111)	(17)	(23)
Long-term borrowings additions		29	40
Net cash (used in) provided by financing activities	(91)	(216)	(304)
Foreign currency translation adjustment	(764)	(186)	(263)
Net (decrease) increase in cash and cash equivalents	(645)	(69)	(97)
Cash and cash equivalents at beginning of the period	1,599	552	777
Cash and cash equivalents at end of the period	954	484	681
Cash paid for interest	96	88	123
Cash paid for taxes			

See accompanying notes to consolidated statements.

PRIVATE MEDIA GROUP, INC.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY

	Common stock		Additional		Accumulated other	Total
	Shares	Amounts EUR	paid-in capital EUR	Retained earnings EUR	comprehensive income EUR	shareholders equity EUR
Balance at January 1, 2008	53,580,494	885	21,718	27,262	(3,118)	46,748
Stock based compensation			9			9
Translation adjustment					(959)	(959)
Net income (loss)				(5,188)		(5,188)
Balance at December 31, 2008	53,580,494	885	21,727	22,074	(4,077)	40,610
Shares issued in acquisition (Note 2)	8,534,309	7	6,637			6,644
Stock based compensation			2			2
Translation adjustment					(186)	(186)
Net income (loss)				(2,388)		(2,388)
Balance at June 30, 2009	62,114,803	892	28,366	19,686	(4,264)	44,681

See accompanying notes to consolidated statements.

PRIVATE MEDIA GROUP, INC.

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS

(UNAUDITED)

1. Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles (U.S. GAAP) for interim financial information. Accordingly they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation of financial position and results of operations have been included. Operating results for the three months period ended June 30, 2009 are not necessarily indicative of the results that may be expected for the year ended December 31, 2009. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company s annual report on form 10-K for the year ended December 31, 2008.

Solely for the convenience of the reader, the accompanying consolidated financial statements as of June 30, 2009 and for the three months then ended have been translated into United States dollars (USD) at the rate of EUR 0.71 per USD 1.00 the interbank exchange rate on June 30, 2009. The translations should not be construed as a representation that the amounts shown could have been, or could be, converted into US dollars at that or any other rate.

Supplemental Accounting Policies

The Company s revenue recognition policies are in accordance with Staff Accounting Bulletin (SAB) No. 104, Revenue Recognition in Financial Statements. One of the Company s primary sources of revenue is sales of its video on-demand offerings, which are sold directly via its on-line retail website and paid for almost exclusively by credit card. The Company recognizes revenue from video-on-demand when the service is rendered and collectibility is reasonably assured, specifically, when the customer s credit card is charged, which is, in most cases, simultaneous with delivery of the on-demand video. Credit card payments accelerate cash flow and reduce the Company s collection risk, subject to the merchant bank s right to hold back cash pending settlement of the transactions. The Company also offers a prepaid video on-demand service in which a customer purchases a number of minutes of on-demand video at a set rate per minute based on the number of minutes purchased. The rate per minute decreases as the number of prepaid minutes increases. The Company records revenue from pre-pay customers as deferred revenue prior to commencement of services and recognizes revenue as the services are rendered. Prepaid minutes purchased under this program do not expire.

The Company also offers a customer loyalty program under which each member s purchase of video on-demand, DVDs, movie downloads, books, novelties or other items earns the member one point for each dollar spent. After accumulating 150 points, a customer may redeem the points for a $5 purchase. Points increase in value as they are accumulated and redeemed, with a maximum accumulation of 2,000 points, which may be redeemed for a $200 purchase. All of a customer s points expire after 180 days of no purchase activity. The Company follows the guidance in Emerging Issues Task Force No. 00-22 (EITF 00-22), Accounting for Points and Certain Other Time-Based or Volume-Based Sales Incentive Offers, and Offers for Free Products or Services to Be Delivered in the Future, Issue No. 2 in accounting for its loyalty program. Because the value of the award points is not significant in relation to the value of the services or products purchased by the customer, the Company records a liability for the estimated cost of the discounted services or products to be provided in the future.

PRIVATE MEDIA GROUP, INC.

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS

(UNAUDITED)

2. Acquisition

On January 20, 2009, Private Media Group, Inc. (Private) completed the acquisition of 100% of the business of Game Link LLC and its affiliate, eLine, LLC collectively (GameLink). The GameLink companies are engaged in the business of digital distribution of adult content over the Internet and online eCommerce development. As a result of the acquisition, Private is expecting to be a leading global digital distributor of adult content over the Internet.

The goodwill of EUR 7,974 thousand arising from the acquisition consists largely of the acquired know-how related to digital distribution of adult content over the Internet and online eCommerce development, economies of scale and synergies expected from combining the operations of Private and GameLink. None of the goodwill recognized is expected to be deductible for income tax purposes.

The following table summarizes the consideration paid for GameLink and the amounts of the assets acquired and liabilities assumed recognized at the acquisition date:

	January, 20 2009 EUR (in thousands)
Consideration	
Equity Instruments (8,534,309 common shares of Private)	6,644
Contingent consideration arrangement (4,595,397 common shares of Private)	3,575
Fair value of total consideration transferred	10,219
Recognized amounts of identifiable assets acquired and liabilities assumed	
Financial assets	233
Inventory	217
Property, plant, and equipment	3,371
Identifiable intangible assets	1,904
Financial liabilities	(3,480)
Total identifiable net assets	2,245
Goodwill	7,974
	10,219

The Company incurred EUR 186 thousand in acquisition-related costs, which are included in selling, general, and administrative expenses in Private s income statement for the six months ending June 30, 2009.

PRIVATE MEDIA GROUP, INC.

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS

(UNAUDITED)

The acquisition was accomplished by the merger of two wholly-owned subsidiaries of Private into the two parent companies of the GameLink businesses, with the shareholders of those entities receiving 8,534,309 shares of Private Common Stock in exchange for 100% of their common stock. In addition, the former shareholders are entitled to receive up to an additional 4,595,397 shares of Private Common Stock if the combined EBITDA of the online digital media operations of Private and GameLink meet specified targets in 2009, 2010 and 2011. The total fair value of the acquisition, which assumes the EBITDA targets are met in 2009, 2010 and 2011, is EUR 10,219 thousand (USD 13,272 thousand).

Using an exchange rate of EUR 0.75 per 1.00 USD, the combined EBITDA targets of the online digital media operations of Private and GameLink which the contingent consideration arrangement stipulates for each of the years below are:

	USD (in thousands)
2009	5,210
2010	8,013
2011	9,329
	22,552

The manner in which the contingent consideration is earned in relation to the combined EBITDA targets is as follows:

For each of the years ended December 31, 2009, 2010 and 2011 in which the actual EBITDA of the online digital media operations equals or exceeds the target EBITDA, the former owners of GameLink (the Former Owners) are entitled to receive 1,531,799 shares of Private Common Stock.

If there is a shortfall in the actual EBITDA compared to the target EBITDA in any year, instead of receiving 1,531,799 target shares for that year, the Former Owners are entitled to receive a pro rata portion of the target shares for that year, based upon the ratio between the actual EBITDA and the target EBITDA for that year. In such event, if the actual EBITDA required in the following year(s) exceeds the target EBITDA, in addition to the 1,531,799 target shares earned for the following year(s), the Former Owners are entitled to recover all or a portion of unearned target shares from the prior year(s) based upon the amount by which actual EBITDA exceeds the target EBITDA in the subsequent year.

The contingent consideration of EUR 3,575 thousand was valued at its acquisition date fair value using the lattice model. The Company believes that the target EBITDA will be reached by the end of the contingency period. The contingent consideration is classified as a liability under FAS 141R and will be re-measured at its current fair value each reporting period until the contingency is resolved.

The fair value of the acquired property, plant, and equipment of EUR 3,371 thousand is provisional pending receipt of the final valuation.

PRIVATE MEDIA GROUP, INC.

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS

(UNAUDITED)

The fair value of the identifiable intangible assets of EUR 1,904 thousand, comprises trade and domain names. The trade and domain names have an indefinite estimated useful life. The fair value of these assets is provisional pending receipt of the final valuation.

The amounts of GameLink s revenue and earnings included in Private s consolidated income statement for the six and three months ended June 30, 2009, and the pro forma revenue and earnings of the combined entity had the acquisition date been January 1, 2008, are:

	Revenue EUR	Earnings EUR
	(in thousands)	
Actual from January 20, 2009 June 30, 2009	4,771	(187)
Supplemental pro forma from January 1, 2009 June 30, 2009	12,569	(2,454)
Supplemental pro forma from January 1, 2008 June 30, 2008	15,875	(1,656)
Actual from April 1, 2009 June 30, 2009	2,618	(95)
Supplemental pro forma from April 1, 2008 June 30, 2008	7,828	(821)

3. Inventories

Inventories consist of the following:

	December 31, 2008 EUR	June 30, 2009 EUR
	(in thousands)	
Magazines for sale and resale	2,394	2,003
DVDs	2,330	2,097
Other	314	294
	5,038	4,394

PRIVATE MEDIA GROUP, INC.

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS

(UNAUDITED)

4. Earnings (loss) per share

The following table sets forth the computation of basic and diluted earnings per share:

	Three-months ended June 30,		Six-months ended June 30,	
	2007	2008	2008	2009
Numerator: (EUR in thousands)				
Net income (loss)	(826)	(1,553	(1,666)	(2,388)
Denominator:				
Denominator for basic earnings per share weighted average shares outstanding	53,587,408	62,114,803	53,580,494	61,109,391
Effect of dilutive securities:				
Common stock warrants, convertible notes, options and other dilutive securities	n/a	n/a		
Denominator for diluted earnings per share weighted average shares and assumed conversions	n/a	n/a		
Earnings (loss) per share (in EUR)				
Basic	(0.02)	(0.03)	(0.03)	(0.04)
Diluted	(0.02)	(0.03)	(0.03)	(0.04)

For the three and six months ended June 30, 2008, diluted impact of potentially dilutive securities is anti-dilutive therefore diluted and basic loss per share are EUR 0.02, and EUR 0.03, respectively. For the three and six months ended June 30, 2008, the equivalent of 6,914, and 8,360 common shares derived from dilutive securities such as options, warrants and convertible notes are excluded from the diluted earnings per share as they are anti-dilutive.

5. Stock-based compensation

The Company has had an Employee Stock Option Plan as described below. The compensation cost charged against income for the six-month periods ended June 30, 2008 and 2009 was EUR 7,000 and EUR 2,000, respectively, which is included in selling, general and administrative expense. The charge of compensation cost had no impact on tax since none of the option beneficiaries are taxable in the U.S. and tax rules are different in the beneficiaries respective tax jurisdictions.

Employee Stock Option Plan

The 1999 Employee Stock Option Plan (the Plan), which was in effect until its expiration on March 1, 2009, allowed the Company to grant options to purchase common stock to designated employees, executive officers, directors, consultants, advisors and other corporate and divisional officers of Private Media Group. The Plan authorized the Company to grant stock options exercisable for up to an aggregate of 7,200,000 shares of common stock. No stock options may be granted under the Plan, following its expiration, on March 1, 2009.

PRIVATE MEDIA GROUP, INC.

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS

(UNAUDITED)

Under the expired plan, the purchase price (exercise price) of option shares had to be at least equal to the fair market value of such shares on the date the stock option was granted. The stock option was exercisable for a period of ten years from the date of grant or such shorter period as was determined by the Company. Each stock option under the plan provided that it was exercisable in full or in cumulative or non-cumulative installments, and each stock option was exercisable from the date of grant or any later date specified in the option. Unless otherwise provided by the Company, an optionee could not exercise a stock option unless from the date of grant to the date of exercise the optionee remained continuously in the Company s employ.

The Company calculated the fair value of each option award on the date of grant using the Black-Scholes option pricing model. The following general assumptions were used: a) expected volatility was based on historical volatility of our stock, b) expected life was determined based on historical experience of similar awards, giving consideration to the contractual terms of the stock-based awards, vesting schedules and expectations of future employee behavior, c) risk-free interest rate was based on the U.S. Treasury yield curve in effect at the time of grant and d) dividend yield was zero based on the Company s Dividend Policy. During the six month periods ended June 30, 2008 and 2009 no grants were made.

A summary of stock option activity for the six month period ended June 30, 2009 is a follows:

	Number of Shares	Weighted-Average Exercise Price in USD	Weighted-Average Remaining Contractual Term in Years	Aggregate Intrinsic Value[1] in Thousands of USD
Outstanding January 1, 2009	1,888,920	4.99		
Granted				
Exercised				
Expired/Forfeited	1,306,920	5.09		
Outstanding June 30, 2009	582,000	4.69	0.4	
Exercisable June 30, 2009	569,000	4,77	0.3	

During the six month periods ended June 30, 2008 and 2009, no options under our stock option plan were exercised.

As of June 30, 2009, there was USD 1,710 of total unrecognized compensation cost related to nonvested option granted under the Plan. That cost is expected to be recognized over a weighted-average period of 0.3 years. The total fair value of all shares vested and outstanding at June 30, 2008 and 2009, was USD 4.6 million and USD 0.4 million, respectively.

[1] The aggregate intrinsic value is calculated as the difference between the exercise price of the underlying awards and the quoted price of our common stock for the options that were in-the-money at June 30, 2009.

PRIVATE MEDIA GROUP, INC.

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS

(UNAUDITED)

6. Income Taxes

On January 1, 2007 the Company adopted FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes, an Interpretation of FASB Statement No. 109 (FIN 48).

The Company s subsidiaries file income tax returns in numerous tax jurisdictions, including the United States, several U.S. states and several non-U.S. jurisdictions, primarily in Europe. The statute of limitations varies by the various jurisdictions in which we operate. Because of the number of jurisdictions in which we file tax returns, in any given year the statute of limitations in certain jurisdictions may lapse without examination within the 12-month period from the balance sheet date. Other than the recurring effect of changes in unrecognized tax benefits due to the lapse of the statute of limitations, none of which are expected to be individually significant, management believe there are no other reasonably possible changes that will significantly impact the amount of tax benefits recognized in the Company s financial statements within the 12-month period from the balance sheet date. The Company has substantially concluded all US Federal and State income tax matters for years up to and including 2003 and 2001 respectively, and all foreign income tax matters for years up to 2002.

The Company s practice is to recognize interest and penalties related to income tax matters in interest and other expenses respectively. Interest and penalties amounting to EUR 438 thousand were accrued as of June 30, 2009, of which EUR 32 thousand was recognized as interest expense during the six-month period then ended.

In December 1999 the Company received final notification from the Swedish Tax Authority assessing its subsidiary in Cyprus for the tax years 1995-1998 for a total amount of SEK 42,000,000 (approx. EUR 4.5 million) plus fines amounting to SEK 16,800,000 (approx. EUR 1.8 million) plus interest. The Swedish Tax Authority has taken the position that the subsidiary carried on business in Sweden from a permanent establishment during the period in question and should therefore be taxed on the income attributable to the permanent establishment. The Company is of the view that no permanent establishment is at hand in Sweden. However, the Administrative Court of Appeal has finally decided that a permanent establishment is at hand. The litigation is, however, still going on and the purpose is to finally decide the amounts to be attributed to the permanent establishment and thus being taxed in Sweden. In February 2009, the County Administrative Court reduced the assessment for the tax years 1995-1998 to a total amount of SEK 12,600,000 (approx. EUR 1.1 million) plus fines amounting to SEK 5,040,000 (approx. EUR 0.5 million) plus interest. However, as a matter of fact the tax claim on the Company has been extinguished according to Administrative Law. Only the claim related to the tax fine amounting to SEK 5,040,000 (approx. EUR 0.5 million) plus interest is valid, should the Administrative Court s decision prevail. The Company has appealed the decision to the Administrative Court of Appeal. The final outcome of this litigation will not be known for several years. Due to the fact that the final outcome of this matter is still uncertain, and the relatively minor claim now at stake, no amounts have been provided in the Company s financial statements for this dispute.

PRIVATE MEDIA GROUP, INC.

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS

(UNAUDITED)

7. Recent Accounting Pronouncements

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 141(R), Business Combinations (FAS 141(R)), to further enhance the accounting and financial reporting related to business combinations. FAS 141 (R) establishes principles and requirements for how the acquirer in a business combination (1) recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any non-controlling interest in the acquiree, (2) recognizes and measures the goodwill acquired in the business combination or a gain from a bargain purchase, and (3) determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. FAS 141 (R) applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. Therefore, the effects of the adoption of FAS 141 (R) will depend upon the extent and magnitude of acquisitions after December 31, 2008. The GameLink acquisition, which took place on January 20, 2009, was accounted for under FAS 141 (R).

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements, (FAS 157). This Statement defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. FAS 157 applies to other accounting pronouncements that require or permit fair value measurements, the FASB having previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. The Statement does not require any new fair value measurements and was originally effective beginning January 1, 2008. In February 2008, the FASB issued FASB Staff Position (FSP) FAS 157-2. FSP FAS 157-2 defers the effective date of FAS 157 until January 1, 2009 for non-financial assets and non-financial liabilities except those items recognized or disclosed at fair value on an annual or more frequently recurring basis.

We adopted SFAS No. 157 effective January 1, 2008 for financial assets and liabilities measured on a recurring basis. The Company has no level 2 or level 3 assets as all of the cash and cash equivalents are considered to be level 1, therefore there was no impact for the partial adoption of SFAS No. 157 on our consolidated financial statements. The application of SFAS No. 157 to our non-financial assets and liabilities did not have any material effect on our consolidated financial statements. The fair value of the assets acquired and liabilities assumed from our GameLink acquisition was determined using FAS 157.

8. Contingency

On May 1, 2009, Consipio Holding BV filed a lawsuit against the Company asserting a claim for unspecified damages under a note. The Company has filed its Answer and asserted several affirmative defenses which, if successful, will reduce or eliminate its liability under the note, and intends to vigorously defend the lawsuit. However, there are no assurances that Private will ultimately prevail on its claims and defenses.

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

You should read this section together with the consolidated financial statements and the notes and the other financial data in this Report. The matters that we discuss in this section, with the exception of historical information, are forward-looking statements within the meaning of the Private Securities Reform Act of 1995. Such forward-looking statements are subject to risks, uncertainties and other factors which could cause our actual results to differ materially from those expressed or implied by such forward-looking statements. Potential risks and uncertainties relate to factors such as (1) the timing of the introduction of new products and services and the extent of their acceptance in the market; (2) our expectations of growth in demand for our products and services; (3) our ability to successfully implement expansion and acquisition plans; (4) the impact of expansion on our revenue, cost basis and margins; (5) our ability to respond to changing technology and market conditions; (6) the effects of regulatory developments and legal proceedings with respect to our business; (7) the impact of exchange rate fluctuations; and (8) our ability to obtain additional financing.

The following discussion should be read in conjunction with the consolidated financial statements and related notes included elsewhere in this Report. References in this report to we, us, the Company and Private refer to Private Media Group, Inc., a Nevada corporation, including its consolidated subsidiaries.

Overview

We are an international provider and distributor of adult media content. We acquire or license content from independent studios and directors and process these images into products suitable for popular media formats such as digital media content for Broadcasting, Mobile and Internet distribution, and print publications and DVDs. In addition to media content, we also market and distribute branded leisure and novelty products oriented to the adult entertainment lifestyle and generate additional sales through the licensing of our Private trademark to third parties.

On January 20, 2009 we expanded our Internet operations through the acquisition of Game Link LLC and its affiliates, companies engaged in digital distribution of adult content over the Internet and eCommerce development. GameLink is a leading US adult entertainment VOD and eCommerce platform through its GameLink.com website. The site s installed user base represents over one million domestic and international customers and it serves over 100,000 users daily. Including 70,000 video titles, GameLink has the largest library of digital and physical adult media and novelties in the United States

We operate in a highly competitive, service-oriented market and are subject to changes in business, economic and competitive conditions. Nearly all of our products compete with other products and services that utilize adult leisure time and disposable income.

We generate revenues primarily through:

- Internet e-commerce, subscriptions and licensing;
- the broadcasting of movies through IPTV (Internet Protocol Television), cable, satellite and hotel television programming;
- sales of DVDs and magazines;
- sales of adult mobile content (wireless); and
- content, brand name and trademark licensing.

Over time, we expect net sales from DVDs & magazines to continue to decline as a percentage of net sales in relation to total net sales from Internet, broadcasting and wireless. We expect net sales from Internet, wireless and broadcasting to grow during the coming years.

We recognize net sales on delivery (for further information, see Critical Accounting Estimates).

Even though we recognize net sales upon delivery, we generally provide extended payment terms to our distributors of between 90 and 180 days. Although our extended payment terms increase our exposure to accounts receivable write-offs, we believe our risk is minimized by our generally long-term relationships with our distributors. In addition, we view our extended payment terms as an investment in our distribution channels which are important to the growth of our business.

Our primary expenses include:

- acquisition and licensing of content for our library of photographs and videos;
- web page development costs;
- printing, processing and duplication costs; and
- selling, general and administrative expenses.

With respect to proprietary video titles, we released 87 titles during 2008, 101 titles during 2007, and 110 titles during 2006, including both new and archival material. We plan to release approximately 70 titles in 2009.

Over the years, our cost of sales has been fluctuating relative to net sales due to our use of new mediums for our products, such as the Internet, DVD broadcasting and wireless. We also incur significant intangible expenses in connection with the amortization of our library of photographs and movies and capitalized development costs, which include the Internet. We amortize these tangible and intangible assets on a straight-line basis for periods of between three and five years.

Critical Accounting Estimates

General

Our discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amount of assets and liabilities revenues and expenses. On an ongoing basis, we evaluate our estimates, including those related to impairment of the library of photographs and videos and other long lived assets, allowances for bad debt, income taxes and contingencies and litigation. Accounts receivable and sales related to certain products are, in accordance with industry practice, subject to distributors right of return to unsold items. We base our estimates on historical experience and on various assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily available from other sources. Management periodically reviews such estimates. Actual results may differ from these estimates as a result of unexpected changes in trends.

We believe the following critical accounting policies are significantly affected by judgments and estimates used in the preparation of our consolidated financial statements.

Recognition of Revenue

The Company s revenue recognition policies are in accordance with Staff Accounting Bulletin (SAB) No. 104, Revenue Recognition in Financial Statements. One of the Company s primary sources of revenue is sales of its video on-demand offerings, which are sold directly via its on-line retail website and paid for almost exclusively by credit card. The Company recognizes revenue from video on demand when the service is rendered and collectibility is reasonably assured, specifically, when the customer s credit card is charged, which is, in most cases, simultaneous with delivery of the on-demand video. Credit card payments accelerate cash flow and reduce the Company s collection risk, subject to the merchant bank s right to hold back cash pending settlement of the transactions. The Company also offers a prepaid video on-demand service in which a customer purchases a number of minutes of on-demand video at a set rate per minute based on the number of minutes purchased. The rate per minute decreases as the number of prepaid minutes increases. The Company records revenue from pre-pay customers as deferred revenue prior to commencement of services and recognizes revenue as the services are rendered. Prepaid minutes purchased under this program do not expire.

The Company also offers a customer loyalty program under which each member s purchase of video on-demand, DVDs, movie downloads, books, novelties or other items earns the member one point for each dollar spent. After accumulating 150 points, a customer may redeem the points for a $5 purchase. Points increase in value as they are accumulated and redeemed, with a maximum accumulation of 2,000 points, which may be redeemed for a $200 purchase. All of a customer s points expire after 180 days of no purchase activity. The Company follows the guidance in Emerging Issues Task Force No. 00-22 (EITF 00-22), Accounting for Points and Certain Other Time-Based or Volume-Based Sales Incentive Offers, and Offers for Free Products or Services to Be Delivered in the Future, Issue No. 2 in accounting for its loyalty program. Because the value of the award points is not significant in relation to the value of the services or products purchased by the customer, The Company records a liability for the estimated cost of the discounted services or products to be provided in the future.

Revenues from IPTV (Internet Protocol Television), satellite & cable broadcasting are recognized based on sales reported each month by its IPTV, cable and satellite affiliates. The affiliates do not report actual monthly sales for each of their systems to the Company until approximately 60 - 90 days after the month of service ends. This practice requires management to make monthly revenue estimates based on historical experience for each affiliated system. Revenue is subsequently adjusted to reflect the actual amount earned upon receipt. Adjustments made to adjust revenue from estimated to actual have historically been immaterial.

Revenues from mobile content sales (wireless) are recognized based on sales reported each month by mobile operators via aggregators. The aggregators do not report actual monthly sales for each of their operators to the Company until approximately 60 - 90 days after the month of service ends. This practice requires management to make monthly revenue estimates based on historical experience for each affiliated system. Revenue is subsequently adjusted to reflect the actual amount earned upon receipt. Adjustments made to adjust revenue from estimated to actual have historically been immaterial.

The Company sells magazines to wholesalers on firm sale basis and via national newsstand distributors with the right to return. Our magazines are multi-lingual and the principal magazine market is in Europe.

Revenues from the sale of magazines under agreements that grant distributors rights-of-return are recognized upon transfer of title, which generally occurs on delivery, net of an allowance for returned magazines. Distributors with the right to return are primarily national newsstand distributors. Most of our magazines are bi-monthly (six issues per year) and remain on sale at a newsstand for a period of two months. Normally, all unsolds are reported to us within a period of four to six months from delivery. There are normally two to four national newsstand distributors for all newspapers and periodicals operating in each country. A majority of our national newsstand distributors are members of Distripress, the international organization for publishers and distributors, and carry out the distribution of the largest national and international newspapers and periodicals, including: Financial Times, Herald Tribune, Time, Newsweek, Vogue, etc.

The Company uses specific return percentages per title and distributor based on estimates and historical data. The percentages vary from 50-80%. Higher percentages generally reflect newer markets and/or products. Percentages are reviewed on an on-going basis.

The magazines have an approximate retail price of EUR 11.50 (USD 16.90) per copy and are printed on glossy high-quality paper at a cost of EUR 1.25 (USD 1.84). They are often shrink-wrapped in order to comply with local regulation or guidance for the sale of adult publications. In view of the high retail price, the margin and the physical quality of the magazines and the fact that the content has a very long shelf-life since it is not particularly linked to time, trends, fashion or current events, the Company has always collected the returns from newsstands in order to make them available for sale again.

The Company has scheduled re-distribution of the returned magazines, via national newsstand distributors, as Megapacks or Superpacks (three different copies per pack) where the retail price is EUR 14.95 (USD 21.99). As the national newsstand distributors have the right to return, the packs come back to us and are then broken up in individual copies in order to be sent out in DVD packs, see below, or sold on firm sale basis to wholesalers as back numbers at a lower price than new issues.

The Company also operates scheduled re-distribution of returned magazines, via national newsstand distributors, together with DVDs as Magazine/DVD packs as a way of increasing DVD distribution. The retail price of the Magazine/DVD packs is EUR 14.95 (USD 21.99). Since the national newsstand distributors have the right to return, the DVD packs are returned and the magazines are broken out in order to be sold on firm sale basis to wholesalers as back numbers at a lower price than new issues. The Company has historically sold all copies printed at an average price higher than, or equal, to cost.

Revenues from the sale of DVD products under consignment agreements with distributors are recognized based upon reported sales by the Company s distributors. Revenues from the sale of subscriptions to the Company s internet website are deferred and recognized ratably over the subscription period. Revenues from licensing of broadcasting rights to the Company s video and film library are recognized upon delivery when the following conditions have been met (i) license period of the arrangement has begun and the customer can begin its exploitation, exhibition, or sale (ii) the arrangement fee is fixed or determinable and (iii) collection of the arrangement fee is reasonably assured.

Accounts receivable

We are required to estimate the collectibility of our trade receivables and notes receivable. A considerable amount of judgment is required in assessing the ultimate realization of these receivables including the current credit-worthiness of each customer. Significant changes in required reserves have been recorded in the past and may occur in the future due to the current market environment.

Management reviews the allowance for doubtful accounts on at least a quarterly basis and adjusts the balance based on their estimate of the collectibility of specific accounts as well as a reserve for a portion of other accounts which have been outstanding for more than 180 days. This estimate is based on historical losses and information about specific customers. After collection attempts have failed, the Company writes off the specific account.

Goodwill and Other Intangible Assets

On January 1, 2002 the Company adopted Financial Accounting Standards Board Statement (SFAS) No. 142, Goodwill and Other Intangible Assets . Under SFAS 142, goodwill and indefinite lived intangible assets will no longer be amortized but will be reviewed annually for impairment (or more frequently if indicators of impairment arise).

The Company performs impairment tests of goodwill and indefinite lived intangible assets annually. The Company is required to assess these assets for recoverability when events or circumstances indicate a potential impairment by estimating the undiscounted cash flows to be generated from the use of these assets. There has historically been no effect on the earnings and financial position of the Company as a result of the impairment testing.

Other Intangible Assets represents the value attributable to certain acquisitions. Amortization expense is calculated on a straight-line basis over 10 years.

Impairment of Long-Lived Assets

The Company periodically evaluates the carrying value of long-lived assets including its library of photographs and videos for potential impairment. Upon indication of impairment, the Company will record a loss on its long-lived assets if the undiscounted cash flows that are estimated to be generated by those assets are less than the related carrying value of the assets. An impairment loss is then measured as the amount by which the carrying value of the asset exceeds the estimated discounted future cash flows. Management s estimated future revenues are based upon assumptions about future demand and market conditions and additional write downs may be required if actual conditions are less favorable than those assumed.

Website Development Costs

The Company follows the guidance of Statement of Position 98-1, Accounting for the Costs of Computer Software Developed or Obtained for Internal Use (SOP 98-1) and Emerging Issues Task Force Issue No. 00-2, Accounting for Web Site Development Costs (EITF 00-2). EITF 00-2 prescribes the accounting for website development costs based on the type of website development activity. In accordance with SOP 98-1 and the transition provisions of EITF 00-2, The Company has elected to apply this standard to costs incurred to develop its websites from January 1, 2000 forward. The Company capitalizes qualifying development costs which are incurred during the application development stage and in website enhancement activities, including graphics and related software. Capitalized website development costs for The Company s on-demand and retail services are amortized on a straight-line basis over periods of three to five years and are included in property and equipment in the accompanying consolidated balance sheets. Costs related to website maintenance are expensed as incurred.

Inventories

Inventories are valued at the lower of cost or market, with cost principally determined on an average basis. Inventories principally consist of DVD s, videocassettes and magazines held for sale or resale. The inventory is written down to the estimated market value based upon assumptions about future demand and market conditions. If actual market conditions are less favorable than those projected by management, additional write-downs may be required.

Results of Operations

Three months ended June 30, 2009 compared to the three months ended June 30, 2008

Net sales. For the three months ended June 30, 2009, we had net sales of EUR 6.2 million compared to net sales of EUR 5.2 million for the three months ended June 30, 2008, an increase of EUR 1.0 million, or 19%. The increase was the result of increased Internet sales offset by decreases in sales of DVD & Magazines and broadcasting. Internet sales increased EUR 2.4 million to EUR 3.4 million, which represents an increase of 235% compared to the same period last year. The increase in Internet sales was the result of the acquisition of GameLink. Broadcasting sales decreased EUR 0.7 million, or 39%, to EUR 1.1 million primarily as a result of a decrease in title sales, offset by increases in TV-channel sales and video on demand sales via IPTV and cable. Wireless sales in the period was EUR 0.4 million, which represented no change. DVD & Magazine sales decreased EUR 0.7 million, or 37%, to EUR 1.2 million. The reduction in DVD & Magazine sales was primarily attributable to an industry wide decrease in DVD sales (see discussion under *Outlook* below).

Going forward, we expect Internet, wireless and Broadcasting sales to increase (see discussion under *Outlook* below).

Cost of Sales. Our cost of sales was EUR 4.0 million for the three months ended June 30, 2009 compared to EUR 3.6 million for the three months ended June 30, 2008, an increase of EUR 0.4 million.

Included in cost of sales is Internet, broadcasting and wireless cost. printing, processing and duplication and amortization of library. Internet cost was EUR 1.8 million for the three months ended June 30, 2009 compared to EUR 0.3 million for the three months ended June 30, 2008. Internet cost as a percentage of related sales in the period was 54% compared to 28% in the same period last year. The increase of EUR 1.6 million was primarily the result of the acquisition of GameLink. Broadcasting and wireless cost was EUR 0.1 million for the three months ended June 30, 2009 compared to EUR 0.4 million for the three months ended June 30, 2008. Broadcasting and wireless cost as a percentage of related sales in the period was 5% compared to 19% in the same period last year. The decrease of EUR 0.3 million was primarily the result of lower wireless and broadcasting cost as result of more cost efficient content delivery. Printing, processing and duplication cost was EUR 0.5 million for the three months ended June 30, 2009 compared to EUR 1.3 million for the three months ended June 30, 2008, a decrease of EUR 0.7 million, or 58%. Printing, processing and duplication cost as a percentage of DVD & Magazine sales was 45% for the three months ended June 30, 2009 compared to 66% in the same period last year. Amortization of library was EUR 1.6 million for the three months ended June 30, 2009 compared to EUR 1.5 million for the three months ended June 30, 2008, which represents an increase of EUR 0.1 million. Amortization of library does not vary with sales since it reflects the amortization of our investments in content which has been available for sale for a period of three to five years.

Gross Profit. In the three months ended June 30, 2009, we realized a gross profit of EUR 2.1 million, or 35% of net sales compared to EUR 1.6 million, or 31% of net sales for the three months ended June 30, 2008. The increase in gross profit was the result of the acquisition of GameLink.

Selling, general and administrative expenses. Our selling, general and administrative expenses were EUR 4.4 million for the three months ended June 30, 2009 compared to EUR 2.9 million for the three months ended June 30, 2008, an increase of EUR 1.5 million, or 53%. The increase was the result of the acquisition of GameLink which added EUR 1.4 million and bad debt provision, which increased by EUR 0.1 million.

Operating loss. We reported an operating loss of EUR 2.2 million for the three months ended June 30, 2009 compared to an operating loss of EUR 1.2 million for the three months ended June 30, 2008. The increase in operating loss was the result of the increase in selling, general and administrative expenses which was offset by the increase in gross profit.

Interest expense. We reported interest expense of EUR 0.1 million for the three months ended June 30, 2009, compared to EUR 0.1 million for the three months ended June 30, 2008.

Income tax benefit. We reported income tax benefit of EUR 0.7 million for the three months ended June 30, 2009, compared to EUR 0.6 million for the three months ended June 30, 2008.

Net loss. We reported a loss of EUR 1.6 million for the three months ended June 30, 2009, compared to EUR 0.8 million for the three months ended June 30, 2008.

Six months ended June 30, 2009 compared to the six months ended June 30, 2008

Net sales. For the six months ended June 30, 2009, we had net sales of EUR 12.0 million compared to net sales of EUR 10.5 million for the six months ended June 30, 2008, an increase of EUR 1.5 million, or 15%. The increase was the result of increased Internet sales offset by decreases in sales of DVD & Magazines, broadcasting and wireless. Internet sales increased EUR 4.2 million to EUR 6.4 million, which represents an increase of 195% compared to the same period last year. The increase in Internet sales was the result of the acquisition of GameLink. Broadcasting sales decreased EUR 1.0 million, or 34%, to EUR 2.0 million primarily as a result of a decrease in title sales, offset by increases in TV-channel sales and video on demand sales via IPTV and cable. Wireless sales in the period decreased EUR 0.1 million, or 8%, to EUR 0.9 million. DVD & Magazine sales decreased EUR 1.6 million, or 38%, to EUR 2.6 million. The reduction in DVD & Magazine sales was primarily attributable to an industry wide decrease in DVD sales (see discussion under *Outlook* below).

Going forward, we expect Internet, wireless and Broadcasting sales to increase (see discussion under *Outlook* below).

Cost of Sales. Our cost of sales was EUR 7.6 million for the six months ended June 30, 2009 compared to EUR 7.0 million for the six months ended June 30, 2008, an increase of EUR 0.6 million.

Included in cost of sales is Internet, broadcasting and wireless cost. printing, processing and duplication and amortization of library. Internet cost was EUR 3.2 million for the six months ended June 30, 2009 compared to EUR 0.6 million for the six months ended June 30, 2008. Internet cost as a percentage of related sales in the period was 51% compared to 27% in the same period last year. The increase of EUR 2.7 million was primarily the result of the acquisition of GameLink. Broadcasting and wireless cost was EUR 0.2 million for the six months ended June 30, 2009 compared to EUR 0.6 million for the six months ended June 30, 2008. Broadcasting and wireless cost as a percentage of related sales in the period was 6% compared to 16% in the same period last year. The decrease of EUR 0.5 million was primarily the result of lower wireless and broadcasting cost as result of more cost efficient content delivery. Printing, processing and duplication cost was EUR 1.2 million for the six months ended June 30, 2009 compared to EUR 2.6 million for the six months ended June 30, 2008, a decrease of EUR 1.4 million, or 54%. Printing, processing and duplication cost as a percentage of DVD & Magazine sales was 45% for the six months ended June 30, 2009 compared to 61% in the same period last year. Amortization of library was EUR 3.0 million for the six months ended June 30, 2009 compared to EUR 3.2 million for the six months ended June 30, 2008, which represents a decrease of EUR 0.2 million. Amortization of library does not vary with sales since it reflects the amortization of our investments in content which has been available for sale for a period of six to five years.

Gross Profit. In the six months ended June 30, 2009, we realized a gross profit of EUR 4.4 million, or 37% of net sales compared to EUR 3.5 million, or 33% of net sales for the six months ended June 30, 2008. The increase in gross profit was the result of the acquisition of GameLink.

Selling, general and administrative expenses. Our selling, general and administrative expenses were EUR 8.0 million for the six months ended June 30, 2009 compared to EUR 6.1 million for the six months ended June 30, 2008, an increase of EUR 1.9 million, or 31%. The increase was the result of the acquisition of GameLink which added EUR 2.5 million, which was offset by EUR 0.8 million in reduced selling, general and administrative expenses in all other areas except bad debt provision, which increased by EUR 0.2 million.

Operating loss. We reported an operating loss of EUR 3.6 million for the six months ended June 30, 2009 compared to an operating loss of EUR 2.6 million for the six months ended June 30, 2008. The increase in operating loss was the result of the increase in selling, general and administrative expenses which was offset by the increase in gross profit.

Interest expense. We reported interest expense of EUR 0.2 million for the six months ended June 30, 2009, compared to EUR 0.2 million for the six months ended June 30, 2008.

Income tax benefit. We reported income tax benefit of EUR 1.3 million for the six months ended June 30, 2009, compared to EUR 1.0 million for the six months ended June 30, 2008.

Net loss. We reported a loss of EUR 2.4 million for the six months ended June 30, 2009, compared to EUR 1.7 million for the six months ended June 30, 2008.

Liquidity and Capital Resources

We reported a working capital surplus of EUR 12.8 million at June 30, 2009, a decrease of EUR 2.6 million compared to the year ended December 31, 2008. The decrease is principally attributable to a increase in current liabilities as a result of the acquisition of GameLink.

Operating Activities

Net cash provided by operating activities was EUR 2.6 million for the six months ended June 30, 2009, and was primarily the result of net income, as adjusted for non-cash transactions, and cash related to changes in operating assets and liabilities. The net loss of EUR 2.4 million was adjusted to reconcile net income to net cash flows from operating activities with depreciation of EUR 0.5 million, bad debt provision of EUR 0.2 million, amortization of other intangible assets of EUR 0.1 million, amortization of web pages of EUR 0.8 million and amortization of photographs and videos of EUR 3.0 million making a total of EUR 4.5 million, providing a net balance of EUR 2.1 million. The total of EUR 2.1 million was added to by changes in trade accounts receivable, inventories, prepaid expenses and other current assets and accrued other liabilities totaling EUR 1.8 million offset by EUR 1.3 million from related party receivable, income taxes payable and accounts payable trade. Net cash provided by operating activities was EUR 3.7 million for the six months ended June 30, 2008. The decrease in net cash provided by operating activities of EUR 1.1 million for the six months ended June 30, 2009 compared to the same period last year was primarily the result of net income, as adjusted for non-cash transactions, and cash related to changes in operating assets and liabilities.

Investing Activities

Net cash used in investing activities for the six months ended June 30, 2009 was EUR 2.3 million. The investing activities were principally capital expenditure of EUR 1.0 million and investment in library of photographs and videos of EUR 1.4 million, which was carried out in order to maintain the 2009 release schedules. Net cash used in investing activities decreased EUR 1.2 million over the same period last year. The decrease is principally due to lower investment activity in library of photographs and videos as a result of a lower demand for new releases on new media platforms as opposed to traditional media which required a higher frequency.

Financing Activities

Net cash used in financing activities for the six-month period ended June 30, 2009 was EUR 0.2 million. Compared to the six-month 2008 period there was no material change.

Contractual obligations

During the six-month period ended June 30, 2009, we have not experienced any material changes in our contractual obligations compared to what was reported in our Form 10-K for the year ended December 31, 2008.

Disputed Contractual Obligation

In December 2001 the group s holding company, Private Media Group, Inc., borrowed $ 4.0 million from Commerzbank AG pursuant to a Note originally due on December 20, 2002. The Note bore interest at an annual rate of 7%, payable quarterly, with the entire principal amount and accrued interest originally due on December 20, 2002. The Note is guaranteed by Slingsby Enterprises Limited, an affiliate of Private s Chairman and principal shareholder, and the guaranty is secured by 4,950,000 shares of Private Media Group, Inc. Common Stock. In December 2002 Commerzbank AG agreed to extend the maturity date of the Note to March 20, 2003.

In April 2003 the Note was acquired by Consipio Holding B.V. from Commerzbank AG, and Consipio and Private reached an agreement-in-principle with Consipio to extend the maturity of the Note until April 2008. However, Consipio and Private were unable to reach final agreement on other terms and conditions relating to the restructured Note. Accordingly, in December 2003 Consipio notified Private and Slingsby Enterprises that Private was in default under the Note, and demanded $3.4 million as payment in full of all outstanding principal and interest under the Note. The Company continued to make regular payments on the Note, including principal and accrued interest, through February 2008. In April 2008 Consipio requested Private to pay the remaining balance of the Note, without indicating the amount due. Private in turn requested that Consipio provide a statement of the amount due and the basis for its calculation. In response, Consipio demanded payment of $3,194,000 as settlement in full of the Note, to be received by May 9, 2008. This calculation was made using an interest rate of 9.9%, as opposed to the 7% rate provided under the original terms of the Note. Consipio also advised that if payment was not received on such date it would institute litigation, in which event Consipio would claim that the amount due under the Note should be denominated in Euro, rather than U.S. dollars. Private believes that the amount due under the Note at May 9, 2008, including accrued interest, was no more than $2.4 million, utilizing an interest rate of 7%. In August 2008 Consipio notified Private that the Note was in default and that it intended to exercise its rights under the Note and the pledge of shares by Slingsby of Private Common Stock. No payments have been made under the Note since February 2008, and the Note provides for interest to accrue on the unpaid principal amount of the Note until paid in full. Private believes that the amount due under the Note at June 30, 2009, including accrued interest, was no more than $2.6 million, utilizing an interest rate of 7%.

On May 1, 2009, Consipio Holding BV filed a lawsuit against the Company asserting a claim for unspecified damages under the Note. The Company has filed its Answer and asserted several affirmative defenses which, if successful, will reduce or eliminate its liability under the Note, and intends to vigorously defend the lawsuit. However, there are no assurances that Private will ultimately prevail on its claims and defenses. For additional information regarding the lawsuit, see *Part II Item 1. Litigation* appearing elsewhere in this Report.

Outlook

We have been transitioning our business model from linear to digital content production and distribution over the last 18 months and this has affected our margins. As DVD and magazines sales have rapidly declined, we have made great progress moving to digital business with significant new media distribution deals and the monetization of our expansive library of content. We are now a leading adult content provider on all major digital platforms in Europe, and as they continue to build out and get larger, we project significant growth in both sales and net income. Specifically, we project the biggest gains to be achieved through: Internet, broadcasting and wireless. During the six-month period ending June 30, 2009, these platforms were responsible for 78% percent of our sales. Following is a discussion highlighting some of the important factors of our business going forward.

Internet

On January 20, 2009 we expanded our Internet operations through the acquisition of Game Link LLC and its affiliates, companies engaged in digital distribution of adult content over the Internet and eCommerce development. GameLink is a leading US adult entertainment VOD and eCommerce platform through its GameLink.com website. The site s installed user base represents over one million domestic and international customers and it serves over 100,000 users daily. Including 70,000 video titles, GameLink has the largest library of digital and physical adult media and novelties in the United States. The Company offers VOD in multiple media formats including streaming and downloads to computers and iPhones. GameLink s infrastructure is the most robust in the industry and is highly flexible, customizable and scalable designed to support multiple retail strategies and products simultaneously. Additionally, through its related companies, GameLink offers third-party and white-label ecommerce solutions and development. For the year ended 2008 Gamelink and its affiliates reported net sales of USD 16.4 million.

The acquisition of GameLink is a significant development that will substantially contribute to our growth, while creating economies of scale. We have been establishing our digital strategy for the last year, and concluded that the combination of Private with a major online retailer and accomplished platform developer is the approach to achieving our goals in the rapidly changing business landscape. The combined content assets of Private and core competencies of GameLink offer a compelling new business model. We will be expanding our joint internet strategies globally with new formats and applications to be launched in 2009. Additionally, we will be developing improved interactive functionality for new media platforms such as IPTV and mobile, and maximizing our content monetization with the existing vast Private library as well as aggregation of select international studios offering a wide range of content and genres for all platform needs. With this expanded digital strategic focus we expect to announce a variety of compelling new initiatives during 2009, including additional strategic acquisitions of Internet businesses.

Broadcasting

We are successfully implementing our new media strategy for growth of VOD (Video-on-Demand) via IPTV and to date we have contracted with 38 major platform operators in 24 countries in Europe, as the leading supplier of adult content. Currently we have gained more than 75% coverage of the European IPTV market[2] and across all platforms, quarter by quarter, sales are growing continuously in line with the general growth of the market, or faster. Going forward, we expect to increase our market coverage in this rapidly expanding market, which compared to traditional pay-TV generates substantially higher sales per subscriber at a considerably better margin and subsequently this will contribute significantly to operating profit going forward.

Furthermore, the introduction of IPTV in Europe has challenged the Cable-TV industry and subsequently cable operators are rapidly upgrading their systems to provide the same functionality as IPTV. Recently we have contracted with two leading cable operators in Western Europe and going forward we expect to add further Cable/VOD platforms to our portfolio.

In relation to Private branded TV channels carrying our content in Europe and Latin America our partners Playboy TV Latin America and Playboy TV International continue to improve distribution. During the past twelve months, Playboy TV Latin America increased the distribution significantly in Brazil, Argentina and Central America and we expect to see positive impact from this going forward.

Wireless Adult Mobile Content

With respect to mobile content, Private content is available to 1.2 billion handsets via 104 mobile network operators in 45 countries. In the end of 2008, we started optimizing our content delivery network of aggregators in order to secure a more aggressive long-term growth. Now this process is completed and consequently we expect sales to increase significantly going forward. Additionally, we are implementing a new off-portal strategy in 2009 to capitalize on the expected transition and growth with this new consumer access to mobile content.

The markets of Asia and the North America are still underexploited by us and therefore represent a significant growth potential. In addition, Mobile TV, increased penetration of smart-phones and the implementation of age verification systems offer additional significant growth potential with both current and future operators in 2009 and beyond[3] .

DVDs & Magazines

As we further transition into global digital content delivery, DVD pricing and volume is being affected considerably and as a result the industry in general is experiencing a severe downturn in DVD sales. In view of the aforementioned, we continue to re-strategize our distribution of DVDs and Magazines to reduce any further negative impact of this downward DVD trend.

2 According to Global IPTV Forecasts made by MRG (Multimedia Research Group, Inc.), the number of global IPTV subscribers is estimated to grow from 13.5 million in 2007 to 92.8 million in 2012, a compound annual growth rate of 47 percent. Europe continues to be the biggest market for IPTV, with France significantly leading the growth projections through its principal telcos. The number of IPTV subscribers in Europe is forecasted to grow from approximately 6.4 million in 2007 to 36.4 million in 2012, a compound annual growth rate of 42 percent.

3 Juniper Research estimates in its white paper Adult Content in the Palm of Your Hand (November 2007) that the global mobile adult content market will increase from US$1.7 billion in 2007 to just over US$4.6 billion by 2012.

Liquidity

We expect that our available cash resources and cash generated from operations will be sufficient to meet our presently anticipated working capital and capital expenditure requirements for at least the next twelve months. However, we are presently engaged in litigation regarding our obligations under a promissory note. An adverse outcome in this proceeding would likely have a material impact upon our liquidity if we are unable to obtain additional debt or equity financing to satisfy any resulting liability. In addition, we may need to raise additional funds to support more rapid expansion or respond to unanticipated requirements. Presently we have no commitments to obtain additional debt or equity financing. For further information regarding this litigation, see *Part I Item 2. - Management s Discussion and Analysis of Financial Condition and Results of Operations Contractual Obligations - Disputed Contractual Obligation* and *Part II Item 1. Litigation* appearing elsewhere in this Report.

If additional funds are raised through the issuance of equity securities, our shareholders percentage ownership will be reduced, they may experience additional dilution, or these newly issued equity securities may have rights, preferences, or privileges senior to those of our current shareholders. Additional financing may not be available when needed on terms favorable to us, or at all. If adequate funds are not available or are not available on acceptable terms, we may be unable to develop or enhance our products and services, take advantage of future opportunities, maintain the scope of our operations or respond to competitive pressures or unanticipated requirements, which could harm our business.

Item 3. Quantitative and Qualitative Disclosures about Market Risk.

We do not use derivative financial instruments for trading purposes and were never a party to any derivative, swap or option contracts. We do not hedge our interest rate or foreign currency exchange rate exposures.

As our cash and cash equivalents and short-term investments consist principally of money market securities and investments in short-term debt or equity securities and our borrowings are primarily at fixed rates of interest our market risk related to fluctuations in interest rates is limited. Accordingly, a one percentage change in market interest rates would not have a material impact on our results of operations.

We transact our business in various currencies, principally the Euro and the U.S dollar and certain other European Union currencies. We generally attempt to limit exposure to currency rate fluctuations by matching transaction currencies (revenues/expenses) to the functional currency of its operating subsidiaries. Our exposure to market risk for fluctuations in foreign currency exchange rates relates primarily to fluctuations in the Euro versus the U.S dollar. We translate our consolidated subsidiaries whose functional currency is not the euro into the euro for reporting purposes. Income statement amounts are translated into euros using the average exchange rate for the fiscal year. The balance sheet is translated at the year-end exchange rate. Due to the significance of the results reported in dollars the impact of the euro/dollar exchange rate on our major categories of revenue and expense can be material.

Item 4T. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

The Company maintains disclosure controls and procedures designed to ensure that information required to be disclosed in reports filed under the Securities Exchange Act of 1934, is recorded, processed, summarized and reported within the specified time periods. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934 is accumulated and communicated to its management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. As of the end of the period covered by this report, the Company s management evaluated, with the participation of the Company s Chief Executive Officer and Chief Financial Officer, the effectiveness of the Company s disclosure controls and procedures. Based on the evaluation, the Company s Chief Executive Officer and Chief Financial Officer concluded that the Company s disclosure controls and procedures were effective as of June 30, 2009.

Changes in Internal Control Over Financial Reporting

There were no changes in the Company s internal control over financial reporting that occurred during the Company s fiscal quarter ended June 30, 2009, that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

Inherent Limitations in Internal Control Over Financial Reporting

The Company does not expect that its disclosure controls and procedures will prevent all error and all fraud. A control procedure, no matter how well conceived and operated, can provide only reasonable not absolute, assurance that the objectives of the control procedure are met. Because of the inherent limitations in all control procedures, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any control procedure also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control procedure, misstatements due to error or fraud may occur and not be detected.

PART II OTHER INFORMATION

Item 1. Legal Proceedings

Consipio Holding BV vs. Private Media Group, Inc. and Slingsby Enterprises Limited, *United States District Court, Southern District of New York, Case No. 09-cv-4284.*

On May 1, 2009, Consipio Holding BV filed a lawsuit against the Company asserting a claim for unspecified damages under a Note dated December 21, 2001 in the original principal amount of $4,000,000, which was guaranteed by Slingsby Enterprises Limited, an affiliate of the Company s Chairman and principal shareholder. The guarantee is secured by 4,950,000 shares of the Company s common stock. The Company has filed its Answer and asserted several affirmative defenses. The Company intends to vigorously defend the lawsuit. For additional information relating to this litigation see *Part I Item 2. - Management s Discussion and Analysis of Financial Condition and Results of Operations Contractual Obligations - Disputed Contractual Obligation* appearing elsewhere in this Report.

Item 6. Exhibits

31.1	Certifications pursuant to Rule 13a-14 under the Securities Exchange Act of 1934.
31.2	Certifications pursuant to Rule 13a-14 under the Securities Exchange Act of 1934.
32.1	Certification of CEO and CFO Pursuant to 18 U.S.C. § 1350, as Adopted Pursuant to § 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned thereunto duly authorized.

PRIVATE MEDIA GROUP, INC.
(Registrant)

Date: August 14, 2009

/s/ Johan Gillborg
Johan Gillborg, Chief Financial Officer