SUPPORTSOFT INC
Form S-3/A
October 31, 2003

**Table of Contents**

**Index to Financial Statements**

**As filed with the Securities and Exchange Commission on October 31, 2003**

**Registration No. 333-109752**

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# UNITED STATES

# SECURITIES AND EXCHANGE COMMISSION

**WASHINGTON, D.C. 20549**

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# Amendment No. 2

# to

# FORM S-3

# REGISTRATION STATEMENT

***Under***

***THE SECURITIES ACT OF 1933***

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# SUPPORTSOFT, INC.

**(Exact name of registrant as specified in its charter)**

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| Delaware | 7389 | 94-3282005 |
|---|---|---|
| (State or other jurisdiction of incorporation or organization) | (Primary Standard Industrial Classification Code Number) | (I.R.S. Employer Identification No.) |

**575 Broadway**

**Redwood City, California 94063**

**(650) 556-9440**

**(Address, including zip code, and telephone number, including area code, of registrant s principal executive offices)**

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**RADHA R. BASU**

***Chief Executive Office*r**

**SUPPORTSOFT, INC.**

**575 Broadway**

**Redwood City, California 94063**

**(650) 556-9440**

**(Name, address, including zip code, and telephone number, including area code, of agent for service)**

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***Copies to:***

| | |
|---|---|
| **JORGE DEL CALVO**<br>**DAVINA K. KAILE**<br>**Pillsbury Winthrop LLP**<br>**2550 Hanover Street**<br>**Palo Alto, California 94304** | **JEFFREY D. SAPER**<br>**ROBERT G. DAY**<br>**JACK HELFAND**<br>**Wilson Sonsini Goodrich & Rosati,**<br>**Professional Corporation**<br>**650 Page Mill Road**<br>**Palo Alto, California 94304** |

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**Approximate date of commencement of proposed sale to the public:** As soon as practicable after this Registration Statement becomes effective.

If the only securities being registered on this Form are being offered pursuant to dividend or interest reinvestment plans, please check the following box. ¨

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, other than securities offered only in connection with dividend or interest reinvestment plans, check the following box. ¨

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨ ___________

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨ ___________

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box. ¨

**The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until the Registration Statement shall become effective on such date as the Securities and Exchange Commission, acting pursuant to said Section 8(a), may determine.**

**Table of Contents**

**Index to Financial Statements**

The information in this preliminary prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is declared effective. This preliminary prospectus is not an offer to sell these securities and it is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.

**Subject to Completion, Dated October 31, 2003**

# SupportSoft, Inc.

## 6,000,000 Shares

## Common Stock

This is a public offering of common stock of SupportSoft, Inc. We are offering 6,000,000 shares of our common stock. Our common stock is traded on the Nasdaq National Market under the symbol SPRT. On October 28, 2003, the last reported sale price of our common stock was $12.34 per share.

**Investing in our common stock involves risk. See Risk Factors beginning on page 5.**

**Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or passed upon the adequacy or accuracy of this prospectus. Any representation to the contrary is a criminal offense.**

| | Per Share | Total |
|---|---|---|
| Public offering price | $ | $ |
| Underwriting discounts and commissions | $ | $ |
| Proceeds, before expenses, to SupportSoft | $ | $ |

We have granted the underwriters the right to purchase up to 900,000 additional shares of our common stock to cover over-allotments.

**Deutsche Bank Securities**

**Citigroup** | **Lehman Brothers**

**First Albany Corporation** | **RBC Capital Markets**

The date of this prospectus is October , 2003.

**Table of Contents**

**Index to Financial Statements**

## PROSPECTUS SUMMARY

*You should read the summary below together with the more detailed information regarding our company and the common stock being sold in this offering appearing elsewhere in this prospectus and in our consolidated financial statements and related notes and other documents incorporated herein by reference. Except as otherwise noted, all information in this prospectus assumes the underwriters will not exercise their over-allotment option.*

### SupportSoft

We are a leading provider of support and service management software designed to accelerate and automate enterprise technical support, customer service and IT infrastructure management. We refer to this as real-time service management software. Our software solutions are utilized by enterprises to service customers, partners and employees either directly or as part of an outsourced solution from managed service providers, and by consumers and businesses through digital service providers. We believe that our real-time service management software, including its self-healing and mass-healing capabilities that preemptively diagnose and resolve software problems, allows organizations to keep up with the growing complexity and cost of IT infrastructure and related support and service problems. Organizations can benefit from our software by reducing costs and improving productivity and customer satisfaction by keeping key software and technology-based services operating and accessible on devices when using the Internet, or cable, wireless and wireline networks.

Technology has become a critical and fundamental element of business operations. The proliferation of technologies throughout an organization s business network includes personal computers and mobile devices, as well as customer-, supplier- and consumer-oriented technologies such as sales kiosks and digital service and supplier networks. We believe that organizations depend on the reliability and accessibility of their information technology, or IT, infrastructure to compete successfully. Given this dependence, organizations face increasing costs and challenges related to managing these complex, distributed and diverse technology environments. Traditional approaches to resolving support and service issues and managing IT infrastructures have proven to be inefficient and difficult to scale in meeting the requirements of consumers and business users. Our software suites and component products provide organizations with automated alternatives to the technical support and service offered today through phone support or on-site visits from technical professionals, which are typically labor intensive, time-consuming and costly.

Enterprises that have purchased our products and services include: ADP, Inc., Bank of America Corporation, Cisco Systems, Inc., IBM Corporation, The Procter & Gamble Company, Siebel Systems, Inc., Sony Electronics, Inc. and Thomson Financial Inc.; managed service providers that have purchased our products to provide outsourced services to enterprises include: Accenture Limited, Affiliated Computer Services, Inc., CompuCom Systems, Inc., Computer Sciences Corporation, IBM Global Services and Perot Systems Corporation; and digital service providers incorporating our software into their service offerings include: Adelphia Communications Corporation, BellSouth Corporation, Charter Communications, Inc., Comcast Corporation, Cox Communications, Inc., SBC Communications, Inc., TeliaSonera, AB and Time Warner Cable.

**Table of Contents**

**Index to Financial Statements**

Our objective is to be the global leader of real-time service management software for enterprises and digital service providers. Key elements of our strategy include:

- extend our support and service automation leadership;
- maintain and enhance technology leadership position;
- expand international presence;
- expand relationships with managed service providers; and
- pursue strategic acquisitions.

We were incorporated in Delaware in December 1997 under the name Replicase, Inc. We changed our name to Tioga Systems, Inc. in October 1998, to Support.com, Inc. in December 1999 and to SupportSoft, Inc. in March 2002. Our principal executive offices are located at 575 Broadway, Redwood City, California 94063 and our telephone number at this address is (650) 556-9440. Our website address is www.supportsoft.com. The information on our website is not part of this prospectus.

**Table of Contents**

**Index to Financial Statements**

**The Offering**

| | |
|---|---|
| Common stock offered by SupportSoft. | 6,000,000 shares |
| Common stock to be outstanding after this offering | 40,518,635 shares |
| Use of proceeds | For working capital and general corporate purposes, including expansion of our sales efforts and international operations. We may use a portion of the net proceeds for acquisitions of complementary businesses, products or technologies. We currently have no agreements or commitments with respect to any acquisitions. See Use of Proceeds. |
| Nasdaq National Market symbol | SPRT |

Unless otherwise indicated, the number of shares of our common stock outstanding after this offering is based on shares outstanding as of September 30, 2003 and assumes no exercise of the underwriters over-allotment option. This number does not include:

8,015,854 shares of common stock issuable upon exercise of stock options outstanding under our stock option plans as of September 30, 2003 at a weighted average exercise price of $5.43 per share;

3,765,750 shares of common stock reserved and available for future issuance under our stock option plans as of September 30, 2003; and

2,411,208 shares of common stock reserved and available for future issuance under our employee stock purchase plan as of September 30, 2003.

Table of Contents

Index to Financial Statements

**Summary Consolidated Financial Data**

**(in thousands, except share and per share data)**

| | Period From Incorporation on December 3, 1997 to December 31, 1998 | Year Ended December 31, 1999 | 2000 | 2001 | 2002 | Nine Months Ended September 30, 2002 | 2003 |
|---|---|---|---|---|---|---|---|
| | | | | | | (Unaudited) | |
| **Consolidated Statement of Operations Data:** | | | | | | | |
| Total revenue | $ 18 | $ 3,211 | $ 18,666 | $ 30,430 | $ 41,160 | $ 29,344 | $ 38,137 |
| Income (loss) from operations | (2,804) | (13,684) | (38,586) | (29,758) | (4,105) | (5,104) | 6,075 |
| Net income (loss) | (2,750) | (13,514) | (36,868) | (28,180) | (3,642) | (4,591) | 6,055 |
| Net income (loss) attributable to common stockholders | (2,964) | (14,586) | (37,753) | (28,180) | (3,642) | (4,591) | 6,055 |
| Net income (loss) per share: | | | | | | | |
| Basic | (0.57) | (2.20) | (2.09) | (0.91) | (0.11) | (0.14) | 0.18 |
| Diluted | (0.57) | (2.20) | (2.09) | (0.91) | (0.11) | (0.14) | 0.17 |
| Weighted average shares: | | | | | | | |
| Basic | 5,227 | 6,643 | 18,102 | 31,078 | 32,486 | 32,290 | 33,705 |
| Diluted | 5,227 | 6,643 | 18,102 | 31,078 | 32,486 | 32,290 | 36,404 |

| | September 30, 2003 Actual | Pro Forma as Adjusted |
|---|---|---|
| | (Unaudited) | |
| **Consolidated Balance Sheet Data:** | | |
| Cash, cash equivalents and short-term investments | $ 37,406 | $ 106,759 |
| Working capital | 32,839 | 102,192 |
| Total assets | 55,382 | 124,735 |
| Total stockholders equity | 31,926 | 101,279 |

The statement of operations for the year ended December 31, 1998 is presented for the period from our incorporation on December 3, 1997. Operating expenses totaled approximately $9,000 for the period from our incorporation on December 3, 1997 to December 31, 1997.

Please see note 1 of the notes to the financial statements for an explanation of the determination of the number of shares used in computing per share data.

The pro forma as adjusted balance sheet data assumes the sale of the 6,000,000 shares of common stock that we are offering under this prospectus at an assumed public offering price of $12.34 per share and the deduction of the estimated underwriting discounts and commissions and estimated offering expenses payable by us.

**Table of Contents**

**Index to Financial Statements**

## RISK FACTORS

*You should read carefully this entire prospectus, as well as the documents incorporated by reference in this prospectus, before making an investment decision. You should carefully consider the risk factors described below, as well as the factors listed in Forward-Looking Statements.*

### Risks Related to Our Business

**Our quarterly results are difficult to predict and may fluctuate, which may cause our stock price to decline.**

Our quarterly revenue and operating results are difficult to predict and may fluctuate from quarter to quarter. As a result, we believe that quarter-to-quarter and year-to-year comparisons of our revenue and operating results are not necessarily meaningful, and that these comparisons may not be accurate indicators of future performance. Our operating results in some quarters may fall below our guidance or the expectations of securities analysts or investors, which would likely cause the market price of our common stock to decline.

Several factors that have contributed or may in the future contribute to fluctuations in our operating results include:

- demand for our support and service automation software;
- size and timing of customer orders and our ability to receive payment and recognize revenue in a given quarter;
- the mix of license revenue from perpetual arrangements with up-front recognition versus license revenue from ratable arrangements;
- the price and mix of products and services we or our competitors offer;
- our ability to attract and retain customers;
- the amount and timing of operating costs and capital expenditures relating to expansion of our business, infrastructure and marketing activities;
- general economic conditions and their affect on our operations; and

the effects of external events such as terrorist acts and any related conflicts or similar events worldwide.

We license our support and service automation software under perpetual and term licenses. Perpetual licenses typically result in our immediate recognition of a larger amount of revenue in the particular quarter or period in which we grant the license and deliver the product as compared with term licenses. Revenue from a term license is recognized ratably on a monthly basis over the agreement term, which is typically three years. In addition, we typically derive a significant portion of our revenue each quarter from a number of orders received in the last month of a quarter. If we fail to close orders expected to be completed toward the end of a quarter, particularly if these orders are for perpetual licenses, which are representing an increasing percentage of our revenue, or if there is any cancellation of or delay in the closing of orders, particularly any large customer orders, our quarterly results would suffer.

**Table of Contents**

**Index to Financial Statements**

**Because a small number of customers have historically accounted for and may in future periods account for substantial portions of our revenue, our revenue could decline because of delays of customer orders.**

A small number of customers have historically accounted for, and may in future periods account for, substantial portions of our revenue in any given quarter. For example, two, one and three customers accounted for 56%, 49% and 40% of our total revenue in the three months ended September 30, 2003, June 30, 2003 and March 31, 2003, respectively. One customer accounted for 16% of our total revenue and another customer accounted for 12% of our total revenue for the nine months ended September 30, 2003. Because a small number of customers are likely to continue to account for a significant portion of our revenue in any given quarter, our revenue could decline because of the loss or delay of a single customer order or the failure of an existing customer to renew its term license. We may not obtain additional customers. The failure to obtain additional customers, particularly customers that purchase perpetual licenses, the loss or delay of customer orders and the failure of existing customers to renew licenses or pay fees due would harm our operating results.

**We have a history of losses and only recently became profitable on a quarterly basis and may not maintain profitability.**

We incurred net losses of approximately $78.9 million for the period from December 3, 1997 through September 30, 2003 and have only been profitable on a quarterly basis since the third quarter of 2002. If we fail to sustain or increase profitability, we may not be able to increase our number of employees in sales, marketing and research and development programs or increase our investments in capital equipment or otherwise execute our business plan.

**Our sales cycle can be lengthy and if revenue forecasted for a particular quarter is not realized in that quarter, significant expenses incurred may not be offset by corresponding sales.**

Our sales cycle for our support and service automation software typically ranges from three to nine months or more and may vary substantially from customer to customer. The purchase of our products and services generally involves a significant commitment of capital and other resources by a customer. This commitment often requires significant technical review, assessment of competitive products and approval at a number of management levels within a customer s organization. While our customers are evaluating our products and services, we may incur substantial sales and marketing expenses and spend significant management effort to complete these sales. Any delay in completing sales in a particular quarter could cause our operating results to be below expectations.

**We must achieve broad adoption and acceptance of our support and service automation products and services or we will not increase our market share or expand our business.**

We must achieve broad market acceptance and adoption of our products and services or our business and operating results will suffer. Specifically, we must encourage our customers to transition from using traditional support and service methods to our support and service automation solutions. To accomplish this, we must:

continually improve the performance, features and reliability of our products and services to address changing industry standards and customer needs; and

develop integration with other support-related technologies.

**Table of Contents**

**Index to Financial Statements**

**If we fail to manage growth in our business effectively, then our infrastructure, management and resources might be strained and our ability to manage our business could be diminished.**

If we experience rapid growth in the future, it will likely place a significant strain on our resources. For example, we are currently planning to hire additional sales, marketing and development personnel. Competition for the hiring of qualified employees in these areas is intense, and we may be unable to attract and retain the required personnel to meet our business objectives. In addition, if we experience significant and rapid growth, we may need to expand and otherwise improve our internal systems, including our management information systems, customer relationship and support systems, and operating, administrative and financial systems and controls. This effort may cause us to make significant capital expenditures or incur significant expenses, and divert the attention of management, sales, support and finance personnel from our core business operations, which may adversely affect our financial performance in one or more quarters. Moreover, our growth has resulted, and any future growth will result, in increased responsibilities of management personnel. Managing this growth will require substantial resources that we may not have or otherwise be able to obtain.

**We are expanding our international operations and if our revenue from this effort does not exceed the expense of establishing and maintaining international operations, our business could suffer.**

We are expanding the sales and marketing of our products and services and our operations into international markets, including in Europe and Asia. For example, we have recently opened a new office in India to conduct research and development. We have incurred and expect to incur costs and expend resources associated with commencing operations in a foreign country. We have limited experience in international operations and may not be able to compete effectively in international markets. If we do not generate enough revenue from international operations to offset the expense of these operations, our business and our ability to increase revenue and enhance our operating results could suffer. Risks we face in conducting business internationally include:

- difficulties and costs of staffing and managing international operations;
- differing technology standards and legal considerations;
- longer sales cycles and collection periods;
- dependence on local vendors;
- difficulties in staffing and managing international operations, including the difficulty in managing a geographically dispersed workforce in compliance with diverse local laws and custom;
- potential adverse tax consequences;
- changes in currency exchange rates and controls;

restrictions on repatriation of earnings from our international operations; and

the effects of external events such as terrorist acts and any related conflicts or similar events worldwide.

**If our existing customers do not renew term licenses or maintenance services or purchase additional products, our operating results could suffer.**

Historically, we have derived, and expect to continue to derive, a significant portion of our total revenue from existing customers who purchase additional products and renew term

7

**Table of Contents**

**Index to Financial Statements**

licenses and maintenance services. A significant portion of our customers license our products under term licenses, which typically cover a period of three years. Our customers may not renew term licenses or maintenance services, purchase additional products and may not expand their use of our products. In addition, as we deploy new versions of our products or introduce new products, our current customers may not require or desire the functionality of our new products and may not ultimately purchase these products. If our customers do not renew term licenses or maintenance services or do not purchase additional products, our revenue levels and operating results could suffer.

**Our product innovations may not achieve the market penetration necessary for us to expand our market share.**

If we fail to develop new or enhanced versions of our support and service automation software in a timely manner or to provide new products and services that achieve rapid and broad market acceptance, we may not maintain or expand our market share. We may fail to identify new product and service opportunities for our current market or new markets that we enter into in the future. For example, in the near term, we intend to expand our business with managed service providers. In addition, our existing products will become obsolete if we fail to introduce new products or product enhancements that meet new customer demands, support new standards or integrate with new or upgraded versions of packaged applications. We have limited control over factors that affect market acceptance of our product and services, including:

- the willingness of enterprises, including management service providers, to transition to support and service automation solutions; and

- acceptance of competitors support and service automation solutions or other similar technologies.

**Our software may not operate with the hardware and software platforms that are used by our customers now or in the future, and as a result our business and operating results may suffer.**

We currently serve a customer base with a wide variety of constantly changing hardware, packaged software applications and networking platforms. Our applications are based on the Microsoft, Linux and Unix operating systems, and if we fail to release versions of our support and service automation software that are compatible with other operating systems, software applications or hardware devices used by our customers, our business and operating results would suffer. Our future success also depends on:

- the ability of our product to inter-operate with multiple platforms and to modify our product as new versions of packaged applications are introduced and used by our customer base; and

- our management of software being developed by third parties for our customers or for use with our products.

**Table of Contents**

**Index to Financial Statements**

**We may engage in investments or acquisitions that could divert management attention and prove difficult to integrate with our business and technology.**

We may engage in investments in, or acquisitions of, complementary companies, products or technologies. If we fail to integrate successfully any future acquisitions, or the technologies associated with such acquisitions, into our company, the revenue and operating results of the combined company could decline. The process of integrating an acquired business, technology, service or product into our business and operations may result in unforeseen operating difficulties and expenditures. Acquisitions involve a number of other potential risks to our business, including the following:

- potential adverse effects on our operating results, including unanticipated costs and liabilities, unforeseen accounting charges or fluctuations resulting from failure to accurately forecast the financial impact of an acquisition;
- failure to integrate acquired products or technologies with our existing products, technologies and business model;
- failure to integrate management information systems, personnel, research and development and marketing, sales and support operations;
- potential loss of key employees from the acquired company;
- diversion of management s attention from other business concerns and disruption of our ongoing business;
- difficulty in maintaining controls and procedures;
- potential loss of the acquired company s customers;
- uncertainty on the part of our existing customers about our ability to operate on a combined basis;
- failure to realize the potential financial or strategic benefits of the acquisition; and
- failure to successfully further develop the acquired company s technology, resulting in the impairment of amounts capitalized as intangible assets.

**We rely on third-party technologies and our inability to use or integrate third-party technologies could delay product or service development.**

We intend to continue to license technologies from third parties, including applications used in our research and development activities and technologies such as third-party search engine technology, which are integrated into our products and services. Our inability to obtain or integrate any of these technologies with our own products could delay product and service development until equivalent technology can be identified, licensed and integrated. These technologies may not continue to be available to us on commercially reasonable terms or at all. We may fail to successfully integrate any licensed technology into our products or services, which would harm our business and operating results. Third-party licenses also expose us to increased risks that include:

- risks of product malfunction after new technology is integrated;
- the diversion of resources from the development of our own proprietary technology; and
- our inability to generate revenue from new technology sufficient to offset associated acquisition and maintenance costs.

**Table of Contents**

**Index to Financial Statements**

**Our failure to establish and expand third-party alliances would harm our ability to sell our support and service automation software.**

We have several alliances with third parties that are important to our business. Our existing relationships include those with software and hardware vendors, and relationships with companies who provide outsourced support and service capabilities to enterprise customers. If these relationships fail, we may have to devote substantially more resources to the sales and marketing of our products and services than we would otherwise, and our efforts may not be as effective. For example, companies that provide outsourced support and services often have extensive relationships with our existing and potential customers and significant input in the purchase decisions of these customers. Our failure to maintain these existing technology relationships, or to establish new technology relationships with key third parties, could significantly harm our ability to sell our products and services.

**We may need additional capital and if funds are not available on acceptable terms, we may not be able to hire and retain employees, fund our expansion or compete effectively.**

We believe that our existing capital resources will enable us to maintain our operations for at least the next 12 months. However, if our capital requirements vary materially from those currently planned, we may require additional financing sooner than anticipated. This financing may not be available in sufficient amounts or on terms acceptable to us and may be dilutive to existing stockholders. If adequate funds are not available or are not available on acceptable terms, our ability to hire, train or retain employees, fund our expansion, take advantage of business opportunities, develop or enhance services or products or respond to competitive pressures would be significantly limited.

**We may lose the services of our key personnel, which in turn would harm the market s perception of our business and our ability to achieve our business goals.**

Our success will depend on the skills, experience and performance of our senior management, engineering, sales, marketing and other key personnel. The loss of the services of any of our senior management or other key personnel, including Radha R. Basu, our president, chief executive officer and chairman, Brian Beattie, our executive vice president of finance and administration and chief financial officer, Scott W. Dale, our vice president of engineering and chief technical officer and Cadir B. Lee, our chief software officer, as well as Chris Grejtak, our senior vice president of marketing and chief marketing officer, and John Van Siclen, our senior vice president of worldwide field operations, both of whom joined us recently, could harm the market s perception of our business and our ability to achieve our business goals. In addition, if the integration of new members of our senior management team does not go as smoothly as anticipated, it could negatively affect our ability to execute our business plans.

**We must compete successfully in the support and service automation market or we will lose market share and our business will suffer.**

We compete in markets that are highly competitive, subject to rapid change and significantly affected by new product introductions and other market activities of industry participants. We compete with a number of companies in the market for automated delivery of support and service and other vendors who may offer products or services with features that compete with specific elements of our software suites or with our component products. In addition, our customers and potential customers have developed or may develop support and service automation software systems in-house. We expect that internally developed applications will continue to be a principal source of competition in the foreseeable future.

**Table of Contents**

**Index to Financial Statements**

The markets for our products are still rapidly evolving, and we may not be able to compete successfully against current and potential competitors. Our ability to expand our business will depend on our ability to maintain our technological advantage, introduce timely enhanced products to meet the growing support needs, deliver on-going value to our customers and scale our business. Our potential competitors may have longer operating histories, significantly greater financial, technical and other resources or greater name recognition than we do. Competition in our markets could reduce our market share or require us to reduce the price of products and services, which could harm our business, financial condition and operating results.

**Our system security is important to our customers and we may need to spend significant resources to protect against or correct problems caused by security breaches.**

A fundamental requirement for online communications, transactions and support is the secure transmission of confidential information. Third parties may attempt to breach our security or that of our customers. We may be liable to our customers for any breach in security and any breach could harm our business and reputation. Also, computers are vulnerable to computer viruses, physical or electronic break-ins and similar disruptions, which could lead to interruptions, delays or loss of data. We may be required to expend significant capital and other resources to further protect against security breaches or to correct problems caused by any breach.

**We may face claims of invasion of privacy or inappropriate disclosure, use or loss of our customers information and any liability imposed could harm our reputation and cause us to lose customers.**

Our software contains features which may allow us or our customers to control, monitor or collect information from computers running the software without notice to the computing users. Therefore we may face claims about invasion of privacy or inappropriate disclosure, use or loss of this information. Any imposition of liability could harm our reputation, cause us to lose customers and cause our operating results to suffer.

**Any system failure that causes an interruption in our customers ability to use our products or services or a decrease in their performance could harm our relationships with our customers and result in reduced revenue.**

Our software may depend on the uninterrupted operation of our internal and outsourced communications and computer systems. These systems are vulnerable to damage or interruption from computer viruses, human error, natural disasters, electricity grid failures and intentional acts of vandalism and similar events. Our disaster recovery plan may not be adequate and business interruption insurance may not be enough to compensate us for losses that occur. These problems could interrupt our customers ability to use our support and service automation products or services, which could harm our reputation and cause us to lose customers and revenue.

**We may not obtain sufficient patent protection, which could harm our competitive position, increase our expenses and harm our business.**

Our success and ability to compete depend to a significant degree upon the protection of our software and other proprietary technology. It is possible that:

- our pending patent applications may not be issued;
- competitors may independently develop similar technologies or design around any of our patents;

11

**Table of Contents**

**Index to Financial Statements**

- patents issued to us may not be broad enough to protect our proprietary rights; and
- our issued patents could be successfully challenged.

**Our products depend on and work with products containing complex software and if our products fail to perform properly due to errors in the software, we may need to devote resources to correct the errors or compensate for losses from these errors and our reputation could be harmed.**

Our products depend on complex software, both internally developed and licensed from third parties. Also, our customers may use our products with other companies products which also contain complex software. Complex software often contains errors and may not perform properly. These errors could result in:

- delays in product shipments;
- unexpected expenses and diversion of resources to identify the source of errors or to correct errors;
- damage to our reputation;
- lost sales;
- demands, claims and litigation and related defense costs; and
- product returns, refunds or other damages claims.

If our products fail to perform properly due to errors, bugs or similar problems in the software, we could be required to devote valuable resources to correct the errors or compensate for losses from these errors. Furthermore, if our products are found to contain errors or bugs, whether resulting from internally developed or third-party licensed software, our reputation with our customer base could be harmed and our business could suffer.

**We rely upon trademarks, copyrights and trade secrets to protect our proprietary rights and if these rights are not sufficiently protected, it could harm our ability to compete and to generate revenue.**

We rely on a combination of laws, such as patents, copyright, trademark and trade secret laws, and contractual restrictions, such as confidentiality agreements and licenses, to establish and protect our proprietary rights. Our ability to compete and grow our business could suffer if these rights are not adequately protected. Our proprietary rights may not be adequately protected because:

laws and contractual restrictions may not adequately prevent misappropriation of our technologies or deter others from developing similar technologies; and

policing unauthorized use of our products and trademarks is difficult, expensive and time-consuming, and we may be unable to determine the existence or extent of this unauthorized use.

Also, the laws of other countries in which we market our products may offer little or no protection of our proprietary technologies. Reverse engineering, unauthorized copying or other misappropriation of our proprietary technologies could enable third parties to benefit from our technologies without paying us for them, which would harm our competitive position and market share.

**Table of Contents**

**Index to Financial Statements**

**We may face intellectual property infringement claims that could be costly to defend and result in our loss of significant rights.**

Other parties may assert intellectual property infringement claims against us or our customers and our products may infringe the intellectual property rights of third parties. Intellectual property litigation is expensive and time-consuming and could divert management s attention from our business. If there is a successful claim of infringement, we may be required to develop non-infringing technology or enter into royalty or license agreements which may not be available on acceptable terms, if at all. Our failure to develop non-infringing technologies or license the proprietary rights on a timely basis would harm our business.

## Risks Related To Our Industry

**Because our support and service automation software is designed to support businesses operating over the Internet, our success depends on the continued growth and levels of performance of Internet usage.**

Because a majority of our products are designed to support businesses operating over or benefiting from the Internet, the success of our business will depend on the continued improvement of the Internet as a convenient means of consumer interaction and commerce, as well as an efficient medium for the delivery and distribution of information by enterprises to their employees and extended enterprise. Because global commerce on the Internet and the online exchange of information is evolving, we cannot predict whether the Internet will continue to be a viable commercial marketplace or whether access to the Internet via a broadband connection will continue to be widely adopted.

**We may experience a decrease in market demand due to uncertain economic conditions in the United States and in international markets, which has been further exacerbated by the concerns of terrorism, war and social and political instability.**

Economic growth in the United States and international markets has slowed significantly and the United States economy has been in a recession. The timing of a full economic recovery is uncertain. In addition, the terrorists attacks in the United States and turmoil in the Middle East have increased the uncertainty in the United States economy and may further exacerbate the decline in economic conditions, both domestically and internationally. Terrorist acts and similar events, or war in general, could contribute further to a slowdown of the market demand for goods and services, including support and service automation software. If the economy declines as a result of the recent economic, political and social turmoil, or if there are further terrorist attacks in the United States or elsewhere, we may experience decreases in the demand for our products and services, which may harm our operating results.

**Governmental regulation and legal changes could impair the growth of the Internet and decrease demand for our products or increase our cost of doing business.**

The laws and regulations that govern our business can change rapidly. Any change in laws and regulations could impair the growth of the Internet and could reduce demand for our products, subject us to liability or increase our cost of doing business. The United States government and the governments of states and foreign countries have attempted to regulate activities on the Internet and the distribution of software. Also, in 1998, the Internet Freedom Act was enacted into law, which imposed a three-year moratorium on state and local taxes on Internet-based transactions. In late 2001, this moratorium was extended for two years. In

**Table of Contents**

**Index to Financial Statements**

January 2003, several members of Congress proposed a bill that would make the moratorium on state and local taxes on Internet-based transactions permanent. Failure to renew this moratorium or to pass a bill that would permanently prohibit state and local taxes on Internet-based transactions would allow states to impose taxes on Internet-based commerce. This might harm our business directly and indirectly by harming the businesses of our customers, potential customers and the parties to our technology relationships. The applicability to the Internet of existing laws is uncertain and may take years to resolve. Evolving areas of law that are relevant to our business include privacy laws, intellectual property laws, proposed encryption laws, content regulation and sales and use tax laws and regulations.

**We may be required to change our business practices if there are changes in accounting regulations and related interpretations and policies.**

Accounting standards groups and regulators are actively re-examining various accounting policies, guidelines and interpretations related to revenue recognition, expensing stock options, income taxes, investments in equity securities, facilities consolidation, accounting for acquisitions, allowances for doubtful accounts and other financial reporting matters. These standards groups and regulators could promulgate interpretations and guidance that could result in material and potentially adverse changes to our business practices and accounting policies.

**New rules and regulations for public companies may increase our administrative costs.**

The Sarbanes-Oxley Act of 2002, as well as new rules subsequently implemented by the Securities and Exchange Commission, have required changes in corporate governance practices of public companies. In addition to final rules and rule proposals already made by the Securities and Exchange Commission, Nasdaq has proposed revisions to its requirements for listed companies. We expect these new rules and regulations to increase our legal and financial compliance costs, and to make some activities more time-consuming and costly. We also expect these new rules and regulations to make it more difficult and more expensive for us to obtain director and officer liability insurance, and we may be required to accept reduced coverage or incur substantially higher costs to obtain coverage. These new rules and regulations could also make it more difficult for us to attract and retain qualified members of our board of directors, particularly to serve on our audit committee, and qualified executive officers.

## Risks Related to this Offering and Our Common Stock

**The market price for our common stock may be particularly volatile, and our stockholders may be unable to resell their shares at a profit.**

The market price of our common stock has been subject to significant fluctuations and may continue to fluctuate or decline. The stock markets have experienced significant price and trading volume fluctuations. The market for technology stocks has been particularly volatile and frequently reaches levels that bear no relationship to the past or present operating performance of those companies. General economic conditions, such as recession or interest rate or currency rate fluctuations in the United States or abroad, could negatively affect the market price of our common stock. In addition, our operating results may not meet the expectations of securities analysts and investors. If this were to occur, the market price of our common stock would likely significantly decrease.

14

[Table of Contents](#)

[Index to Financial Statements](#)

**A decline in our stock price could result in securities class action litigation against us. Securities class action litigation diverts management attention and could harm our business.**

In the past, securities class action litigation has often been brought against public companies after periods of volatility in the market price of securities. For example, in November 2001, a securities class action lawsuit was filed against us. We may again in the future be a target of similar litigation. Securities litigation could result in substantial costs and divert management s attention and resources, which could harm our ability to execute our business plan.

**As a new investor, you will incur immediate and substantial dilution as a result of this offering and future equity issuances.**

The public offering price is substantially higher than the pro forma book value per share of our common stock. As a result, investors purchasing common stock in this offering at a public offering price of $12.34 per share will incur immediate dilution of $9.84 in net tangible book value per share. This dilution is due in large part to earlier investors in our company having paid less than the offering price when they purchased their shares. Investors will incur additional dilution upon the exercise of outstanding stock options.

**You will be relying on our management s judgment, with which you may disagree, regarding the use of proceeds from this offering. If our management does not use the proceeds in a manner that increases our operating results or market value, our business could suffer.**

We do not have a definite, quantified plan with respect to the use of the net proceeds from this offering and have not committed the substantial majority of these proceeds to any particular purpose, as more fully described in the section entitled Use of Proceeds. Accordingly, our management will have broad discretion as to the use of the net proceeds from this offering. Investors will be relying on the judgment of our management regarding the application of these proceeds, and we may not be able to invest these proceeds to yield a significant return. We have made only preliminary determinations as to the amount of net proceeds to be used based on our current expectations regarding our financial performance and business needs over the foreseeable future. These expectations may prove to be inaccurate, as our financial performance may differ from our current expectations or our business needs may change as our business and the industry we address evolve. As a result, the proceeds we receive in this offering may be used in a manner significantly different from our current plans.

**Our directors and executive officers own a significant portion of our common stock and this concentration of ownership may allow them to elect most of our directors and could delay or prevent a change in control of SupportSoft.**

Our directors and executive officers collectively beneficially own approximately 17% of our outstanding common stock as of September 30, 2003. These stockholders, if they vote together, will be able to influence significantly all matters requiring stockholder approval. For example, they may be able to elect most of our directors, delay or prevent a transaction in which stockholders might receive a premium over the market price for their shares or prevent changes in control or management.

**We have implemented anti-takeover provisions that could make it more difficult to acquire us.**

Our certificate of incorporation, our bylaws and Delaware law contain provisions that may inhibit potential acquisition bids for us and prevent changes in our management. Certain provisions of our charter documents could discourage potential acquisition proposals and could

**Table of Contents**

**Index to Financial Statements**

delay or prevent a change in control transaction. These provisions of our charter documents could have the effect of discouraging others from making tender offers for our shares, and as a result, these provisions may prevent the market price of our common stock from reflecting the effects of actual or rumored takeover attempts. These provisions may also prevent changes in our management.

These provisions include:

- authorizing only our chief executive officer or a majority of our board of directors to call special meetings of stockholders;
- establishing advance notice procedures with respect to stockholder proposals and the nomination of candidates for election of directors, other than nominations made by or at the direction of the board of directors or a committee of the board of directors;
- prohibiting stockholders action by written consent;
- eliminating cumulative voting in the election of directors; and
- authorizing the issuance of shares of undesignated preferred stock without a vote of stockholders.

**Table of Contents**

**Index to Financial Statements**

## FORWARD-LOOKING STATEMENTS

This prospectus contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These forward-looking statements may be identified by terminology such as may, will, could, should, intend, anticipate, believe, estimate, expect, plan, potential, designed to, or continue and the negative of these terms or other similar expressions. These are statements that relate to future events and include, but are not limited to, statements relating to industry statistics and projections and statements relating to:

- our expectation that we will continue to depend upon a small number of large orders for a significant portion of our license revenue;
- our current estimate that revenue from ratable licensing arrangements will represent approximately 25% to 30% of total revenue over the next 12 months;
- our current estimate that revenue we recognize on an immediate basis from perpetual licensing arrangements will be approximately 45% to 55% of total revenue over the next 12 months;
- our current estimate that revenue from services will represent approximately 20% to 25% of total revenue over the next 12 months;
- our ability to maintain or increase profitability;
- our expectation as to the anticipated impact on us of new rules and regulations applicable to public companies;
- our ability to attract and retain key personnel;
- our future contractual obligations and the effect these contractual obligations are expected to have on our liquidity and cash flows in future periods;
- our belief that there is not material market risk exposure due to the nature of our cash equivalents and short-term investments;
- our expectation that we will continue to devote significant resources to research and development for the foreseeable future;
- our intent to hire additional sales, marketing and development personnel and expand our sales and marketing efforts and international operations;

our future capital requirements and our belief as to the adequacy of our existing cash balances and capital resources;

our anticipated use of the net proceeds from this offering;

our intent to expand in new and existing markets, including beyond broadband services into related applications and enhanced services;

future acquisitions of, or investments in, complementary businesses, products or technologies;

our ability to compete successfully;

our dividend policy;

our intent to establish, and the anticipated benefits of entering into, alliances with software and hardware vendors, alliances with managed service providers and technology alliances;

**Table of Contents**

**Index to Financial Statements**

- our beliefs as to our market opportunity to automate the technical support, customer service and IT infrastructure management processes;

- our intention to extend our support and service automation, maintain and enhance our technology leadership position and to expand into related applications and enhanced digital services;

- our intention to continue to invest significant resources to technology development and to introduce new suites and component products that facilitate real-time service management; and

- our intention to release our Service Automation Suite Video by the end of 2003 and the anticipated features and benefits of our products and services.

Forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from those discussed in these forward-looking statements. These risks and uncertainties include, but are not limited to, the risks set forth above under the caption Risk Factors and from time to time in the periodic reports we file with the Securities and Exchange Commission.

Except for our obligations under the federal securities laws, we expressly disclaim any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained herein to reflect any change in our expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based.

**Table of Contents**

**Index to Financial Statements**

## USE OF PROCEEDS

The net proceeds to us from the sale of the 6,000,000 shares of common stock being offered by us are estimated to be approximately $69.4 million, based upon an assumed public offering price of $12.34 per share and after deducting the estimated underwriting discounts and commissions and estimated offering expenses payable by us. If the underwriters fully exercise the over-allotment option, the net proceeds to us are estimated to be approximately $79.9 million.

We expect to use the net proceeds of this offering for working capital and general corporate purposes, including expansion of our sales efforts and international operations. In addition we may use a portion of these net proceeds for acquisitions of complementary businesses, products or technologies. We currently have no agreements or commitments with respect to any such acquisition, and we are not involved in any negotiations with respect to any such transactions. Pending these uses, we intend to invest the net proceeds of the offering in investment grade interest bearing marketable securities.

## DIVIDEND POLICY

We have not declared or paid any cash dividends on our capital stock since our inception and do not expect to do so in the foreseeable future. We anticipate that all future earnings, if any, generated from operations will be retained by us to develop and expand our business. Any future determination with respect to the payment of dividends will be at the discretion of the board of directors and will depend upon, among other things, our operating results, financial condition and capital requirements, the terms of then-existing indebtedness, general business conditions and such other factors as the board of directors deems relevant.

**Table of Contents**

**Index to Financial Statements**

**PRICE RANGE OF COMMON STOCK**

Our common stock has been traded publicly on the Nasdaq National Market under the symbol SPRT since July 19, 2000. Before July 19, 2000, there was no public market for our common stock. The following table sets forth the highest and lowest sale price of our common stock for the quarters indicated:

| | High | Low |
|---|---|---|
| **2001:** | | |
| First Quarter | $ 20.19 | $ 4.00 |
| Second Quarter | 7.65 | 2.50 |
| Third Quarter | 6.41 | 2.04 |
| Fourth Quarter | 6.50 | 2.00 |
| **2002:** | | |
| First Quarter | $ 8.05 | $ 3.02 |
| Second Quarter | 4.87 | 2.55 |
| Third Quarter | 2.84 | 1.75 |
| Fourth Quarter | 4.00 | 1.95 |
| **2003:** | | |
| First Quarter | $ 4.29 | $ 1.89 |
| Second Quarter | 7.81 | 2.20 |
| Third Quarter | 12.05 | 6.25 |
| Fourth Quarter (through October 28) | 13.97 | 10.69 |

**Holders of Record**

On October 28, 2003, the last reported sale price of our common stock on the Nasdaq National Market was $12.34 per share. As of September 30, 2003, there were approximately 337 holders of record (not including beneficial holders of stock held in street name) of the common stock.

**Table of Contents**

**Index to Financial Statements**

**CAPITALIZATION**

This table presents our capitalization at September 30, 2003:

on an actual basis; and

on an as adjusted basis to reflect the sale by us of 6,000,000 shares of common stock at an assumed public offering price of $12.34 per share in this offering, less the estimated underwriting discounts and commissions and estimated offering expenses.

| | As of September 30, 2003 | |
|---|---|---|
| | Actual | As Adjusted |
| | (Unaudited) (in thousands) | |
| Long-term capital lease obligations | $ | $ |
| Stockholders equity: | | |
| Preferred stock: $0.0001 par value; 5,000,000 shares authorized; no shares issued and outstanding | | |
| Common stock: $0.0001 par value; 150,000,000 shares authorized; 34,518,635 actual shares issued and outstanding, 40,518,635 shares issued and outstanding, as adjusted | 3 | 4 |
| Additional paid-in capital | 110,765 | 180,117 |
| Accumulated other comprehensive income | 57 | 57 |
| Accumulated deficit | (78,899) | (78,899) |
| Total stockholders equity | 31,926 | 101,279 |
| Total capitalization | $ 31,926 | $ 101,279 |

The above table does not include additional shares of common stock that may be issued under the plans and arrangements listed below:

8,015,854 shares of common stock issuable upon exercise of options outstanding under our stock option plans as of September 30, 2003, at a weighted average exercise price of $5.43 per share; and

2,411,208 shares of common stock reserved for future issuance under our employee stock purchase plan as of September 30, 2003, and 3,765,750 shares reserved for future issuance under our stock option plans.

You should read the capitalization information above together with the sections of this prospectus entitled Selected Financial Data, Management s Discussion and Analysis of Financial Condition and Results of Operations and Description of Capital Stock and our consolidated financial statements and related notes found elsewhere or incorporated by reference in this prospectus.

**Table of Contents**

**Index to Financial Statements**

**DILUTION**

Our net tangible book value as of September 30, 2003 was approximately $31.9 million, or $0.92 per share. Net tangible book value per share is equal to our total tangible assets less our total liabilities, divided by the total number of shares of our common stock outstanding.

After giving effect to the receipt of the proceeds from this offering, based on an assumed public offering price of $12.34 per share, and after deducting estimated underwriting discounts and commissions and estimated offering expenses, our as adjusted net tangible book value as of September 30, 2003 would have been approximately $101.3 million, or approximately $2.50 per share. This represents an immediate increase in net tangible book value of $1.58 per share to existing stockholders and an immediate dilution of $9.84 per share to new investors purchasing shares of our common stock in this offering.

The following table illustrates the per share dilution to the new investors:

| | | |
|---|---|---|
| Assumed public offering price per share | | $ 12.34 |
| Net tangible book value per share as of September 30, 2003 | $ 0.92 | |
| Increase in net tangible book value per share attributable to this offering | 1.58 | |
| As adjusted net tangible book value per share as adjusted after offering | | 2.50 |
| Dilution per share to new investors in this offering | | $ 9.84 |

If the underwriters exercise their over-allotment option in full, there will be an increase in as adjusted net tangible book value of $1.78 per share to existing stockholders and an immediate dilution in as adjusted net tangible book value of $9.64 per share to new investors.

The preceding discussion and table assume that no stock options outstanding as of September 30, 2003, are exercised and that none of the 2,411,208 shares reserved for issuance under our employee stock purchase plan as of September 30, 2003, are issued. As of September 30, 2003, there were 8,015,854 shares issuable on exercise of outstanding options, at a weighted average exercise price of $5.43 per share.

**Table of Contents**

**Index to Financial Statements**

**SELECTED CONSOLIDATED FINANCIAL DATA**

**(in thousands, except share and per share data)**

Our selected consolidated financial data set forth below as of December 31, 2001 and 2002 and for each of the three years ended December 31, 2002 are derived from our consolidated financial statements that have been audited by Ernst & Young LLP, independent accountants, and are included elsewhere in this prospectus. Our selected consolidated financial data set forth below as of December 31, 1998, 1999 and 2000 and for the period from our incorporation on December 3, 1997 to December 31, 1998 and for the year ended December 31, 1999 are derived from our audited consolidated financial statements not included elsewhere herein. Our selected consolidated financial data as of September 30, 2003 and for the nine months ended September 30, 2002 and 2003 are derived from our unaudited consolidated financial statements which, in management s opinion, include all adjustments, consisting only of normal recurring adjustments, necessary for the fair presentation of our financial position and results of operations for those periods, included elsewhere in this prospectus. The information set forth below is not necessarily indicative of results of future operations and should be read together with Management s Discussion and Analysis of Financial Condition and Results of Operations and the consolidated financial statements and related notes.

| | Period from Incorporation on December 3, 1997 to December 31, | Year Ended December 31, | | | | Nine Months Ended September 30, | |
|---|---|---|---|---|---|---|---|
| | 1998 | 1999 | 2000 | 2001 | 2002 | 2002 | 2003 |
| | | | | | | (Unaudited) | |
| **Consolidated Statements of Operations Data:** | | | | | | | |
| Revenue: | | | | | | | |
| License fees | $ 18 | $ 2,642 | $ 13,732 | $ 22,534 | $ 31,260 | $ 22,148 | $ 29,686 |
| Services | | 569 | 4,934 | 7,896 | 9,900 | 7,196 | 8,451 |
| Total revenue | 18 | 3,211 | 18,666 | 30,430 | 41,160 | 29,344 | 38,137 |
| Costs and expenses: | | | | | | | |
| Cost of license fees | | 4 | 1,405 | 621 | 289 | 197 | 270 |
| Cost of services | | 965 | 5,910 | 6,234 | 5,883 | 4,384 | 4,990 |
| Amortization of purchased technology | | | 1,158 | 2,812 | 1,580 | 1,581 | |
| Research and development | 1,132 | 2,348 | 10,913 | 12,637 | 8,834 | 6,698 | 6,818 |
| Sales and marketing | 1,197 | 7,924 | 22,754 | 27,482 | 22,464 | 16,833 | 16,059 |
| General and administrative | 451 | 1,845 | 4,325 | 6,131 | 5,637 | 4,177 | 3,925 |
| Amortization of deferred compensation | 42 | 3,809 | 10,787 | 4,271 | 578 | 578 | |
| Total costs and expenses | 2,822 | 16,895 | 57,252 | 60,188 | 45,265 | 34,448 | 32,062 |
| Income (loss) from operations | (2,804) | (13,684) | (38,586) | (29,758) | (4,105) | (5,104) | 6,075 |
| Interest income and other, net | 54 | 170 | 1,718 | 1,578 | 640 | 513 | 311 |
| Income (loss) before income taxes | (2,750) | (13,514) | (36,868) | (28,180) | (3,465) | (4,591) | 6,386 |
| Income tax expense | | | | | (177) | | (331) |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Net income (loss) | (2,750) | (13,514) | (36,868) | (28,180) | (3,642) | (4,591) | 6,055 |
| Accretion on redeemable convertible preferred stock | (214) | (1,072) | (885) | | | | |
| Net income (loss) attributable to common stockholders | $ (2,964) | $ (14,586) | $ (37,753) | $ (28,180) | $ (3,642) | $ (4,591) | $ 6,055 |
| Basic net income (loss) per share attributable to common stockholders | $ (0.57) | $ (2.20) | $ (2.09) | $ (0.91) | $ (0.11) | $ (0.14) | $ 0.18 |
| Shares used in computing basic net income (loss) per common share | 5,227 | 6,643 | 18,102 | 31,078 | 32,486 | 32,290 | 33,705 |
| Diluted net income (loss) per share attributable to common stockholders | $ (0.57) | $ (2.20) | $ (2.09) | $ (0.91) | $ (0.11) | $ (0.14) | $ 0.17 |
| Shares used in computing diluted net income (loss) per common share | 5,227 | 6,643 | 18,102 | 31,078 | 32,486 | 32,290 | 36,404 |

**Table of Contents**

**Index to Financial Statements**

| | December 31, | | | | | September 30, |
|---|---|---|---|---|---|---|
| | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 |
| | | | | | | (Unaudited) |
| **Consolidated Balance Sheet Data:** | | | | | | |
| Cash, cash equivalents and short-term investments | $ 2,807 | $ 12,489 | $ 51,513 | $ 26,272 | $ 30,615 | $ 37,406 |
| Working capital | 2,979 | 10,478 | 41,853 | 22,945 | 23,918 | 32,839 |
| Total assets | 3,672 | 17,692 | 70,572 | 46,363 | 42,160 | 55,382 |
| Long-term obligations | 449 | 2,277 | 3,385 | 1,590 | 67 | |
| Redeemable convertible preferred stock | 5,237 | 21,449 | | | | |
| Accumulated deficit | (2,750) | (16,264) | (53,132) | (81,312) | (84,954) | (78,899) |
| Total stockholders equity (deficit) | (2,423) | (12,473) | 46,159 | 24,297 | 23,147 | 31,926 |

24

**Table of Contents**

**Index to Financial Statements**

## MANAGEMENT S DISCUSSION AND ANALYSIS OF

## FINANCIAL CONDITION AND RESULTS OF OPERATIONS

*The following discussion of our financial condition and results of operations should be read together with the consolidated financial statements and the related notes included in this prospectus or referred to herein. This discussion contains, in addition to historical information, forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from the results discussed in the forward-looking statements. Factors that could cause or contribute to these differences include, but are not limited to, those discussed below as well as those discussed under Risk Factors and elsewhere in this prospectus. We disclaim any obligation to update information contained in any forward-looking statement.*

### Overview

*General*

We are a leading provider of support and service management software designed to accelerate and automate enterprise technical support, customer service and IT infrastructure management. We refer to this as real-time service management software. Our software solutions are utilized by enterprises to service customers, partners and employees either directly or as part of an outsourced solution from managed service providers, and by consumers and businesses through digital service providers.

From our incorporation in December 1997 through the end of 1998, we primarily engaged in research activities and developing and marketing our products. We first began generating revenue from software license fees from the initial version of our products in December 1998. During 1999, we continued to enhance the functionality of our products, build our management team and operational infrastructure and began shipping the second version of our products. From January 2000 through September 2003, we expanded our product offerings to address a wider range of support and service functions and now offer three comprehensive software suites, Resolution Suite, Service Automation Suite Broadband and Knowledge Center Suite as well as a number of component products. We also intend to release a fourth suite by the end of 2003, which will be known as Service Automation Suite Video.

*Revenue*

We generate revenue primarily from the sale of software licenses and related services. We offer our products through a combination of direct sales, managed service providers, alliances and resellers. In 2002 and the nine months ended September 30, 2003, 14% and 10% of our revenue, respectively, was generated from customers outside of North America. We plan to expand our international operations, particularly in Europe and Asia.

We license our software under term and perpetual licenses. Revenue from term licenses is recognized monthly over the term of the agreement beginning at the time the first payment is due or as payments become due depending on whether the fee is fixed or determinable. Initial term licenses typically have a duration of 36 months, with pre-payments generally made at the beginning of each 12 month period. Upon expiration of the initial term, our customers have the option to renew the license. The renewals may be made on a term basis for a period that does not necessarily correspond to the initial term. The customers may also renew the license by purchasing the software on a perpetual basis. Perpetual licenses typically result in revenue being recognized up-front.

Term and perpetual licensing arrangements may include service elements. Services revenue consists primarily of fees from professional services, such as deployment and

**Table of Contents**

**Index to Financial Statements**

consulting services, training, maintenance and support. Consulting services include a range of services including installation, implementation and building interfaces for customer-specific applications. Our maintenance agreements provide technical support and include the right to unspecified upgrades on purchased products, if and when available.

We intend to continue to invest in product development and technologies to enhance our products and services and develop new products and services. We also intend to expand our operations and employee base and build our sales, marketing, customer support, technical and operational resources.

**Critical Accounting Policies and Estimates**

The preparation of our consolidated financial statements in conformity with accounting principles generally accepted in the United States requires us to make estimates and assumptions that affect the amounts reported in our financial statements and accompanying notes. Our significant accounting policies are described in Note 1 to the consolidated financial statements. We believe the following critical accounting policies affect our more significant judgments and estimates used in preparing our consolidated financial statements.

*Revenue Recognition*

We recognize revenue in accordance with the American Institute of Certified Public Accountants (AICPA) Statement of Position ( SOP ) 97-2, Software Revenue Recognition, as amended by SOP 98-4 and SOP 98-9. License revenue is recognized when all of the following criteria are met:

- Persuasive evidence of an arrangement exists;
- Delivery has occurred;
- No uncertainties surrounding product acceptance exist;
- Collection is considered probable; and
- The fees are fixed or determinable.

We consider all arrangements with payment terms extending beyond 12 months and other arrangements with payment terms longer than normal not to be fixed or determinable. If the fee is determined not to be fixed or determinable, revenue is recognized as payments become due from the customer.

License revenue is comprised of fees for term and perpetual licenses of our software. Perpetual license revenue is recognized using the residual method described in SOP 98-9 for arrangements in which licenses are sold with multiple elements. We allocate revenue on these licenses based upon the fair value of each undelivered element (for example, undelivered maintenance and support, training and consulting). The determination of fair value is based upon vendor specific objective evidence, or VSOE. VSOE for maintenance and support is determined by the customer s annual renewal rate for these services. VSOE for training or consulting is based upon separate sales of these services to other customers. Assuming all other revenue recognition criteria are met, the difference between the total arrangement fee and the amount deferred for each undelivered element is recognized as license revenue. Our perpetual arrangements may include contractual obligations such as rights to unspecified future products or initial maintenance extending over a period of time with no renewal rate, which requires license revenue to be taken ratably (monthly) over the contract period.

**Table of Contents**

**Index to Financial Statements**

Term licenses are sold with maintenance for which we do not have VSOE to determine fair value. As a result, license revenue for term licenses is recognized ratably over the service period of the agreement and license revenue includes maintenance for term licenses. We do not allocate maintenance revenue from term licenses to services revenue, as we do not believe there is an allocation methodology that provides a meaningful and supportable allocation between license and maintenance revenues.

The following is an example of our revenue recognition for a term license. If we receive an order from a customer for a 36-month term license in December of a year, we would recognize only one month of license fees for that year even if that customer prepaid 12 months of the 36-month term. Pursuant to this arrangement, we would record one year of fees in accounts receivable and 11 months of fees in deferred revenue upon signing a new term license agreement, while recognizing only one month of revenue. As a result, our accounts receivable balance could represent a significant portion of our total revenue and increase our days sales outstanding, or DSO, calculation.

We also recognize license revenue from arrangements with resellers. These arrangements may be either term or perpetual licenses of our software. When these arrangements include guaranteed minimum amounts due, revenue is recognized ratably over the term of the arrangement commencing when payments are made or become due. When the arrangements do not include guaranteed minimum amounts due and are based upon sell through activity, we recognize revenue when we receive evidence of sell-through, that is, persuasive evidence that the products have been sold to an end user if the reseller has been deemed credit-worthy. When resellers are not deemed credit-worthy, revenue is recognized upon cash receipt.

Services revenue is primarily comprised of revenue from professional services, such as deployment and consulting services, training, maintenance and support. Arrangements that include software services are evaluated to determine whether those services are essential to the functionality of other elements of the arrangement. Non-essential consulting and training revenues are generally recognized as the services are performed. When non-essential software services are bundled in a term licensing arrangement, revenue from the software services is recognized ratably over the period associated with the initial payment. Post-contract customer maintenance and support revenues are recognized over the term of the support period (generally one year). When the software services are considered essential to the functionality of other elements of the arrangement, revenue under the arrangement is recognized using contract accounting, typically using the percentage of completion method.

*Allowance for Bad Debt*

We maintain reserves for estimated credit losses resulting from the inability of our customers to make required payments. A considerable amount of judgment is required when we assess the realization of receivables, including assessing the probability of collection and the current credit-worthiness of each customer. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, additional reserves may be required.

**Table of Contents**

**Index to Financial Statements**

**Results of Operations**

The following table presents certain consolidated statement of operations data for the periods indicated as a percentage of total revenue.

| | Year Ended December 31, | | | Nine Months Ended September 30, | |
|---|---|---|---|---|---|
| | 2000 | 2001 | 2002 | 2002 | 2003 |
| | | | | (Unaudited) | |
| Revenue: | | | | | |
| License fees | 74% | 74% | 76% | 75% | 78% |
| Services | 26 | 26 | 24 | 25 | 22 |
| Total revenue | 100 | 100 | 100 | 100 | 100 |
| Costs and expenses: | | | | | |
| Cost of license fees | 8 | 2 | 1 | 1 | 1 |
| Cost of services | 32 | 21 | 14 | 15 | 13 |
| Amortization of purchased technology | 6 | 9 | 4 | 5 | |
| Research and development | 58 | 42 | 21 | 23 | 18 |
| Sales and marketing | 122 | 90 | 55 | 57 | 42 |
| General and administrative | 23 | 20 | 14 | 14 | 10 |
| Amortization of deferred compensation | 58 | 14 | 1 | 2 | |
| Total costs and expenses | 307 | 198 | 110 | 117 | 84 |
| Income (loss) from operations | (207) | (98) | (10) | (17) | 16 |
| Interest income and other, net | 9 | 5 | 2 | 1 | 1 |
| Income (loss) before income taxes | (198) | (93) | (8) | (16) | 17 |
| Income tax expense | | | (1) | | (1) |
| Net income (loss) | (198)% | (93)% | (9)% | (16)% | 16% |

**Nine Months Ended September 30, 2002 and 2003**

*Revenue*

For the nine months ended September 30, 2002 and 2003, ratable license revenue represented approximately 41% and 27% of total revenue, respectively. Although the percentage of revenue we recognize in the future from ratable licensing arrangements will vary from period to period, we currently anticipate that revenue from such arrangements will represent approximately 25% to 30% of total revenue over the next 12 months. We anticipate that revenue we recognize on an immediate basis from perpetual licensing arrangements will be approximately 45% to 55% of total revenue over the next 12 months. Although the percentage of revenue we recognize in the future from services will vary from period to period, we currently anticipate that revenue from services will represent approximately 20% to 25% of total revenue over the next 12 months.

For the nine months ended September 30, 2002, one customer accounted for 14% of our total revenue. No other customer individually accounted for 10% or more of our total revenue for the nine months ended September 30, 2002. For the nine months ended September 30, 2003, two of our customers accounted for 10% or more of our total revenue. One of these customers accounted for 16% of our total revenue and the other customer accounted for 12% of our total revenue. No other customer individually accounted for 10% or more of our total revenue for the nine months ended September 30, 2003. Revenue from customers outside the United States accounted for approximately 13% of our total revenue for the nine months ended September 30, 2002, compared with 10% for the nine months ended September 30, 2003.

**Table of Contents**

**Index to Financial Statements**

*License fees*. License fees increased from $22.1 million for the nine months ended September 30, 2002 to $29.7 million for the nine months ended September 30, 2003. The increase in license revenue was due primarily to greater demand for our software products, an expansion of our product offerings and an increase in our license revenue mix to more immediate arrangements relative to ratable arrangements.

*Services revenue*. Services revenue increased from $7.2 million for the nine months ended September 30, 2002 to $8.5 million for the nine months ended September 30, 2003. The increase in services revenue was primarily due to increased maintenance revenue associated with the growth in our customer base from prior years and corresponding growth in the overall number of maintenance contracts.

*Cost of license fees*

Cost of license fees consists primarily of costs related to third-party software royalty fees under license arrangements for technology embedded into our products. Cost of license fees increased from $197,000 for the nine months ended September 30, 2002 to $270,000 for the nine months ended September 30, 2003. This increase was primarily due to increased license fees paid to third parties under technology license arrangements.

*Cost of services*

Cost of services consists primarily of compensation costs, travel costs, related overhead expenses for services personnel and payments made to third parties for subcontracted consulting services. Cost of services increased from $4.4 million for the nine months ended September 30, 2002 to $5.0 million for the nine months ended September 30, 2003. These increases were due primarily to an increase in salary expenses as a result of an increase in services personnel headcount.

*Amortization of purchased technology*

Amortization of purchased technology was $1.6 million for the nine months ended September 30, 2002. As of September 30, 2002, the purchased intangibles balance was fully amortized.

*Operating Expense*

*Research and development*. Research and development expense is expensed as incurred. Research and development expense consists primarily of compensation costs, consulting expenses and related overhead costs for research and development personnel. Research and development expense increased from $6.7 million for the nine months ended September 30, 2002 to $6.8 million for the nine months ended September 30, 2003. This increase was due to an increase in salary and related expenses offset by a slight decrease in third-party consulting services.

*Sales and marketing*. Sales and marketing expense consists primarily of compensation costs, including salaries and commissions and related overhead costs for sales and marketing personnel and promotional expenses, including public relations, advertising and trade shows. Sales and marketing expense decreased from $16.8 million for the nine months ended September 30, 2002 to $16.1 million for the nine months ended September 30, 2003. This decrease was due primarily to a reduction in travel expense and promotional expenses, including trade shows and other program events, offset by increases in salary and related expenses.

**Table of Contents**

**Index to Financial Statements**

*General and administrative*. General and administrative expense consists primarily of compensation costs and related overhead costs for administrative personnel and professional fees for legal, accounting and other professional services. General and administrative expense decreased from $4.2 million for the nine months ended September 30, 2002 to $3.9 million for the nine months ended September 30, 2003. This decrease was due primarily to a reduction in salary and related expenses partially offset by an increase in professional fees for legal and accounting services.

*Amortization of deferred stock compensation*. We amortized deferred compensation expense of $578,000 during the nine months ended September 30, 2002. This compensation expense related to options awarded to individuals in all operating expense categories. As of June 30, 2002, all existing deferred stock compensation balances had been fully amortized.

*Interest income and other, net*. Interest income and other, net was $513,000 for the nine months ended September 30, 2002, as compared to interest income and other, net of $311,000 for the nine months ended September 30, 2003. The decrease in interest income and other, net was attributable primarily to a slight decrease in interest earned on our cash, cash equivalents and short-term investments as well as a decrease in interest earned on the repayment of notes receivables from officers. As of September 30, 2002, all notes receivables from officers had been fully repaid.

*Income tax expense*. Income tax expense was zero for the nine months ended September 30, 2002, and $331,000 for the nine months ended September 30, 2003. This increase was due to income generated from operations. No provision for income taxes was recorded in the nine months ended September 30, 2002 due to a loss in the period and a history of operating losses in all prior periods. Given our limited operating history, our losses incurred to date and the difficulty in accurately forecasting our future results, we do not believe that the realization of the related deferred income tax asset meets the criteria required by generally accepted accounting principles. Therefore, we have recorded a 100% valuation allowance against the deferred income tax asset.

**Years Ended December 31, 2000, 2001 and 2002**

*Revenue*

For the years ended December 31, 2000, 2001 and 2002, ratable license revenue primarily from term licenses represented approximately 49%, 55% and 40% of total revenue, respectively.

Revenue from customers outside the United States accounted for approximately 15% of our total revenue in 2000, 19% of our total revenue in 2001 and 14% of our total revenue in 2002.

*License fees*. License fees were $13.7 million in 2000, $22.5 million in 2001 and $31.3 million in 2002. License fees increased by approximately $8.8 million or 64%, in 2001 from 2000, and $8.7 million or 39%, in 2002 from 2001. These increases were primarily due to an increase in our licensing mix to more perpetual arrangements where typically more revenue is recognized in the period that the license arrangements are signed than as compared to term license arrangements, recognition of a full year of term-based license revenue in 2002 and 2001 from arrangements entered into in previous years and an expansion of our product offerings.

*Services revenue*. Services revenue was $4.9 million in 2000, $7.9 million in 2001 and $9.9 million in 2002. Services revenue increased by approximately $3.0 million or 60%, in 2001 from 2000, and increased by approximately $2.0 million or 25%, in 2002 from 2001. These increases were due primarily to increased implementation, training and consulting services and maintenance revenue due to an increase in the total number of customers.

**Table of Contents**

**Index to Financial Statements**

*Cost of license fees*

Cost of license revenue was $1.4 million in 2000, $621,000 in 2001 and $289,000 in 2002. Cost of license revenue decreased approximately $784,000 or 56%, in 2001 from 2000 and decreased approximately $332,000 or 53%, in 2002 from 2001. The decrease in cost of revenue in 2001 from 2000 was primarily due to a one time payment of $1.0 million to a third party in 2000 for source code license used in our software products. The decrease in cost of license revenue in 2002 from 2001 was primarily due to the decrease in the use of third-party software sold or embedded with our products. In 2000, 2001 and 2002, we incurred minimal shipping, packaging and documentation costs, as our product is typically delivered electronically over the Internet.

*Cost of services*

Cost of services was $5.9 million in 2000, $6.2 million in 2001 and $5.9 million in 2002. Cost of services increased approximately $324,000 or 5% in 2001 from 2000 and decreased approximately $351,000 or 6% in 2002 from 2001. The increase in cost of services revenue in 2001 from 2000 was primarily due to an increase in compensation costs and related overhead costs offset by a reduction in travel, consulting and recruiting expenses. The decrease in cost of services in 2002 from 2001 was due primarily to a decrease in travel costs and a decrease in the number of third-party consultants utilized offset by a slight increase in compensation costs and related overhead costs.

*Amortization of purchased technology*

Amortization of purchased technology was $1.2 million in 2000, $2.8 million in 2001 and $1.6 million in 2002. The increase in amortization of purchased technology in 2001 from 2000 was primarily due to a full year of amortization in 2001 of the purchased technology from our acquisition of source code and related intellectual rights from a third party in September 2000. The decrease in amortization of purchased technology in 2002 from 2001 was attributable to the balance of these intangible assets being fully amortized by September 2002.

*Operating expense*

*Research and development*. Research and development expense was $10.9 million in 2000, $12.6 million in 2001 and $8.8 million in 2002. Research and development expense increased approximately $1.7 million or 16%, in 2001 from 2000 and decreased approximately $3.8 million or 30%, in 2002 from 2001. The increase in research and development expenses in 2001 from 2000 was primarily due to an increase in compensation costs, consulting expenses and related overhead costs for research and development personnel. The decrease in research and development expense in 2002 from 2001 was primarily due to a reduction in third-party consulting services and compensation costs due to lower research and development personnel headcount.

*Sales and marketing*. Sales and marketing expense was $22.8 million in 2000, $27.5 million in 2001 and $22.5 million in 2002. Sales and marketing expense increased approximately $4.7 million, or 21%, in 2001 from 2000 and decreased by approximately $5.0 million, or 18%, in 2002 from 2001. The increase in sales and marketing expenses in 2001 from 2000 was due to an increase in compensation costs, the opening of new sales offices in the United States, Europe and Asia and commission expense associated with increased revenue in 2001. The decrease in sales and marketing expense in 2002 from 2001 was due to a number of factors including a reduction in compensation costs due to lower headcount, recruiting expenses, related overhead expense and promotional expenses, including public relations, advertising and trade shows, partially offset by a smaller increase in sales commission expense associated with higher revenues.

**Table of Contents**

**Index to Financial Statements**

*General and administrative*. General and administrative expense was $4.3 million in 2000, $6.1 million in 2001 and $5.6 million in 2002. General and administrative expense increased approximately $1.8 million, or 42%, in 2001 from 2000 and decreased approximately $494,000, or 8% in 2002 from 2001. The increase in general and administrative expenses in 2001 from 2000 was primarily because of an increase in compensation costs and from additional legal, accounting and other professional services costs incurred in connection with supporting business activities. The decrease in general and administrative expense in 2002 from 2001 was primarily due to a reduction in compensation costs due to lower headcount, reduced fees for outside legal and consulting services and reduced annual report costs.

*Amortization of deferred compensation*. Deferred stock compensation represents the difference between the exercise price of options granted to employees and board of directors and the deemed fair value for financial statement reporting purposes of our common stock on their respective grant dates. Deferred stock compensation also includes the fair value of options and restricted stock granted to non-employees as determined using the Black Scholes model. We amortized deferred compensation expense related to employee and director option grants of approximately $10.8 million in 2000, $4.3 million in 2001 and $578,000 in 2002. We reduced deferred stock compensation by $4.3 million in 2000, $2.0 million in 2001 and $419,000 in 2002 to reflect the cancellation of unvested stock options. At December 31, 2002, the deferred compensation balance was fully amortized and therefore we do not anticipate future deferred compensation expense as a result of prior option grants.

In 2000, we recorded $501,000 of expense related to the amortization of deferred compensation for options to non-employees and the acceleration of vesting of certain restricted stock arrangements.

*Interest income and other, net*. Interest income and other, net was $1.7 million in 2000, $1.6 million in 2001 and $640,000 in 2002. Interest income and other, net decreased approximately $140,000 or 8%, in 2001 from 2000 and decreased approximately $938,000 or 59%, in 2002 from 2001. These decreases in interest income and other, net in 2001 from 2000 and in 2002 from 2001 were primarily attributable to less interest income recorded due to lower cash, cash equivalents and short-term investment balances and to a lesser extent a lower rate of return on our invested cash balances.

*Provision for income taxes*. The provision for income taxes in 2002 is related to foreign income and withholding taxes. In 2000, 2001 and 2002, we incurred net losses for U.S. federal and U.S. state tax purposes and have not recognized any tax benefit for these operating losses. As of December 31, 2002, we had federal and state net operating loss carryforwards of $46.5 million and $24.2 million, respectively. The net operating loss carryforwards expire on various dates beginning in 2005 through 2022. Given our limited operating history, our losses incurred to date and the difficulty in accurately forecasting our future results, we do not believe that the realization of the related deferred income tax asset meets the criteria required by generally accepted accounting principles. Therefore, we have recorded a 100% valuation allowance against the deferred income tax asset.

**Table of Contents**

**Index to Financial Statements**

**Quarterly Results of Operations**

The following table sets forth our unaudited quarterly results of operations data for the eight quarters ended September 30, 2003, as well as such data expressed as a percentage of our total revenue for the periods presented. The information in the table below should be read with our consolidated financial statements and the related notes included elsewhere in this prospectus. We have prepared this information on the same basis as the consolidated financial statements and the information includes all adjustments, consisting only of normal recurring adjustments, that we consider necessary for a fair presentation of our financial position and operating results for the quarters presented. Our quarterly operating results have varied substantially in the past and may vary substantially in the future. You should not draw any conclusions about our future results from the results of operations for any particular quarter.

| | Three Months Ended | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Dec. 31, 2001 | Mar. 31, 2002 | June 30, 2002 | Sept. 30, 2002 | Dec. 30, 2002 | Mar. 31, 2003 | June 30, 2003 | Sept. 30, 2003 |
| | (in thousands, except share and per share amounts) | | | | | | | |
| | (Unaudited) | | | | | | | |
| **Statements of Operations Data:** | | | | | | | | |
| Revenue: | | | | | | | | |
| License fees | $ 6,537 | $ 6,587 | $ 6,999 | $ 8,562 | $ 9,112 | $ 9,593 | $ 9,647 | $ 10,446 |
| Services | 1,941 | 2,178 | 2,467 | 2,551 | 2,704 | 2,401 | 2,964 | 3,086 |
| Total revenue | 8,478 | 8,765 | 9,466 | 11,113 | 11,816 | 11,994 | 12,611 | 13,532 |
| Costs and expenses: | | | | | | | | |
| Cost of license fees | 121 | 65 | 65 | 67 | 92 | 90 | 90 | 90 |
| Cost of services | 1,499 | 1,372 | 1,564 | 1,448 | 1,499 | 1,690 | 1,824 | 1,476 |
| Amortization of purchased technology | 598 | 598 | 598 | 385 | | | | |
| Research and development | 2,820 | 2,275 | 2,195 | 2,228 | 2,136 | 2,334 | 2,289 | 2,195 |
| Sales and marketing | 5,759 | 5,592 | 5,500 | 5,741 | 5,631 | 5,048 | 5,098 | 5,913 |
| General and administrative | 1,416 | 1,339 | 1,348 | 1,490 | 1,460 | 1,425 | 1,262 | 1,238 |
| Amortization of deferred compensation | 717 | 470 | 108 | | | | | |
| Total costs and expenses | 12,930 | 11,711 | 11,378 | 11,359 | 10,818 | 10,587 | 10,563 | 10,912 |
| Income (loss) from operations | (4,452) | (2,946) | (1,912) | (246) | 998 | 1,407 | 2,048 | 2,620 |
| Interest income and other, net | 211 | 125 | 105 | 283 | 127 | 140 | 91 | 80 |
| Income (loss) before income taxes | (4,241) | (2,821) | (1,807) | 37 | 1,125 | 1,547 | 2,139 | 2,700 |
| Income tax expense | | | | | (177) | (73) | (119) | (139) |
| Net income (loss) | $ (4,241) | $ (2,821) | $ (1,807) | $ 37 | $ 948 | $ 1,474 | $ 2,020 | $ 2,561 |
| Basic net income (loss) per share attributable to common stockholders | $ (0.13) | $ (0.09) | $ (0.06) | $ 0.00 | $ 0.03 | $ 0.04 | $ 0.06 | $ 0.07 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Shares used in computing basic net income (loss) per common share | 31,637 | 32,003 | 32,318 | 32,643 | 32,975 | 33,306 | 33,628 | 34,173 |
| Diluted net income (loss) per share attributable to common stockholders | $ (0.13) | $ (0.09) | $ (0.06) | $ 0.00 | $ 0.03 | $ 0.04 | $ 0.06 | $ 0.07 |
| Shares used in computing diluted net income (loss) per common share | 31,637 | 32,003 | 32,318 | 34,074 | 34,749 | 34,532 | 35,793 | 37,918 |

**Table of Contents**

**Index to Financial Statements**

| | Three Months Ended | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Dec. 31, 2001 | Mar. 31, 2002 | June 30, 2002 | Sept. 30, 2002 | Dec. 31, 2002 | Mar. 31, 2002 | June 30, 2003 | Sept. 30, 2003 |
| | (Unaudited) | | | | | | | |
| **Statements of Operations Data as a Percentage of Total Revenue:** | | | | | | | | |
| Revenue: | | | | | | | | |
| License fees | 77% | 75% | 74% | 77% | 77% | 80% | 76% | 77% |
| Services | 23 | 25 | 26 | 23 | 23 | 20 | 24 | 23 |
| Total revenue | 100 | 100 | 100 | 100 | 100 | 100 | 100 | 100 |
| Costs and expenses: | | | | | | | | |
| Cost of license fees | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 1 |
| Cost of services | 18 | 16 | 17 | 13 | 13 | 14 | 14 | 11 |
| Amortization of purchased technology | 7 | 7 | 6 | 3 | | | | |
| Research and development | 33 | 26 | 23 | 20 | 18 | 19 | 18 | 16 |
| Sales and marketing | 68 | 64 | 58 | 52 | 48 | 42 | 40 | 44 |
| General and administrative | 17 | 15 | 14 | 13 | 12 | 12 | 10 | 9 |
| Amortization of deferred compensation | 8 | 5 | 1 | | | | | |
| Total costs and expenses | 153 | 134 | 120 | 102 | 92 | 88 | 84 | 81 |
| Income (loss) from operations | (53) | (34) | (20) | (2) | 8 | 12 | 16 | 19 |
| Interest income and other, net | 2 | 2 | 1 | 2 | 1 | 1 | 1 | 1 |
| Income (loss) before income taxes | (50) | (32) | (19) | 0 | 10 | 13 | 17 | 20 |
| Income tax expense | | | | | (1) | (1) | (1) | (1) |
| Net income (loss) | (50)% | (32)% | (19)% | 0% | 8% | 12% | 16% | 19% |

**Liquidity and Capital Resources.**

Since our incorporation in December 1997, we have financed our operations primarily through cash flows from operations, our initial public offering and, to a lesser extent, from the private placement of our preferred and common stock, bank borrowings and capital equipment lease financing.

*Operating Activities*

Net cash used in operating activities was $16.5 million in 2000 and $24.2 million in 2001 and net cash generated by operating activities was $5.0 million in 2002. Amounts included in net loss, which do not require the use of cash, including the depreciation and amortization of fixed assets, amortization of deferred stock compensation and amortization of purchased intangibles, amounted to $13.4 million in 2000, $9.5 million in 2001 and $4.2 million in 2002. Net cash generated by operating activities during 2002 was also the result of a decrease in accounts receivable, net of $4.8 million, a decrease in prepaids and other current assets of $1.3 million and an increase in deferred revenue of $788,000, offset by a net loss of $3.6 million, a decrease in accounts payable of $1.2 million and a decrease in other accrued liabilities of $1.0 million.

Net cash generated by operating activities was $2.6 million and $5.7 million for the nine months ended September 30, 2002 and 2003, respectively. Amounts included in net income (loss), which do not require the use of cash, including the depreciation and amortization of fixed assets, amortization of deferred stock compensation and amortization of purchased intangibles, amounted to $3.7 million and $1.1 million for the nine months ended September 30, 2002 and 2003, respectively. Net cash generated by operating activities for the nine months ended September 30, 2002 was also the result of an increase of $5.3 million in deferred revenue and a decrease in prepaids and other current assets of $892,000, offset by a net loss of $4.6 million and an increase in accounts receivable, net of $1.8 million. Net cash generated by operating

**Table of Contents**

**Index to Financial Statements**

activities for the nine months ended September 30, 2003 was primarily the result of net income of $6.1 million and an increase of $5.8 million in deferred revenue offset by an increase of $6.5 million in accounts receivable, net and $405,000 in prepaids and other current assets and a decrease of $190,000 in accrued compensation and $196,000 in other accrued liabilities.

*Investing Activities*

Net cash used in investing activities was $35.8 million in 2000, net cash generated by investing activities was $28.8 million in 2001 and net cash used in investing activities was $7.2 million in 2002. Net cash used in investing activities in 2000, was primarily due to the purchase of $45.2 million in short-term investments and to a lesser extent the purchase of $1.7 million in property and equipment and $2.8 million of purchases of technology offset by the sale and maturity of $13.9 million in short-term investments. Net cash generated by investing activities in 2001, was primarily due to the sale and maturity of $65.4 million in short-term investments offset by the purchase of $34.2 million in short-term investments and to a lesser extent the purchase of $1.9 million in property and equipment and $613,000 of purchases of technology. Net cash used in investing activities in 2002, was primarily due to the purchase of $25.5 million in short-term investments and to a lesser extent the purchase of $1.4 million in property and equipment and $714,000 of purchases of technology offset by the sale and maturity of $20.4 million in short-term investments.

Net cash used in investing activities was $5.7 million and $9.6 million for the nine months ended September 30, 2002 and 2003, respectively. Net cash used in investing activities for the nine months ended September 30, 2002, resulted from the purchase of $14.0 million in short-term investments and $1.2 million in property and equipment offset by the sale and maturity of $10.0 million in short-term investments. Net cash used in investing activities for the nine months ended September 30, 2003, was due primarily to the purchase of $25.3 million in short-term investments offset by the sale and maturity of $16.6 million in short-term investments.

*Financing Activities*

Net cash generated by financing activities was $60.1 million in 2000, $1.3 million in 2001 and $1.5 million for 2002. In 2000, net cash generated by financing activities was primarily attributable to $61.8 million from the issuance of our common stock in our initial public offering in July 2000 and to a lesser extent the exercise of employee stock options. In 2001, net cash generated by financing activities was primarily attributable to the purchase of common stock under the employee stock purchase plan and to a lesser extent the repayment of notes receivable from stockholders. In 2002, net cash generated by financing activities was attributable primarily to the repayment of notes receivable from stockholders and to a lesser extent the purchase of common stock under the employee stock purchase plan and the exercise of employee stock options offset by principal repayments under capital lease obligations.

Net cash generated by financing activities was $1.4 million and $2.0 million for the nine months ended September 30, 2002 and 2003, respectively. For the nine months ended September 30, 2002, cash provided by financing activities was attributable primarily to net proceeds from the repayment of notes receivable from stockholders and a lesser extent the purchase of common stock under the employee stock purchase plan offset by principal repayments under capital lease obligations. For the nine months ended September 30, 2003, net cash provided by financing activities was primarily attributable to net proceeds of $2.5 million from the purchase of common stock under the employee stock purchase plan and the exercise of employee stock options offset by the repayment of $530,000 in principal payments under capital lease obligations.

35

**Table of Contents**

**Index to Financial Statements**

*Commitments*

At September 30, 2003, our principal commitments consisted of obligations outstanding under operating leases. The following summarizes our contractual obligations as of September 30, 2003 and the effect these contractual obligations are expected to have on our liquidity and cash flows in future periods.

| | Payments Due By Period (in thousands) | | | | |
|---|---|---|---|---|---|
| | <1 Year | 1-3 Years | 4-5 Years | >5 Years | Total |
| Operating Leases | $ 644 | $ 829 | $ 22 | $ | $ 1,495 |
| Total | $ 644 | $ 829 | $ 22 | $ | $ 1,495 |

*Working Capital and Capital Expenditure Requirements*

At September 30, 2003, we had stockholders equity of $31.9 million and working capital of $32.8 million. Included as a reduction to working capital is deferred revenue of $18.2 million, which will not require dollar for dollar of cash to settle, but will be recognized as revenue in the future. We believe that our existing cash balances will be sufficient to meet our working capital and capital expenditure requirements for at least the next 12 months.

If we require additional capital resources to grow our business internally or to acquire complementary technologies and businesses at any time in the future, we may seek to sell additional equity or debt securities. The sale of additional equity or debt securities could result in more dilution to our stockholders. Financing arrangements may not be available to us, or may not be available in amounts or on terms acceptable to us.

**Qualitative and Quantitative Disclosures about Market Risk**

We develop products in the United States and market and sell in North America, South America, Asia and Europe. As a result, our financial results could be affected by factors such as changes in foreign currency exchange rates or weak economic conditions in foreign markets. As most sales are currently made in United States dollars, a strengthening of the dollar could make our products less competitive in foreign markets.

Our interest income is sensitive to changes in the general level of United States interest rates. However, due to the nature of our cash equivalents and short-term investments, we have concluded that there is not material market risk exposure.

Our investment policy requires us to invest funds in excess of operating requirements in:

- obligations of the United States government and its agencies;
- securities of United States corporations rated A1 or the equivalent for short-term ratings and A2 or the equivalent for long-term ratings by Standard and Poors or the Moody s equivalent; and
- money market funds or deposits issued or guaranteed by United States and non-United States commercial banks, meeting credit rating and net worth requirements with maturities of less than 18 months.

36

**Table of Contents**

**Index to Financial Statements**

At September 30, 2003, our cash and cash equivalents consisted primarily of money market funds held by large institutions in the United States and our short-term investments were primarily invested in government debt securities, corporate bonds and auction backed securities maturing or resetting in less than 18 months.

**Recent Accounting Pronouncements**

In January 2003, the FASB issued FIN 46, Consolidation of Variable Interest Entities. FIN 46 requires us to consolidate a variable interest entity if we are subject to a majority of the risk of loss from the variable interest entity s activities or entitled to receive a majority of the entity s residual returns or both. A variable interest entity is a corporation, partnership, trust or any other legal structure used for business purposes that either does not have equity investors with voting rights or has equity investors that do not provide sufficient financial resources for the entity to support its activities. A variable interest entity often holds financial assets, including loans or receivables, real estate or other property. SupportSoft does not currently have any interests in variable interest entities and, accordingly, our adoption of FIN 46 has not had any impact on our historical financial position, results of operations or cash flows.

On December 31, 2002, the FASB issued SFAS 148, Accounting for Stock-Based Compensation Transition and Disclosure. This statement amends SFAS 123, Accounting for Stock-Based Compensation, to provide alternative methods of transition for an entity that voluntarily changes to the fair value based method of accounting for stock-based employee compensation. It also amends the disclosure provisions of that statement to require prominent disclosure about the effects on reported net income of an entity s accounting policy decisions with respect to stock-based employee compensation. Finally, this statement amends APB Opinion No. 28, Interim Financial Reporting, to require disclosure about those effects in interim financial statements. The amendment of the transition and annual disclosure requirements of SFAS 123 are effective for fiscal years ending after December 15, 2002. The amendment of the disclosure requirements of APB Opinion No. 28 is effective for financial reports containing condensed consolidated financial statements for interim periods beginning after December 15, 2002. Because we have not changed to the fair value based method of accounting for stock-based employee compensation, the transition provisions of SFAS 148 have not had a significant impact on our financial position, results of operations or cash flows. The required amended annual disclosures are included in Notes 1 and 5 of these consolidated financial statements and our future interim financial statements will include appropriate disclosure information.

In November 2002, the FASB issued Financial Interpretation No. ( FIN ) 45, Guarantor s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others. FIN 45 elaborates on the existing disclosure requirements for most guarantees, including residual value guarantees issued in conjunction with operating lease agreements. It also clarifies that at the time a company issues a guarantee, the company must recognize an initial liability for the fair value of the obligation it assumes under that guarantee and must disclose that information in its interim and annual financial statements. The initial recognition and measurement provisions of this interpretation apply on a prospective basis to guarantees issued or modified after December 31, 2002. The disclosure requirements are effective for financial statements of interim or annual periods ending after December 15, 2002. Our adoption of FIN 45 has not had any impact on our historical financial position, results of operations or cash flows.

In July 2002, the FASB approved SFAS No. 146, Accounting for Costs Associated with Exit or Disposal Activities. SFAS No. 146 addresses the financial accounting and reporting for

37

**Table of Contents**

**Index to Financial Statements**

obligations associated with an exit activity, including restructuring, or with a disposal of long-lived assets. Exit activities include, but are not limited to, eliminating or reducing product lines, terminating employees and contracts and relocating plant facilities or personnel. SFAS No. 146 specifies that a company will record a liability for a cost associated with an exit or disposal activity only when that liability is incurred and can be measured at fair value. Therefore, commitment to an exit plan or a plan of disposal expresses only management s intended future actions and, therefore, does not meet the requirement for recognizing a liability and the related expense. SFAS No. 146 is effective prospectively for exit or disposal activities initiated after December 31, 2002, with earlier adoption encouraged. The adoption of SFAS No. 146 did not have a material effect on our historical financial position or results of operations.

Table of Contents

Index to Financial Statements

## BUSINESS

### Overview

We are a leading provider of support and service management software designed to accelerate and automate enterprise technical support, customer service and IT infrastructure management. We refer to this as real-time service management software. Our software solutions are utilized by enterprises to service customers, partners or employees either directly or as part of an outsourced solution from managed service providers, and by consumers and businesses through digital service providers. We believe that our real-time service management software, including its self-healing and mass-healing capabilities that preemptively diagnose and resolve software problems, allows organizations to keep up with the growing complexity and cost of IT infrastructure and related support and service problems. Organizations can benefit from our software by reducing costs and improving productivity and customer satisfaction by keeping key software and technology-based services operating and accessible on devices when using the Internet, or cable, wireless and wireline networks.

Our software suites and component products offer organizations automated alternatives to phone support or on-site visits by technical professionals. These traditional approaches are typically labor intensive, time consuming and costly methods of resolving support, service and IT infrastructure management problems. Organizations can utilize our software to help preempt, respond to and resolve support problems for their employees or customer networks. IT departments can use our software to proactively address technical problems before they occur, to respond more effectively to their employees when problems do occur through our self-healing and mass-healing capabilities, to enable knowledge-based self-service and to help the ongoing management of their technical resources and computing assets through automated discovery and management functionality. Similarly, broadband and other digital service providers utilize our software throughout their customer network to help acquire subscribers through automated installation and self-provisioning of services, retain subscriber loyalty via enhanced technical support and grow their business relationship with subscribers over time through automated provisioning of new added-value services such as home networking.

Enterprises that have purchased our products and services include: ADP, Inc., Bank of America Corporation, Cisco Systems, Inc., IBM Corporation, The Procter & Gamble Company, Siebel Systems, Inc., Sony Electronics, Inc. and Thomson Financial Inc.; managed service providers that have purchased our products to provide outsourced services to enterprises include: Accenture Limited, Affiliated Computer Services, Inc., CompuCom Systems, Inc., Computer Sciences Corporation, IBM Global Services and Perot Systems Corporation; and digital service providers incorporating our software into their service offerings include: Adelphia Communications Corporation, BellSouth Corporation, Charter Communications, Inc., Comcast Corporation, Cox Communications, Inc., SBC Communications, Inc., TeliaSonera, AB and Time Warner Cable.

### Industry Background

Technology has become a critical and fundamental element of business operations. The proliferation of technologies throughout an organization s business network includes personal computers and mobile devices, as well as customer-, supplier- and consumer-oriented technologies such as sales kiosks and digital service and supplier networks. We believe that organizations depend on the reliability and accessibility of their IT infrastructure to compete successfully. Given this dependence, organizations face increasing costs and challenges related to managing these complex, distributed and diverse technology environments. In addition, as the Internet and Internet-based networks become a primary medium of business activity,

39

**Table of Contents**

**Index to Financial Statements**

organizations must be able to respond rapidly and proactively to business challenges related to their IT infrastructure. Traditional approaches to resolving support and service issues and managing IT infrastructure have proven to be inefficient and difficult to scale in meeting the requirements of consumers and business users. We believe a real-time service management platform allows organizations to keep up with the growing complexity and cost of IT infrastructure and related support and service problems.

*Enterprises*

IT support and service departments of enterprises are tasked with supporting employees needs within a complex infrastructure consisting of multiple networks, operating systems and devices with remote access alternatives. In addition to maintaining uptime of the IT environment, the often resource-constrained departments must manage ongoing modifications to the IT environment through configurations, upgrades, migrations and provisioning of IT assets. As enterprises extend technology-based service offerings to customers, enterprise IT professionals will have the additional burden of servicing and supporting primary, customer facing business activities thereby increasing the cost of failure of poorly performing enterprise technology infrastructure. International Data Corporation, or IDC, an independent research firm, estimates that enterprises spent $4.0 billion on customer service and support, and PC and device management software during 2002, and projects that this spending will increase to $6.1 billion by 2006, representing a compound annual growth rate of 11%.

Given the reliance on IT for internal and external activities, enterprises have sought ways to more effectively and efficiently manage IT resources, prevent and address resource failure, provide technical support and service, accelerate installation of additional IT resources and support end user activities. Traditional approaches to addressing these challenges included reliance upon heavily staffed internal IT help desks and call centers, on-site support professionals and third-party vendor support. These approaches to meeting technical support and service needs have generally proven to be ineffective for enterprises given their costly and time-intensive nature and the difficulty to scale across expanding and distributed business networks. Gartner, Inc., an independent research firm, estimates that service and support costs account for 71% to 77% of the total cost of ownership for an enterprise s desktop or notebook computer.

We provide enterprises with a full spectrum of automated capabilities, including self-healing and mass-healing, that enable them to support and service their customers, partners and employees and manage their overall IT infrastructure more effectively. Our support and service capabilities are available to enterprises directly or through outsourced relationships with managed service providers. Enterprises that utilize our solutions can improve end user productivity and reduce technology support and service costs by reducing manual interventions, duplicative processes, technology downtime and more efficiently managing IT resources.

*Digital Service Providers*

The increasing availability of broadband delivery options and value-added services such as home networking, video on demand, or VoD, and voice over Internet protocol, or VoIP, are driving broadband subscriber growth. RHK, an independent research firm, estimates that the number of worldwide broadband access subscribers was 63 million in 2002, and projects that the number of subscribers will grow to 227 million by 2007, representing a compound annual growth rate of 29%. A broad range of digital service providers including cable companies, wireless and wireline network operators and device manufacturers have invested heavily across

40

**Table of Contents**

**Index to Financial Statements**

the globe to address and profit from the growing demand. Individual service providers continue to seek solutions that enable them to increase profitability per digital subscriber and overall return on investment. We believe that the ability to address the growing number of subscriber technical support and service issues are critical to successfully acquiring new subscribers, reducing subscriber turnover, introducing new services and increasing overall customer satisfaction.

Challenging support and service issues emerge at the outset of a potential subscriber s decision to purchase a broadband service and stem from the often time-consuming and difficult installation process. The challenges typically continue through resolving difficulties related to properly accessing broadband or digital services due to the need to address complex technical issues such as clearing a browser cache or configuring a number of interconnected network devices. In the past, resolution of these issues has typically involved an inconvenient or difficult to schedule on-site visit or phone support from call center personnel with limited knowledge of subscriber difficulties who often are not able to properly diagnose and resolve users problems.

We provide digital subscribers with a range of automated and intuitive self-install capabilities that facilitate use of new and existing service provider offerings. We also allow users to manage service offerings post-installation through self-service capabilities that enable subscribers to resolve technical service issues without requiring contact with technical service professionals. Service providers that provide our automation software to end users benefit from increased user satisfaction and profitability that stems from reducing delays in subscriber access of new and existing services, reducing costs of subscriber support and service and enhancing the overall user experience.

We believe that there is a significant opportunity to help enterprises and digital service providers automate their technical support, customer service and IT infrastructure management processes. Our real-time service management software can help these organizations avoid and resolve problems quickly and cost effectively, while improving productivity and user satisfaction.

**Strategy**

Our objective is to be the global leader of real-time service management software for enterprises and digital service providers. Key elements of our strategy include:

*Extend our Support and Service Automation Leadership*

We intend to extend our leadership position with our core products in customer service automation and enterprise technical support to IT infrastructure management to offer our customers a more comprehensive real-time service management platform. This includes extending our self-healing and mass-healing capabilities. In the enterprise market, we intend to deepen our presence based on our experience in technical support to provide a broader IT infrastructure management solution. In the digital service providers market, we intend to expand into related applications and enhanced digital services, including VoD, VoIP and next generation consumer applications such as digital media and video games. We intend to continue to offer our customers the flexibility to purchase and use our software in a variety of ways, including on an outsourced basis from managed service providers, embedded in computing devices from original equipment manufacturers, through a hosted delivery model or directly from us. By providing a comprehensive, real-time service management platform, we enable our enterprise and digital service provider customers to preempt, resolve and respond

41

**Table of Contents**

**Index to Financial Statements**

faster and more efficiently to service and support issues related to IT systems, wireline and wireless networks, personal computers, servers, mobile devices and software applications.

*Maintain and Enhance Technology Leadership Position*

We intend to continue to devote significant resources to technology development in order to introduce new suites and component products. Our products are designed to provide self-healing and mass-healing capabilities, manage and resolve difficult technical service and support problems across a variety of devices, including personal computers, servers and mobile devices. As Internet access and digital media expand through increasing adoption of new technologies, we intend to continue to invest significant resources in developing technologies that enhance the personalization, automation and overall effectiveness of our product offerings to meet requirements of next generation devices and technology. We intend to continue to foster an environment to obtain feedback from our customers through our customer advisory councils to provide us with valuable customer insights that we can integrate into future generations of our products.

*Expand International Presence*

We currently derive a substantial majority of our sales from our North American operations. We believe there is a significant opportunity to increase penetration of our products and services outside of North America. Currently, we have international offices in Australia, Germany, India, Japan, Singapore and the United Kingdom. We intend to further expand our sales, including direct and indirect channels, marketing and support efforts in Asia, Europe and India. For example, we believe the European digital service provider and enterprise markets represent key growth opportunities for us.

*Expand Relationships with Managed Service Providers*

We have developed relationships with key managed service providers to address growing customer demand for outsourced IT services. Enterprises are increasingly outsourcing a growing portion of their IT responsibility to managed service providers such as CSC and IBM Global Services. Managed service providers use our software to differentiate their outsourced IT management solutions and enable us to expand our reach to potential customers. We intend to enhance our current relationships and develop new relationships with managed service providers and to devote additional resources to sales, support and research and development in support of this effort.

*Pursue Strategic Acquisitions*

We believe that acquisitions of complementary technologies may allow us to expand our product offerings, augment our distribution channels and expand our market opportunities or broaden our customer base. We have acquired technology in the past to expand our product offerings and may in the future evaluate and pursue similar opportunities.

**Products**

Our software products enable enterprises and digital service providers to automate the delivery and management of technical service and support. Our real-time service management products automate the traditionally manual operations of technical support, customer service and IT infrastructure management. Our software provides self-healing capabilities by recognizing, diagnosing and resolving potential problems prior to an impact on the user either with or without user involvement or the user requesting assistance. Our software products have been architected and are built on a common software platform. This platform, based on a set of patented technologies, serves as the foundation for SupportSoft s software products.

We sell our software to enterprises and digital service providers as comprehensive suites and as component products. Our comprehensive suites offer customers integrated solutions to address a broad range of service and support issues, whereas our component solutions enable customers to address specific pain points.

The following diagram illustrates the enterprise technical support, customer service automation and IT infrastructure functions that our customers use our products to address:

*SupportSoft Suites*

We have three comprehensive software suites, Resolution Suite, Service Automation Suite  Broadband and Knowledge Center Suite, to address the unique needs of different market requirements. We also intend to release a fourth suite by the end of 2003, which will be known as Service Automation Suite  Video.

*Resolution Suite*.    Resolution Suite is our principal product offering for corporate enterprises interested in providing support automation to their employees. Resolution Suite enables organizations to reduce support costs and increase user productivity by automating the support of

**Table of Contents**

**Index to Financial Statements**

employees and devices through self-healing and mass-healing capabilities. Resolution Suite can decrease the volume of calls that a help desk receives, increase call resolution rates, minimize issue escalations and prevent costly desk-side visits by IT professionals.

Resolution Suite works across a wide range of software applications, hardware platforms and mobile devices. The suite utilizes the User Center and Support Center application modules, which are described in detail in Technology. Furthermore, Resolution Suite is not dependent on preloaded software or agents on the end-user s machine, and consequently it can be deployed via browser plug-ins that are downloaded when the end-user first requests support.

*Service Automation Suite Broadband*. Service Automation Suite Broadband has been designed to address the unique needs of broadband service providers, whether the broadband delivery is via digital subscriber line, or DSL, or cable. It is a fully integrated, comprehensive solution designed to automate all aspects of subscriber assistance, from connection through the ongoing support during the customer lifecycle. Service Automation Suite Broadband can decrease the volume of calls that a service provider receives, increase call resolution rates and minimize issue escalations and prevent expensive customer visits, or truck rolls.

Service Automation Suite Broadband has been developed using SupportSoft s core support automation infrastructure. The suite utilizes the User Center and Support Center application modules, which are described in detail in Technology. Service Automation Suite Broadband is not dependent on preloaded software or agents on the subscriber s machine, and consequently it can be deployed via browser plug-ins that are downloaded when the subscriber first requests support.

*Service Automation Suite Video*. Service Automation Suite Video is designed to expand our product offerings to the digital service providers market. We expect to release the new suite by the end of 2003. We have announced an alliance with Scientific-Atlanta s SciCare Broadband Services to bring this product to market. We expect that this new suite will offer many of the same benefits as our existing Service Automation Suite Broadband, except that it will be targeted at the digital video market.

*Knowledge Center Suite*. Knowledge Center Suite is a knowledge automation solution that provides web-based access to an organization s various knowledge bases to enable users and support analysts to help themselves. The Knowledge Center Suite allows employees, customers, partners and support professionals to gain self-service knowledge access through a natural language search engine that can provide them with precise answers to their questions based on a personal profile of their software or hardware characteristics. Support professionals can gain more advanced personalized access to a company s various repositories of information to assist in resolving their own problems or those of other users. This support resource can reduce the number of phone calls and other manual processes typically associated with knowledge retrieval.

Knowledge Center Suite is designed to allow an organization s support professionals to easily and rapidly author new content with powerful but easy-to-use personalization. Knowledge Center Suite also includes reporting capabilities that track the effectiveness of the content, allowing service and support professionals to update ineffective answers within their knowledge base, so that only precise answers are readily available to questions posed by requestors.

**Table of Contents**

**Index to Financial Statements**

*SupportSoft Component Products*

In addition to our software suites, we provide component software products that can be purchased individually or in combination with our other offerings. These products are generally available at lower price points than a comprehensive software suite and address specific needs for enterprises and digital service providers. Our component products are designed to work together easily.

*Auto Discovery and Metering*. Auto Discovery and Metering is a component product designed to discover detailed information about an organization s personal computing software and hardware. It can remotely and automatically gather hundreds of details about a computing device, populate a central database with information about user devices and report on what is being used, by whom and how often. As a result, the product allows organizations to manage personal computing resources, monitor the utilization of their software applications and determine whether such use is in compliance with applicable licenses. Using the product s reporting feature, organizations can determine when they should re-deploy software licenses for optimum usage, remove unlicensed software from users machines and better allocate hardware to individuals or departments. The information generated from the software can help an organization cost effectively manage its technology assets through more efficient deployment and higher license utilization.

*RemoteAssist*. RemoteAssist is a component product designed to enable IT support analysts to remotely take control of a user s Microsoft Windows computing system, with the user s permission, to speed problem resolution. By remotely managing and controlling a device, a support analyst can diagnose problems in detail, including whether the problem is at the application, hardware or operating system level, determine the necessary action to resolve the problem and implement the resolution. No complex software installation or re-boot of the computer is required and a complete audit trail of all remote sessions is retained to expedite resolution should the problem be encountered again.

*SmartAccess*. SmartAccess is a component product designed to provide digital service providers with the capabilities to automatically determine if a subscriber s computing system is adequately qualified for a broadband connection and, if so, enables self-installation and activation of high-speed Internet services. Once connected, SmartAccess also allows subscribers to easily order, install and configure additional value-added services such as home networking. SmartAccess complements the functionality of the Service Automation Suite Broadband.

*HomeNet*. HomeNet is a component product designed to offer digital service providers a wide range of capabilities to streamline the entire home networking process for broadband subscribers including installation, configuration and ongoing support.

*LiveAssist.* We are introducing LiveAssist, a component product designed to provide high-volume call center organizations and IT help desks with the ability to service online customers with a scalable, interactive chat solution.

**Technology**

Our technology consists of a software platform, application modules and core intellectual property. Our technology is designed to enable our suites and component products to be extended and easily adapt to and integrate with varying environments.

**Table of Contents**

**Index to Financial Statements**

*Real-Time Service Management Platform*

Real-Time Service Management Platform, formerly called our Problem Resolution Platform, is the foundation upon which all of our other modular products and suites are installed and operated. Real-Time Service Management Platform provides a single point of integration for all of our suites and component products.

The platform supports a high degree of scalability using industry standard web server infrastructure and supports datacenter practices such as load balancing, clustering and data partitioning. Our products are web-based and cross-platform and provide similar functionality on a variety of web servers, application servers, operating systems and databases. The architecture has been used in implementations that have scaled beyond one million devices.

Real-Time Service Management Platform includes common services that are shared by many of our products, allowing for faster product development, more flexible behavior and consistent usability. Common services include user and group management, security, user interface navigation, database access, XML handling, reporting and integration.

The platform provides web interface frameworks designed to house component functionality for users, support professionals, system administrators and authors. These interfaces are designed to allow personalized, securable views depending on which component products are installed. The user and group management services provide for internal management as well as integration with various user directory standards systems such as Active Directory and lightweight directory access protocol, or LDAP. In normal practice, installation of new products would enable additional capabilities within one or more interfaces.

The database access is centralized within the platform to provide a common interface to the supported Microsoft, Oracle and IBM databases. The reporting services provide a common structure for authoring reports and a hierarchy for report organization as additional products are installed. Numerous integration points are provided by the platform to exchange incident information, leverage existing directories for security and group management and retrieve additional content.

*Standards.* Real-Time Service Management Platform and products built upon it utilize many open standards to facilitate their development, implementation and use, including standards for communication between systems, data storage, transfer, reporting, integration and user interface abstraction, as well as development standards. In addition, our products leverage many platform and language specific standards. For the customizable portions of our software, we use widely accepted development standards in order make customization simpler.

*Application Modules*

*User Center.* User Center provides users with self-healing and automated self-service capabilities to resolve problems and questions that would otherwise require a call to the contact center or help desk. User Center acts as the user s personalized, context-sensitive support assistant, identifying and automatically solving problems before they cause users to experience problems. User Center provides a single source of information for addressing software and system malfunctions and responding to users queries.

*Support Center.* Support Center provides a centralized support infrastructure and software components for analysts to provide remote assisted service, enterprise-wide problem resolution and administration of the overall support environment. Support Center provides support analysts with the ability to deliver context-sensitive diagnosis and resolution of user problems.

**Table of Contents**

**Index to Financial Statements**

Support Center is designed to enable the support organization to identify and solve problems for a large number of users across the organization before user productivity becomes impaired, which we refer to as mass healing. The administration capabilities of the Support Center provide centralized user management, usage and status reporting, storage maintenance, security administration and instructions for the Center. The Support Center manages characteristics and privileges for users and support analysts and reports on support activities. The Support Center is designed to provide customizable levels of privileges for users and support analysts and records support activities.

*Web Administrator.* Web Administrator is designed to provide a centralized web interface for management of the entire system. Our modular architecture is used to provide varying levels of control to different administrators while still housing all of the administration features in one place. The administration capabilities of the Web Administrator include common platform services such as security, reporting and user management as well as product specific administration.

*Content Center.* Content Center is designed to provide an authoring environment with content versioning, security and workflow. As products are installed, new types of content and additional tools may become available including an integrated development environment for automated solutions that leverages multiple scripting languages, debugging and context-sensitive help.

*Complementary Technologies*

We work closely with our customers to understand how our alliances can provide the greatest benefit, whether it be for ease of integration with legacy applications, a complement to existing user support applications or to leverage a fully developed knowledge base. Through this customer dialogue, we have integrated with a variety of call tracking systems, including Amdocs (formerly Clarify), Peregrine, PeopleSoft and BMC s Remedy. We have also worked with M-Tech, Qarbon and RightAnswers to provide additional depth and content to current functionality.

*Core Intellectual Property*

Our core intellectual property is fundamental to our platform and product offering. We have six patents related to our SmartIssue, DNA Probe and Software Vault technologies and three additional patents pending. The following is a summary of our core intellectual property:

*SmartIssue Technology.* Our patented SmartIssue technology is designed to automatically collect relevant information about a user, system and problem. This information is delivered to the support professional only upon the user s consent. Based on this information, SmartIssue technology is designed to automatically and intelligently connect users to the support tools, personnel and communication channels that best address the support issue.

*SmartResult System.* The SmartResult system combines SmartIssue information with advanced search technology to automate problem resolution for how-to questions to help deliver the best, most precise answer to an inquiry. The SmartResult system can target users based upon defined characteristics such as which department the user is in, whether the user is a mobile user or whether the user speaks a foreign language.

*DNA Probe.* Our patented DNA Probe can provide detailed data about users, their system and their software. DNA Probe technology is designed to automatically identify the characteristics of each user s software applications and operating system components and

**Table of Contents**

**Index to Financial Statements**

tracks them over time. This personalized data can be used to filter through large amounts of information, compare historical data and highlight potential fundamental causes of problems. For example, DNA Probe technology automatically identifies all of the network settings for each individual user, including the network address, machine name, Internet configuration and the specific drivers for their network card. DNA Probe can learn about an individual computing environment to efficiently provide a user with personalized support solutions.

*SupportAction.* SupportAction is a custom packaged support solution, or active content, that is designed to enable the automation of common support requirements, such as solving problems or answering questions. Support analysts create a SupportAction using a point-and-click interface. Support organizations can program existing applications, commands and content into a SupportAction to turn static information into automated knowledge. For example, the support organization could integrate a diagnostic program into a SupportAction so that the user can automatically perform the steps described by the diagnostics program. A SupportAction can accommodate many scripting languages and a wide range of content.

*DNA Infrastructure.* DNA Infrastructure provides a common mechanism for the distribution and application of changes to one or more devices. This infrastructure is used across our products so that changes made to a user s device are consistent, reversible and recorded. Repair to a user s device, comparison of one device to another, installation, modification and distribution can all be achieved using our DNA Infrastructure. Support solutions are easier to develop with this infrastructure because steps that are done manually are potentially error-prone and are replaced by automatic and consistent mechanisms. DNA Infrastructure facilitates rapid development and can reduce the cost of on-going maintenance.

*Nexus.* Nexus acts as an intermediary that enables our products to communicate if a firewall or other device prevents direct communication or if direct communication is unreliable or impossible. Our products communicate directly with each other using secure protocols, even through firewalls and other network components often restrict direct communication across the Internet.

*Software Vaults.* Software Vault is designed to provide efficient and redundant storage, retrieval and management of support content. Files and programs for supported applications, operating system components and all SupportActions are stored in the Software Vault. Once a user s problem is diagnosed, the solution in the form of files, programs and other information, is delivered to the user from the Software Vault.

**Sales and Distribution**

We sell our software directly to enterprises, managed service providers and digital service providers and indirectly through distribution alliances. Currently, we manage regional sales resources in the United States, Canada, the United Kingdom, Germany, Singapore, Australia and Japan.

We have established reseller relationships that deliver our solutions to multiple markets. We believe these relationships allow us to benefit from their marketing and lead generation capabilities, and are intended to increase geographic sales coverage and to address other market opportunities. These relationships are complementary to our direct sales effort.

48

**Table of Contents**

**Index to Financial Statements**

**Customers**

Our support and service automation software is utilized by Global 2000 enterprise customers, managed service providers, broadband and digital services providers and other organizations.

Customers with revenue or orders of $100,000 or greater during 2002 and 2003 include:

| Enterprises and Managed Service Providers | | Digital Service Providers |
|---|---|---|
| 3M Company | Dimension Data Network Services Ltd. | Adelphia Communications Corporation |
| Accenture Limited | Fujitsu Siemens Computers GmbH | BellSouth Corporation |
| Affiliated Computer Services, Inc. | General Electric Company | Charter Communications, Inc. |
| ADP, Inc. | Health Care Services Corp. of America | Comcast Corporation |
| Automated Systems (HK) Limited | IBM Corporation | Cox Communications, Inc. |
| Assurant Group | NEC Corporation | SBC Communications, Inc. |
| Bank of America Corporation | Perot Systems Corporation | TeliaSonera, AB |
| Belgacom, NV | The Procter & Gamble Company | Time Warner Cable |
| British Telecommunications plc | RWE Systems, AG | |
| Cap Gemini Ernst & Young UK plc | Schlumberger Omnes, Inc. | |
| Cisco Systems, Inc. | Siebel Systems, Inc. | |
| CompuCom Systems, Inc. | Sony Electronics, Inc. | |
| Computer Sciences Corporation | Telewest Communications, PLC | |
| Delta Air Lines, Inc. | Thomson Financial Inc. | |

**Alliances**

We establish software and hardware alliances to ensure that our support and service automation software can be integrated with the software and hardware technology infrastructure of our customers. We engage in alliances that we believe can enhance our solution or can assist customers in gaining more return on their investment from our software. We have existing alliances with software and hardware vendors such as IBM Corporation, Siebel Systems, Inc. and Sony Electronics, Inc. For example, we have entered into an alliance with Siebel Systems, Inc., which has licensed our software for incorporation in its Employee Relationship

Management, or ERM, software product for resale to its customers.

We have formed relationships with managed service providers that represent both a key customer base and a strategic delivery option for our products. We have developed relationships with key managed service providers, including Accenture Limited, Affiliated Computer Services, Inc., Automated Systems (HK) Limited, Cap Gemini Ernst & Young UK plc, CompuCom Systems, Inc., Computer Sciences Corporation, IBM Global Services and Perot Systems Corporation, to address growing customer demand for outsourced IT management services. Managed service providers seek ways to provide new value and increase service levels to current and prospective customers. Our software can help managed service providers differentiate their IT solutions by improving customer satisfaction and reducing the time and expense to resolve technical problems for a customer s software applications. In addition, managed service providers enable us to reach a segment of the market that would otherwise be difficult for us to address.

We have formed a relationship with Scientific-Atlanta s SciCare Broadband Services to develop the Service Automation Suite Video. We believe this alliance will allow us to develop products that cable providers can use to reduce costs and offer better service to their customers.

**Global Services**

Our Global Services organization provides professional service offerings to our customers ranging from architectural design to ongoing support. Our Global Services group provides

**Table of Contents**

**Index to Financial Statements**

solutions for our customers that can be used across all or parts of their organizations. Its capabilities are principally divided into five areas:

*Implementation*. Provides architectural design, transformation, product integration and deployment services.

*Education*. Trains customers and those parties with whom we have alliances in the design, implementation and use of our products.

*Technical Support*. Responds to design, feature, implementation and deployment questions.

*Customer Care*. Provides ongoing assistance to optimize customer communication and feedback for smooth technology deployment, including using our own software to provide an Internet support portal, entitled ExpertExchange, as well as regular user group forums by which customers can assist each other in discussing product issues and opportunities.

*Strategic Services*. Educates customers on best practices for supporting and servicing users and encouraging users to move from traditional support processes, such as a phone call to the help desk, to an automated approach, in order to accelerate the customer s return on investment.

Under our standard maintenance contract, our customers receive generally available upgrades, corrections, enhancements and updates to the products they have licensed.

**Research and Development**

We devote a substantial portion of our resources to developing new and enhanced versions of our support and service automation software, conducting product testing and quality assurance testing and improving our core technologies. Fundamental to our research and development strategy are rapid product develop cycles, continuous improvement and customer feedback. We believe that customers serve as an extension of our research and development process by providing us with valuable feedback from their hands-on usage to assist with our product improvements, implementation services and new market opportunities and strategy. We have created a customer advisory council with a representative sample of our customers to formalize this input.

Our research and development expenditures were approximately $6.8 million for the nine months ended September 2003, $8.8 million in 2002, $12.6 million in 2001 and $10.9 million in 2000. We expect to continue to devote significant resources to research and development for the foreseeable future.

**Intellectual Property**

*Patents*

We have six patents in the general areas of automated discovery of dynamic configurations, our SmartIssue technology and our software vault technology. We have three patent applications pending in the United States, and we may seek additional patents in the future. We do not know if our patent applications or any future patent application will result in a patent being issued with the scope of the claims we seek, if at all. Also, we do not know whether any patents we have or may receive will be challenged or invalidated. It is difficult to monitor unauthorized use of technology, particularly in foreign countries where the laws may not protect our proprietary rights as fully as in the United States, and our competitors may independently develop technology similar to ours.

**Table of Contents**

**Index to Financial Statements**

*Copyright, Trademark and other Proprietary Rights*

Our trademarks and service marks include SupportSoft and related designs, Support.com and related designs, the support man logo, ContextResponse Technology, DNA, DNA Probe, HomeNet, LiveAssist, Nexus, RapidReset, Resolution Suite, Resolution Suite Integration Toolkit, Satisfaction Suite, SmartAccess, SmartIssue, SmartResult, SupportAction and SupportTrigger. We claim common law rights for other marks. Third parties may infringe or misappropriate our copyrights, trademarks and similar proprietary rights. We rely on a combination of copyright, trade secret, trademark and contractual protection to establish and protect our proprietary rights that are not protected by patent. We also enter into confidentiality agreements with our employees and consultants involved in product development. We routinely require our employees, customers and potential business partners to enter into confidentiality agreements before we will disclose any sensitive aspects of our business. Also, we require employees to agree to surrender to us any proprietary information, inventions or other intellectual property they generate or come to possess while employed by us. These precautions may not prevent misappropriation or infringement of our intellectual property.

**Competition**

We compete in markets that are highly competitive, subject to rapid change and significantly affected by new product introductions and other market activities of industry participants. Although we do not believe there is one principal competitor in the market for all aspects of our support and service automation solutions for the enterprise and digital service provider markets, we do compete with a number of companies in the market for automated delivery of support and service and other vendors who may offer products or services with features that compete with specific elements of our suite solutions or with our component products.

Software companies we encounter in competitive situations include a broad range of public and private companies. Our principal competition comes from public companies such as Altiris, Inc., Computer Associates International, Inc., Novadigm, Inc., Peregrine Systems, Inc. and Primus Knowledge Solutions, Inc., and private companies such as Motive Communications, Inc. and RightNow Technologies, Inc. In addition, we expect that internally developed applications will continue to be a significant source of competition in the foreseeable future. We believe that the principal competitive factors in our market include the following:

- product functionality;
- demonstrated return-on-investment;
- breadth of platform and integrated architecture;
- quality and performance and reputation of solutions;
- pricing;
- implementation services and support; and

product innovation.

We believe that we presently compete favorably with respect to each of these factors. However, the markets for our products are still rapidly evolving, and we may not be able to compete successfully against current and potential competitors. Our ability to expand our business will depend on our ability to maintain our technological advantage, introduce timely enhanced products to meet the growing support needs, deliver on-going value to our customers and scale our business.

**Table of Contents**

**Index to Financial Statements**

Our competitors may be able to respond more quickly to new or emerging technologies and changes in customer requirements. Our potential competitors may have longer operating histories, significantly greater financial, technical and other resources or greater name recognition than we do. Furthermore, it is possible that new competitors or alliances or mergers among competitors may emerge and rapidly acquire significant market share. Competition could seriously harm our ability to sell additional software, maintenance renewals and services on terms favorable to us. Competitive pressures could also reduce our market share or require us to reduce the price of products and services, which could harm our business, financial condition and operating results.

**Employees**

As of September 30, 2003, we had 154 full-time employees, of which 61 were in sales and marketing, 49 were in research and development, 31 were in professional services and 13 were in general and administrative. None of our employees are covered by collective bargaining agreements. We believe our relations with our employees are good.

**Properties**

Our corporate headquarters are located in Redwood City, California, where we lease approximately 23,600 square feet under a lease that expires in May 2005, with an option to extend for an additional two years. As of September 30, 2003, we also leased office space in 12 other cities for our sales and support personnel. The terms of these leases expire beginning in January 2004 and ending in October 2006, and automatically renew unless earlier terminated. We may require additional space to meet our needs within the next 12 months.

**Legal Proceedings**

In November 2001, a class action lawsuit was filed against us and two of our officers in the United States District Court for the Southern District of New York. The lawsuit alleged that our registration statement and prospectus dated July 18, 2000 for the issuance and initial public offering of 4,250,000 shares of our common stock contained material misrepresentations and/or omissions, related to alleged inflated commissions received by the underwriters of the offering. The defendants named in the lawsuit are SupportSoft, Radha Basu, Brian Beattie, Credit Suisse First Boston Corporation, Bear, Stearns & Co. Inc. and FleetBoston Robertson Stephens Inc. The lawsuit seeks unspecified damages as well as interest, fees and costs. Similar complaints have been filed against 55 underwriters and more than 300 other companies and other individual officers and directors of those companies. All of the complaints against the underwriters, issuers and individuals have been consolidated for pre-trial purposes before U.S. District Court Judge Scheindlin of the Southern District of New York. On June 26, 2003, the plaintiffs announced that a proposed settlement between the issuer defendants and their directors and officers had been reached. As a result of the proposed settlement, which is subject to court approval, our insurance carrier will be responsible for any payments other than attorneys fees prior to June 1, 2003. On September 2, 2003, plaintiffs executive committee advised the court that individuals identified as lead plaintiffs in six of the consolidated IPO cases, one of them being the action against us, were unwilling to serve as class representatives, and sought leave to seek new class representatives. On October 20, 2003, we were notified that new class representatives would be substituted into the case. While we cannot predict with certainty the outcome of the litigation or whether the settlement will be approved, we believe that the claims against us and our officers are without merit.

We are also subject to other routine legal proceedings, as well as demands, claims and threatened litigation, that arise in the normal course of our business. The ultimate outcome of

52

**Table of Contents**

**Index to Financial Statements**

any litigation is uncertain, and either unfavorable or favorable outcomes could have a material negative impact. Regardless of outcome, litigation can have an adverse impact on SupportSoft because of defense costs, diversion of management resources and other factors.

**Table of Contents**

**Index to Financial Statements**

## MANAGEMENT

### Executive Officers and Directors of the Registrant

Our executive officers and directors and their ages as of September 30, 2003, are:

| Name | Age | Position |
| --- | --- | --- |
| Radha R. Basu | 53 | Chief Executive Officer, President and Chairman of the Board |
| Brian M. Beattie | 50 | Chief Financial Officer, Executive Vice President of Finance and Administration |
| Scott W. Dale | 34 | Chief Technical Officer and Vice President of Engineering |
| Cadir B. Lee | 32&nbs | |