MANUGISTICS GROUP INC
Form 10-Q
October 15, 2001

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

FORM 10-Q
(Mark One)
[X]QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended August 31, 2001

OR

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

For the transition period from __________ to __________

Commission File Number 0-22154

MANUGISTICS GROUP, INC.
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	52-1469385 (I.R.S. Employer Identification Number)
2115 East Jefferson Street, Rockville, Maryland (Address of principal executive offices)	20852 (Zip code)

(301) 984-5000
(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes X No _________

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date: 68.1 million shares of common stock, $.002 par value per share, as of October 9, 2001.

MANUGISTICS GROUP, INC. AND SUBSIDIARIES

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

MANUGISTICS GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands, except per share data)

	August 31, 2001	February 28, 2001
	(Unaudited)	
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$231,822	$196,362
Marketable securities	20,000	103,946
Accounts receivable, net of allowance for doubtful accounts of $11,062 and $5,604 at August 31, 2001 and February 28, 2001, respectively	72,171	84,211
Deferred tax assets	8,930	9,175
Other current assets	8,821	12,536
Total current assets	341,744	406,230
NONCURRENT ASSETS:		
Property and equipment, net of accumulated depreciation	22,388	19,275
Software development costs, net of accumulated amortization	14,865	15,709
Goodwill, net of accumulated amortization	305,240	335,651
Other intangible assets and noncurrent assets, net of accumulated amortization	99,089	70,396
TOTAL ASSETS	$783,326	$847,261
LIABILITIES AND STOCKHOLDERS EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$7,414	$9,923
Accrued compensation	9,372	19,539
Other accrued liabilities	28,350	34,371
Deferred revenue	46,525	41,729

Total current liabilities91,661105,562 **NONCURRENT LIABILITIES:**Long-term debt250,391250,133Deferred tax liabilities4,84316,062Other4,7985,183

Total noncurrent liabilities260,032271,378 **COMMITMENTS AND CONTINGENCIES (Note 3) STOCKHOLDERS EQUITY:**Preferred stock Common stock, $.002 par value per share; 300,000 and 100,000 shares authorized at August 31, 2001 and February 28, 2001, respectively; 68,867 and 67,518 issued, and 68,114 and 66,765 outstanding at August 31, 2001 and February 28, 2001, respectively138135Additional paid-in capital623,558621,824Treasury stock, 753 shares, at cost(717)(717)Deferred compensation(13,006)(19,316)Accumulated other comprehensive loss(2,969)(1,324)Accumulated deficit(175,371)(130,281)

Total stockholders equity431,633470,321

TOTAL LIABILITIES AND STOCKHOLDERS EQUITY$783,326$847,261

See accompanying notes to the condensed consolidated financial statements.

MANUGISTICS GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)
(in thousands, except per share data)

	Three Months Ended August 31,		Six Months Ended August 31,	
REVENUE:	**2001**	**2000**	**2001**	**2000**
Software	$24,809	$28,510	$69,865	$54,483

Services27,52116,57255,05428,539Support18,63413,06835,85525,647

Total revenue70,96458,150160,774108,669

OPERATING EXPENSES:Cost of revenue:Cost of software4,9633,87210,0988,657Amortization of acquired technology2,319373,89974 Cost of services and support24,27413,47747,61425,015Non-cash stock compensation (benefit) expense for cost of services and support(2,654)6,237(925)6,237 Sales and marketing expenses30,11425,15764,11348,134Non-cash stock compensation (benefit) expense for sales and marketing(5,215)7,349(2,703)7,349 Product development expenses20,3268,44536,76116,215Non-cash stock compensation (benefit) expense for product and development(2,694)5,343(1,508)5,343 General and administrative expenses6,9975,30614,79510,310Non-cash stock compensation (benefit) expense for general and administrative(807)1,782(327)1,782 Amortization of intangibles21,00256440,9301,139 Restructuring costs2,419 2,419

Total operating expenses101,04477,569215,166130,255

LOSS FROM OPERATIONS(30,080)(19,419)(54,392)(21,586)OTHER (EXPENSE) INCOME, NET(865)432(183)715

LOSS BEFORE INCOME TAXES(30,945)(18,987)(54,575)(20,871)(BENEFIT FROM) PROVISION FOR INCOME TAXES(9,281)697(9,485)(36)

NET LOSS$(21,664)$(19,684)$(45,090)$(20,835)

NET LOSS PER SHARE:BASIC(0.32)(0.34)(0.67)(0.37)

DILUTED(0.32)(0.34)(0.67)(0.37)

SHARES USED IN LOSS PER SHARE CALCULATION:BASIC67,88457,29867,54857,082

DILUTED67,88457,29867,54857,082

See accompanying notes to the condensed consolidated financial statements.

MANUGISTICS GROUP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
(in thousands)

Six Months Ended
August 31,
2001 2000

CASH FLOWS FROM OPERATING ACTIVITIES
Net loss$(45,090)$(20,835)Adjustments to reconcile net loss to net cash used in operating activities:Depreciation and amortization55,0359,166Amortization of debt issuance costs569 Deferred income taxes(11,448)(4,910)Tax benefit from stock options exercised 4,408Non-cash stock compensation (benefit) expense(5,463)20,711Other501904Changes in assets and liabilities:Accounts receivable13,555(26,393)Other assets3,6561,221Accounts payable(2,781)140Accrued compensation(10,211)2,680Other liabilities(6,170)(978)Deferred revenue4,6682,449

Net cash used in operating activities(3,179)(11,437)

CASH FLOWS FROM INVESTING ACTIVITIES Acquisitions, net of cash acquired(29,573) Investments in businesses(10,150) Investments and sales (purchases) of marketable securities, net85,2542,431Purchase of property and equipment, net(6,555)(3,582)Capitalization and purchases of software(7,673)(5,751)

Net cash provided by (used in) investing activities31,303(6,902)

CASH FLOWS FROM FINANCING ACTIVITIES Payments of long-term debt and capital lease obligations, net(94)(96)Payments of debt issuance costs convertible debt(179) Proceeds from exercise of stock options and employee stock plan purchases8,2435,414

Net cash provided by financing activities7,9705,318

EFFECTS OF EXCHANGE RATES ON CASH BALANCES(634)(246) **NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS**35,460(13,267)**CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD**196,36241,803

CASH AND CASH EQUIVALENTS, END OF PERIOD$231,822$28,536

See accompanying notes to the condensed consolidated financial statements.

MANUGISTICS GROUP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
August 31, 2001

1. *Basis of Presentation*

The accompanying unaudited condensed consolidated financial statements of Manugistics Group, Inc. (the Company) have been prepared in accordance with generally accepted accounting principles for interim reporting and in accordance with the instructions to the Quarterly Report on Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting only of normal, recurring adjustments) which are necessary for a fair presentation of the unaudited results for the interim periods presented have been included. The results of operations for the period presented herein are not necessarily indicative of the results of operations for the entire fiscal year, which ends on February 28, 2002.

These financial statements should be read in conjunction with the financial statements and notes thereto for the fiscal year ended February 28, 2001 included in the Annual Report on Form 10-K of the Company for that year filed with the Securities and Exchange Commission.

2. *Net Loss Per Share*

Basic net loss per share is computed using the weighted average number of shares of common stock outstanding. Diluted net loss per share is computed using the weighted average number of shares of common stock and, when dilutive, potential common shares from options and warrants to purchase common stock using the treasury stock method and the effect of the assumed conversion of the Company s convertible subordinated debt. The dilutive effect of options and warrants of 5.7 million shares, 6.5 million shares, 6.1 million shares and 6.5 million shares were excluded from the calculation of diluted net loss per share for the three month periods ended August 31, 2001 and 2000, and the six month periods ended August 31, 2001 and 2000, respectively, as including them would have been anti-dilutive due to the Company s reported net loss. The assumed conversion of the Company s convertible debt was excluded from the computation of diluted net loss per share for the three and six months ended August 31, 2001 since it was anti-dilutive. The Company s convertible debt may be exchanged for up to approximately 5.7 million shares of the Company s common stock in future periods.

3. *Commitments and Contingencies*

The Company is involved in disputes and litigation in the normal course of business. The Company does not believe that the outcome of any pending disputes or litigation will have a material effect on the Company s financial condition or operating results. However, an unfavorable outcome of legal matters could have a material effect on the Company s business, operating results, financial condition or cash flows. The Company has established accruals related to legal matters where a loss is probable and reasonably estimable.

The Company has previously reported its legal proceedings with Information Resources, Inc. (IRI) arising from the acquisition of certain assets in March 1997. A dispute over revenue streams that IRI alleges it is entitled to is being arbitrated. IRI seeks a total of $15.9 million in damages. The Company contends that the conditions to these amounts becoming due have not been satisfied and that no amounts are due IRI, because, among other reasons, of a failure of consideration in the overall transaction. Arbitration of this matter was scheduled to commence in early November 2001. We have recently been advised that the arbitrator will not be able to serve in this dispute. No replacement arbitrator has yet been chosen. Accordingly, the Company does not know when the arbitration will be conducted. A related claim concerning the breach of a separate Non-

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Competition and Non-Solicitation Agreement filed in the Circuit Court of Cook County, Illinois is awaiting resolution of the arbitration.

As previously reported, on November 29, 2000, the Company filed a lawsuit against VirtualFund.com, Inc., in the United States District Court for the District of Maryland alleging that VirtualFund.com, Inc. is in anticipatory breach of its obligations under a software license agreement among the Company and VirtualFund.com, Inc. and its affiliates. The Company sought at least $4.5 million in damages. VirtualFund.com, Inc. counterclaimed that the contract is invalid and sought return of $2.5 million in fees and other unspecified damages. In July 2001, the Company and VirtualFund.com, Inc. settled all claims. The settlement of these claims did not have a material impact on the Company s results of operations.

4. *Comprehensive Loss*

Other comprehensive loss relates primarily to foreign currency translation losses and unrealized gains or losses on investments in marketable securities. The following table sets forth the comprehensive loss for the three and six months ended August 31, 2001 and 2000 (dollar amounts in thousands):

	Three months ended August 31, 2001	2000	Six months ended August 31, 2001	2000
Net loss	$ (21,664)	$ (19,684)	$ (45,090)	$ (20,835)
Other comprehensive income (loss)	197	422	(1,645)	189
Total comprehensive loss	$(21,467)	$(19,262)	$(46,735)	$(20,646)

5. *Acquisitions*

On May 17, 2001, the Company acquired One Release, LLC and its affiliates (the One Release Acquisition), a software engineering services and systems business, for $4.3 million of common stock (135,793 shares). The Company may also pay up to an additional $1.0 million in contingent consideration if certain performance criteria are attained during the first year after the acquisition date. The One Release Acquisition was accounted for using the purchase method of accounting. The results of operations for One Release have been included in the Company s operations since the acquisition date. The Company allocated approximately $4.7 million of the purchase price to assembled workforce, which is included in other intangible assets and noncurrent assets, net of accumulated amortization, in the condensed consolidated balance sheet as of August 31, 2001.

On May 31, 2001, the Company acquired the collaborative sourcing and design assets of Partminer CSD, Inc., as well as related assets from its parent, Partminer, Inc. and its affiliates (the CSD Acquisition) for cash. Partminer CSD, Inc. is a developer of product design and sourcing software. The CSD Acquisition included developed technology, existing customer contracts, personnel and other intangible assets. The CSD Acquisition was accounted for using the purchase method of accounting. The purchase price has been allocated to the assets acquired and liabilities assumed based on there estimated fair values at the acquisition date. Intangible assets related to the CSD Acquisition include developed technology and goodwill. Contemporaneously, in another transaction, the Company entered into a software license agreement with Partminer, Inc. for various products for use in its electronic components procurement and sourcing business.

On July 25, 2001, the Company acquired the intellectual property and other certain assets of SpaceWorks, Inc. (the SpaceWorks Transaction) for cash. SpaceWorks, Inc. software provides solutions that help enable companies to automate complex order-related activities. The SpaceWorks Transaction was accounted for as a purchase of developed technology, which is included in other intangible assets and noncurrent assets in the condensed consolidated balance sheet as of August 31, 2001.

Total aggregate cash consideration paid for the CSD Acquisition and the SpaceWorks Transaction was $27.5 million during the six months ended August 31, 2001.

6. *Investments in Businesses*

On May 30, 2001, the Company purchased $10.2 million of preferred stock of Converge, Inc. (the Converge Investment). Converge, Inc. is a private marketplace exchange for components used by electronics and high technology manufacturers. Founding investors in Converge, Inc. include Agilent Technologies, Inc., Compaq Computer Corporation and Hewlett-Packard Company, among others. The Converge Investment is included in other intangible assets and noncurrent assets in the condensed consolidated balance sheet as of August 31, 2001 and will be accounted for under the cost method of accounting for investments. In a transaction approximately two weeks prior to the Converge Investment, the Company entered into a software license agreement with Converge, Inc. for various products for use in its marketplace exchange business.

7. *New Accounting Pronouncements*

On March 1, 2001, the Company adopted Statement of Financial Accounting Standards No. 133 (SFAS 133), *Accounting for Derivative Instruments and Hedging Activities* , as amended by SFAS 137 and 138. SFAS 133 requires all derivatives to be recorded at fair value. Unless designated as hedges, changes in these fair values will be recorded in the income statement. Fair value changes involving hedges will generally be recorded by offsetting gains and losses on the hedge and on the hedged item, even if the fair value of the hedged item is not otherwise recorded. Adoption of this standard had no impact on the Company s financial statements.

On July 20, 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 141 (SFAS 141) *Business Combinations.* and Statement of Financial Accounting Standards No. 142 (SFAS 142) *Goodwill and Other Intangible Assets.* SFAS 141 establishes new standards for accounting and reporting requirements for business combinations and requires that the purchase method of accounting be used for all business combinations initiated after June 30, 2001. Goodwill and certain intangible assets will remain on the balance sheet and not be amortized. On an annual basis, and when there is reason to suspect that their values have been impaired, these assets must be tested for impairment and write-downs may be necessary. SFAS 142 changes the accounting for goodwill from an amortization method to an impairment-only approach. Amortization of goodwill, including goodwill recorded in past business combinations, will cease upon adoption of this statement. SFAS 142 will also require recognized intangible assets to be amortized over their respective estimated useful lives and reviewed for impairment in accordance with Statement of Financial Accounting Standards No 121 (SFAS 121) *Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of.* Any recognized intangible asset determined to have an indefinite useful life will not be amortized, but instead tested for impairment in accordance with the Standard until its life is determined to no longer be indefinite.

In connection with the goodwill impairment evaluation, SFAS 142 will require the Company to perform an assessment of whether there is an indication that goodwill is impaired at the date of adoption. To accomplish this, the Company will identify its reporting units and determine the carrying value of each reporting unit by assigning the assets and liabilities, including existing goodwill and intangible assets, to those reporting units as of the date of adoption to determine the fair value of each reporting unit and compare it to the reporting unit s carrying amount. To the extent a reporting unit s carrying amount exceeds its fair value, an indication exists that the reporting unit s goodwill may be impaired and the Company must perform the second step of the impairment test. In the second step, the Company must compare the implied fair value of the reporting unit s goodwill, determined by allocating the reporting unit s fair value to all of its assets and liabilities in a manner similar to a purchase price allocation in accordance with SFAS 141, to its carrying amount, both of which would be measured as of the date of adoption. Any impairment loss will be recognized as the cumulative effect of a change in accounting principle in the Company s statement of operations.

The Company is required to adopt the provisions of SFAS 141 and SFAS 142 on March 1, 2002, with the exception of the immediate requirement to use the purchase method of accounting for all business combinations completed after June 30, 2001. Early adoption and retroactive application of these Standards are not permitted. However, any goodwill and any intangible asset determined to have an indefinite useful life that is acquired in a business combination completed after June 30, 2001 will not be amortized. Goodwill and intangible assets acquired in business combinations completed before July 1, 2001 will continue to be amortized until February 28, 2002. The Company will stop amortizing goodwill at that time, but will continue amortizing other intangible assets. At this time we have not determined how goodwill will be allocated to specific reporting units upon adoption of SFAS 142 on March 1, 2002. Additionally, we have not appraised the value of any such reporting units. Accordingly, we have not yet made a determination about whether or not an impairment charge will be necessary upon adoption of the new standard. The Company will need to periodically evaluate the recoverability of its goodwill. It is possible that the Company may incur impairment charges in the future. Beginning in our fiscal year 2003, we expect a reduction in our quarterly amortization expense of approximately $20.0 million for the quarters ending May 31, 2002, August 31, 2002 and November 30, 2002 and $19.1 million for the quarter ending February 28, 2003, based on our current amortization schedule.

8. *Product Development Consolidation*

During June 2001, the Company decided to centralize certain of its product development functions in Rockville, MD from two remote offices. This resulted in the closure of one office and reduction of space occupied in another office, as well as the relocation and termination of approximately 10 and 40 employees, respectively. As a result, the Company recorded a restructuring charge to operations related to the product development consolidation of approximately $2.4 million during the three months ended August 31, 2001. The components of the charge and remaining accrual balance are as follows (in thousands):

	Initial Charge	Utilization of Cash	Remaining Accrual
Lease obligations and terminations	$1,353	$58	$1,295
Relocation	497	138	359
Severance and related benefits	425	171	254
Write-down of leasehold improvements	144		
Total	$2,419	$367	$1,908

9. *Income Taxes*

An income tax benefit of $9.3 million and $9.5 million was recorded for the three and six month periods ended August 31, 2001, respectively. Management regularly evaluates the realizability of its deferred tax assets given the nature of its operations and the tax jurisdictions in which it operates. Based on the Company s historical taxable income and estimates of future profitability, management has concluded that future operating income will more likely than not be insufficient to cover all of its deferred tax assets. An appropriate valuation allowance was recorded at August 31, 2001 based upon the Company s estimates. Management is continuing to monitor its estimates of future profitability based on business conditions.

10. *Reclassifications*

In the three and six months ended August 31, 2001, the Company reclassified amortization of acquired technology to include this as a component of cost of revenue. Prior periods have been reclassified to be consistent with this presentation.

11. *Subsequent Events*

On October 3, 2001, the Company announced plans to reduce its workforce by approximately 12%. The reduction in workforce will be achieved through a combination of attrition and involuntary terminations. In addition, we announced other cost containment measures including a mandatory unpaid leave program for most employees, a reduction in the use of outside contractors, professional fees and travel. These cost containment measures have been devised to align the Company s cost structure with expected revenues in the near-term. The Company expects to record a restructuring charge in the quarter ended November 30, 2001 for severance and related benefits associated with involuntary terminations.

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

OVERVIEW

We are a leading global provider of Enterprise Profit OptimizationTM (EPO) solutions, which we believe is a new and important category of solutions for enterprise management. We are also a leading provider of solutions for supply chain management (SCM), pricing and revenue optimization (PRO) and electronic marketplaces (eMarketplaces). Our solutions help companies lower operating costs, increase revenues, enhance profitability and accelerate revenue and earnings growth. They do this by creating efficiencies in both how goods and services are brought to market (supply chain management) and how they are sold (pricing and revenue optimization). EPO solutions provide additional benefits by combining the proven cost-reduction power of supply chain management solutions and the revenue-enhancing capacity of pricing and revenue optimization solutions.

We help our clients monitor and streamline their own core internal operational processes involving the design, purchase, manufacture, storage, transportation, pricing, marketing and selling of their goods and services. Our solutions also help our clients integrate their own internal processes with those of their customers and suppliers to assist in providing collaboration and efficiencies across extended eMarketplaces. In addition, our solutions help our clients improve customer service and the allocation of resources by providing information and forecasts that allow them to make more effective operational decisions. We also provide strategic consulting and implementation services to our clients as part of our solutions.

Increasing global competition, shortening product life cycles and developing eMarketplace initiatives are forcing businesses to provide improved levels of customer service while shortening the time it takes to bring their products and services to market. We were an early innovator in solutions that allow collaboration among our clients and their customers and suppliers. Our first Internet-ready products were commercially available in late 1997. We focus the development of our technology on meeting the changing needs of companies in the markets we serve, including the need to do business in new electronic marketplaces. We offer solutions to companies in many industries including agriculture, apparel, automotive, chemical, consumer durables, consumer packaged goods, electronics & high technology, energy, financial services, food & beverage, government, logistics, metals, pharmaceuticals, pulp & paper, retail, services and transport, travel & hospitality. Our customer base of approximately 1,100 clients includes large, multinational enterprises such as 3Com; Amazon.com; Boeing Co.; BP Amoco Corp.; Brown & Williamson Tobacco Corp.; Caterpillar; Cisco Systems Inc.; Coca-Cola Bottling Co. Consolidated; Compaq; DuPont; eConnections; Ford Motor Company; General Electric; Harley-Davidson, Inc.; Hormel Foods Corp.; Levi Strauss & Co.; Marriott; Nestle; Texas Instruments; Timberland; Unilever Home & Personal Care, USA and United Airlines; as well as mid-sized enterprises and emerging eMarketplaces.

During the three months ended August 31, 2001, we experienced delays in consummating software license transactions, especially during the last few days of such period. The delays were caused primarily by prospects concerns about committing to large capital projects in the face of further weakening global economic conditions. We believe that these concerns were heightened further after the terrorist attacks in the United States on September 11, 2001 making it difficult for us to accurately forecast our revenues until global economic conditions stabilize. Our software revenue and total revenue decreased $20.2 million and $18.8 million during the three months ended August 31, 2001 compared to the three months ended May 31, 2001, or 44.9% and 21.0%, respectively. We anticipate further declines in software revenue and total revenue during the three months ended November 30, 2001. In response to current and expected decreases in revenue, the Company has enacted several cost containment measures that it expects will reduce its operating cost structure (excluding amortization of intangibles and acquired technology, non-cash stock compensation (benefit) expense and restructuring charges) by 12% or more during the three months ended November 30, 2001. See note 11 Subsequent Events in the Notes to Condensed Consolidated Financial

Statements.

RESULTS OF OPERATIONS

The following table includes the consolidated statements of operations data for the three and six months ended August 31, 2001 and 2000 expressed as a percentage of revenue:

	Three Months Ended August 31, 2001	2000	Six Months Ended August 31, 2001	2000
REVENUE:				
Software	35.0%	49.0%	43.5%	50.1%
Services	38.8%	28.5%	34.2%	26.3%
Support	26.2%	22.5%	22.3%	23.6%
Total revenue	100.0%	100.0%	100.0%	100.0%
OPERATING EXPENSES:				
Cost of revenue:				
Cost of software	7.0%	6.7%	6.3%	8.0%
Amortization of acquired technology	3.3%		2.4%	0.1%
Cost of services and support	34.2%	23.2%	29.6%	23.0%
Sales and marketing	42.4%	43.3%	39.9%	44.3%
Product development	28.6%	14.5%	22.8%	14.9%
General and administrative	9.9%	9.1%	9.2%	9.5%
Amortization of intangibles	29.6%	1.0%	25.5%	1.0%
Non-cash stock compensation (benefit) expense	(16.0)%	35.6%	(3.4)%	19.1%
Restructuring charge	3.4%		1.5%	
Total operating expenses	142.4%	133.4%	133.8%	119.9%
Loss from operations	(42.4)%	(33.4)%	(33.8)%	(19.9)%
Other (expense) income, net	(1.2)%	0.7%	(0.1)%	0.7%
Loss before income taxes	(43.6)%	(32.7)%	(33.9)%	(19.2)%
(Benefit from) provision for income taxes	(13.1)%	1.2%	(5.9)%	(0.0)%
Net loss	(30.5)%	(33.9)%	(28.0)%	(19.2)%

The percentages shown above for cost of services and support, sales and marketing, product development and general and administrative expenses have been calculated, excluding non-cash stock compensation (benefit) expense which are shown below (in thousands):

	Three months ended August 31,		Six months ended August 31,	
	2001	2000	2001	2000
Cost of services and support	$(2,654)	$6,237	$(925)	$6,237
Sales and marketing	(5,215)	7,349	(2,703)	7,349
Product development	(2,694)	5,343	(1,508)	5,343
General and administrative	(807)	1,782	(327)	1,782
Total	$(11,370)	$20,711	$(5,463)	$20,711

See Non-cash Stock Compensation (Benefit) Expense for further detail.

REVENUES:

General. Our revenue is derived from three categories: software, services and support. Software revenue is generally recognized upon execution of a software license agreement and shipment of the software, provided the fees are fixed and determinable and collection is considered probable in accordance with the American Institute of Certified Public Accountants (AICPA) Statement of Position (SOP) 97-2, *Software Revenue Recognition"*, as modified by SOP 98-9, *Modification of SOP 97-2, Software Revenue Recognition with Respect to Certain Transactions,* and Securities and Exchange Commission (SEC) Staff Accounting Bulletin 101 (SAB 101), *Revenue Recognition.* Fees are allocated to the various elements of software license agreements based on historical fair value experience. We generate the majority of our software revenue from our direct sales force with lesser amounts coming through indirect sales channels such as complementary software vendors, consulting firms, systems integrators and resellers. Services revenue is recognized as the services are performed. Support revenue is recognized ratably over the support period defined in the software license agreement.

When we provide services that are considered essential to the functionality of software products sold or if software sold requires significant production, modification or customization, we account for the software and services revenue in accordance with SOP 81-1, *Accounting for Performance of Construction Type and Certain Production Type Contracts* , which requires us to use the percentage-of-completion method of revenue recognition. Revenue is recognized based on labor hours incurred to date compared to total estimated labor hours for the contract.

Total revenue increased 22.0% and 47.9% during the three and six months ended August 31, 2001, respectively, compared to the same period in 2000. The increase in total revenue during the three-month comparable period resulted primarily from the acquisition of Talus Solutions, Inc. (Talus). The increase in total revenue during the six-month comparable period resulted primarily from increased market acceptance for our products and services, increased selling activities resulting from a larger sales force, increased average selling price (ASP) for our software and the acquisition of Talus.

Software. Software revenue decreased 13.0%, or $3.7 million, and increased 28.2%, or $15.4 million, for the three and six months ended August 31, 2001, respectively, as compared to the same periods in 2000. The decrease in software revenue during the three months ended August 31, 2001 was primarily due to economic uncertainty and a related decline in information technology spending, including software. Late in