

Tree.com, Inc.
Form 10-Q
November 14, 2011

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended September 30, 2011

or

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

For the transition period from _____ to _____
Commission File No. 001-34063

TREE.COM, INC.

(Exact name of Registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

26-2414818
(I.R.S. Employer
Identification No.)

11115 Rushmore Drive, Charlotte, North Carolina 28277
(Address of principal executive offices)

(704) 541-5351
(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

(Do not check if a
smaller reporting company)

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

As of November 8, 2011 there were 11,045,274 shares of the Registrant's common stock, par value \$.01 per share, outstanding, excluding treasury shares.

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Table of Contents**PART 1 FINANCIAL INFORMATION****Item 1. Financial Statements****TREE.COM, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF OPERATIONS****(Unaudited)**

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--|---|-------------|--|-------------|
| | 2011 | 2010 | 2011 | 2010 |
| | (In thousands, except per share amounts) | | | |
| Revenue | \$ 13,101 | \$ 15,204 | \$ 43,951 | \$ 48,013 |
| Cost of revenue (exclusive of depreciation shown separately below) | 1,001 | 1,346 | 3,529 | 3,654 |
| Gross margin | 12,100 | 13,858 | 40,422 | 44,359 |
| Operating expenses | | | | |
| Selling and marketing expense | 8,475 | 12,944 | 39,246 | 38,901 |
| General and administrative expense | 4,388 | 6,295 | 15,059 | 18,666 |
| Product development | 681 | 805 | 2,677 | 2,554 |
| Litigation settlements and contingencies | 212 | 74 | 5,206 | 102 |
| Restructuring expense | 498 | 46 | 990 | 2,718 |
| Amortization of intangibles | 213 | 307 | 787 | 922 |
| Depreciation | 1,393 | 823 | 3,677 | 2,297 |
| Asset impairments | | | 250 | |
| Total operating expenses | 15,860 | 21,294 | 67,892 | 66,160 |
| Operating loss | (3,760) | (7,436) | (27,470) | (21,801) |
| Other income (expense) | | | | |
| Interest income | | | | 7 |
| Interest expense | (110) | (60) | (266) | (392) |
| Total other expense, net | (110) | (60) | (266) | (385) |
| Loss before income taxes | (3,870) | (7,496) | (27,736) | (22,186) |
| Income tax benefit (provision) | 185 | (42) | (117) | (850) |
| Net loss from continuing operations | (3,685) | (7,538) | (27,853) | (23,036) |
| Gain from sale of discontinued operations, net of tax | 7,752 | | 7,752 | |
| Income (loss) from operations of discontinued operations, net of tax | 8,531 | 9,357 | (24,615) | 17,910 |
| Income (loss) from discontinued operations | 16,283 | 9,357 | (16,863) | 17,910 |

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| | | | | |
|--|-----------|-----------|-------------|------------|
| Net income (loss) available to common shareholders | \$ 12,598 | \$ 1,819 | \$ (44,716) | \$ (5,126) |
| Weighted average common shares outstanding | 11,037 | 11,023 | 10,978 | 10,993 |
| Weighted average diluted shares outstanding | 11,120 | 11,163 | 10,978 | 10,993 |
| Net loss per share from continuing operations | | | | |
| Basic | \$ (0.33) | \$ (0.68) | \$ (2.54) | \$ (2.10) |
| Diluted | \$ (0.33) | \$ (0.68) | \$ (2.54) | \$ (2.10) |
| Net income (loss) per share available to common shareholders | | | | |
| Basic | \$ 1.14 | \$ 0.16 | \$ (4.07) | \$ (0.47) |
| Diluted | \$ 1.13 | \$ 0.16 | \$ (4.07) | \$ (0.47) |

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

Table of Contents**TREE.COM, INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS**

| | September 30, 2011 | December 31, 2010 |
|---|--|----------------------|
| | (unaudited) | |
| | (In thousands, except par value and share amounts) | |
| ASSETS: | | |
| Cash and cash equivalents | \$ 10,331 | \$ 68,819 |
| Restricted cash and cash equivalents | 12,955 | 8,155 |
| Accounts receivable, net of allowance of \$118 and \$131, respectively | 5,443 | 3,564 |
| Prepaid and other current assets | 1,038 | 1,043 |
| Current assets of discontinued operations | 203,950 | 130,701 |
| Total current assets | 233,717 | 212,282 |
| Property and equipment, net | 9,191 | 7,598 |
| Goodwill | 3,632 | 3,632 |
| Intangible assets, net | 40,295 | 41,319 |
| Other non-current assets | 241 | 116 |
| Non-current assets of discontinued operations | 10,094 | 17,855 |
| Total assets | \$ 297,170 | \$ 282,802 |
| LIABILITIES: | | |
| Accounts payable, trade | \$ 11,691 | \$ 6,562 |
| Deferred revenue | 216 | 312 |
| Deferred income taxes | 4,221 | 2,358 |
| Accrued expenses and other current liabilities | 19,116 | 23,881 |
| Current liabilities of discontinued operations | 167,565 | 118,220 |
| Total current liabilities | 202,809 | 151,333 |
| Income taxes payable | 59 | 96 |
| Other long-term liabilities | 4,156 | 3,168 |
| Deferred income taxes | 12,201 | 13,962 |
| Non-current liabilities of discontinued operations | 18,797 | 12,422 |
| Total liabilities | 238,022 | 180,981 |
| Commitments and contingencies (Note 9) | | |
| SHAREHOLDERS' EQUITY: | | |
| Preferred stock \$.01 par value; authorized 5,000,000 shares; none issued or outstanding | | |
| Common stock \$.01 par value; authorized 50,000,000 shares; issued 12,165,992 and 11,893,468 shares, respectively, and outstanding 11,042,731 and 10,770,207 shares, respectively | 121 | 118 |
| Additional paid-in capital | 910,877 | 908,837 |
| Accumulated deficit | (843,318) | (798,602) |
| Treasury stock 1,123,261 shares | (8,532) | (8,532) |
| Total shareholders' equity | 59,148 | 101,821 |
| Total liabilities and shareholders' equity | \$ 297,170 | \$ 282,802 |

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The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

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TREE.COM, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY

(Unaudited)

| | Total | Common Stock Number of Shares | Amount | Additional Paid-in Capital | Accumulated Deficit | Treasury Stock Number of Shares | Amount |
|--|----------------|--|--------|----------------------------------|------------------------|--|------------|
| | (In thousands) | | | | | | |
| Balance as of December 31, 2010 | \$ 101,821 | 11,893 | \$ 118 | \$ 908,837 | \$ (798,602) | 1,123 | \$ (8,532) |
| Comprehensive loss: | | | | | | | |
| Net loss for the nine months ended September 30, 2011 | (44,716) | | | | (44,716) | | |
| Comprehensive loss | (44,716) | | | | | | |
| Non-cash compensation | 2,993 | | | 2,993 | | | |
| Issuance of common stock upon exercise of stock options and vesting of restricted stock units, net of withholding taxes | (950) | 273 | 3 | (953) | | | |
| Balance as of September 30, 2011 | \$ 59,148 | 12,166 | \$ 121 | \$ 910,877 | \$ (843,318) | 1,123 | \$ (8,532) |

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

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TREE.COM, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

Nine Months Ended
September 30,

2011 2010

(In thousands)

| | | |
|--|-----------------|-----------------|
| Cash flows from operating activities attributable to continuing operations: | | |
| Net loss | \$ (44,716) | \$ (5,126) |
| Less (income) loss from discontinued operations, net of tax | 16,863 | (17,910) |
| Net loss from continuing operations | (27,853) | (23,036) |
| Adjustments to reconcile net loss from continuing operations to net cash used in operating activities attributable to continuing operations: | | |
| Loss on disposal of fixed assets | 210 | 3 |
| Amortization of intangibles | 787 | 922 |
| Depreciation | 3,677 | 2,297 |
| Intangible impairment | 250 | |
| Non-cash compensation expense | 2,731 | 2,423 |
| Non-cash restructuring expense | | 93 |
| Deferred income taxes | 101 | 1,023 |
| Bad debt expense | 32 | 45 |
| Changes in current assets and liabilities: | | |
| Accounts receivable | (1,911) | 212 |
| Prepaid and other current assets | (122) | (898) |
| Accounts payable and other current liabilities | 385 | (15,658) |
| Income taxes payable | (58) | (388) |
| Deferred revenue | (96) | (155) |
| Other, net | 988 | 3,043 |
| Net cash used in operating activities attributable to continuing operations | (20,879) | (30,074) |
| Cash flows from investing activities attributable to continuing operations: | | |
| Capital expenditures | (5,480) | (3,743) |
| Acquisitions | | (50) |
| Other, net | (1,488) | 2,186 |
| Net cash used in investing activities attributable to continuing operations | (6,968) | (1,607) |
| Cash flows from financing activities attributable to continuing operations: | | |
| Issuance of common stock, net of withholding taxes | (950) | (575) |
| Purchase of treasury stock | | (4,705) |
| (Increase) decrease in restricted cash | (3,325) | 150 |
| Net cash used in financing activities attributable to continuing operations | (4,275) | (5,130) |

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| | | |
|---|-----------|-----------|
| Total cash used in continuing operations | (32,122) | (36,811) |
| Net cash used in operating activities attributable to discontinued operations | (58,317) | (52,362) |
| Net cash used in investing activities attributable to discontinued operations | (9,310) | (1,256) |
| Net cash provided by financing activities attributable to discontinued operations | 41,261 | 61,630 |
| Total cash provided by (used in) discontinued operations | (26,366) | 8,012 |
| Net decrease in cash and cash equivalents | (58,488) | (28,799) |
| Cash and cash equivalents at beginning of period | 68,819 | 86,093 |
| Cash and cash equivalents at end of period | \$ 10,331 | \$ 57,294 |

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 ORGANIZATION

Company Overview

Tree.com, Inc. ("we," "Tree.com" or the "Company") is the parent of LendingTree, LLC, which owns several brands and businesses that provide information, tools, advice, products and services for critical transactions in our customers' lives. Our family of brands includes: LendingTree.com®, GetSmart.com®, DegreeTree.comSM, HealthTree.comSM, LendingTreeAutos.com, DoneRight.com®, and InsuranceTree.comSM. Together, these brands serve as an ally for consumers who are looking to comparison shop for loans and other services from multiple businesses and professionals that will compete for their business.

Segment Reporting

The overall concept that Tree.com employs in determining its reportable segments and related financial information is to present them in a manner consistent with how the chief operating decision maker and executive management view the Tree.com businesses, how the businesses are organized as to segment management, and the focus of the Tree.com businesses with regards to the types of products or services offered or the target market.

Through the quarter ended March 31, 2011, we operated in two reportable business segments: LendingTree Loans and Exchanges. The LendingTree Loans segment originates, processes, approves and funds various residential real estate loans through Home Loan Center, Inc. dba LendingTree Loans ("HLC"). The HLC and LendingTree Loans brand names are collectively referred to in these consolidated financial statements as "LendingTree Loans." The Exchanges segment consists of online lead generation networks and call centers that connect consumers and service providers principally in the lending, higher education, home services, insurance and automobile marketplaces.

In connection with entering into an agreement in the second quarter of 2011 that provides for the sale of substantially all of the operating assets of our LendingTree Loans segment to Discover Bank that is discussed below and in Note 6, the Company re-evaluated its reporting segments based on the continuing operations of the Company. We have determined that our continuing operations are now one reportable segment, which represents the previous "Exchanges" segment.

Tree.com maintains operations solely in the United States.

Discontinued Operations

The businesses of RealEstate.com and RealEstate.com, REALTORS® (which together represent the former Real Estate segment) and LendingTree Loans are presented as discontinued operations in the accompanying consolidated balance sheet and consolidated statements of operations and cash flows for all periods presented. The notes accompanying these consolidated financial statements reflect our continuing operations and, unless otherwise noted, exclude information related to the discontinued operations.

Real Estate

On March 10, 2011, management of the Company made the decision and finalized a plan to close all of the field offices of the proprietary full service real estate brokerage business known as RealEstate.com, REALTORS®. The Company exited all markets by March 31, 2011. In September

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 1 ORGANIZATION (Continued)

2011, the Company sold the remaining assets of RealEstate.com, which consisted primarily of internet domain names and trademarks, for \$8.3 million and recognized a gain on sale of \$7.8 million.

LendingTree Loans

On May 12, 2011, we entered into an asset purchase agreement with Discover Bank, a wholly-owned subsidiary of Discover Financial Services. The asset purchase agreement provides for the sale of substantially all of the operating assets of our LendingTree Loans business to Discover Bank.

Under the terms of the asset purchase agreement, Discover Bank has agreed to pay approximately \$55.9 million in cash for the assets, subject to certain adjustments as described in the asset purchase agreement. \$35.9 million is due upon the closing of the transaction and \$10 million is due on each of the first and second anniversaries of the closing, subject to certain conditions as described in the asset purchase agreement, including maintenance of the LendingTree Exchange and certain financial and operational metrics associated with the LendingTree Exchange business, for which we are compliant.

Discover Bank generally will not assume liabilities of the LendingTree Loans business that arose before the closing date, except for certain liabilities directly related to assets included in the purchase. A portion of the initial purchase price payment will be held in escrow pending the discharge of certain liabilities that will remain with us.

The transaction is subject to various closing conditions, including the receipt of regulatory approvals and loan repurchase proposals for Discover Bank. Our stockholders approved the transaction on August 26, 2011.

The asset purchase agreement contains customary representations, warranties, covenants and indemnification obligations of the parties.

The asset purchase agreement also includes covenants of us (for which we are compliant) and Discover Bank. Subject to certain exceptions stated in the asset purchase agreement, we have agreed to operate the LendingTree Loans business in the ordinary course and to maintain certain operational and financial metrics until the closing of the transaction. Our covenants include requirements to maintain personnel in our LendingTree Loans business, to maintain certain quality thresholds for our loan pipeline, to maintain warehouse line capacity and compliance with our warehouse lending agreement, and subject to certain exceptions, not to introduce new loan products without Discover Bank's consent. If the requirements of these covenants are not met, Discover Bank has the option to terminate the asset purchase agreement. Subject to certain exceptions, we have also agreed not to solicit or initiate discussion with third parties regarding other proposals to acquire the assets of the LendingTree Loans business or substantial equity interests in our company, and to certain restrictions on our ability to respond to or accept any such proposals.

The asset purchase agreement also includes customary termination provisions, including that each of our company and Discover Bank may terminate the asset purchase agreement if the other party has materially breached any representation, warranty or covenant contained in the asset purchase agreement and failed to cure such breach, if the closing has not occurred within 150 days from the signing (subject to certain extensions for up to 150 additional days). Discover Bank may terminate the asset purchase agreement if our board of directors determines, after considering any modified proposals from Discover Bank, to change its recommendation to our stockholders because a failure to do so would constitute a breach of its fiduciary duties, or if we materially breach our non-solicitation obligations. If the asset

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 1 ORGANIZATION (Continued)

purchase agreement is terminated under certain circumstances, including due to a change of recommendation by our board of directors, we will be required to pay Discover Bank a termination fee of \$2.2 million. If Discover Bank does not complete the acquisition as a result of its inability to obtain proposals for loan purchase arrangements that are customary for a bank that is similarly situated to Discover Bank, Discover Bank will be required to pay us a termination fee of \$5 million.

On November 7, 2011, Discover Bank elected to extend the end date upon which either party could terminate the Asset Purchase Agreement by 30 days to December 8, 2011, and paid the required extension payment of \$1.0 million to the Company's HLC, Inc. subsidiary. Discover Bank is permitted up to three additional 30-day extensions in certain circumstances. Discover Bank must pay a \$1.0 million extension fee to HLC, Inc. to exercise each of the second and third extensions and a \$2.0 million extension to exercise the fourth extension. All extension payments, including the one received in November, will be credited against the purchase price due at closing. For a more complete discussion of the closing conditions, end date extension rights and associated fees, termination fees and other provisions of the Asset Purchase Agreement, please see the Company's definitive proxy statement filed with the Securities and Exchange Commission on August 2, 2011.

Separate from the asset purchase agreement, Tree.com has also agreed to provide certain marketing related services to Discover Bank in connection with its mortgage origination business for a two-year term commencing on the date of entry into the asset purchase agreement. Discover Bank has also agreed to be a participating lender in the LendingTree Network following the closing of the acquisition.

Business Combinations

On March 15, 2011, Tree.com, through its wholly-owned subsidiary, HLC, completed its acquisition of certain assets of First Residential Mortgage Network, Inc. dba SurePoint Lending ("SurePoint") and certain shareholders of SurePoint. The Asset Purchase Agreement (the "Agreement") was previously announced on November 16, 2010. SurePoint, a LendingTree network lender for eleven years, was a full service residential mortgage provider licensed in 45 states and employing over 500 people, including more than 300 licensed loan officers. The Agreement provides for the purchase by HLC of certain specified assets and liabilities of SurePoint related to its business of originating, refinancing, processing, underwriting, funding and closing residential mortgage loans; providing title and escrow services; and providing other mortgage related services, as further described in the Agreement. The acquired assets also include all of the equity interests of Real Estate Title Services, LLC. Under the terms of the Agreement, HLC paid \$8.0 million in cash upon the closing of the transaction, subject to certain adjustments as described in the Agreement. The Company used available cash to fund the acquisition.

This asset purchase is being accounted for under the acquisition method of accounting. Accordingly, the purchase price is allocated to the acquired assets and liabilities based on their estimated fair values at the acquisition date. The purchase price has been allocated as \$5.6 million to goodwill, \$0.7 million to intangible assets with useful lives of three months to five years, and \$1.7 million to equipment and other assets. The pro forma effect of this purchase was not material to our results of operations.

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 1 ORGANIZATION (Continued)

Basis of Presentation

The accompanying unaudited interim consolidated financial statements as of September 30, 2011 and 2010 and for the three and nine months then ended have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and the rules and regulations of the U.S. Securities and Exchange Commission ("SEC"). Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for annual financial statements. In the opinion of the Company's management, the unaudited interim consolidated financial statements have been prepared on the same basis as the audited financial statements, and include all adjustments, consisting only of normal recurring adjustments, necessary for the fair presentation of the Company's financial position for the periods presented. The results for the three and nine months ended September 30, 2011 are not necessarily indicative of the results to be expected for the year ending December 31, 2011, or any other period. These financial statements and notes should be read in conjunction with the audited financial statements and notes thereto included in the Company's annual report on Form 10-K for the year ended December 31, 2010.

NOTE 2 SIGNIFICANT ACCOUNTING POLICIES

Accounting Estimates

Tree.com's management is required to make certain estimates and assumptions during the preparation of the consolidated financial statements in accordance with U.S. generally accepted accounting principles ("GAAP"). These estimates and assumptions impact the reported amount of assets and liabilities and disclosures of contingent assets and liabilities as of the date of the consolidated financial statements. They also impact the reported amount of net earnings during any period. Actual results could differ from those estimates.

Significant estimates underlying the accompanying consolidated financial statements, including discontinued operations, include: valuation allowance for impaired loans held for sale; loan loss obligations; the fair value of loans held for sale and related derivatives; the recoverability of long-lived assets, goodwill and intangible assets; the determination of income taxes payable and deferred income taxes, including related valuation allowances; restructuring reserves; contingent consideration related to business combinations; various other allowances, reserves and accruals; and assumptions related to the determination of stock-based compensation.

Reclassifications

Certain prior period amounts have been reclassified to conform with the current presentation with no effect on net income (loss) or accumulated deficit. Specifically, certain costs within continuing operations totaling \$0.1 million for both the three and nine months ended September 30, 2010 were reclassified from general and administrative expense to litigation settlements and contingencies.

Cash and Cash Equivalents

Cash and cash equivalents include cash and short-term, highly liquid money market investments.

Table of Contents**TREE.COM, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****NOTE 2 SIGNIFICANT ACCOUNTING POLICIES (Continued)****Restricted Cash**

Restricted cash and cash equivalents consists of the following (in thousands):

| | September 30, 2011 | December 31, 2010 |
|---|-----------------------|----------------------|
| Cash in escrow for surety bonds | \$ 6,500 | \$ 5,030 |
| Cash in escrow for corporate purchasing card program | 800 | 800 |
| Minimum required balances for warehouse lines of credit | 5,250 | 1,925 |
| Other | 405 | 400 |
| Total restricted cash and cash equivalents | \$ 12,955 | \$ 8,155 |

New Accounting Pronouncements

On January 21, 2010, the FASB amended and Tree.com adopted the accounting standard for fair value measurements and disclosures, which added new requirements for disclosures about transfers into and out of Level 1 and 2 and separate disclosures about purchases, sales, issuances and settlements relating to Level 3 measurements. The amendment also clarifies existing fair value disclosures about the level of disaggregation and the inputs and valuation techniques used to measure fair value. This amendment is effective for the first reporting period (including interim periods) beginning after December 15, 2009, except for the requirement to provide the Level 3 activity of purchases, sales, issuances and settlements on a gross basis, which is effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. See Note 6 for further information.

On September 15, 2011, the FASB issued the updated accounting standard on testing goodwill for impairment. The update simplifies how an entity tests goodwill for impairment. The amendments allow both public and nonpublic entities an option to first assess qualitative factors to determine whether it is necessary to perform the two-step quantitative goodwill impairment test. Under that option, an entity no longer would be required to calculate the fair value of a reporting unit unless the entity determines, based on that qualitative assessment, that it is more likely than not that its fair value is less than its carrying amount. The amendments will be effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted. The Company does not plan to early adopt and believes this will not have a material impact on the consolidated financial statements.

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 3 GOODWILL AND INTANGIBLE ASSETS

The balance of goodwill and intangible assets, net is as follows (in thousands):

| | September 30, 2011 | December 31, 2010 |
|---|-----------------------|----------------------|
| Goodwill | \$ 3,632 | \$ 3,632 |
| Intangible assets with indefinite lives | \$ 39,142 | \$ 39,142 |
| Intangible assets with definite lives, net | 1,153 | 2,177 |
| Total intangible assets, net | \$ 40,295 | \$ 41,319 |

Intangible assets with indefinite lives relate principally to the LendingTree trademarks.

At September 30, 2011, intangible assets with definite lives relate to the following (in thousands):

| | Cost | Accumulated Amortization | Net | Weighted Average Amortization Life (Years) |
|---------------------|-----------|-----------------------------|----------|---|
| Purchase agreements | \$ 50,436 | \$ (50,306) | \$ 130 | 5.0 |
| Technology | 25,194 | (24,998) | 196 | 3.0 |
| Customer lists | 6,682 | (6,030) | 652 | 4.2 |
| Other | 1,517 | (1,342) | 175 | 2.5 |
| Total | \$ 83,829 | \$ (82,676) | \$ 1,153 | |

At December 31, 2010, intangible assets with definite lives relate to the following (in thousands):

| | Cost | Accumulated Amortization | Net | Weighted Average Amortization Life (Years) |
|---------------------|-----------|-----------------------------|----------|---|
| Purchase agreements | \$ 50,436 | \$ (50,271) | \$ 165 | 5.0 |
| Technology | 26,091 | (25,438) | 653 | 3.0 |
| Customer lists | 6,682 | (5,986) | 696 | 4.1 |
| Other | 1,609 | (946) | 663 | 2.5 |
| Total | \$ 84,818 | \$ (82,641) | \$ 2,177 | |

Table of Contents**TREE.COM, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****NOTE 3 GOODWILL AND INTANGIBLE ASSETS (Continued)**

Amortization of intangible assets with definite lives is computed on a straight-line basis and, based on September 30, 2011 balances, such amortization for the next five years is estimated to be as follows (in thousands):

| | Amount |
|-------------------------------|-----------------|
| Three months ending | |
| December 31, 2011 | \$ 107 |
| Year ending December 31, 2012 | 363 |
| Year ending December 31, 2013 | 143 |
| Year ending December 31, 2014 | 84 |
| Year ending December 31, 2015 | 60 |
| Thereafter | 396 |
| Total | \$ 1,153 |

NOTE 4 PROPERTY AND EQUIPMENT

The balance of property and equipment, net is as follows (in thousands):

| | September 30, 2011 | December 31, 2010 |
|---|-------------------------------|------------------------------|
| Computer equipment and capitalized software | \$ 26,053 | \$ 19,898 |
| Leasehold improvements | 2,042 | 1,382 |
| Furniture and other equipment | 1,450 | 1,362 |
| Projects in progress | 638 | 2,780 |
| | 30,183 | 25,422 |
| Less: accumulated depreciation and amortization | (20,992) | (17,824) |
| Total property and equipment, net | \$ 9,191 | \$ 7,598 |

Table of Contents**TREE.COM, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****NOTE 5 ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES**

Accrued expenses and other current liabilities consist of the following (in thousands):

| | September 30, 2011 | December 31, 2010 |
|---|-----------------------|----------------------|
| Litigation accruals | \$ 3,726 | \$ 520 |
| Accrued advertising expense | 3,054 | 8,511 |
| Accrued compensation and benefits | 332 | 2,766 |
| Accrued professional fees | 1,083 | 1,166 |
| Accrued restructuring costs | 764 | 1,199 |
| Customer deposits and escrows | 2,234 | 2,240 |
| Deferred rent | 180 | 379 |
| Other | 7,743 | 7,100 |
| Total accrued expenses and other current liabilities | \$ 19,116 | \$ 23,881 |

The other category above reflects an earnout payable related to an acquisition, franchise taxes, self-insured health claims and other miscellaneous accrued expenses.

An additional \$1.0 million and \$1.2 million of accrued restructuring liabilities are classified in other long term liabilities at September 30, 2011 and December 31, 2010, respectively.

NOTE 6 DISCONTINUED OPERATIONS

On March 10, 2011, management of the Company made the decision and finalized a plan to close all of the field offices of the proprietary full service real estate brokerage business known as RealEstate.com, REALTORS®. The Company exited all markets by March 31, 2011. In September 2011, the Company sold the remaining assets of RealEstate.com, which consisted primarily of internet domain names and trademarks. Accordingly, these Real Estate businesses are presented as discontinued operations in the accompanying consolidated balance sheet and consolidated statements of operations and cash flows for all periods presented.

On May 12, 2011, we entered into an asset purchase agreement with Discover Bank, a wholly-owned subsidiary of Discover Financial Services, which provides for the sale of substantially all of the operating assets of our LendingTree Loans business to Discover Bank. The Company has evaluated the facts and circumstances of the pending transaction and the applicable accounting guidance for discontinued operations, and has concluded that the LendingTree Loans business should be reflected as discontinued operations in the accompanying consolidated balance sheet and consolidated statements of operations and cash flows for all periods presented.

Table of Contents**TREE.COM, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****NOTE 6 DISCONTINUED OPERATIONS (Continued)**

The revenue and net income (loss) for the Real Estate businesses that are reported as discontinued operations for the applicable periods were as follows (in thousands):

| | Three Months Ended September 30, | |
|---|---|-------------|
| | 2011 | 2010 |
| Revenue | \$ 515 | \$ 3,213 |
| Loss before income taxes | \$ (637) | \$ (1,182) |
| Income tax provision | | |
| Gain from sale of discontinued operations | 7,752 | |
| Net income (loss) | \$ 7,115 | \$ (1,182) |

| | Nine Months Ended September 30, | |
|---|--|-------------|
| | 2011 | 2010 |
| Revenue | \$ 3,633 | \$ 11,825 |
| Loss before income taxes | \$ (16,936) | \$ (4,454) |
| Income tax provision | | |
| Gain from sale of discontinued operations | 7,752 | |
| Net loss | \$ (9,184) | \$ (4,454) |

Net loss for the nine months ended September 30, 2011 includes goodwill disposal charges totaling \$8.0 million, trademark impairment charges of \$4.1 million and restructuring charges totaling \$2.5 million.

The revenue and net income (loss) for LendingTree Loans that are reported as discontinued operations for the applicable periods were as follows (in thousands):

| | Three Months Ended September 30, | |
|----------------------------|---|-------------|
| | 2011 | 2010 |
| Revenue | \$ 37,094 | \$ 34,760 |
| Income before income taxes | \$ 9,168 | \$ 10,539 |
| Income tax provision | | |
| Net income | \$ 9,168 | \$ 10,539 |

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 6 DISCONTINUED OPERATIONS (Continued)

| | Nine Months Ended September 30, | |
|-----------------------------------|------------------------------------|-----------|
| | 2011 | 2010 |
| Revenue | \$ 81,726 | \$ 87,147 |
| Income (loss) before income taxes | \$ (7,679) | \$ 22,364 |
| Income tax provision | | |
| Net income (loss) | \$ (7,679) | \$ 22,364 |

Net loss for the nine months ended September 30, 2011 includes restructuring charges totaling \$4.0 million.

The assets and liabilities of Real Estate that are reported as discontinued operations as of September 30, 2011 and December 31, 2010 were as follows (in thousands):

| | September 30, 2011 | December 31, 2010 |
|--------------------------|-----------------------|----------------------|
| Current assets | \$ 137 | \$ 305 |
| Property and equipment | | 2,123 |
| Goodwill | | 7,967 |
| Other non-current assets | | 4,285 |
| Non-current assets | | 14,375 |
| Current liabilities | 1,248 | 1,213 |
| Non-current liabilities | 92 | 288 |
| Net assets (liabilities) | \$ (1,203) | \$ 13,179 |

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 6 DISCONTINUED OPERATIONS (Continued)

The assets and liabilities of LendingTree Loans that are reported as discontinued operations as of September 30, 2011 and December 31, 2010 were as follows (in thousands):

| | September 30, 2011 | December 31, 2010 |
|--------------------------------|-----------------------|----------------------|
| Loans held for sale | \$ 185,295 | \$ 116,681 |
| Other current assets | 18,518 | 13,715 |
| Current assets | 203,813 | 130,396 |
| Property and equipment | 3,406 | 3,074 |
| Goodwill | 5,579 | |
| Other non-current assets | 1,108 | 406 |
| Non-current assets | 10,094 | 3,480 |
| Warehouse lines of credit | 141,883 | 100,623 |
| Other current liabilities | 24,434 | 16,384 |
| Current liabilities | 166,317 | 117,007 |
| Non-current liabilities | 18,705 | 12,134 |
| Net assets (liabilities) | \$ 28,885 | \$ 4,735 |

Significant Assets and Liabilities of LendingTree Loans

Upon closing of the sale of substantially all of the operating assets of our LendingTree Loans business to Discover Bank, LendingTree Loans will cease to originate consumer loans and will no longer have additional borrowings available under the warehouse lines of credit. The remaining operations will be wound down over the quarter following the closing of the transaction. These wind-down activities include selling the balance of loans held for sale to investors, which historically has occurred within thirty days of funding, and paying off and then terminating the lines of credit. Additionally, the liability for losses on previously sold loans will remain with LendingTree Loans. Below is a discussion of these significant items.

Loans Held for Sale

LendingTree Loans originates all of its residential real estate loans with the intent to sell them in the secondary market. Loans held for sale consist primarily of residential first mortgage loans that are secured by residential real estate throughout the United States.

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 6 DISCONTINUED OPERATIONS (Continued)

The following table represents the loans held for sale by type of loan as of September 30, 2011 and December 31, 2010 (\$ amounts in thousands):

| | September 30, 2011 | | December 31, 2010 | |
|---------------|-----------------------|-------------|----------------------|-------------|
| | Amount | % | Amount | % |
| Conforming | \$ 153,561 | 83% | \$ 86,451 | 74% |
| FHA and Alt-A | 20,778 | 11% | 20,431 | 18% |
| Jumbo | 10,956 | 6% | 9,129 | 8% |
| Subprime | | % | 580 | % |
| Home equity | | % | 90 | % |
| Total | \$ 185,295 | 100% | \$ 116,681 | 100% |

The following presents the difference between the aggregate principal balance of loans on nonaccrual status for which the fair value option has been elected and for loans measured at lower of cost or market valuation as of September 30, 2011 and December 31, 2010 (in thousands):

| | As of September 30, 2011 | | |
|--|---|--|------------------------------|
| | Loans on Nonaccrual Measured at Fair Value | Loans on Nonaccrual Measured at LOCOM | Total Loans on Nonaccrual |
| Aggregate unpaid principal balance | \$ 558 | \$ | \$ 558 |
| Difference between fair value and aggregate unpaid principal balance | (250) | | (250) |
| Loans on nonaccrual | \$ 308 | \$ | \$ 308 |

| | As of December 31, 2010 | | |
|--|---|--|------------------------------|
| | Loans on Nonaccrual Measured at Fair Value | Loans on Nonaccrual Measured at LOCOM | Total Loans on Nonaccrual |
| Aggregate unpaid principal balance | \$ 1,380 | \$ 2,290 | \$ 3,670 |
| Difference between fair value and aggregate unpaid principal balance | (496) | | (496) |
| Lower of cost or market valuation allowance | | (1,508) | (1,508) |
| Deferred loan fees, net of costs | | (9) | (9) |
| Loans on nonaccrual | \$ 884 | \$ 773 | \$ 1,657 |

Included within the loans on nonaccrual status are repurchased loans with a net book value of \$-0- and \$0.2 million at September 30, 2011 and December 31, 2010, respectively. During the nine months ended September 30, 2011, LendingTree Loans did not repurchase any loans, but sold fifteen loans on nonaccrual status for \$1.2 million, which approximated the net book value. During the nine months ended September 30, 2010, LendingTree Loans repurchased one loan with a balance of \$0.3 million.

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 6 DISCONTINUED OPERATIONS (Continued)

Fair Value Measurements

Tree.com categorizes its assets and liabilities measured at fair value into a fair value hierarchy that prioritizes the assumptions used in pricing the asset or liability into the following three levels:

Level 1: Observable inputs such as quoted prices for identical assets and liabilities in active markets obtained from independent sources.

Level 2: Other inputs that are observable directly or indirectly, such as quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active and inputs that are derived principally from or corroborated by observable market data.

Level 3: Unobservable inputs for which there is little or no market data and which require Tree.com to develop its own assumptions, based on the best information available in the circumstances, about the assumptions market participants would use in pricing the asset or liability.

LendingTree Loans enters into commitments with consumers to originate loans at a specified interest rate (interest rate lock commitments "IRLCs"). Tree.com reports IRLCs as derivative instruments at fair value with changes in fair value being recorded in discontinued operations. IRLCs for loans to be sold to investors using a mandatory or assignment of trade ("AOT") method are hedged using "to be announced mortgage-backed securities" ("TBA MBS") and are valued using quantitative risk models. The IRLCs derive their base value from an underlying loan type with similar characteristics using the TBA MBS market which is actively quoted and easily validated through external sources. The most significant data inputs used in this valuation include, but are not limited to, loan type, underlying loan amount, note rate, loan program, and expected sale date of the loan. IRLCs for loans sold to investors on a best efforts basis are hedged using best efforts forward delivery commitments and are valued on an individual loan basis using a proprietary database program. These valuations are based on investor pricing tables stratified by product, note rate and term. The valuation is adjusted at the loan level to consider the servicing release premium and loan pricing adjustments specific to each loan. The Company applies an anticipated loan funding probability based on its own experience to value IRLCs, which results in the classification of these derivatives as Level 3. The value of the underlying loan and the anticipated loan funding probability are the most significant assumptions affecting the valuation of IRLCs. There were no significant changes to the methods and assumptions for valuing IRLCs in the period ended September 30, 2011. At September 30, 2011 and December 31, 2010, there were \$454.0 million and \$216.6 million, respectively, of IRLCs notional value outstanding.

Loans held for sale measured at fair value and sold to investors using a mandatory or AOT method are also hedged using TBA MBS and valued using quantitative risk models. The valuation is based on the loan amount, note rate, loan program, and expected sale date of the loan. Loans held for sale measured at fair value and sold to investors on a best efforts basis are hedged using best efforts forward delivery commitments and are valued using a proprietary database program. The best efforts valuations are based on daily investor pricing tables stratified by product, note rate and term. These valuations are adjusted at the loan level to consider the servicing release premium and loan pricing adjustments specific to each loan. Loans held for sale, excluding impaired loans, are classified as Level 2. Loans held for sale measured at fair value that become impaired are transferred from Level 2 to Level 3, as the estimate of fair value is based on the Company's experience considering lien position

Table of Contents**TREE.COM, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****NOTE 6 DISCONTINUED OPERATIONS (Continued)**

and current status of the loan. There were no significant changes to the method and assumptions used to estimate the fair value of impaired loans in the period ended September 30, 2011. LendingTree Loans recognizes interest income separately from other changes in fair value.

Under LendingTree Loans' risk management policy, LendingTree Loans economically hedges the changes in fair value of IRLCs and loans held for sale caused by changes in interest rates by using TBA MBS and entering into best efforts forward delivery commitments. These hedging instruments are recorded at fair value with changes in fair value recorded in current earnings as a component of revenue from the origination and sale of loans. There were no significant changes to the methods and assumptions for valuing hedging instruments in the period ended September 30, 2011. TBA MBS used to hedge both IRLCs and loans are valued using quantitative risk models based primarily on inputs related to characteristics of the MBS stratified by product, coupon, and settlement date. These derivatives are classified as Level 2. Best efforts forward delivery commitments are valued using a proprietary database program using investor pricing tables considering the current base loan price. An anticipated loan funding probability is applied to value best efforts commitments hedging IRLCs, which results in the classification of these contracts as Level 3. The current base loan price and the anticipated loan funding probability are the most significant assumptions affecting the value of the best efforts commitments. The best efforts forward delivery commitments hedging loans held for sale are classified as Level 2, so such contracts are transferred from Level 3 to Level 2 at the time the underlying loan is originated. For the purposes of the tables below, we refer to TBA MBS and best efforts forward delivery commitments collectively as "Forward Delivery Contracts".

The following presents Tree.com's assets and liabilities that are measured at fair value on a recurring basis at September 30, 2011 and December 31, 2010 (in thousands):

| | As of September 30, 2011 | | | |
|--|--|--|--|--|
| | Recurring Fair Value Measurements Using | | | |
| | Quoted Market Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total Fair Value Measurements |
| Loans held for sale | \$ | \$ 184,987 | \$ 308 | \$ 185,295 |
| Interest rate lock commitments ("IRLCs") | | | 12,747 | 12,747 |
| Forward delivery contracts | | (2,898) | 32 | (2,866) |
| Total | \$ | \$ 182,089 | \$ 13,087 | \$ 195,176 |

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 6 DISCONTINUED OPERATIONS (Continued)

| | As of December 31, 2010 | | | |
|--|--|---|--|-------------------------------------|
| | Recurring Fair Value Measurements Using | | | |
| | Quoted Market Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total Fair Value Measurements |
| Loans held for sale | \$ | \$ 115,024 | \$ 884 | \$ 115,908 |
| Interest rate lock commitments ("IRLCs") | | | 5,986 | 5,986 |
| Forward delivery contracts | | 1,001 | 3 | 1,004 |
| Total | \$ | \$ 116,025 | \$ 6,873 | \$ 122,898 |

The following presents the changes in Tree.com's assets and liabilities that are measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the three and nine months ended September 30, 2011 and 2010 (in thousands):

| | Three Months Ended September 30, 2011 | | |
|--|--|----------------------------------|---------------------------|
| | Interest Rate Lock Commitments | Forward Delivery Contracts | Loans Held for Sale |
| Balance at July 1, 2011 | \$ 6,278 | \$ 220 | \$ 861 |
| Transfers into Level 3 | | | 72 |
| Transfers out of Level 3 | | (257) | |
| Total net gains (losses) included in earnings (realized and unrealized) | 40,680 | 69 | (83) |
| Purchases, sales, and settlements | | | |
| Purchases | | | |
| Sales | | | (538) |
| Settlements | (2,255) | | (4) |
| Transfers of IRLCs to closed loans | (31,956) | | |
| Balance at September 30, 2011 | \$ 12,747 | \$ 32 | \$ 308 |

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 6 DISCONTINUED OPERATIONS (Continued)

| | Nine Months Ended September 30, 2011 | | |
|--|---|----------------------------------|---------------------------|
| | Interest Rate Lock Commitments | Forward Delivery Contracts | Loans Held for Sale |
| Balance at January 1, 2011 | \$ 5,986 | \$ 3 | \$ 884 |
| Transfers into Level 3 | | | 732 |
| Transfers out of Level 3 | | (215) | |
| Total net gains (losses) included in earnings (realized and unrealized) | 81,847 | 302 | (86) |
| Purchases, sales, and settlements | | | |
| Purchases(a) | 970 | (58) | |
| Sales | | | (1,041) |
| Settlements | (8,252) | | (181) |
| Transfers of IRLCs to closed loans | (67,804) | | |
| Balance at September 30, 2011 | \$ 12,747 | \$ 32 | \$ 308 |

(a) Purchased in conjunction with the acquisition of certain assets of SurePoint.

| | Three Months Ended September 30, 2010 | | |
|--|--|----------------------------------|---------------------------|
| | Interest Rate Lock Commitments | Forward Delivery Contracts | Loans Held for Sale |
| Balance at July 1, 2010 | \$ 10,848 | \$ (20) | \$ 957 |
| Transfers into Level 3 | | | 378 |
| Transfers out of Level 3 | | (17) | |
| Total net gains (losses) included in earnings (realized and unrealized) | 33,683 | 20 | (34) |
| Purchases, sales, and settlements | | | |
| Purchases | | | |
| Sales | | | (262) |
| Settlements | (3,533) | | (3) |
| | (30,749) | | |

Transfers of IRLCs
to closed loans

Balance at
September 30, 2010 \$ 10,249 \$ (17) \$ 1,036

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 6 DISCONTINUED OPERATIONS (Continued)

| | Nine Months Ended September 30, 2010 | | |
|--|---|----------------------------------|---------------------------|
| | Interest Rate Lock Commitments | Forward Delivery Contracts | Loans Held for Sale |
| Balance at January 1, 2010 | \$ 3,680 | \$ 487 | \$ 777 |
| Transfers into Level 3 | | | 640 |
| Transfers out of Level 3 | | 109 | |
| Total net gains (losses) included in earnings (realized and unrealized) | 83,752 | (613) | (111) |
| Purchases, sales, and settlements | | | |
| Purchases | | | |
| Sales | | | (262) |
| Settlements | (12,250) | | (8) |
| Transfers of IRLCs to closed loans | (64,933) | | |
| Balance at September 30, 2010 | \$ 10,249 | \$ (17) | \$ 1,036 |

The following presents the gains (losses) included in earnings for the three and nine months ended September 30, 2011 and 2010 relating to Tree.com's assets and liabilities that are measured at fair value on a recurring basis using significant unobservable inputs (Level 3) (in thousands):

| | Three Months Ended September 30, 2011 | | | Nine Months Ended September 30, 2011 | | |
|--|--|----------------------------------|---------------------------|---|----------------------------------|---------------------------|
| | Interest Rate Lock Commitments | Forward Delivery Contracts | Loans Held for Sale | Interest Rate Lock Commitments | Forward Delivery Contracts | Loans Held for Sale |
| Total net gains (losses) included in earnings, which are included in discontinued operations | \$ 40,680 | \$ 69 | \$ (83) | \$ 81,847 | \$ 302 | \$ (86) |
| Change in unrealized gains (losses) relating to assets and liabilities still held at September 30, 2011, which are included in discontinued operations | \$ 12,747 | \$ 32 | \$ | \$ 12,747 | \$ 32 | \$ (44) |

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 6 DISCONTINUED OPERATIONS (Continued)

| | Three Months Ended September 30, 2010 | | | Nine Months Ended September 30, 2010 | | |
|--|--|----------------------------------|---------------------------|---|----------------------------------|---------------------------|
| | Interest Rate Lock Commitments | Forward Delivery Contracts | Loans Held for Sale | Interest Rate Lock Commitments | Forward Delivery Contracts | Loans Held for Sale |
| Total net gains (losses) included in earnings, which are included in discontinued operations | \$ 33,683 | \$ 20 | \$ (34) | \$ 83,752 | \$ (613) | \$ (111) |
| Change in unrealized gains (losses) relating to assets and liabilities still held at September 30, 2010, which are included in discontinued operations | \$ 10,249 | \$ (17) | \$ (112) | \$ 10,249 | \$ (17) | \$ 2 |

The following table summarizes the Company's derivative instruments not designated as hedging instruments as of September 30, 2011 and December 31, 2010 (in thousands):

| | September 30, 2011 | | December 31, 2010 | |
|--------------------------------|--|-----------------|--|-----------------|
| | Balance Sheet Location | Fair Value | Balance Sheet Location | Fair Value |
| Interest Rate Lock Commitments | Current assets of discontinued operations | \$ 12,784 | Current assets of discontinued operations | \$ 5,991 |
| Forward Delivery Contracts | Current assets of discontinued operations | 323 | Current assets of discontinued operations | 2,633 |
| Interest Rate Lock Commitments | Current liabilities of discontinued operations | (37) | Current liabilities of discontinued operations | (5) |
| Forward Delivery Contracts | Current liabilities of discontinued operations | (3,189) | Current liabilities of discontinued operations | (1,629) |
| Total Derivatives | | \$ 9,881 | | \$ 6,990 |

The gain/(loss) recognized in the consolidated statements of operations for derivatives for the periods ended September 30, 2011 and 2010 was as follows (in thousands):

| | Location of Gain/(Loss) Recognized in Income on Derivative | Three Months Ended | | Nine Months Ended | |
|--------------------------------|--|--------------------|--------------------|--------------------|--------------------|
| | | September 30, 2011 | September 30, 2010 | September 30, 2011 | September 30, 2010 |
| Interest Rate Lock Commitments | Discontinued operations | \$ 40,680 | \$ 33,683 | \$ 81,847 | \$ 83,752 |
| Forward Delivery Contracts | Discontinued operations | (3,262) | 3,252 | (3,818) | (3,905) |
| Total | | \$ 37,418 | \$ 36,935 | \$ 78,029 | \$ 79,847 |

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Tree.com has elected to account for loans held for sale originated on or after January 1, 2008 at fair value. Electing the fair value option allows a better offset of the changes in fair values of the loans and the forward delivery contracts used to economically hedge them without the burden of complying with the requirements for hedge accounting.

Table of Contents**TREE.COM, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****NOTE 6 DISCONTINUED OPERATIONS (Continued)**

Tree.com did not elect the fair value option on loans held for sale originated prior to January 1, 2008 and on loans that were repurchased from investors on or subsequent to that date. As of September 30, 2011 and December 31, 2010, -0- and 23 such loans, respectively, all of which were impaired, were included in loans held for sale and were carried at the lower of cost or market ("LOCOM") value assessed on an individual loan basis. The market value (or fair value) of these impaired loans at September 30, 2011 and December 31, 2010, measured on a non-recurring basis using significant unobservable inputs (Level 3), was \$-0- and \$0.8 million, respectively. This fair value measurement is management's best estimate of the market value of such loans and considers the lien position and loan status. During the nine months ended September 30, 2011, fifteen impaired loans were sold for \$1.2 million, which approximated the net book value.

The following presents the difference between the aggregate principal balance of loans held for sale for which the fair value option has been elected and for loans measured at LOCOM as of September 30, 2011 and December 31, 2010 (in thousands):

| | As of September 30, 2011 | | |
|--|---|--|---------------------------------|
| | Loans Held for Sale Measured at Fair Value | Loans Held for Sale Measured at LOCOM | Total Loans Held For Sale |
| Aggregate unpaid principal balance | \$ 177,471 | \$ | \$ 177,471 |
| Difference between fair value and aggregate unpaid principal balance | 7,824 | | 7,824 |
| Loans held for sale | \$ 185,295 | \$ | \$ 185,295 |

| | As of December 31, 2010 | | |
|--|---|--|---------------------------------|
| | Loans Held for Sale Measured at Fair Value | Loans Held for Sale Measured at LOCOM | Total Loans Held For Sale |
| Aggregate unpaid principal balance | \$ 113,116 | \$ 2,290 | \$ 115,406 |
| Difference between fair value and aggregate unpaid principal balance | 2,792 | | 2,792 |
| Lower of cost or market valuation allowance | | (1,508) | (1,508) |
| Deferred loan fees, net of costs | | (9) | (9) |
| Loans held for sale | \$ 115,908 | \$ 773 | \$ 116,681 |

During the nine months ended September 30, 2011 and 2010, the change in fair value of loans held for sale for which the fair value option was elected was a gain of \$3.7 million and \$5.5 million, respectively, and is included in discontinued operations in the accompanying consolidated statements of operations.

Loan Loss Obligations

LendingTree Loans sells loans it originates to investors on a servicing released basis so the risk of loss or default by the borrower is generally transferred to the investor. However, LendingTree Loans is required by these investors to make certain representations relating to credit information, loan

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 6 DISCONTINUED OPERATIONS (Continued)

documentation and collateral. These representations and warranties may extend through the contractual life of the mortgage loan. Subsequent to the sale, if underwriting deficiencies, borrower fraud or documentation defects are discovered in individual mortgage loans, LendingTree Loans may be obligated to repurchase the respective mortgage loan or indemnify the investors for any losses from borrower defaults if such deficiency or defect cannot be cured within the specified period following discovery.

In the case of early loan payoffs and early defaults on certain loans, LendingTree Loans may be required to repay all or a portion of the premium initially paid by the investor. The estimated obligation associated with early loan payoffs and early defaults is calculated based on historical loss experience by type of loan.

The obligation for losses related to the representations and warranties and other provisions discussed above is initially recorded at its estimated fair value, which includes a projection of expected future losses as well as a market based premium. Because LendingTree Loans does not service the loans it sells, it does not maintain nor have access to the current balances and loan performance data with respect to the individual loans previously sold to investors. Accordingly, the Company is unable to determine, with precision, its maximum exposure under its representations and warranties. However, LendingTree Loans utilizes the original loan balance (before it was sold to an investor), historical and projected loss frequency and loss severity ratios by loan type as well as analyses of losses in process to estimate its exposure to losses on loans previously sold. The Company maintains a liability related to this exposure based, in part, on historical and projected loss frequency and loss severity using its loan loss history (adjusted for recent trends in loan loss experience), the original principal amount of the loans previously sold, the year the loans were sold, and loan type. Accordingly, subsequent adjustments to the obligation, if any, are not made based on changes in the fair value of the obligation, which might include an estimated change in losses that may be expected in the future, but are made once further losses are determined to be both probable and estimable. As such, given current general industry trends in mortgage loans as well as housing prices, market expectations around losses related to the Company's obligations could vary significantly from the obligation recorded as of the balance sheet date or the range estimated below. In estimating its exposure to loan losses, LendingTree Loans segments its loan sales into four segments based on the extent of the documentation provided by the borrower to substantiate income and/or assets (full or limited documentation) and the lien position of the mortgage in the underlying property (first or second position). Each of these segments has a different loss experience with full documentation, first lien position loans generally having the lowest loss ratios and limited documentation, second lien position loans generally having the highest loss ratios.

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 6 DISCONTINUED OPERATIONS (Continued)

The following table represents the loans sold for the period shown and the aggregate loan losses through September 30, 2011:

| Period of Loan Sales | As of September 30, 2011 | | | | |
|--------------------------------------|--------------------------|----------------------------|-----------------------------|---|----------------------------|
| | Number of loans sold | Original principal balance | Number of loans with losses | Original principal balance of loans with losses | Amount of aggregate losses |
| | | (in billions) | | (in millions) | (in millions) |
| Nine months ended September 30, 2011 | 8,500 | \$ 1.8 | | \$ | \$ |
| 2010 | 12,400 | 2.8 | 3 | 0.7 | 0.1 |
| 2009 | 12,800 | 2.8 | 3 | 0.8 | 0.1 |
| 2008 | 11,000 | 2.2 | 22 | 4.7 | 1.1 |
| 2007 | 36,300 | 6.1 | 149 | 20.2 | 7.3 |
| 2006 | 55,000 | 7.9 | 202 | 23.4 | 13.0 |
| 2005 and prior years | 86,700 | 13.0 | 87 | 11.7 | 4.8 |
| Total | 222,700 | \$ 36.6 | 466 | \$ 61.5 | \$ 26.4 |

The pipeline of 219 loan repurchase requests and indemnifications as of September 30, 2011 was considered in determining the appropriate reserve amount. The status of these 219 loans varied from an initial review stage, which may result in a rescission of the request, to in process, where the probability of incurring a loss is high, to indemnification, whereby the Company has agreed to reimburse the purchaser of that loan if and when losses are incurred. The indemnification may have a specific term, thereby limiting the Company's exposure. The original principal amount of these loans is approximately \$44.3 million, comprised of approximately 80% full documentation first liens, 2% full documentation second liens, 15% limited documentation first liens, and 3% limited documentation second liens.

In the fourth quarter of 2009, LendingTree Loans entered into settlement negotiations with two buyers of previously purchased limited documentation loans. The settlement with one buyer was completed in December 2009 and included a payment of \$1.9 million related to all second lien loans sold to this buyer, including both full and limited documentation. This amount was not determined on an individual loan basis and is, therefore, not included in the loss amounts disclosed above based on the year such loans were sold. The settlement was included as a charge off to the reserve in 2009. Negotiations with the second buyer were completed in January 2010. This settlement of \$4.5 million, which was paid in four equal quarterly installments in 2010, relates to all future losses on limited documentation second lien loans sold to this buyer. LendingTree Loans must also pay an additional amount of up to \$0.3 million in conjunction with this settlement since it did not sell a certain volume of loans to this buyer in 2010. This amount is included in the total settlement amount and the estimated settlement payments remaining to be paid. This settlement amount was included as a charge off to the reserve in 2010 and is not included in the table above.

Based on historical experience, it is anticipated that the Company will continue to receive repurchase requests and incur losses on loans sold in prior years. However, the two settlements discussed above will eliminate future repurchase requests from those buyers for the loan types included in those settlements. As of September 30, 2011, LendingTree Loans estimated the range of remaining

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 6 DISCONTINUED OPERATIONS (Continued)

possible losses due to representations and warranty issues based on the methodology described above, excluding the \$0.3 million settlement remaining to be paid in 2011, as \$25 million to \$33 million. The Company believes that it has adequately reserved for these losses.

The activity related to loss reserves on previously sold loans for the nine months ended September 30, 2011 and 2010, is as follows (in thousands):

| | Nine Months Ended September 30, | |
|------------------------------|------------------------------------|-----------|
| | 2011 | 2010 |
| Balance, beginning of period | \$ 16,984 | \$ 16,985 |
| Provisions | 11,050 | 8,132 |
| Charge offs to reserves(a) | (1,014) | (10,172) |
| Balance, end of period | \$ 27,020 | \$ 14,945 |

(a)

The nine months ended September 30, 2010 includes a charge off for the amount of the \$4.5 million loan loss settlement plus a portion of the \$0.3 million additional accrual discussed above. The remaining settlement payment due of \$0.3 million is tracked as a liability separate from the loan loss reserve (see table below).

Based on an analysis of the Company's historical loan loss experience, it has been determined that a portion of the loan losses expected to be made by investors will be made more than twelve months following the initial sale of the underlying loans. Accordingly, the Company has estimated the portion of its loans sold reserve that it anticipates it will be liable for after twelve months and has classified that portion of the reserve as a long-term liability. The liability for losses on previously sold loans is presented in the accompanying consolidated balance sheet as of September 30, 2011 and December 31, 2010 as follows (in thousands):

| | As of September 30, 2011 | As of December 31, 2010 |
|---|--------------------------------|-------------------------------|
| Current portion related to settlement above, included in current liabilities of discontinued operations | \$ 300 | \$ 300 |
| Other current portion, included in current liabilities of discontinued operations | 9,809 | 5,459 |
| Long term portion, included in non-current liabilities of discontinued operations | 17,211 | 11,525 |
| Total | \$ 27,320 | \$ 17,284 |

Warehouse Lines of Credit

Borrowings on warehouse lines of credit were \$141.9 million and \$100.6 million at September 30, 2011 and December 31, 2010, respectively.

As of September 30, 2011, LendingTree Loans had two committed lines of credit totaling \$150.0 million of borrowing capacity. LendingTree Loans also had a \$25.0 million uncommitted line

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 6 DISCONTINUED OPERATIONS (Continued)

with one of these lenders, which was terminated on October 31, 2011. In addition, LendingTree Loans obtained a third warehouse line for \$100.0 million on October 13, 2011 and increased the second line to \$125.0 million on October 28, 2011, bringing the total borrowing capacity to \$275.0 million. Borrowings under these lines of credit are used to fund, and are secured by, consumer residential loans that are held for sale. Loans under these lines of credit are repaid using proceeds from the sales of loans by LendingTree Loans.

The \$50.0 million first line is scheduled to expire on the earliest of (i) the closing date of the proposed asset sale transaction with Discover Bank or (ii) January 30, 2012. On November 1, 2011, the terms of this line were amended so that it can be cancelled at the option of the lender at any time upon notice. This first line included an additional uncommitted credit facility of \$25.0 million, which was terminated on October 31, 2011. This first line is guaranteed by Tree.com, Inc., LendingTree, LLC and LendingTree Holdings Corp. The interest rate under the first line is the 30-day London InterBank Offered Rate ("LIBOR") or 2.00% (whichever is greater) plus 2.25%. The interest rate under the \$25.0 million uncommitted line was the 30-day LIBOR plus 1.50%.

The \$100.0 million second line was scheduled to expire on October 28, 2011, but subsequent to September 30, 2011 the line was increased to \$125.0 million and the expiration date extended to the earliest of (i) forty-five days after the closing date of the proposed asset sale transaction with Discover Bank or (ii) April 25, 2012. This line is also guaranteed by Tree.com, Inc., LendingTree, LLC and LendingTree Holdings Corp. Before the extension, the interest rate under this line was the 30-day Adjusted LIBOR or 2.0% (whichever was greater) plus 2.25% to 2.5% for loans being sold to the lender and 30-day Adjusted LIBOR or 2.0% (whichever was greater) plus 2.25% for loans not being sold to the lender. Upon extension of this line, the interest rate was changed to the 30-day Adjusted LIBOR or 2.0% (whichever is greater) plus 1.5% to 1.75% for loans being sold to the lender and 30-day Adjusted LIBOR or 2.0% (whichever is greater) plus 1.5% for loans not being sold to the lender.

The \$100.0 million third line is scheduled to expire on December 13, 2011. This line is guaranteed by Tree.com, Inc. and LendingTree, LLC. The interest rate under this line is 30-day LIBOR plus 3.25% (LIBOR may be adjusted upward for any increase in the reserve requirement of the lender as further described in the Master Repurchase Agreement).

Under the terms of these warehouse lines, LendingTree Loans is required to maintain various financial and other covenants. These financial covenants include, but are not limited to, maintaining (i) minimum tangible net worth of \$20.0 million, which was increased to \$25.0 million upon renewal of the first line in November 2011 and the second line in October 2011, (ii) minimum liquidity, (iii) a minimum current ratio, (iv) a maximum ratio of total liabilities to net worth, (v) a minimum unrestricted cash amount, (vi) pre-tax net income requirements and (vii) a maximum warehouse capacity ratio. During the quarter ended September 30, 2011, LendingTree Loans was in compliance with the covenants under these lines.

The LendingTree Loans business is highly dependent on the availability of these warehouse lines. Although we believe that our existing lines of credit are adequate for our current operations, reductions in our available credit, or the inability to extend, renew or replace these lines before completion of the pending sale of the operating assets of LendingTree Loans, would have a material adverse effect on our business, financial condition and results of operations. Management has

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 6 DISCONTINUED OPERATIONS (Continued)

determined that it could continue to operate the LendingTree Loans business at a reduced capacity as long as one of the warehouse lines remains available.

NOTE 7 EARNINGS PER SHARE AND STOCK-BASED COMPENSATION

The following table sets forth the computation of Basic and Diluted earnings per share:

| | Three Months Ended September 30, | | | |
|---|----------------------------------|------------|------------|------------|
| | 2011 | | 2010 | |
| | Basic | Diluted | Basic | Diluted |
| (In thousands, except per share data) | | | | |
| Numerator: | | | | |
| Loss from continuing operations | \$ (3,685) | \$ (3,685) | \$ (7,538) | \$ (7,538) |
| Income from discontinued operations, net of tax | 16,283 | 16,283 | 9,357 | 9,357 |
| Net income available to common shareholders | \$ 12,598 | \$ 12,598 | \$ 1,819 | \$ 1,819 |
| Denominator: | | | | |
| Weighted average common shares | 11,037 | 11,120 | 11,023 | 11,163 |
| Loss per Share: | | | | |
| Loss from continuing operations | \$ (0.33) | \$ (0.33) | \$ (0.68) | \$ (0.68) |
| Income from discontinued operations, net of tax | 1.47 | 1.46 | 0.84 | 0.84 |
| Net income per common share | \$ 1.14 | \$ 1.13 | \$ 0.16 | \$ 0.16 |

| | Nine Months Ended September 30, | | | |
|--|---------------------------------|-------------|------------|------------|
| | 2011 | | 2010 | |
| | Basic | Diluted | Basic | Diluted |
| (In thousands, except per share data) | | | | |
| Numerator: | | | | |
| Loss from continuing operations | \$ (27,853) | \$ (27,853) | (23,036) | (23,036) |
| Income (loss) from discontinued operations, net of tax | (16,863) | (16,863) | 17,910 | 17,910 |
| Net loss available to common shareholders | \$ (44,716) | \$ (44,716) | \$ (5,126) | \$ (5,126) |
| Denominator: | | | | |
| Weighted average common shares | 10,978 | 10,978 | 10,993 | 10,993 |
| Loss per Share: | | | | |
| Loss from continuing operations | \$ (2.54) | \$ (2.54) | \$ (2.10) | \$ (2.10) |
| Income (loss) from discontinued operations, net of tax | (1.53) | (1.53) | 1.63 | 1.63 |

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| | | | | | | | | |
|---------------------------|----|--------|----|--------|----|--------|----|--------|
| Net loss per common share | \$ | (4.07) | \$ | (4.07) | \$ | (0.47) | \$ | (0.47) |
|---------------------------|----|--------|----|--------|----|--------|----|--------|

Table of Contents**TREE.COM, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****NOTE 7 EARNINGS PER SHARE AND STOCK-BASED COMPENSATION (Continued)**

Non-cash compensation expense related to equity awards is included in the following line items in the accompanying consolidated statements of operations for the three and nine months ended September 30, 2011 and 2010 (in thousands):

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|------------------------------------|--|--------|---------------------------------------|----------|
| | 2011 | 2010 | 2011 | 2010 |
| Cost of revenue | \$ (1) | \$ (1) | \$ 3 | \$ 14 |
| Selling and marketing expense | 50 | 18 | 314 | 141 |
| General and administrative expense | 712 | 619 | 2,196 | 2,179 |
| Product development | 63 | 20 | 218 | 89 |
| Non-cash compensation expense | \$ 824 | \$ 656 | \$ 2,731 | \$ 2,423 |

The forms of stock-based awards granted to Tree.com employees are principally restricted stock units ("RSUs"), restricted stock and stock options. RSUs are awards in the form of units, denominated in a hypothetical equivalent number of shares of Tree.com common stock and with the value of each award equal to the fair value of Tree.com common stock at the date of grant. RSUs may be settled in cash, stock or both, as determined by the Compensation Committee at the time of grant. Each stock-based award is subject to service-based vesting, where a specific period of continued employment must pass before an award vests. Certain restricted stock awards also include performance-based vesting, where certain performance targets set at the time of grant must be achieved before an award vests. Tree.com recognizes expense for all stock-based awards for which vesting is considered probable. For stock-based awards, the accounting charge is measured at the grant date as the fair value of Tree.com common stock and expensed ratably as non-cash compensation over the vesting term. For performance-based awards, the expense is measured at the grant date as the fair value of Tree.com common stock and expensed as non-cash compensation over the vesting period if the performance targets are considered probable of being achieved.

The amount of stock-based compensation expense recognized in the consolidated statements of operations is reduced by estimated forfeitures, as the amount recorded is based on awards ultimately expected to vest. The forfeiture rate is estimated at the grant date based on historical experience and revised, if necessary, in subsequent periods if the actual forfeiture rate differs from the estimated rate.

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 7 EARNINGS PER SHARE AND STOCK-BASED COMPENSATION (Continued)

A summary of changes in outstanding stock options for the nine months ended September 30, 2011 is as follows:

| | Shares | Weighted Average Exercise Price | Weighted Average Remaining Contractual Term (In years) | Aggregate Intrinsic Value (In thousands) |
|---|-----------|--|---|---|
| Outstanding at January 1, 2011 | 952,669 | \$ 9.58 | | |
| Granted | 153,868 | 5.89 | | |
| Exercised | (5,162) | 4.14 | | |
| Forfeited | (7,633) | 7.46 | | |
| Expired | (27,685) | 9.17 | | |
| Outstanding at September 30, 2011 | 1,066,057 | \$ 9.10 | 6.2 | \$ 14 |
| Options exercisable at September 30, 2011 | 292,183 | \$ 12.22 | 4.1 | \$ 14 |

The following table summarizes the information about stock options outstanding and exercisable as of September 30, 2011:

| Range of Exercise Prices | Options Outstanding | | | Options Exercisable | |
|--------------------------|---|---|--|---|--|
| | Outstanding at September 30, 2011 | Weighted Average Remaining Contractual Life in Years | Weighted Average Exercise Price | Exercisable at September 30, 2011 | Weighted Average Exercise Price |
| \$.01 to \$ 4.99 | 6,580 | 1.84 | \$ 2.90 | 6,580 | \$ 2.90 |
| \$ 5.00 to \$ 7.45 | 161,983 | 9.14 | 5.92 | 8,115 | 6.53 |
| \$ 7.46 to \$ 9.99 | 726,303 | 6.24 | 8.30 | 106,297 | 7.56 |
| \$ 10.00 to \$ 14.99 | 43,103 | 1.67 | 12.30 | 43,103 | 12.30 |
| \$ 15.00 to \$ 19.99 | 81,425 | 3.65 | 15.03 | 81,425 | 15.03 |
| \$ 20.00 to \$ 24.99 | 46,663 | 3.69 | 20.19 | 46,663 | 20.19 |
| | 1,066,057 | 6.16 | \$ 9.10 | 292,183 | \$ 12.22 |

Table of Contents**TREE.COM, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****NOTE 7 EARNINGS PER SHARE AND STOCK-BASED COMPENSATION (Continued)**

Nonvested RSUs and restricted stock outstanding as of September 30, 2011 and changes during the nine months ended September 30, 2011 were as follows:

| | RSUs | | Restricted Stock | |
|---------------------------------|------------------|--|------------------|--|
| | Number of Shares | Weighted Average Grant Date Fair Value | Number of Shares | Weighted Average Grant Date Fair Value |
| Nonvested at January 1, 2011 | 634,771 | \$ 7.53 | 412,500 | \$ 6.80 |
| Granted | 371,618 | 7.07 | 24,642 | 5.55 |
| Vested | (255,094) | 7.32 | (137,500) | 6.80 |
| Forfeited | (173,455) | 7.57 | | |
| Nonvested at September 30, 2011 | 577,840 | \$ 7.36 | 299,642 | \$ 6.70 |

NOTE 8 INCOME TAXES

For the three months ended September 30, 2011 and 2010, Tree.com recorded a tax provision (benefit) of \$(0.2) million and \$0.04 million, respectively, which represents an effective tax rate of 4.8% and (0.6)%, respectively. The tax rates are lower than the federal statutory rate of 35% primarily due to an increase in the valuation allowance on deferred tax assets.

For the nine months ended September 30, 2011 and 2010, Tree.com recorded a tax provision of \$0.1 million and \$0.9 million, respectively, which represents an effective tax rate of (0.4)% and (3.8)%, respectively. The tax rates are lower than the federal statutory rate of 35% primarily due to an increase in the valuation allowance on deferred tax assets.

Tree.com's unrecognized tax benefits decreased by approximately \$0.04 million for the three months ended September 30, 2011. The decrease was due to a partial release of the reserves for uncertain tax positions. Tree.com believes that it is reasonably possible that its remaining unrecognized tax benefits could decrease by approximately \$0.06 million within twelve months of the current reporting date due to the expiration of state statute of limitations. An estimate of other changes in unrecognized tax benefits cannot be made, but are not expected to be significant.

For the three and nine months ended September 30, 2011, Tree.com determined that its activity yielded an unusual effective tax rate; therefore, Tree.com utilized the actual year to date effective tax rate for purposes of determining year to date tax expense. This approach is consistent with the nine months ended September 30, 2010.

The North Carolina Department of Revenue ("NCDOR") has completed its audit of the Company's North Carolina corporate income and franchise tax returns for the years ended December 31, 2006 through 2008, and issued a notice of assessment to the Company in October 2011. The range of possible loss is estimated to be \$-0- to \$3.6 million. No reserve has been established for this matter as the Company has determined that the likelihood of a loss is not probable.

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 9 CONTINGENCIES

During the nine months ended September 30, 2011 and 2010, provisions for litigation settlements and contingencies of \$5.2 million and \$-0-, respectively, were recorded in litigation settlements and contingencies in the accompanying consolidated statements of operations. The litigation matters were either settled, or a firm offer for settlement was extended by the Company, thereby establishing an accrual amount that is both probable and reasonably estimable. The balance of the related liability was \$3.7 million and \$0.5 million at September 30, 2011 and December 31, 2010, respectively.

The Massachusetts Division of Banks (the "Division") delivered to LendingTree, LLC on February 11, 2011 a Report of Examination/Inspection which identified various alleged violations of Massachusetts and federal laws, including the alleged insufficient delivery by LendingTree, LLC of various disclosures to its customers. On October 14, 2011, the Division provided a proposed Consent Agreement and Order to settle the Division's allegations, which the Division had shared with other state mortgage lending regulators. Twenty-four of such state mortgage lending regulators (the "Joining Regulators") indicated that if LendingTree, LLC would enter into the Consent Agreement and Order, they would agree not to pursue any analogous allegations that they otherwise might assert. As of the date of this report, none of the Joining Regulators have asserted any such allegations.

The proposed Consent Agreement and Order calls for a fine to be allocated among the Division and the Joining Regulators and for LendingTree, LLC to adopt various new procedures and practices. We intend to commence negotiations toward an acceptable Consent Agreement and Order. We do not believe our LendingTree Exchange violates any federal or state mortgage lending laws; nor do we believe that any past operations of the LendingTree Exchange have resulted in a material violation of any such laws. Should the Division or any Joining Regulator bring any actions relating to the matters alleged in the February 2011 Report of Examination/Inspection, we intend to defend such actions vigorously. The range of possible loss is not estimable at this time, and no reserve has been established for this matter as the Company has determined that the likelihood of a loss is not probable.

In the ordinary course of business, Tree.com is a party to various lawsuits. Tree.com establishes reserves for specific legal matters when it determines that the likelihood of an unfavorable outcome is probable and the loss is reasonably estimable. Management has also identified certain other legal matters for which it believes an unfavorable outcome is not probable and, therefore, no reserve is established. If no reserve is established but the loss contingency is reasonably possible, we disclose the nature of the contingency and the related estimate of possible loss or range of loss if such an estimate can be made. Although management currently believes that an unfavorable resolution of claims against Tree.com, including claims where an unfavorable outcome is reasonably possible, will not have a material impact on the liquidity, results of operations, or financial condition of Tree.com, these matters are subject to inherent uncertainties and management's view of these matters may change in the future. It is possible that an unfavorable outcome of one or more of these lawsuits could have a material impact on the liquidity, results of operations, or financial condition of Tree.com. Tree.com also evaluates other contingent matters, including tax contingencies, to assess the probability and estimated extent of potential loss.

NOTE 10 RESTRUCTURING EXPENSE

Restructuring expense in 2011 primarily relates to severance costs for headcount reductions in the corporate infrastructure departments. Restructuring expense in 2010 primarily relates to continuing lease obligations on facilities previously used for call center operations, for which management had a

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TREE.COM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NOTE 10 RESTRUCTURING EXPENSE (Continued)

plan to exit at December 31, 2009, but the cease-use date did not occur until January 2010. Costs that relate to ongoing operations are not part of restructuring expense. Restructuring expense by type are as follows (in thousands):

| | For The Three Months Ended September 30, 2011 | | | |
|-----------------------|--|------------------------------------|---------------------|--------|
| | Employee Termination Costs | Continuing Lease Obligations | Asset Write-offs | Total |
| Restructuring expense | \$ 396 | \$ 86 | \$ 16 | \$ 498 |

| | For The Three Months Ended September 30, 2010 | | | |
|-----------------------|--|------------------------------------|---------------------|-------|
| | Employee Termination Costs | Continuing Lease Obligations | Asset Write-offs | Total |
| Restructuring expense | \$ 46 | \$ | \$ | \$ 46 |

| | For The Nine Months Ended September 30, 2011 | | | |
|-----------------------|---|------------------------------------|---------------------|--------|
| | Employee Termination Costs | Continuing Lease Obligations | Asset Write-offs | Total |
| Restructuring expense | \$ 888 | \$ 86 | \$ 16 | \$ 990 |

| | For The Nine Months Ended September 30, 2010 | | | |
|-----------------------|---|------------------------------------|---------------------|----------|
| | Employee Termination Costs | Continuing Lease Obligations | Asset Write-offs | Total |
| Restructuring expense | \$ 162 | \$ 2,463 | \$ 93 | \$ 2,718 |

Restructuring expense and payments against liabilities are as follows (in thousands):

| | For The Nine Months Ended September 30, 2011 | | | |
|------------------------------|---|------------------------------------|---------------------|----------|
| | Employee Termination Costs | Continuing Lease Obligations | Asset Write-offs | Total |
| Balance, beginning of period | \$ 19 | \$ 2,339 | \$ | \$ 2,358 |
| Restructuring expense | 888 | 86 | 16 | 990 |
| Payments | (663) | (925) | | (1,588) |
| Write-offs | | 22 | (16) | 6 |
| Balance, end of period | \$ 244 | \$ 1,522 | \$ | \$ 1,766 |

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At September 30, 2011, restructuring liabilities of \$0.7 million are included in accrued expenses and other current liabilities and \$1.0 million are included in other long-term liabilities in the accompanying consolidated balance sheet. At December 31, 2010, restructuring liabilities of \$1.2 million are included in accrued expenses and other current liabilities and \$1.2 million are included in other long-term liabilities in the accompanying consolidated balance sheet. Tree.com does not expect to incur significant additional costs related to the restructurings noted above.

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

Cautionary Statement Regarding Forward-Looking Information

This quarterly report on Form 10-Q contains "forward-looking statements" within the meaning of the Securities Act of 1933 and the Securities Exchange Act of 1934, as amended by the Private Securities Litigation Reform Act of 1995. These forward-looking statements also include statements related to our anticipated financial performance, business prospects and strategy; anticipated trends and prospects in the various industries in which our businesses operate; new products, services and related strategies; and other similar matters. These forward looking statements are based on management's current expectations and assumptions about future events, which are inherently subject to uncertainties, risks and changes in circumstances that are difficult to predict. The use of words such as "anticipates," "estimates," "expects," "projects," "intends," "plans" and "believes," among others, generally identify forward-looking statements.

Actual results could differ materially from those contained in the forward-looking statements. Factors currently known to management that could cause actual results to differ materially from those in forward-looking statements include those matters discussed in Part II, Item 1A Risk Factors.

Other unknown or unpredictable factors that could also adversely affect our business, financial condition and results of operations may arise from time to time. In light of these risks and uncertainties, the forward-looking statements discussed in this report may not prove to be accurate. Accordingly, you should not place undue reliance on these forward-looking statements, which only reflect the views of Tree.com management as of the date of this report. We undertake no obligation to update or revise forward-looking statements to reflect changed assumptions, the occurrence of unanticipated events or changes to future operating results or expectations, except as required by law.

Management Overview

Tree.com is the parent of LendingTree, LLC which owns several brands and businesses that provide information, tools, advice, products and services for critical transactions in our customers' lives. Our family of brands includes: LendingTree.com®, GetSmart.com®, DegreeTree.comSM, HealthTree.comSM, LendingTreeAutos.com, DoneRight.com®, and InsuranceTree.comSM. Together, these brands serve as an ally for consumers who are looking to comparison shop for loans and other services from multiple businesses and professionals that will compete for their business.

Through the quarter ended March 31, 2011, we operated in two reportable business segments: LendingTree Loans and Exchanges. The LendingTree Loans segment originates, processes, approves and funds various residential real estate loans through Home Loan Center, Inc. dba LendingTree Loans ("HLC"). The HLC and LendingTree Loans brand names are collectively referred to in these consolidated financial statements as "LendingTree Loans." The Exchanges segment consists of online lead generation networks and call centers that connect consumers and service providers principally in the lending, higher education, home services, insurance and automobile marketplaces.

In connection with entering into an agreement in the second quarter of 2011 that provides for the sale of substantially all of the operating assets of our LendingTree Loans segment to Discover Bank that is discussed below and in Notes 1 and 6 to the consolidated financial statements, the Company re-evaluated its reporting segments based on the continuing operations of the Company. We have determined that our continuing operations are now one reportable segment, which represents the previous "Exchanges" segment.

Additionally, on March 10, 2011, management of the Company made the decision and finalized a plan to close all of the field offices of the proprietary full service real estate brokerage business known as RealEstate.com, REALTORS®. The Company exited all markets by March 31, 2011.

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Finally, in September 2011, the Company sold the remaining assets of RealEstate.com, which consisted primarily of internet domain names and trademarks, for \$8.3 million and recognized a gain on sale of \$7.8 million.

The businesses of RealEstate.com and RealEstate.com, REALTORS® (which together represent the former Real Estate segment) and LendingTree Loans are presented as discontinued operations in the accompanying consolidated financial statements for all periods presented. The following discussion, unless otherwise noted, excludes information related to the discontinued operations.

From time to time, we may evaluate the potential acquisition of various assets and other businesses that may complement our current services, enhance our capabilities, improve or sustain our competitive position, or otherwise offer growth opportunities. From time to time, we may also consider the potential disposition of certain of our assets, subsidiaries or lines of businesses. We typically publicly announce any material acquisitions or dispositions when a definitive agreement has been reached.

Recent Mortgage Interest Rate Trends

Interest rate and market risk can be substantial in the mortgage lead generation business. Fluctuations in interest rates drive consumer demand for new mortgages and the level of refinancing activity, which in turn affects lender demand for mortgage leads. Typically, a decline in mortgage interest rates will lead to reduced lender demand for leads, as there are more consumers in the marketplace and lenders receive more organic lead volume. Conversely, an increase in mortgage interest rates will lead to an increase in lender demand for leads, as there are fewer consumers in the marketplace and the overall supply of mortgage leads decreases.

Average 30-year fixed mortgage rates hit a low of 4.2% in November 2010, but swiftly increased to 5.0% by year-end. Consequently, the number of mortgage leads dropped off significantly at the end of 2010 and in the first quarter of 2011. Mortgage rates then declined in the second and third quarters of 2011 to below 4.0%, which resulted in an increase in the number of mortgage leads generated in the second and third quarters.

Real Estate Market

The operations, cash flows and financial position of the Company were negatively impacted by the continued deterioration in the housing market in 2010 and early 2011. In particular, revenue has been negatively impacted by falling home prices and increased foreclosures. While nationwide sales of existing homes have risen in recent months, most of the increase is due to a rise in foreclosure sales and distressed transactions. Overall home prices continued to decline during 2011 and most economic forecasts indicate that conditions are unlikely to improve significantly in 2012. Falling home prices also make it more difficult to make accurate home value appraisals and lenders typically require higher down payments and higher credit scores, which could further restrict the pool of prospective homebuyers.

Expenses

The Company has focused on expense savings and is taking various initiatives to reduce costs. During the first quarter of 2011, the Company commenced a voluntary severance plan for certain corporate employees. In addition, the Company has taken steps to minimize ineffective marketing costs and dynamically align marketing expenses with lender demand for leads.

Discover Asset Sale

On May 12, 2011, the Company entered into an Asset Purchase Agreement (the "APA") with Discover Bank, a wholly-owned subsidiary of Discover Financial Services. The APA provides for the

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sale of substantially all of the operating assets of HLC to Discover Bank. Under the terms of the APA, Discover Bank will pay approximately \$55.9 million in cash for the assets, subject to certain adjustments as described in the APA. \$35.9 million is due upon the closing of the transaction and \$10 million is due on each of the first and second anniversaries of the closing, subject to certain conditions as described in the APA. Discover Bank generally will not assume liabilities of the LendingTree Loans business that arose before the closing date. A portion of the initial purchase price payment will be held in escrow for certain liabilities that will remain with the Company. The transaction is subject to various closing conditions, including regulatory approvals for Discover Bank. Subject to certain exceptions stated in the APA, the Company has agreed to operate the LendingTree Loans business in the ordinary course until the closing of the acquisition.

On November 7, 2011, Discover Bank elected to extend the end date upon which either party could terminate the Asset Purchase Agreement by 30 days to December 8, 2011, and paid the required extension payment of \$1.0 million to the Company's HLC, Inc. subsidiary. Discover Bank is permitted up to three additional 30-day extensions in certain circumstances. Discover Bank must pay a \$1.0 million extension fee to HLC, Inc. to exercise each of the second and third extensions and a \$2.0 million extension to exercise the fourth extension. All extension payments, including the one received in November, will be credited against the purchase price due at closing. For a more complete discussion of the closing conditions, end date extension rights and associated fees, termination fees and other provisions of the Asset Purchase Agreement, please see the Company's definitive proxy statement filed with the Securities and Exchange Commission on August 2, 2011.

Results of operations for the three and nine months ended September 30, 2011 compared to the three and nine months ended September 30, 2010:

Revenue

For the three months ended September 30, 2011 compared to the three months ended September 30, 2010:

| | Three Months Ended September 30, | | | |
|------------------|----------------------------------|------------|----------|-----------|
| | 2011 | \$ Change | % Change | 2010 |
| | (Dollars in thousands) | | | |
| Match fees | \$ 12,383 | \$ (475) | (4)% | \$ 12,858 |
| Closed loan fees | 381 | (1,275) | (77)% | 1,656 |
| Other | 337 | (353) | (51)% | 690 |
| Total revenue | \$ 13,101 | \$ (2,103) | (14)% | \$ 15,204 |

Match fee revenue in 2011 decreased slightly from the same period in 2010. Overall matched requests decreased by 2%, from 282,000 in 2010 to 277,000 in 2011. This reflects an increase of 13% in home loan matches and an aggregate decline of 12% in matches for the new consumer vertical areas of higher education, home services, insurance and automobile. As compared to 2010, the average fee for home loan matches declined by 24%, while the average match fee for the new consumer verticals increased by 49%. The decline in home loan average match fee is due to a product shift toward purchase mortgage, which generates lower revenue per matched lead than refinance. Purchase as a percentage of total mortgage matches increased from 41% in the third quarter of 2010 to 45% in the third quarter of 2011. Additionally, revenue from closed loan fees decreased due to a previously announced shift in pricing on home loan related matches to increase the average match fee while eliminating the closed loan fee.

No single network lender accounts for revenue representing more than 10% of Tree.com's consolidated revenue for any periods presented.

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For the nine months ended September 30, 2011 compared to the nine months ended September 30, 2010:

| Nine Months Ended September 30, | | | | |
|--|---------------|------------------|-----------------|---------------|
| | 2011 | \$ Change | % Change | 2010 |
| (Dollars in thousands) | | | | |
| Match fees | \$ 41,045 | \$ 2,362 | 6% | \$ 38,683 |
| Closed loan fees | 1,770 | (5,238) | (75)% | 7,008 |
| Other | 1,136 | (1,186) | (51)% | 2,322 |
| Total revenue | \$ 43,951 | \$ (4,062) | (8)% | \$ 48,013 |

Match fee revenue in 2011 increased from the same period in 2010. Overall matched requests decreased by 4%, from 601,000 in 2010 to 579,000 in 2011. This reflects a decrease of 5% in home loan matches and an aggregate decline of 3% in matches for the new consumer vertical areas of higher education, home services, insurance and automobile. As compared to 2010, the average fee for home loan matches increased by 4%, while the average match fee for the new consumer verticals increased by 31%. Additionally, revenue from match fees increased and closed loan fees decreased due to a previously announced shift in pricing on home loan related matches to increase the average match fee while eliminating the closed loan fee.

We do not presently record revenue in our Exchanges business for leads provided to Home Loan Center. Instead, we use a cost sharing approach for marketing expenses, whereby the Exchange business and Home Loan Center share the marketing expense on a pro rata basis, based on the quantity of leads received by each. Following completion of the sale to Discover Bank, Discover Bank will pay us for leads generated by the LendingTree Exchange, and that will represent an additional source of revenue, with an associated increase in selling and marketing expenses. We expect revenue from Discover Bank to be accretive to both gross and net margin.

Cost of revenue

For the three months ended September 30, 2011 compared to the three months ended September 30, 2010:

| Three Months Ended September 30, | | | | |
|---|-------------|------------------|-----------------|-------------|
| | 2011 | \$ Change | % Change | 2010 |
| (Dollars in thousands) | | | | |
| Cost of revenue | \$ 1,001 | \$ (345) | (26)% | \$ 1,346 |
| As a percentage of total revenue | 8% | | | 9% |

Cost of revenue consists primarily of costs associated with compensation and other employee related costs (including stock-based compensation) related to customer call centers, credit scoring fees, consumer incentive costs, and website network hosting and server fees.

Cost of revenue in 2011 decreased from the same period in 2010 primarily due to decreases of \$0.1 million in compensation and other employee related costs and \$0.1 million in licensing costs.

For the nine months ended September 30, 2011 compared to the nine months ended September 30, 2010:

| Nine Months Ended September 30, | | | | |
|--|-------------|------------------|-----------------|-------------|
| | 2011 | \$ Change | % Change | 2010 |
| (Dollars in thousands) | | | | |
| Cost of revenue | \$ 3,529 | \$ (125) | (3)% | \$ 3,654 |
| As a percentage of total revenue | 8% | | | 8% |

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Cost of revenue in 2011 decreased slightly from the same period in 2010 primarily due to a decrease of \$0.4 million in compensation and other employee related costs, offset by increases of \$0.3 million in credit scoring fees and licensing costs.

Selling and marketing expense

For the three months ended September 30, 2011 compared to the three months ended September 30, 2010:

| | Three Months Ended September 30, | | | |
|----------------------------------|---|------------------|-----------------|-------------|
| | 2011 | \$ Change | % Change | 2010 |
| | (Dollars in thousands) | | | |
| Selling and marketing expense | \$ 8,475 | \$ (4,469) | (35)% | \$ 12,944 |
| As a percentage of total revenue | 65% | | | 85% |

Selling and marketing expense consists primarily of advertising and promotional expenditures, fees paid to lead sources and compensation and other employee related costs (including stock-based compensation) for personnel engaged in the sales function. Advertising and promotional expenditures primarily include online marketing, as well as television, print and radio spending. Advertising production costs are expensed in the period the related ad is first run.

Advertising expense is the largest component of selling and marketing expense and is comprised of the following:

| | Three Months Ended September 30, | | | |
|---------------------------|---|------------------|-----------------|-------------|
| | 2011 | \$ Change | % Change | 2010 |
| | (Dollars in thousands) | | | |
| Online | \$ 4,085 | \$ (3,825) | (48)% | \$ 7,910 |
| Broadcast | 2,520 | (270) | (10)% | 2,790 |
| Other | 493 | (949) | (66)% | 1,442 |
| Total advertising expense | \$ 7,098 | \$ (5,044) | (42)% | \$ 12,142 |

The Company decreased advertising expense in 2011 in response to interest rates that began declining in the second quarter of 2011. In a declining interest rate environment, the incentive for consumers to come into the market to refinance is much higher, resulting in higher levels of organic traffic to both the Company and for lenders and less demand for externally-generated leads. The Company reduced advertising expense by 42%, while matched requests decreased only 2%. The decrease in other advertising above is primarily due to launching a new television campaign in 2010 that was not repeated in 2011.

Tree.com anticipates that it will continue to adjust selling and marketing expenditures dynamically in relation to revenue producing opportunities and that selling and marketing will continue to represent a high percentage of revenue as it continues to promote its brands both online and offline.

For the nine months ended September 30, 2011 compared to the nine months ended September 30, 2010:

| | Nine Months Ended September 30, | | | |
|----------------------------------|--|------------------|-----------------|-------------|
| | 2011 | \$ Change | % Change | 2010 |
| | (Dollars in thousands) | | | |
| Selling and marketing expense | \$ 39,246 | \$ 345 | 1% | \$ 38,901 |
| As a percentage of total revenue | 89% | | | 81% |

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Advertising expense is the largest component of selling and marketing expense and is comprised of the following:

| Nine Months Ended September 30, | | | | |
|---------------------------------|-----------|------------|----------|-----------|
| | 2011 | \$ Change | % Change | 2010 |
| (Dollars in thousands) | | | | |
| Online | \$ 19,517 | \$ (4,401) | (18)% | \$ 23,918 |
| Broadcast | 11,189 | 2,397 | 27% | 8,792 |
| Other | 4,143 | 540 | 15% | 3,603 |
| Total advertising expense | \$ 34,849 | \$ (1,464) | (4)% | \$ 36,313 |

The Company decreased advertising expense in 2011 in response to interest rates that began declining in the second quarter of 2011. In a declining interest rate environment, the incentive for consumers to come into the market to refinance is much higher, resulting in higher levels of organic traffic to both the Company and for lenders and less demand for externally-generated leads. Additionally, improvements in marketing efficiencies across several of our marketing channels eliminated approximately \$3 million of expense that was incurred in the second quarter of 2011 from future quarters.

The 4% decrease in total advertising expense corresponded to 4% fewer matched requests, and advertising expense increasing to 89% of revenue compared to 81% for the same period in 2010. The increase in other advertising is primarily due to an increase in direct mail campaigns in 2011. The increase in 2011 also reflects non-variable expense associated with expanding the marketing team and investing in marketing tools and technologies that began in the first quarter.

General and administrative expense

For the three months ended September 30, 2011 compared to the three months ended September 30, 2010:

| Three Months Ended September 30, | | | | |
|------------------------------------|----------|------------|----------|----------|
| | 2011 | \$ Change | % Change | 2010 |
| (Dollars in thousands) | | | | |
| General and administrative expense | \$ 4,388 | \$ (1,907) | (30)% | \$ 6,295 |
| As a percentage of total revenue | 33% | | | 41% |

General and administrative expense consists primarily of compensation and other employee related costs (including stock-based compensation) for personnel engaged in finance, legal, tax, corporate information technology, human resources and executive management functions, as well as facilities and infrastructure costs and fees for professional services.

General and administrative expense in 2011 decreased compared to the same period for 2010, primarily reflecting a \$2.5 million decrease in compensation and other employee-related costs (excluding non-cash compensation) due to lower headcount and incentive compensation. Professional fees and software costs also decreased by \$0.6 million and \$0.3 million, respectively. Also impacting the 2010 general and administrative expenses was a \$0.8 million reduction of expense related to post acquisition adjustments, which was a result of the change in fair value of the estimated contingent consideration to be paid for business acquisitions that were completed in 2009. These adjustments are shown as a reduction of expense within general and administrative expense, and are excluded from our definition of Adjusted EBITDA. We expect further cost savings in future quarters related to the realignment of costs as we sharpen our focus on fewer verticals.

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For the nine months ended September 30, 2011 compared to the nine months ended September 30, 2010:

| | Nine Months Ended September 30, | | | |
|------------------------------------|---------------------------------|------------|----------|-----------|
| | 2011 | \$ Change | % Change | 2010 |
| | (Dollars in thousands) | | | |
| General and administrative expense | \$ 15,059 | \$ (3,607) | (19)% | \$ 18,666 |
| As a percentage of total revenue | 34% | | | 39% |

General and administrative expense in 2011 decreased from the same period in 2010 primarily due to a \$3.4 million decrease in compensation and other employee related costs (excluding non-cash compensation) due to lower headcount and incentive compensation. Professional fees and software costs also each decreased by \$0.7 million. Also impacting the general and administrative expenses was a \$0.7 million reduction of expense in 2011 and a \$0.8 million reduction of expense in 2010 related to the post acquisition adjustments discussed above.

Product development

For the three months ended September 30, 2011 compared to the three months ended September 30, 2010:

| | Three Months Ended September 30, | | | |
|----------------------------------|----------------------------------|-----------|----------|--------|
| | 2011 | \$ Change | % Change | 2010 |
| | (Dollars in thousands) | | | |
| Product development | \$ 681 | \$ (124) | (15)% | \$ 805 |
| As a percentage of total revenue | 5% | | | 5% |

Product development expense consists primarily of compensation and other employee related costs (including stock-based compensation) for personnel engaged in the design, development, testing and enhancement of technology that are not capitalized.

Product development expense in 2011 decreased from the same period in 2010 due to reduced headcount and contractor costs.

For the nine months ended September 30, 2011 compared to the nine months ended September 30, 2010:

| | Nine Months Ended September 30, | | | |
|----------------------------------|---------------------------------|-----------|----------|----------|
| | 2011 | \$ Change | % Change | 2010 |
| | (Dollars in thousands) | | | |
| Product development | \$ 2,677 | \$ 123 | 5% | \$ 2,554 |
| As a percentage of total revenue | 6% | | | 5% |

Product development expense in 2011 increased slightly from 2010 due to increased contractor costs.

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For the three months ended September 30, 2011 compared to the three months ended September 30, 2010:

| | Three Months Ended September 30, | | | |
|----------------------------------|----------------------------------|-----------|----------|------------|
| | 2011 | \$ Change | % Change | 2010 |
| | (Dollars in thousands) | | | |
| Operating loss | \$ (3,760) | \$ 3,676 | 49% | \$ (7,436) |
| As a percentage of total revenue | (29)% | | | (49)% |

Operating loss in 2011 decreased from the same period in 2010 primarily due to the decreases in selling and marketing expense and general and administrative expense, offset by the decrease in revenue, discussed above.

For the nine months ended September 30, 2011 compared to the nine months ended September 30, 2010:

| | Nine Months Ended September 30, | | | |
|----------------------------------|---------------------------------|------------|----------|-------------|
| | 2011 | \$ Change | % Change | 2010 |
| | (Dollars in thousands) | | | |
| Operating loss | \$ (27,470) | \$ (5,669) | (26)% | \$ (21,801) |
| As a percentage of total revenue | (63)% | | | (45)% |

Operating loss in 2011 increased from the same period in 2010 primarily due to \$5.2 million in litigation settlements and contingency expense recorded in 2011.

Adjusted Earnings Before Interest, Taxes, Depreciation and Amortization

Adjusted Earnings Before Interest, Taxes, Depreciation and Amortization ("Adjusted EBITDA") is a non-GAAP measure and is defined in "Tree.com's Principles of Financial Reporting". Below is a

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reconciliation of operating loss to EBITDA from continuing operations and Adjusted EBITDA from continuing operations, and operating loss to net income (loss).

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--|-------------------------------------|------------|------------------------------------|-------------|
| | 2011 | 2010 | 2011 | 2010 |
| | (Dollars in thousands) | | | |
| Operating loss | \$ (3,760) | \$ (7,436) | \$ (27,470) | \$ (21,801) |
| Adjustments to reconcile to EBITDA and Adjusted EBITDA: | | | | |
| Amortization of intangibles | 213 | 307 | 787 | 922 |
| Depreciation | 1,393 | 823 | 3,677 | 2,297 |
| EBITDA from continuing operations | (2,154) | (6,306) | (23,006) | (18,582) |
| Restructuring expense | 498 | 46 | 990 | 2,718 |
| Asset impairments | | | 250 | |
| Loss on disposal of assets | 99 | | 211 | 3 |
| Non-cash compensation | 824 | 656 | 2,731 | 2,423 |
| Litigation settlements and contingencies | 212 | 74 | 5,206 | 102 |
| Post acquisition adjustments | | (849) | (652) | (849) |
| Adjusted EBITDA from continuing operations | \$ (521) | \$ (6,379) | \$ (14,270) | \$ (14,185) |
| Reconciliation to net loss: | | | | |
| Operating loss per above | \$ (3,760) | \$ (7,436) | \$ (27,470) | \$ (21,801) |
| Other expense, net | (110) | (60) | (266) | (385) |
| Loss before income taxes | (3,870) | (7,496) | (27,736) | (22,186) |
| Income tax provision | 185 | (42) | (117) | (850) |
| Net loss from continuing operations | (3,685) | (7,538) | (27,853) | (23,036) |
| Income (loss) from discontinued operations, net of tax | 16,283 | 9,357 | (16,863) | 17,910 |
| Net income (loss) | \$ 12,598 | \$ 1,819 | \$ (44,716) | \$ (5,126) |

For the three months ended September 30, 2011 compared to the three months ended September 30, 2010:

| | Three Months Ended September 30, | | | 2010 |
|--|----------------------------------|-----------|----------|------------|
| | 2011 | \$ Change | % Change | |
| | (Dollars in thousands) | | | |
| Adjusted EBITDA from continuing operations | \$ (521) | \$ 5,858 | 92% | \$ (6,379) |
| As a percentage of total revenue | | (4)% | | (42)% |

Adjusted EBITDA from continuing operations in 2011 increased from the same period in 2010, reflecting the decreased selling and marketing expenses and general and administrative expenses as described above, to better align our costs with revenue.

For the nine months ended September 30, 2011 compared to the nine months ended September 30, 2010:

| | Nine Months Ended September 30, | | | 2010 |
|--|---------------------------------|-----------|----------|-------------|
| | 2011 | \$ Change | % Change | |
| | (Dollars in thousands) | | | |
| Adjusted EBITDA from continuing operations | \$ (14,270) | \$ (85) | (1)% | \$ (14,185) |
| As a percentage of total revenue | | (32)% | | (30)% |

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Adjusted EBITDA from continuing operations in 2011 was flat compared to the same period in 2010, reflecting a decrease in revenue for the first quarter of 2011 and a decrease in general and administrative expense as described above, to better align our costs with revenue.

Income tax provision

For the three months ended September 30, 2011 and 2010, Tree.com recorded a tax provision (benefit) of \$(0.2) million and \$0.04 million, respectively, which represents an effective tax rate of 4.8% and (0.6)%, respectively. The tax rates are lower than the federal statutory rate of 35% primarily due to an increase in the valuation allowance on deferred tax assets.

For the nine months ended September 30, 2011 and 2010, Tree.com recorded a tax provision of \$0.1 million and \$0.9 million, respectively, which represents an effective tax rate of (0.4)% and (3.8)%, respectively. The tax rates are lower than the federal statutory rate of 35% primarily due to an increase in the valuation allowance on deferred tax assets.

Tree.com's unrecognized tax benefits decreased by approximately \$0.04 million for the three months ended September 30, 2011. The decrease was due to a partial release of the reserves for uncertain tax positions. Tree.com believes that it is reasonably possible that its remaining unrecognized tax benefits could decrease by approximately \$0.06 million within twelve months of the current reporting date due to the expiration of state statute of limitations. An estimate of other changes in unrecognized tax benefits cannot be made, but are not expected to be significant.

For the three and nine months ended September 30, 2011, Tree.com determined that its activity yielded an unusual effective tax rate; therefore, Tree.com utilized the actual year to date effective tax rate for purposes of determining year to date tax expense. This approach is consistent with the nine months ended September 30, 2010.

Discontinued Operations

Revenue from discontinued operations in the third quarter of 2011 was \$37.6 million, a decrease of 1% as compared to the third quarter 2010 revenue from discontinued operations of \$38.0 million. LendingTree Loans revenue was up \$2.3 million compared to the third quarter of 2010 on 4% more closed units, and revenue from the Real Estate business was down \$2.7 million compared to the third quarter of 2010, reflecting the shutdown of the company-owned brokerage in early 2011.

LendingTree Loans benefited from lower marketing expenses as a result of lower interest rates and improved marketing efficiencies. Although LendingTree Loans produced higher revenue in 2011 compared to the same period in 2010, gross margins were flat due to loan officer compensation regulations that drove a \$2.3 million increase in variable compensation costs. Loan officer compensation increased from 20% of total revenue at LendingTree Loans in the third quarter of 2010 to 25% of total revenue in the third quarter of 2011. In addition, general and administrative costs in discontinued operations in the third quarter of 2011 were \$1.2 million, or 16% higher than the third quarter of 2010. This increase was driven largely by the acquisition of certain assets of First Residential Mortgage Network, Inc. dba SurePoint Lending that was completed in the first quarter of 2011, and partially offset by lower Real Estate fixed costs after the shutdown of the company-owned brokerage in early 2011.

FINANCIAL POSITION, LIQUIDITY AND CAPITAL RESOURCES

As of September 30, 2011, Tree.com had \$10.3 million of cash and cash equivalents and \$13.0 million of restricted cash and cash equivalents, compared to \$68.8 million of cash and cash equivalents and \$8.2 million of restricted cash and cash equivalents as of December 31, 2010. During the third quarter LendingTree Loans utilized an additional \$30 million of unrestricted cash for funding

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loans at LendingTree Loans. These loans were sold in October 2011, and the proceeds were returned to LendingTree Loans as unrestricted cash. LendingTree Loans elected to fund loans with its own cash in order to take advantage of the positive refinance market conditions as it reached borrowing capacity on its warehouse lines. LendingTree Loans has now increased its warehouse lines as discussed below.

Cash Flows from Continuing Operations

Net cash used in operating activities was \$20.9 million in the nine months ended September 30, 2011, compared to \$30.1 million used in operating activities in the same period in 2010. The change from cash used in operating activities in 2010 to cash used by operating activities in 2011 was primarily due to a \$4.8 million increase in the net loss from continuing operations, offset by a \$16.0 million increase in accounts payable and other current liabilities, which principally related to litigation payments of \$12.8 million that were made in the nine months ended September 30, 2010 and managing working capital more closely in 2011.

Net cash used in investing activities in the nine months ended September 30, 2011 of \$7.0 million primarily resulted from capital expenditures of \$5.5 million. Net cash used in investing activities in the nine months ended September 30, 2010 of \$1.6 million primarily resulted from capital expenditures of \$3.7 million, offset by the release of restricted cash of \$2.2 million.

Net cash used in financing activities in the nine months ended September 30, 2011 of \$4.3 million was primarily due to increased restricted cash requirements and the vesting of stock to employees (less withholding taxes). Net cash used by financing activities in the nine months ended September 30, 2010 of \$5.1 million was primarily due to purchases of treasury stock of \$4.7 million.

Warehouse Lines of Credit for LendingTree Loans

As of September 30, 2011, LendingTree Loans had two committed lines of credit totaling \$150.0 million of borrowing capacity. LendingTree Loans also had a \$25.0 million uncommitted line with one of these lenders, which was terminated on October 31, 2011. In addition, LendingTree Loans obtained a third warehouse line for \$100.0 million on October 13, 2011 and increased the second line to \$125.0 million on October 28, 2011, bringing the total borrowing capacity to \$275.0 million. Borrowings under these lines of credit are used to fund, and are secured by, consumer residential loans that are held for sale. Loans under these lines of credit are repaid using proceeds from the sales of loans by LendingTree Loans.

The \$50.0 million first line is scheduled to expire on the earliest of (i) the closing date of the proposed asset sale transaction with Discover Bank or (ii) January 30, 2012. On November 1, 2011, the terms of this line were amended so that it can be cancelled at the option of the lender at any time upon notice. This first line included an additional uncommitted credit facility of \$25.0 million, which was terminated on October 31, 2011. This first line is guaranteed by Tree.com, Inc., LendingTree, LLC and LendingTree Holdings Corp. The interest rate under the first line is the 30-day London InterBank Offered Rate ("LIBOR") or 2.00% (whichever is greater) plus 2.25%. The interest rate under the \$25.0 million uncommitted line was the 30-day LIBOR plus 1.50%.

The \$100.0 million second line was scheduled to expire on October 28, 2011, but subsequent to September 30, 2011 the line was increased to \$125.0 million and the expiration date extended to the earliest of (i) forty-five days after the closing date of the proposed asset sale transaction with Discover Bank or (ii) April 25, 2012. This line is also guaranteed by Tree.com, Inc., LendingTree, LLC and LendingTree Holdings Corp. Before the extension, the interest rate under this line was the 30-day Adjusted LIBOR or 2.0% (whichever was greater) plus 2.25% to 2.5% for loans being sold to the lender and 30-day Adjusted LIBOR or 2.0% (whichever was greater) plus 2.25% for loans not being sold to the lender. Upon extension of this line, the interest rate was changed to the 30-day Adjusted LIBOR or 2.0% (whichever is greater) plus 1.5% to 1.75% for loans being sold to the lender and

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30-day Adjusted LIBOR or 2.0% (whichever is greater) plus 1.5% for loans not being sold to the lender.

The \$100.0 million third line is scheduled to expire on December 13, 2011. This line is guaranteed by Tree.com, Inc. and LendingTree, LLC. The interest rate under this line is 30-day LIBOR plus 3.25% (LIBOR may be adjusted upward for any increase in the reserve requirement of the lender as further described in the Master Repurchase Agreement).

Under the terms of these warehouse lines, LendingTree Loans is required to maintain various financial and other covenants. These financial covenants include, but are not limited to, maintaining (i) minimum tangible net worth of \$20.0 million, which was increased to \$25.0 million upon renewal of the first line in November and the second line in October 2011, (ii) minimum liquidity, (iii) a minimum current ratio, (iv) a maximum ratio of total liabilities to net worth, (v) a minimum unrestricted cash amount, (vi) pre-tax net income requirements and (vii) a maximum warehouse capacity ratio. During the quarter ended September 30, 2011, LendingTree Loans was in compliance with the covenants under these lines.

The LendingTree Loans business is highly dependent on the availability of these warehouse lines. Although we believe that our existing lines of credit are adequate for our current operations, reductions in our available credit, or the inability to renew or replace these lines, would have a material adverse effect on our business, financial condition and results of operations. Management has determined that it could continue to operate the LendingTree Loans business at a reduced capacity as long as one of the warehouse lines remains available. We believe that our sources of liquidity are sufficient to fund our operating needs, including operation of the LendingTree Loans business through a sale to Discover Bank, and including all debt requirements, commitments and contingencies, and capital and investing commitments for the foreseeable future. However, the operations of our LendingTree Loans business through completion of the transaction with Discover Bank have a significant impact on our liquidity, and the results of such operations are highly dependent on interest rates. If interest rates increase above current levels before completion of a transaction with Discover Bank, or if such transaction is not completed, we may need to take more aggressive actions to manage our working capital, sell certain assets or seek equity or debt financing. We cannot assure you that, in such a situation, we would be able to sell assets or raise equity or debt financing on terms acceptable to us, or at all. Moreover, the asset purchase agreement with Discover Bank contains certain covenants and conditions that may limit our ability to take certain of these actions without the consent of Discover Bank while the sale transaction is pending. Additionally, we anticipate that we will want to make capital and other expenditures in connection with the development and expansion of our overall operations. We intend to use proceeds from the sale of this LendingTree Loans business to fund these expenditures. If such proceeds are not sufficient after payments of transaction-related expenses and amounts held in escrow or otherwise restricted, we may seek equity or debt financing. We cannot assure you that such financing will be available on terms acceptable to us, or at all.

Upon closing of the sale of substantially all of the operating assets of our LendingTree Loans business to Discover Bank, LendingTree Loans will cease to originate consumer loans and will no longer have additional borrowings available under the warehouse lines of credit. The remaining operations will be wound down over the quarter following the closing of the transaction. These wind-down activities include selling the balance of loans held for sale to investors, which historically has occurred within thirty days of funding, and paying off and then terminating the lines of credit.

Seasonality

Revenue is subject to the cyclical and seasonal trends of the U.S. housing market. Home sales typically rise during the spring and summer months and decline during the fall and winter months. Refinancing and home equity activity is principally driven by mortgage interest rates as well as real

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estate values. The broader cyclical trends in the mortgage and real estate markets have upset the usual seasonal trends.

New Accounting Pronouncements

Refer to Note 2 to the consolidated financial statements for a description of recent accounting pronouncements.

TREE.COM'S PRINCIPLES OF FINANCIAL REPORTING

Tree.com reports Earnings Before Interest, Taxes, Depreciation and Amortization ("EBITDA"), and adjusted for certain items discussed below ("Adjusted EBITDA"), as supplemental measures to GAAP. These measures are two of the primary metrics by which Tree.com evaluates the performance of its businesses, on which its internal budgets are based and by which management is compensated. Tree.com believes that investors should have access to the same set of tools that it uses in analyzing its results. These non-GAAP measures should be considered in addition to results prepared in accordance with GAAP, but should not be considered a substitute for or superior to GAAP results. Tree.com provides and encourages investors to examine the reconciling adjustments between the GAAP and non-GAAP measure discussed below.

Definition of Tree.com's Non-GAAP Measures

Tree.com reports EBITDA as operating income or loss (which excludes interest expense and taxes) adjusted to exclude amortization of intangibles and depreciation.

Tree.com reports Adjusted EBITDA as EBITDA excluding (1) non-cash compensation expense, (2) non-cash intangible asset impairment charges, (3) gain/loss on disposal of assets, (4) restructuring expenses, (5) litigation settlements and contingencies, (6) pro forma adjustments for significant acquisitions or dispositions, and (7) one-time items. Adjusted EBITDA has certain limitations in that it does not take into account the impact to Tree.com's statement of operations of certain expenses, including depreciation, non-cash compensation and acquisition related accounting. Tree.com endeavors to compensate for the limitations of the non-GAAP measure presented by also providing the comparable GAAP measure with equal or greater prominence and descriptions of the reconciling items, including quantifying such items, to derive the non-GAAP measure.

Pro Forma Results

Tree.com will include Adjusted EBITDA pro forma adjustments for significant acquisitions and dispositions only if it views a particular transaction as significant in size or transformational in nature. For the periods presented in this report, there are no pro forma adjustments for significant acquisitions or dispositions included in EBITDA and Adjusted EBITDA.

One-Time Items

Adjusted EBITDA is adjusted for one-time items, if applicable. Items are considered one-time in nature if they are non-recurring, infrequent or unusual, and have not occurred in the past two years or are not expected to recur in the next two years, in accordance with SEC rules. For the periods presented in this report, there are no adjustments for one-time items.

Non-Cash Expenses That Are Excluded From Tree.com's Non-GAAP Measures

Non-cash compensation expense consists principally of expense associated with the grants of restricted stock units and stock options. These expenses are not paid in cash, and Tree.com will include the related shares in its calculations of fully diluted shares outstanding. Upon vesting of restricted stock

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units and the exercise of certain stock options, the awards will be settled, at Tree.com's discretion, on a net basis, with Tree.com remitting the required tax withholding amount from its current funds.

Amortization and impairment of intangibles are non-cash expenses relating primarily to acquisitions. At the time of an acquisition, the intangible assets of the acquired company, such as purchase agreements, technology and customer relationships, are valued and amortized over their estimated lives.

OTHER

REALTORS® a registered collective membership mark that identifies a real estate professional who is a member of the National Association of REALTORS® and subscribes to its strict Code of Ethics.

Item 3. *Quantitative and Qualitative Disclosures about Market Risk*

Under the rules and regulations of the SEC, as a smaller reporting company we are not required to provide the information required by this item.

Item 4. *Controls and Procedures*

Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this report, an evaluation of the effectiveness of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) was performed under the supervision and with the participation of the Company's management, including the principal executive officer and principal financial officer. Based on that evaluation, the Company's principal executive officer and principal financial officer have concluded that due to a material weakness in internal control over financial reporting related to income taxes as of December 31, 2010, as described in the Company's 2010 Form 10-K, the Company's disclosure controls and procedures are not effective as of September 30, 2011. The Company has taken appropriate actions in 2011 to address and remediate the deficiencies that gave rise to the material weakness, including evaluating our available resources to provide effective oversight of the work performed by our third party tax advisors and evaluating the resources provided by the third party tax advisors. However, the material weakness will not be fully remediated until, in the opinion of management, the revised control procedures have been operating for a sufficient period of time to provide reasonable assurances as to their effectiveness, and management does not believe that a sufficient period of time has passed to make this determination.

Changes in Internal Control Over Financial Reporting

Other than as noted above, there has been no change in the Company's internal controls over financial reporting during the third quarter of 2011 that has materially affected, or is reasonably likely to materially affect, the Company's internal controls over financial reporting.

Table of Contents**PART II****OTHER INFORMATION****Item 1. Legal Proceedings**

In the ordinary course of business, the Company and its subsidiaries are parties to litigation involving property, contract, intellectual property and other claims. We included a discussion of certain legal proceedings in Part I, Item 3, of our Annual Report on Form 10-K for the year ended December 31, 2010 (the "2010 Form 10-K") and an update in Part II, Item 1, of our Quarterly Reports on Form 10-Q for the quarters ended March 31, 2011 and June 30, 2011 ("1st and 2nd Quarter 2011 10-Qs"). During the quarter ended September 30, 2011, there were no material developments to the legal proceedings disclosed in the 2010 Form 10-K or 1st and 2nd Quarter 2011 10-Qs and no new material proceedings except as set forth below.

Mortgage Store, Inc. v. LendingTree Loans d/b/a Home Loan Center, Inc., No. 06CC00250 (Cal. Super. Ct., Orange Cty.). On November 30, 2006, The Mortgage Store, Inc. and Castlevue Home Loans, Inc. filed this putative class action against HLC in the California Superior Court for Orange County. Plaintiffs, two former Network Lenders, allege that HLC interfered with LendingTree's contracts with Network Lenders by taking referrals from LendingTree. The complaint is largely based upon the factual allegations made in the *Schnee* complaint (described in the 2nd Quarter 2011 10-Q). Based upon these factual allegations, Plaintiffs assert claims for intentional interference with contractual relations, intentional interference with prospective economic advantage, and violation of the California Unfair Competition Law ("UCL") and California Business and Professions Code § 17500. Plaintiffs purport to represent all Network Lenders from December 14, 2004 to date, and seek damages, restitution, attorneys' fees, and punitive damages.

Plaintiffs' motion for class certification was granted April 29, 2010. HLC's motion for summary judgment was filed April 12, 2011. On October 17, 2011 HLC's motion for summary judgment was granted.

Boschma v. Home Loan Center, Inc., No. SACV07-613 (U.S. Dist. Ct., C.D. Cal.). On May 25, 2007, Plaintiffs filed this putative class action against HLC in the U.S. District Court for the Central District of California. Plaintiffs allege that HLC sold them an option "ARM" (adjustable-rate mortgage) loan but failed to disclose in a clear and conspicuous manner, among other things, that the interest rate was not fixed, that negative amortization could occur and that the loan had a prepayment penalty. Based upon these factual allegations, Plaintiffs assert violations of the federal Truth in Lending Act (the "TILA"), violations of the UCL, breach of contract, and breach of the covenant of good faith and fair dealing. Plaintiffs purport to represent a class of all individuals who between June 1, 2003 and May 31, 2007 obtained through HLC an option ARM loan on their primary residence located in California, and seek rescission, damages, attorneys' fees and injunctive relief. Plaintiffs have not yet filed a motion for class certification. Plaintiffs have filed a total of eight complaints in connection with this lawsuit. Each of the first seven complaints has been dismissed by the federal and state courts. Plaintiffs filed the eighth complaint (a Second Amended Complaint) in Orange County (California) Superior Court on March 4, 2010 alleging only the fraud and UCL claims. As with each of the seven previous versions of Plaintiffs' complaint, the Second Amended Complaint was dismissed in April 2010. Plaintiffs appealed and filed their opening brief in November 2010. Company's responsive appellate brief was filed in February 2011. On August 10, 2011 the appellate court reversed the trial court's dismissal indicating that Plaintiffs' complaint was sufficient to withstand demur despite Plaintiffs' lack of damages. The case will be remanded to superior court. We believe plaintiff's allegations lack merit and we intend to defend against this action vigorously.

Gaines v. Home Loan Center, Inc., No. SACV08-667 (U.S. Dist. Ct., C.D. Cal.). On June 13, 2008, Plaintiffs filed this putative class action against HLC and LendingTree in the U.S. District Court for the

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Central District of California. Plaintiffs allege, in essence, that (1) HLC failed to disclose that the bundled amount for certain loan closing services (called the "TrueCost") that HLC charged to Plaintiffs was greater than HLC's actual costs for those services; (2) HLC's option ARM note failed to tell Plaintiffs that the stated interest rate and payment amounts would change after the first month and that the payment amount stated in the note was not sufficient to pay interest charges, resulting in negative amortization; and (3) HLC misrepresented that Plaintiffs would have to obtain a home equity line of credit in order to obtain a low interest rate on their option ARM loans. Based upon these factual allegations, Plaintiffs assert violations of the federal Racketeer Influenced and Corrupt Organizations Act ("RICO"), the TILA, the California UCL, California Business and Professions Code § 17500, the CLRA, breach of contract, breach of the implied covenant of good faith and fair dealing, unjust enrichment, conversion, and money had and received.

Plaintiffs purport to represent all HLC customers who, since December 14, 2004 (1) were charged by HLC and paid an amount that exceeded HLC's actual costs for those services; and/or (2) entered into option ARM loan agreements with HLC; and/or (3) were misled into taking out a home equity line of credit along with their option ARM mortgage. Plaintiffs seek restitution, disgorgement, damages, attorneys' fees and injunctive relief.

A RICO claim, certain claims alleging problems involving home equity lines of credit and all contract-based claims were dismissed with prejudice in May, 2010. This lawsuit was scheduled for trial in April, 2011, but has been continued indefinitely.

Massachusetts Division of Banks

The Massachusetts Division of Banks (the "Division") delivered to LendingTree, LLC on February 11, 2011 a Report of Examination/Inspection which identified various alleged violations of Massachusetts and federal laws, including the alleged insufficient delivery by LendingTree, LLC of various disclosures to its customers. On October 14, 2011, the Division provided a proposed Consent Agreement and Order to settle the Division's allegations, which the Division had shared with other state mortgage lending regulators. Twenty-four of such state mortgage lending regulators (the "Joining Regulators") indicated that if LendingTree, LLC would enter into the Consent Agreement and Order, they would agree not to pursue any analogous allegations that they otherwise might assert. As of the date of this report, none of the Joining Regulators have asserted any such allegations.

The proposed Consent Agreement and Order calls for a fine to be allocated among the Division and the Joining Regulators and for LendingTree, LLC to adopt various new procedures and practices. We intend to commence negotiations toward an acceptable Consent Agreement and Order. We do not believe our LendingTree Exchange violates any federal or state mortgage lending laws; nor do we believe that any past operations of the LendingTree Exchange have resulted in a material violation of any such laws. Should the Division or any Joining Regulator bring any actions relating to the matters alleged in the February 2011 Report of Examination/Inspection, we intend to defend such actions vigorously.

Item 1A. Risk Factors

Other than the risk factors set forth below, there have been no material changes to the risk factors included in Part I, Item 1A, of the 2010 Form 10-K.

Adverse Events and Trends *Adverse conditions in the credit markets could materially and adversely affect our business, financial condition and results of operations.*

The credit markets, in particular those financial institutions that provide warehouse financing and similar arrangements to mortgage lenders, have been experiencing unprecedented and continued disruptions resulting from instability in the mortgage and housing markets. LendingTree Loans

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originates, processes, approves and funds various consumer mortgage loans through HLC, which operates primarily under the brand name "LendingTree Loans®." These direct lending operations have significant financing needs that are currently being met through borrowings under warehouse lines of credit or repurchase agreements to fund and close loans, followed by the sale of substantially all loans funded to investors in the secondary mortgage markets. Current credit market conditions, such as significantly reduced and limited availability of credit, increased credit risk premiums for certain market participants and increased interest rates generally, increase the cost and reduce the availability of debt and may continue for a prolonged period of time or worsen in the future.

As of the date of this report, LendingTree Loans had three committed lines of credit totaling \$275.0 million of borrowing capacity. One line with \$50.0 million of borrowing capacity expires on the earliest of (i) the closing date of the proposed asset sale with Discover Bank or (ii) January 30, 2012. Another \$125.0 million of borrowing capacity expires on the earliest of (i) forty-five days after the closing date of the proposed asset sale transaction with Discover Bank or (ii) April 25, 2012, and a third warehouse line with \$100.0 million of borrowing capacity expires on December 13, 2011. Each of these warehouse lines may be terminated by the lender in certain circumstances. Borrowings under these lines of credit are used to fund, and are secured by, consumer residential loans that are held for sale. Loans under these lines of credit are repaid using proceeds from the sales of loans by LendingTree Loans. At September 30, 2011, there was \$141.9 million outstanding under the lines of credit. See "Financial Position, Liquidity and Capital Resources" above for more information on our warehouse lines.

Although we believe that our existing lines of credit are adequate for our current operations, further reductions in our available credit, or the inability to extend, renew or replace these lines before completion of the pending sale of the operating assets of LendingTree Loans, could have an adverse effect on our business, financial condition and results of operations. LendingTree Loans attempts to mitigate the impact of current conditions and future credit market disruptions by maintaining committed and uncommitted warehouse lines of credit with several financial institutions. However, these financial institutions, like all financial institutions, are subject to the same adverse market conditions and may be affected by recent market disruptions, which may affect the decision to reduce or renew these lines or the pricing for these lines. As a result, current committed warehouse lines of credit may be reduced or not renewed, and alternative financing may be unavailable or inadequate to support operations or the cost of such alternative financing may not allow LendingTree Loans to operate at profitable levels. Because LendingTree Loans is highly dependent on the availability of credit to finance its operations, the continuation of current credit market conditions for a prolonged period of time or the worsening of such conditions could have an adverse effect on our business, financial condition and results of operations, particularly over the next few years. In addition, Discover Bank may terminate the agreement to acquire substantially all of the assets of our LendingTree Loans business if, with respect to either of our committed warehouse lines we fail to make a payment when due with respect to any indebtedness outstanding under any such agreement, we breach any other agreement, condition or covenant, relating to such indebtedness, or we obtain a waiver of any breach of or failure to satisfy any agreement, condition or covenant contained in such agreement without the prior written consent of Discover Bank, subject to certain exceptions.

Compliance and Changing Laws, Rules and Regulations Failure to comply with past, existing or new laws, rules and regulations, or to obtain and maintain required licenses, could adversely affect our business, financial condition and results of operations.

Our businesses market and provide services in heavily regulated industries through a number of different online and offline channels across the United States. As a result, our businesses have been and remain subject to a variety of statutes, rules, regulations, policies and procedures in various jurisdictions in the United States, which are subject to change at any time. The failure of our

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businesses to comply with past, existing or new laws, rules and regulations, or to obtain and maintain required licenses, could result in administrative fines and/or proceedings against us or our businesses by governmental agencies and/or litigation by consumers, which could adversely affect our business, financial condition and results of operations and our brand.

Our businesses conduct marketing activities via the telephone, the mail and/or through online marketing channels, which general marketing activities are governed by numerous federal and state regulations, such as the Telemarketing Sales Rule, state telemarketing laws, federal and state privacy laws, the CAN-SPAM Act, and the Federal Trade Commission Act and its accompanying regulations and guidelines, among others.

Additional federal, state and in some instances, local, laws regulate residential lending activities. These laws generally regulate the manner in which lending and lending-related activities are marketed or made available, including advertising and other consumer disclosures, payments for services and record keeping requirements; these laws include the Real Estate Settlement Procedures Act ("RESPA"), the Fair Credit Reporting Act, the Truth in Lending Act, the Equal Credit Opportunity Act, the Fair Housing Act and various state laws. State laws often restrict the amount of interest and fees that may be charged by a lender or mortgage broker, or otherwise regulate the manner in which lenders or mortgage brokers operate or advertise.

Failure to comply with applicable laws and regulatory requirements may result in, among other things, revocation of or inability to renew required licenses or registrations, loss of approval status, termination of contracts without compensation, administrative enforcement actions and fines, private lawsuits, including those styled as class actions, cease and desist orders and civil and criminal liability.

Most states require licenses to solicit, broker or make loans secured by residential mortgages and other consumer loans to residents of those states, as well as to operate real estate referral and brokerage services, and in many cases require the licensure or registration of individual employees engaged in aspects of these businesses. In 2008, Congress mandated that all states adopt certain minimum standards for the licensing of individuals involved in mortgage lending or loan brokering, and many state legislatures and state agencies are in the process of adopting or implementing additional licensing, continuing education, and similar requirements on mortgage lenders, brokers and their employees. Compliance with these new requirements may render it more difficult to operate or may raise our internal costs. While our businesses have endeavored to comply with applicable requirements, the application of these requirements to persons operating online is not always clear. Moreover, any of the licenses or rights currently held by our businesses or our employees may be revoked prior to, or may not be renewed upon, their expiration. In addition, our businesses or our employees may not be granted new licenses or rights for which they may be required to apply from time to time in the future.

Likewise, states or municipalities may adopt statutes or regulations making it unattractive, impracticable, or infeasible for our businesses to continue to conduct business in that jurisdiction. The withdrawal from any jurisdiction due to emerging legal requirements could adversely affect our business, financial condition and results of operations.

Our businesses are also subject to various state, federal and/or local laws, rules and regulations that regulate the amount and nature of fees that may be charged for transactions and incentives, such as rebates, that may be offered to consumers by our businesses, as well as the manner in which these businesses may offer, advertise or promote transactions. For example, RESPA generally prohibits the payment or receipt of referral fees and fee shares or splits in connection with residential mortgage loan transactions, subject to certain exceptions. The applicability of referral fee and fee sharing prohibitions to lenders and real estate providers, including online networks, may have the effect of reducing the types and amounts of fees that may be charged or paid in connection with real estate-secured loan offerings or activities, including mortgage brokerage, lending and real estate brokerage services, or otherwise limiting the ability to conduct marketing and referral activities. Although we believe that our

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businesses have been structured in such a way so as to comply with RESPA, the relevant regulatory agency may take a contrary position.

Various federal, state and in some instances, local, laws also prohibit unfair and deceptive sales practices. We have adopted appropriate policies and procedures to address these requirements (such as appropriate consumer disclosures and call scripting, call monitoring, and other quality assurance and compliance measures), but it is not possible to ensure that all employees comply with our policies and procedures at all times.

As employers, our businesses are subject to federal and state employment laws. In particular, the Fair Labor Standards Act and California wage and hour laws govern the treatment of "non-exempt" employees, which may include loan officers, underwriters, and loan processors at Home Loan Center, Inc. Failure to comply with applicable employment laws may result in, among other things, administrative fines, class action lawsuits, damages awards and injunctions, any of which could adversely affect our business, financial condition and results of operations.

Compliance with these laws, rules and regulations is a significant component of our internal costs, and new laws, rules and regulations are frequently proposed and adopted, requiring us to adopt new procedures and practices.

Parties through which our businesses conduct business similarly may be subject to federal and state regulation. These parties typically act as independent contractors and not as agents in their solicitations and transactions with consumers. We cannot ensure that these entities will comply with applicable laws and regulations at all times. Failure on the part of a lender, secondary market purchaser, website operator or other third party to comply with these laws or regulations could result in, among other things, claims of vicarious liability or a negative impact on the reputation of Tree.com and its businesses.

Regardless of the effectiveness of our compliance activities, relevant regulatory authorities and private plaintiffs may allege that we failed to comply with applicable laws, rules and regulations. These allegations may relate to past conduct and/or past business operations, such as our discontinued real estate brokerage operations (which was subject to various state and local laws, rules and regulations). Even allegations that our activities have not complied or do not comply with all applicable laws and regulations may have an adverse effect on our business, financial condition and results of operations. Such allegations typically require legal fee expenditures to defend. We have in the past and may in the future decide to settle allegations of non-compliance with laws, rules and regulations when we determine that the cost of settlement is less than the cost and risk of continuing to defend against an allegation. Settlements may require us to pay monetary fines and may require us to adopt new procedures and practices, which may render it more difficult to operate or may raise our internal costs. The future occurrence of one or more of these events could have an adverse effect on our business, financial condition and results of operations.

The sale of LendingTree Loans assets to Discover Bank may not be completed unless important conditions to the closing are satisfied and unless we maintain certain operational or financial metrics.

Completion of the transaction with Discover Bank is subject to certain conditions, including receipt of regulatory approvals. If these conditions are not satisfied or waived (to the extent permitted by law), the transaction may be delayed or may not occur, and we could lose some or all of the intended benefits of the transaction, which could have a material adverse effect on our business, results of operations or financial condition. Discover Bank may not receive the applicable regulatory approvals, or governmental authorities may impose conditions upon the completion of the transaction or require changes in the terms of the transaction. These conditions or changes could result in the termination of the asset purchase agreement or could have the effect of delaying the completion of the transaction or

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imposing additional costs, which could have a material adverse effect on our business, results of operations or financial condition.

Additionally, the asset purchase agreement imposes on the Company covenants regarding maintenance of certain operational and financial metrics until the closing of the transaction. If the requirements of these covenants are not met, Discover Bank has the option to terminate the asset purchase agreement, which could have a material adverse effect on our business, results of operations or financial condition.

Further, the purchase price for the assets is comprised of a payment of \$35.9 million at closing and future contingent payments of \$10 million on each of the first and second anniversaries of the closing, subject to the Company satisfying certain conditions, including maintenance of the LendingTree Exchange and certain financial and operational metrics. If these conditions are not met, these future contingent payments could be reduced or eliminated, which could have a material adverse effect on our business, results of operations or financial condition.

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For more information on the conditions to the closing, see the proxy statement we prepared in connection with the solicitation of stockholder approval for the transaction, which we filed with the SEC on August 2, 2011.

The transaction with Discover Bank may distract our management from other responsibilities.

The transaction to sell assets of LendingTree Loans to Discover Bank could cause our management to focus its time and energies on matters related to the transaction that otherwise would be directed to our business and operations.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**Issuer Purchases of Equity Securities**

The following table provides information about the Company's purchases of equity securities during the quarter ended September 30, 2011.

| Period | Total Number of Shares Purchased(1) | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs(2) | Maximum Number/Approximate Dollar Value of Shares that May Yet be Purchased Under the Plans or Programs (in thousands) |
|---------------------|-------------------------------------|------------------------------|---|--|
| 07/01/11 - 07/31/11 | 4,447 | \$ | | \$ 4,274 |
| 08/01/11 - 08/31/11 | 2,557 | \$ | | \$ 4,274 |
| 09/01/11 - 09/30/11 | 490 | \$ | | \$ 4,274 |
| Total | 7,494 | \$ | | \$ 4,274 |

(1) During the quarter ended September 30, 2011, 7,494 shares of the Company's common stock were delivered by employees to satisfy federal and state withholding obligations upon the vesting of restricted stock awards granted to those individuals under the Tree.com Second Amended and Restated 2008 Stock and Award Incentive Plan. The withholding of those shares does not affect the dollar amount or number of shares that may be purchased under the publicly announced plans or programs described below.

(2) On January 11, 2010, the Company announced that its Board of Directors approved a stock repurchase program for an amount up to \$10 million. The program authorizes repurchases of common shares in the open market or through privately-negotiated transactions. The Company began this program in February 2010 and expects to use available cash to finance these repurchases. It will determine the timing and amount of such repurchases based on its evaluation of market conditions, applicable SEC guidelines and regulations, and other factors. This program may be suspended or discontinued at any time at the discretion of the Board of Directors.

Table of Contents**Item 6. Exhibits**

| Exhibit | Description | Location |
|----------------|---|---|
| 2.1 | Asset Purchase Agreement dated September 15, 2011 by and among LendingTree, LLC, RealEstate.com, Inc. and Market Leader, Inc.* | Exhibit 2.1 to the Registrant's Current Report on Form 8-K filed September 21, 2011 |
| 10.1 | Bill of Sale | Exhibit 2.2 to the Registrant's Current Report on Form 8-K filed September 21, 2011 |
| 10.2 | Assignment and Assumption Agreement | Exhibit 2.3 to the Registrant's Current Report on Form 8-K filed September 21, 2011 |
| 10.3 | Amendment No. 2 to Transactions Terms Letter dated as of July 12, 2011, which supplements that certain Master Repurchase Agreement dated as of May 1, 2009 by and between Home Loan Center, Inc. and Bank of America, N.A. | Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed July 15, 2011 |
| 10.4 | Amendment No. 2 to Early Purchase Program Addendum to Loan Purchase Agreement dated as of July 12, 2011, which supplements that certain Loan Purchase Agreement by and between Bank of America, N.A. and Home Loan Center, Inc. dated April 16, 2002. | Exhibit 10.2 to the Registrant's Current Report on Form 8-K filed July 15, 2011 |
| 10.5 | Extension Letter Agreement dated as of August 11, 2011, regarding the Master Repurchase Agreement by and between Bank of America, N.A. and Home Loan Center, Inc. dated May 1, 2009 | Exhibit 10.12 to the Registrant's Quarterly Report on Form 10-Q filed August 15, 2011 |
| 10.6 | Master Repurchase Agreement, dated as of October 13, 2011, by and between Home Loan Center, Inc. and Citibank, N.A. | Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed October 19, 2011 |
| 10.7 | Pricing Side Letter dated as of October 13, 2011, by and between Home Loan Center, Inc. and Citibank, N.A. | Exhibit 10.2 to the Registrant's Current Report on Form 8-K filed October 19, 2011 |
| 10.8 | Amendment No. 3 to Transaction Terms Letter dated as of September 30, 2011, which supplements that certain Master Repurchase Agreement dated as of May 1, 2009 by and between Home Loan Center, Inc. and Bank of America, N.A. | Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed October 5, 2011 |

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| Exhibit | Description | Location |
|----------------|---|-----------------|
| 10.9 | Amendment No. 7 to Master Repurchase Agreement dated as of October 28, 2011, by and between Home Loan Center, Inc. and JPMorgan Chase Bank, N.A. | |
| 10.10 | Amendment No. 5 to Side Letter dated as of October 28, 2011, which supplements that certain Master Repurchase Agreement dated as of October 30, 2009 by and between Home Loan Center, Inc. and JPMorgan Chase Bank, N.A. | |
| 10.11 | Amendment No. 2 to Master Repurchase Agreement dated as of November 1, 2011, which supplements that certain Master Repurchase Agreement dated as of May 1, 2009 by and between Home Loan Center, Inc. and Bank of America, N.A. | |
| 10.12 | Amendment No. 4 to Transaction Terms Letter dated as of November 1, 2011, which supplements that certain Master Repurchase Agreement dated as of May 1, 2009 by and between Home Loan Center, Inc. and Bank of America, N.A. | |
| 31.1 | Certification of the principal executive officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 | |
| 31.2 | Certification of the principal financial officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 | |
| 32.1 | Certification of the principal executive officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 | |
| 32.2 | Certification of the principal financial officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 | |
| 101.INS | XBRL Instance Document | |
| 101.SCH | XBRL Taxonomy Extension Schema Document | |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document | |

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| Exhibit | Description | Location |
|----------------|--|-----------------|
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document | |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document | |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document | |

Filed herewith

This certification is being furnished solely to accompany this report pursuant to 18 U.S.C. 1350, and is not being filed for purposes of Section 18 of the Securities Exchange Act of 1934 and is not to be incorporated by reference into any filing of the registrant, whether made before or after the date hereof, regardless of any general incorporation language in such filing.

Furnished herewith. Pursuant to Rule 406T of Regulation S-T, the Interactive Data Files on Exhibit 101 hereto are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Securities and Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.

*

Certain schedules to this Exhibit have been omitted in accordance with Regulation S-K Item 6.01(b)(2). The Company agrees to furnish supplementally a copy of all omitted schedules to the SEC upon its request.

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| 10.11 | Amendment No. 2 to Master Repurchase Agreement dated as of November 1, 2011, which supplements that certain Master Repurchase Agreement dated as of May 1, 2009 by and between Home Loan Center, Inc. and Bank of America, N.A | |
| 10.12 | Amendment No. 4 to Transaction Terms Letter dated as of November 1, 2011, which supplements that certain Master Repurchase Agreement dated as of May 1, 2009 by and between Home Loan Center, Inc. and Bank of America, N.A | |
| 31.1 | Certification of the principal executive officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 | |
| 31.2 | Certification of the principal financial officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 | |
| 32.1 | Certification of the principal executive officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 | |
| 32.2 | Certification of the principal financial officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 | |
| 101.INS | XBRL Instance Document | |
| 101.SCH | XBRL Taxonomy Extension Schema Document | |

Table of Contents

| Exhibit | Description | Location |
|----------------|--|-----------------|
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document | |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document | |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document | |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document | |

Filed herewith

This certification is being furnished solely to accompany this report pursuant to 18 U.S.C. 1350, and is not being filed for purposes of Section 18 of the Securities Exchange Act of 1934 and is not to be incorporated by reference into any filing of the registrant, whether made before or after the date hereof, regardless of any general incorporation language in such filing.

Furnished herewith. Pursuant to Rule 406T of Regulation S-T, the Interactive Data Files on Exhibit 101 hereto are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Securities and Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.

*

Certain schedules to this Exhibit have been omitted in accordance with Regulation S-K Item 6.01(b)(2). The Company agrees to furnish supplementally a copy of all omitted schedules to the SEC upon its request.