

ACTUATE CORP
Form 10-Q
November 07, 2012
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2012

OR

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

For the transition period from _____ to _____

Commission File No. 0-24607

Actuate Corporation

(Exact name of Registrant as specified in its charter)

Edgar Filing: ACTUATE CORP - Form 10-Q

Delaware
(State of incorporation)

94-3193197
(I.R.S. Employer
Identification No.)

951 Mariners Island Boulevard,
San Mateo, California 94404
(650) 645-3000
(including area code, of Registrant's principal executive offices)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practicable date.

| Title of Class | Outstanding as of October 31, 2012 |
|--|------------------------------------|
| Common Stock, par value \$.001 per share | 48,968,373 |

Table of Contents

Actuate Corporation

Table of Contents

PART I FINANCIAL INFORMATION

| | | |
|---------|--|----|
| Item 1. | <u>Financial Statements</u> | 3 |
| | <u>Condensed Consolidated Balance Sheets as of September 30, 2012 and December 31, 2011</u> | 3 |
| | <u>Condensed Consolidated Statements of Income for the three and nine months ended September 30, 2012 and 2011</u> | 4 |
| | <u>Condensed Consolidated Statements of Comprehensive Income for the three and nine months ended September 30, 2012 and 2011</u> | 5 |
| | <u>Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2012 and 2011</u> | 6 |
| | <u>Notes to Condensed Consolidated Financial Statements</u> | 7 |
| Item 2. | <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> | 21 |
| Item 3. | <u>Quantitative and Qualitative Disclosures about Market Risk</u> | 33 |
| Item 4. | <u>Controls and Procedures</u> | 34 |

PART II OTHER INFORMATION

| | | |
|----------|--|----|
| Item 1. | <u>Legal Proceedings</u> | 34 |
| Item 1A. | <u>Risk Factors</u> | 34 |
| Item 2. | <u>Unregistered Sales of Equity Securities and Use of Proceeds</u> | 45 |
| Item 6. | <u>Exhibits</u> | 46 |
| | <u>Signatures</u> | 47 |

Table of Contents**Part I. Financial Information****Item 1. Financial Statements****ACTUATE CORPORATION****CONDENSED CONSOLIDATED BALANCE SHEETS****(in thousands except share and per share data)****(unaudited)**

| | September 30, 2012 | December 31, 2011 |
|---|-------------------------------|------------------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 39,453 | \$ 38,759 |
| Short-term investments | 35,147 | 28,669 |
| Accounts receivable, net of allowances of \$400 and \$720 at September 30, 2012 and December 31, 2011, respectively | 20,140 | 26,844 |
| Other current assets | 10,012 | 7,131 |
| Total current assets | 104,752 | 101,403 |
| Property and equipment, net | 7,966 | 1,927 |
| Goodwill | 46,424 | 46,424 |
| Purchased intangibles, net | 9,733 | 11,421 |
| Non-current deferred tax assets, net | 12,952 | 14,876 |
| Other assets | 783 | 853 |
| | \$ 182,610 | \$ 176,904 |
| LIABILITIES AND STOCKHOLDERS EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 1,345 | \$ 1,521 |
| Current portion of restructuring liabilities | 108 | 98 |
| Accrued compensation | 5,355 | 5,992 |
| Other accrued liabilities | 4,612 | 5,872 |
| Deferred revenue | 37,073 | 43,045 |
| Total current liabilities | 48,493 | 56,528 |
| Long-term liabilities: | | |
| Other liabilities | 3,158 | 20 |
| Long-term deferred revenue | 1,305 | 1,717 |
| Long-term income taxes payable | 1,350 | 1,670 |
| Restructuring liabilities, net of current portion | 27 | 106 |
| Total long-term liabilities | 5,840 | 3,513 |

Edgar Filing: ACTUATE CORP - Form 10-Q

Stockholders' equity:

| | | |
|---|----------------|----------------|
| Preferred stock, \$0.001 par value, issuable in series; 5,000,000 shares authorized; none issued or outstanding | | |
| Common stock, \$0.001 par value, 100,000,000 shares authorized; issued 88,064,036 and 85,270,644 shares, respectively; outstanding 48,940,248 and 48,518,460 shares, respectively | 49 | 48 |
| Additional paid-in capital | 232,393 | 214,770 |
| Treasury stock, at cost; 39,123,788 and 36,752,184 shares, respectively | (163,321) | (147,331) |
| Accumulated other comprehensive income | 1,654 | 1,419 |
| Retained earnings | 57,502 | 47,957 |
| Total stockholders' equity | 128,277 | 116,863 |
| | \$ 182,610 | \$ 176,904 |

The accompanying notes are an integral part of these condensed consolidated financial statements.

Table of Contents

ACTUATE CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(in thousands, except per share data)

(unaudited)

| | Three Months Ended September 30, | | Nine months Ended September 30, | |
|---|-------------------------------------|-----------------|------------------------------------|-----------------|
| | 2012 | 2011 | 2012 | 2011 |
| Revenues: | | | | |
| License fees | \$ 13,304 | \$ 11,815 | \$ 42,389 | \$ 35,914 |
| Services | 18,875 | 21,994 | 60,854 | 63,721 |
| Total revenues | 32,179 | 33,809 | 103,243 | 99,635 |
| Costs and expenses: | | | | |
| Cost of license fees | 482 | 424 | 1,439 | 1,366 |
| Cost of services | 5,187 | 4,998 | 15,267 | 15,653 |
| Sales and marketing | 12,067 | 10,423 | 35,811 | 31,819 |
| Research and development | 6,060 | 5,830 | 17,668 | 18,480 |
| General and administrative | 5,360 | 4,885 | 16,918 | 15,623 |
| Amortization of other purchased intangibles | 289 | 289 | 867 | 1,007 |
| Asset impairment | | | | 1,681 |
| Restructuring charges | 21 | 158 | 54 | 889 |
| Total costs and expenses | 29,466 | 27,007 | 88,024 | 86,518 |
| Income from operations | 2,713 | 6,802 | 15,219 | 13,117 |
| Interest income and other income/(expense), net | 174 | 982 | 763 | (840) |
| Interest expense | (55) | (136) | (255) | (781) |
| Income before income taxes | 2,832 | 7,648 | 15,727 | 11,496 |
| Provision for income taxes | 2,725 | 2,926 | 6,182 | 4,514 |
| Net income | \$ 107 | \$ 4,722 | \$ 9,545 | \$ 6,982 |
| Basic net income per share | \$ 0.00 | \$ 0.10 | \$ 0.19 | \$ 0.15 |
| Shares used in basic per share calculation | 49,207 | 48,058 | 49,156 | 46,873 |
| Diluted net income per share | \$ 0.00 | \$ 0.09 | \$ 0.18 | \$ 0.14 |
| Shares used in diluted per share calculation | 52,794 | 52,285 | 52,794 | 51,224 |

The accompanying notes are an integral part of these condensed consolidated financial statements.

Table of Contents

ACTUATE CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(in thousands, unaudited)

| | Three Months Ended | | Nine months Ended | |
|---|---------------------------|-------------|--------------------------|-------------|
| | September 30, | | September 30, | |
| | 2012 | 2011 | 2012 | 2011 |
| Net income | \$ 107 | \$ 4,722 | \$ 9,545 | \$ 6,982 |
| Other comprehensive income, before tax: | | | | |
| Foreign currency translation gain/(loss) | \$ 257 | \$ (1,381) | \$ 161 | \$ 633 |
| Net unrealized gain/(loss) on securities | 60 | (48) | 74 | (59) |
| Other comprehensive income/(loss), before tax | \$ 317 | \$ (1,429) | \$ 235 | \$ 574 |
| Tax provision (benefit) related to other comprehensive income | 124 | (547) | 92 | 225 |
| Other comprehensive income/(loss), net of tax | \$ 193 | \$ (882) | \$ 143 | \$ 349 |
| Comprehensive income | \$ 300 | \$ 3,840 | \$ 9,688 | \$ 7,331 |

The accompanying notes are an integral part of these condensed consolidated financial statements.

Table of Contents**ACTUATE CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(in thousands, unaudited)

| | Nine months Ended September 30, | |
|--|--|-----------------|
| | 2012 | 2011 |
| Operating activities | | |
| Net income | \$ 9,545 | \$ 6,982 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Share-based compensation expense | 5,454 | 3,888 |
| Excess tax benefit from exercise of stock options | (2,440) | (2,729) |
| Amortization of other purchased intangibles | 1,687 | 1,827 |
| Amortization of debt issuance cost | 51 | 216 |
| Depreciation | 1,587 | 1,524 |
| Change in valuation allowance on deferred tax assets | 1,767 | 1 |
| Impairment of intangible assets | 89 | 1,681 |
| Accretion/amortization on short-term debt securities | 189 | (294) |
| Changes in operating assets and liabilities, net of acquired assets and assumed liabilities: | | |
| Accounts receivable, net of allowance | 6,704 | 6,650 |
| Other current assets | (2,635) | 96 |
| Accounts payable | (241) | (388) |
| Accrued compensation | (637) | (1,329) |
| Other accrued liabilities | (521) | (363) |
| Deferred tax assets, net of liabilities | 170 | 584 |
| Income taxes receivable/payable, net | (872) | (2,187) |
| Other deferred liabilities | 3,138 | (247) |
| Restructuring liabilities | (69) | (1,069) |
| Deferred revenue | (6,384) | (555) |
| Net cash provided by operating activities | 16,582 | 14,288 |
| Investing activities | | |
| Purchases of property and equipment | (5,038) | (509) |
| Proceeds from sale and maturity of investments | 22,694 | 59,366 |
| Purchases of short-term investments | (29,286) | (33,176) |
| Security deposits and other | (55) | 115 |
| Net cash provided by (used in) investing activities | (11,685) | 25,796 |
| Financing activities | | |
| Repayment of long term debt | (34) | (40,000) |
| Excess tax benefit from exercise of stock options | 2,440 | 2,729 |
| Proceeds from issuance of common stock | 9,223 | 11,698 |
| Stock repurchases | (15,993) | (4,999) |
| Net cash used in financing activities | (4,364) | (30,572) |
| Effect of exchange rates on cash and cash equivalents | 161 | 633 |
| Net increase in cash and cash equivalents | 694 | 10,145 |

Edgar Filing: ACTUATE CORP - Form 10-Q

| | | |
|---|-----------|-----------|
| Cash and cash equivalents at the beginning of the period | 38,759 | 33,269 |
| Cash and cash equivalents at the end of the period | \$ 39,453 | \$ 43,414 |
| Supplemental cash flow disclosures: | | |
| Cash paid for interest and unused fees on the revolving credit line | \$ 212 | \$ 559 |
| Cash paid for income taxes | \$ 3,448 | \$ 6,321 |
| Non-cash Investing activities: | | |
| Leasehold incentives subsidized by the landlord | \$ 2,613 | \$ |

The accompanying notes are an integral part of these condensed consolidated financial statements.

Table of Contents

ACTUATE CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Summary of Significant Accounting Policies

The Company

Actuate Corporation (we , Actuate or the Company) was incorporated in November 1993 in the State of California and reincorporated in the State of Delaware in July 1998. Actuate provides software and services to develop and deploy custom Business Intelligence and information applications that deliver rich interactive content to improve customer loyalty and corporate performance. Applications built on Actuate s open source-based platform provide stakeholders inside and outside the firewall, including employees, customers, partners and citizens with information that they can access and understand to maximize revenue, cut costs, improve customer satisfaction, streamline operations, create competitive advantage and make better decisions. Our goal is to ensure that all users can use decision-making information in their day-to-day activities, opening up completely new avenues for improving corporate performance.

As of the date of filing this 10-Q, Actuate s principal executive offices are located at the BayCenter Campus in San Mateo, California. Actuate s telephone number is 650-645-3000. Actuate maintains Web sites at www.actuate.com, www.birt-exchange.org and www.birt-exchange.com.

Basis of Presentation

The Company has prepared the accompanying unaudited condensed consolidated financial statements pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Pursuant to these rules and regulations, the Company has condensed or omitted certain information and footnote disclosures it normally includes in its annual consolidated financial statements prepared in accordance with U.S. generally accepted accounting principles (GAAP). In management s opinion, the Company has made all adjustments (consisting only of normal, recurring adjustments, except as otherwise indicated) necessary to fairly present its financial position, results of operations and cash flows. The Company s interim period operating results do not necessarily indicate the results that may be expected for any other interim period or for the full fiscal year. These financial statements and accompanying notes should be read in conjunction with the consolidated financial statements and notes thereto in Actuate s Annual Report on Form 10-K for the fiscal year ended December 31, 2011 filed with the SEC on March 9, 2012.

To prepare financial statements in conformity with GAAP, management must make estimates and assumptions that affect the amounts reported in the unaudited condensed consolidated financial statements and accompanying notes. Actual results could differ from these estimates and may result in material effects on the Company s operating results and financial position.

The consolidated financial statements include the accounts of Actuate and its wholly-owned and majority-owned subsidiaries. Actuate has offices throughout North America, Europe and Asia including offices in the United States, Canada, Switzerland, United Kingdom, Germany, Singapore, Japan and China. All intercompany balances and transactions have been eliminated.

Revenue Recognition

Actuate generates revenues from the sales of software licenses and related services. The Company receives software license revenues from licensing its products directly to end-users and indirectly through resellers, system integrators and original equipment manufacturers (OEMs). The Company receives service revenues from maintenance contracts, consulting services and training that Actuate performs for customers.

For sales to end-user customers, Actuate recognizes license revenues when a license agreement has been signed by both parties or a definitive agreement has been received from the customer, the product has been physically shipped or electronically made available, there are no unusual uncertainties surrounding the product acceptance, the fees are fixed or determinable, collectability is probable and vendor-specific objective evidence of fair value exists to allocate the fee to the undelivered elements of the arrangement. Vendor-specific objective evidence of fair value of sales to end users is based on the price charged when an element is sold separately.

Actuate has not established vendor-specific objective evidence of fair value for its licenses. Therefore, the Company recognizes revenues from software arrangements with multiple elements involving software licenses under the residual method, which means the fair value of the undelivered elements is deferred while the remaining value of the arrangement is allocated to the delivered elements. If an agreement includes a

Edgar Filing: ACTUATE CORP - Form 10-Q

bundled fee comprised of license and services, then the company separates this bundled fee into its individual revenue components based on the vendor-specific objective evidence (VSOE) of fair value of the services, with the remainder being allocated to license revenue. If the license agreement contains payment terms that would indicate that the fee is not fixed or determinable, revenues are recognized as the payments become due and payable, assuming that all other revenue recognition criteria are met.

Table of Contents

Actuate enters into reseller and distributor arrangements that typically give such distributors and resellers the right to distribute its products to end-users headquartered in specified territories. Actuate recognizes license revenues from arrangements with resellers and distributors when there is persuasive evidence of an arrangement with the reseller or distributor, the product has been shipped, the fees are fixed or determinable, collectability is probable and vendor-specific objective evidence of fair value exists to allocate the fee to the undelivered elements of the arrangement. Actuate recognizes license revenues from arrangements with resellers and distributors when all other revenue recognition criteria have been met.

Actuate also enters into OEM arrangements that provide for license fees based on the bundling or embedding of its products with the OEM's products. These arrangements generally provide for fixed, irrevocable royalty payments. Actuate recognizes license fee revenues from U.S. and international OEM arrangements when a license agreement has been executed by both parties, the product has been shipped, there are no unusual uncertainties surrounding the product acceptance, the fees are fixed or determinable, collectability is probable and vendor-specific objective evidence of fair value exists to allocate the fee to the undelivered elements of the arrangement.

Actuate also has two software-as-a-service (SaaS) offerings called OnPerformance and BIRT On Demand. Actuate recognizes revenue on these licenses ratably over the term of the underlying arrangement.

The Company typically establishes vendor specific objective evidence of fair value for maintenance and support, consulting and training using a bell-shaped curve approach. However, for certain types of license transactions, including OEM and site licenses, the Company uses a stated maintenance renewal approach.

The Company assesses the collectability of fees from end-users based on payment history and current credit profile. When a customer is not deemed credit-worthy, revenues are deferred and recognized upon cash receipt.

Actuate recognizes maintenance revenues, which consist of fees for ongoing support and unspecified product updates, ratably over the term of the contract, typically one year. Consulting revenues are primarily related to standard implementation and configuration. Training revenues are generated from classes offered at the Company's offices and customer locations. Revenues from consulting and training services are typically recognized as the services are performed. When a contract includes both license and service elements, the license fee is typically recognized on delivery of the software, assuming all other revenue recognition criteria are met, provided services do not include significant customization or modification of the product and are not otherwise essential to the functionality of the software. Our license agreements include indemnification for infringement of third party intellectual property rights and certain warranties. Historically, the Company has not experienced significant claims under these contractual rights. Therefore, no amounts have been accrued relating to those indemnities and warranties.

Share-Based Compensation

The Company has various types of share-based compensation plans. These plans are administered by the compensation committee of the Board of Directors, which selects persons to receive awards and determines the number of shares subject to each award and the terms, conditions, performance measures and other provisions of the award. Readers should refer to Note 9 of the Company's consolidated financial statements in the Annual Report on Form 10-K for the fiscal year ended December 31, 2011, for additional information related to these share-based compensation plans. Share-based compensation expense and the related income tax benefit reflected in the Condensed Consolidated Statements of Income in connection with stock options, restricted stock units and the Employee Stock Purchase Plan (ESPP) for three and nine months ended September 30, 2012 and 2011 were as follows (in thousands):

| | Three Months Ended | | Nine months Ended | |
|---------------------------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 30, 2012 | September 30, 2011 | September 30, 2012 | September 30, 2011 |
| Stock options | \$ 1,490 | \$ 579 | \$ 3,994 | \$ 3,199 |
| Restricted stock units | 341 | 203 | 865 | 617 |
| Performance stock units (MSUs) | 229 | | 353 | |
| ESPP | 150 | 192 | 392 | 680 |
| Total share-based compensation | \$ 2,210 | \$ 974 | \$ 5,604 | \$ 4,496 |
| Income tax benefit | \$ 711 | \$ 256 | \$ 1,805 | \$ 1,294 |

Table of Contents

Included in the total share-based compensation for the three and nine months ending September 30, 2012 are approximately \$16,000 of credits to stock based compensation and approximately \$150,000 of stock based compensation classified as liability based awards.

In May 2012, market-performance based restricted stock units (MSUs) were granted to the Chief Executive Officer and Chief Financial Officer of the Company. Each MSU represents the right to one share of Actuate s common stock. The actual number of MSUs which will be eligible to vest will be based on the performance of Actuate s stock price relative to the performance of the S&P Small Cap 600 Index over a two-year vesting period, up to 200% of the MSUs initially granted. After the initial performance period, 50% of the earned award vests immediately and the remaining 50% is subject to an additional one year service period. We valued the MSUs using the Monte Carlo simulation model and amortize the compensation expense over the three year performance and service period.

The fair value of each stock option award is estimated on the date of grant using the Black-Scholes-Merton option pricing model. We estimated the expected term of options granted by analyzing actual historical experience of exercises and cancellations under our plan. We also looked at the average length of time in which our current outstanding options are expected to be exercised or cancelled based on past experience and the vesting and contractual term. We estimated the volatility of our common stock by using historical volatility over the calculated expected term. We based the risk-free interest rate that we use in the option valuation model on the published Treasury rate. We do not anticipate paying any cash dividends in the foreseeable future and therefore used an expected dividend yield of zero in the option valuation model. The assumptions used to estimate the fair value of stock options granted and stock purchase rights granted under our ESPP Plan for the nine months ended September 30, 2012 and 2011 are as follows:

| | Options | | | | ESPP | | | |
|-------------------------|--------------------|--------|--------------------|--------|--------------------|--------|--------------------|--------|
| | Nine months Ended | | | | Nine months Ended | | | |
| | September 30, 2012 | | September 30, 2011 | | September 30, 2012 | | September 30, 2011 | |
| Volatility | 53.67 | 54.17% | 53.88 | 54.38% | 42.12 | 44.17% | 37.36 | 42.34% |
| Expected term (years) | 5.60 | 5.63 | 5.57 | 5.69 | 1.25 | | 1.25 | |
| Risk free interest rate | 0.63 | 1.01% | 0.96 | 2.21% | 0.13 | 0.17% | 0.22% | 0.27% |
| Expected dividend yield | | 0% | | 0% | | 0% | | 0% |
| Forfeiture rate | | 2 4% | | 2 4% | | N/A | | N/A |

Beginning January 2010, restricted stock units (RSUs) were granted to senior management as part of the Company s annual incentive compensation program under the Amended and Restated 1998 Equity Incentive Plan. RSUs are valued based on the closing price of the Company s common stock on the grant date. In general, restricted stock units vest over four years with annual cliff vesting and are subject to the employees continuing service to the Company. For each restricted stock unit granted under the 1998 Plan, a share reserve ratio is applied for the purpose of determining the remaining number of shares reserved for future grants under the plan. The share reserve ratio is 1:1 for each restricted stock unit granted, and an equivalent of 1 share will be deducted from the share reserve for each restricted stock unit issued. Likewise, each forfeited restricted stock unit increases the number of shares available for issuance by the applicable rate at the time of forfeiture. As of September 30, 2012, a total of 873,750 RSUs were issued and granted to the Company s senior management and non-employee Board of Directors.

In February 2011, the Board of Directors approved the acceleration of 333,333 stock options that had been previously granted to a senior executive who had passed away in December 2010. In addition, the exercise terms for these accelerated options along with 129,167 of vested options were extended from one to two years. As such, the full fair value of these options was measured as of the modification date and fully expensed at that time. Since there was no longer a performance obligation at the date of modification associated with these options, an alternate classification and accounting under GAAP was required. As a result, these accelerated options were to be measured and classified as liability rather than equity. Accordingly, at the end of each quarter, we calculate the revised fair value of these options and recognize any corresponding gain or loss to income. We will continue this accounting treatment until these options are fully exercised. In the quarter ending September 30, 2012, 212,500 options were exercised resulting in approximately \$448,000 in accrued liabilities reduction. Of these share-based awards, approximately \$16,000 was a credit to compensation expense in the third quarter of fiscal year 2012 and approximately \$94,000 was classified as other accrued liabilities on the Company s Consolidated Balance Sheet at September 30, 2012.

Net Income Per Share

The Company computes basic net income per share using the weighted-average number of common shares outstanding during the period, less weighted average shares subject to repurchase. The Company computes diluted net income per share using the weighted-average number of common shares and dilutive share-based awards during the period determined by using the treasury stock method.

Edgar Filing: ACTUATE CORP - Form 10-Q

The table below reconciles the weighted-average common shares used to calculate basic net income per share with the weighted-average common shares used to calculate diluted net income per share (in thousands):

Table of Contents

| | Three Months Ended September 30, | | Nine months Ended September 30, | |
|--|-------------------------------------|--------|------------------------------------|--------|
| | 2012 | 2011 | 2012 | 2011 |
| Weighted-average common shares outstanding | 49,207 | 48,058 | 49,156 | 46,873 |
| Weighted-average dilutive common equivalent shares under the treasury stock method | 3,587 | 4,227 | 3,638 | 4,351 |
| Weighted-average common shares used in computing diluted net income per share | 52,794 | 52,285 | 52,794 | 51,224 |

Under the treasury stock method, stock options with exercise prices exceeding the average share price of the Company's common stock during the applicable period are excluded from the diluted earnings per share computation. The weighted-average number of shares excluded from the calculation of diluted net income was 2,222,368 and 2,151,624 in the three and nine months ended September 30, 2012, respectively. The weighted-average number of restricted stock unit shares excluded from the calculation of diluted net income was 216,200 and 113,349 in the three and nine months ended September 30, 2012, respectively. The weighted-average number of shares excluded from the calculation of diluted net income was 3,516,394 and 4,105,173 in the three and nine months ended September 30, 2011, respectively. No restricted stock units were excluded from the diluted earnings per share computation as they were all dilutive for the three and nine months ended September 30, 2011. Such stock options, had they been dilutive, would have been included in the computation of diluted net income per share.

The weighted average exercise price of excluded stock options was \$6.41 and \$6.34 for the three and nine months ended September 30, 2012, respectively. The weighted average exercise price of excluded stock options was \$5.89 and \$5.87 for the three and nine months ended September 30, 2011, respectively.

Income Taxes

The Company calculates its interim income tax provision in accordance with Financial Accounting Standards Board (FASB) authoritative guidance on income taxes and obligations for uncertain tax positions. At the end of each interim period, the Company estimates the annual effective tax rate and applies that rate to its ordinary quarterly earnings. The tax expense or benefit related to significant, unusual, or extraordinary items that will be separately reported or reported net of their related tax effect, is recognized in the interim period in which those items occur. Additionally, the effect of changes in enacted tax laws, tax rates, or tax status is recognized in the interim period in which the change occurs.

The computation of the annual estimated effective tax rate at each interim period requires certain estimates and significant judgment including, but not limited to, the expected operating income for the year, projections of the proportion of income earned and taxed in foreign jurisdictions, permanent and temporary differences, and the likelihood of recovering deferred tax assets generated in the current year. The accounting estimates used to compute the provision for income taxes may change as new events occur, more experience is acquired, additional information is obtained or as the tax environment changes. Although we believe our assumptions, judgments and estimates are reasonable, changes in tax laws or our interpretation of tax laws and the resolution of any tax audits could significantly impact the amounts provided for income taxes in our consolidated financial statements.

A valuation allowance is required, if based on the weight of available evidence it is more likely than not that some portion or all of the recorded deferred tax assets will not be realized in future periods. In evaluating our ability to recover our deferred tax assets, in full or in part, we consider all available positive and negative evidence, including our past operating results, the existence of cumulative losses in the most recent years and our forecast of future taxable income on a jurisdiction by jurisdiction basis. In determining future taxable income, we are responsible for assumptions made, including the amount of state, federal and international pre-tax operating income, the reversal of temporary differences and the implementation of feasible and prudent tax planning strategies. These assumptions require significant judgment about the forecasts of future taxable income and are consistent with the plans and estimates we are using to manage the underlying businesses.

We continue to believe there is sufficient evidence to support the utilization of certain deferred tax assets. If sufficient positive evidence exists and it is more likely than not that the benefit will be realized with respect to the remaining deferred tax assets, we will release the valuation allowance. This adjustment to the valuation allowance would decrease tax expense. Likewise, if there is a reduction in the projection of future U.S. and foreign income, we may need to increase the valuation allowance. Any increase in the valuation allowance would increase tax expense in the period such a determination was made.

We did not recognize certain tax benefits from uncertain tax positions within the provision for income taxes. The Company only recognizes the tax benefit from an uncertain tax position if it is more likely than not that the tax position, based on its technical merits, will be sustained upon examination by the taxing authorities. The tax benefits recognized in the financial statements from such positions are then measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. Due to uncertainties in any tax audit outcome,

Edgar Filing: ACTUATE CORP - Form 10-Q

our estimates of the ultimate settlement of our unrecognized tax positions may change and the actual tax benefits may differ significantly from the estimates.

Table of Contents

Sales Taxes

The Company presents its revenues net of sales tax in its Consolidated Statements of Income.

Recent Accounting Pronouncements

In July 2012, the FASB issued guidance regarding indefinite-lived intangibles impairment tests. The revised standard allows an entity the option to first assess qualitatively whether it is more likely than not that an indefinite-lived intangible asset is impaired, thus necessitating that it perform the quantitative impairment test. An entity is not required to calculate the fair value of an indefinite-lived intangible asset and perform the quantitative impairment test unless the entity determined that it is more likely than not that the asset is impaired. The new guidance will be effective in the first quarter of fiscal 2013 and early adoption is permitted. The Company does not believe the adoption of the guidance will have a material impact on its consolidated financial statements.

2. Investment in Actuate Japan

Noncontrolling (minority) Interest As of September 30, 2012, Actuate owns 100% of the outstanding voting stock of Actuate Japan Company Ltd. (Actuate Japan). The minority shareholder of Actuate Japan had a non-expiring option to put its equity interest (non-controlling interest) in Actuate Japan to the Company and the Company had the option to call the Non-controlling interest. In the fourth quarter of fiscal 2011, the minority shareholder of Actuate Japan notified the Company that it wished to exercise its rights to put its 12% equity interest in Actuate Japan. This minority shareholder exercised its right on December 28, 2011 resulting in a payment of approximately \$594,000 for this interest. As a result of this payment, noncontrolling interest in Actuate Japan was reduced to zero at December 31, 2011. The difference between the adjustment to the noncontrolling interest and the fair value of the consideration paid totaling approximately \$99,000 was reported as increase to additional paid in capital in the Company's Consolidated Balance Sheet on December 31, 2011.

Prior to this exercise by the minority shareholder, the Company measured and disclosed the redeemable non-controlling interest in accordance with the accounting guidance for noncontrolling interests in subsidiaries as issued by the FASB at the calculated redemption value of the put option embedded in the non-controlling interest.

3. Fair Value Measurements of Financial Assets and Liabilities

The Company adheres to the FASB's authoritative guidance related to the fair value measurements of assets and liabilities. Under this standard, fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. For certain of our financial instruments, including cash and cash equivalents, short-term investments, accounts receivable, accounts payable, and other current liabilities the carrying amounts approximate their fair value due to the relatively short maturity of these balances.

The Company has assets that are valued in accordance with the provisions of the authoritative guidance that addresses fair value measurements. This guidance establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. The hierarchy is broken down into three levels based on the reliability of inputs as follows:

Level 1 Valuations based on quoted prices in active markets for identical assets that the Company has the ability to access.

Level 2 Valuations based on inputs other than quoted prices included within level 1, for which all significant inputs are observable, either directly or indirectly.

Level 3 Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

Table of Contents

Assets Measured at Fair Value on a Recurring Basis

The following table represents information about the Company's investments measured at fair value (in thousands):

| | Fair value of investments as of September 30, 2012 | | | |
|---------------------------------------|--|---|---|--|
| | Total | Quoted Prices In Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Money market funds (1) | \$ 5,874 | \$ 5,874 | \$ | \$ |
| Term deposits (1) | 12,850 | 12,850 | | |
| Commercial paper (2) | 6,095 | | 6,095 | |
| Corporate bonds (2) | 27,052 | | 27,052 | |
| Federal and municipal obligations (2) | 2,000 | | 2,000 | |
| | \$ 53,871 | \$ 18,724 | \$ 35,147 | \$ |

| | Fair value of investments as of December 31, 2011 | | | |
|---------------------------------------|---|---|---|--|
| | Total | Quoted Prices In Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Money market funds (1) | \$ 6,082 | \$ 6,082 | \$ | \$ |
| Term deposits (1) | 801 | 801 | | |
| Commercial paper (3) | 9,991 | | 9,991 | |
| Corporate bonds (3) | 18,286 | | 18,286 | |
| Federal and municipal obligations (2) | 2,998 | | 2,998 | |
| | \$ 38,158 | \$ 6,883 | \$ 31,275 | \$ |

- (1) Included in cash and cash equivalents in the Company's Consolidated Balance Sheet.
- (2) Included in short-term investments in the Company's Consolidated Balance Sheet.
- (3) Of these amounts, approximately \$2.6 million was included in cash and cash equivalents at December 31, 2011 and the remainder was included in short-term investments in the Company's Consolidated Balance Sheet.

Certain items in the table above are classified as Level 2 items because quoted prices in an active market are not readily accessible for those specific financial assets, and the Company may have relied on alternative pricing methods that do not rely exclusively on quoted prices to determine the fair value of the investments.

The Company's cash, cash equivalents, short-term investments and non-current investments are as follows (in thousands):

| | Cost | Gross Unrealized Gains | Gross Unrealized (Losses) | Estimated Fair Value |
|--|-----------|------------------------------|---------------------------------|-------------------------|
| Balance at September 30, 2012 | | | | |
| Classified as cash and cash equivalents: | | | | |
| Cash | \$ 20,729 | \$ | \$ | \$ 20,729 |

Edgar Filing: ACTUATE CORP - Form 10-Q

| | | | | |
|---------------------------------------|-----------|-------|---------|-----------|
| Term deposits | 12,850 | | | 12,850 |
| Money market funds | 5,874 | | | 5,874 |
| | 39,453 | | | 39,453 |
| Classified as short-term investments: | | | | |
| Commercial paper (4) | 6,096 | | (1) | 6,095 |
| Corporate bonds (4) | 27,026 | 35 | (9) | 27,052 |
| Federal and municipal obligations (4) | 2,000 | | | 2,000 |
| | 35,122 | 35 | (10) | 35,147 |
| Total | \$ 74,575 | \$ 35 | \$ (10) | \$ 74,600 |

- (4) Securities totaling approximately \$13 million were in an unrealized loss position at September 30, 2012. None of these securities were in a continuous unrealized loss position for greater than 12 months.

Table of Contents

| | Cost | Gross Unrealized Gains | Gross Unrealized (Losses) | Estimated Fair Value |
|--|-----------|------------------------------|---------------------------------|-------------------------|
| Balance at December 31, 2011 | | | | |
| Classified as cash and cash equivalents: | | | | |
| Cash | \$ 29,270 | \$ | \$ | \$ 29,270 |
| Term deposits | 801 | | | 801 |
| Money market funds | 6,082 | | | 6,082 |
| Commercial paper | 2,000 | | | 2,000 |
| Corporate bonds (5) | 606 | | | 606 |
| | 38,759 | | | 38,759 |
| Classified as short-term investments: | | | | |
| Commercial paper (5) | 7,997 | | (6) | 7,991 |
| Corporate bonds (5) | 17,705 | 2 | (27) | 17,680 |
| Federal and municipal obligations (5) | 3,000 | | (2) | 2,998 |
| | 28,702 | 2 | (35) | 28,669 |
| Total | \$ 67,461 | \$ 2 | \$ (35) | \$ 67,428 |

(5) Securities totaling approximately \$27 million were in an unrealized loss position at December 31, 2011. None of these securities were in a continuous unrealized loss position for greater than 12 months.

Our cash equivalent and short-term investment portfolio as of September 30, 2012, consists of investment grade U.S. Government Agency securities, taxable money market mutual funds and taxable commercial paper and corporate notes. We follow an established investment policy and set of guidelines to monitor, manage and limit our exposure to interest rate and credit risk. The policy sets forth credit quality standards and limits our exposure to any one issuer. As of September 30, 2012, we had no direct holdings in structured investment vehicles, sub-prime mortgage-backed securities or collateralized debt obligations and no exposure to these financial instruments through our indirect holdings in money market mutual funds. During fiscal years 2012 and 2011 we had no impairment charge associated with our short-term investment portfolio. While we cannot predict future market conditions or market liquidity, we regularly review our investments and associated risk profiles, which we believe will allow us to effectively manage the risks of our investment portfolio.

Short-term investments are classified as available-for-sale and are recorded on the Company's Consolidated Balance Sheet at fair market value with unrealized gains or losses reported as a separate component of Accumulated Other Comprehensive Income. At September 30, 2012, the Company has classified all of its securities with original maturities beyond 90 days as short-term investments, even though the stated maturity dates may be one year or more beyond the current balance sheet date as these investments remain highly liquid and available for use in current operations.

4. Restructuring Charges

During the first nine months of fiscal 2012, the Company incurred a restructuring charge of approximately \$54,000 associated with an idle Xenos facility in Europe. The lease agreement on this idle facility will expire in December 2013. Historically, restructuring charges have included costs associated with reductions in workforce, exits of idle facilities and disposals of fixed assets. Restructuring charges were based on actual and estimated costs incurred including estimates of sublease income on portions of our idle facilities that we periodically update based on market conditions and in accordance with our restructuring plans. These estimates were impacted by the rules governing the termination of employees, especially those in foreign countries.

Table of Contents

The following table summarizes the restructuring accrual activity during the nine months ended September 30, 2012 (in thousands):

| | Facility Related |
|---|-----------------------------|
| Balance at December 31, 2011 | \$ 204 |
| Restructuring charges | 54 |
| Cash payments | (123) |
| Balance at September 30, 2012 | 135 |
| Less: current portion | (108) |
| Long-term balance at September 30, 2012 | \$ 27 |

5. Segment and Geographic Information

Our primary operations are located in the United States. Revenues from international sources relate to export sales, primarily to Europe and Asia. Our revenues by geographic area were as follows (in thousands):

| | Three Months Ended | | Nine months Ended | |
|--|-------------------------------|------------------|-------------------------------|------------------|
| | September 30, 2012 | 2011 | September 30, 2012 | 2011 |
| Revenues: | | | | |
| North America | \$ 25,064 | \$ 26,022 | \$ 77,211 | \$ 77,380 |
| Europe, Middle East, and Africa (EMEA) | 4,799 | 6,368 | 18,817 | 17,168 |
| Asia Pacific and others | 2,316 | 1,419 | 7,215 | 5,087 |
| | \$ 32,179 | \$ 33,809 | \$ 103,243 | \$ 99,635 |

The Company has determined that it operates in only one segment, the development, marketing and support of our enterprise reporting application platforms, as it only reports profit and loss information on an aggregate basis to its chief operating decision maker. There were no customers that accounted for more than 10% of total revenues in the nine months ended September 30, 2012 or 2011.

6. Goodwill and Other Purchased Intangible Assets

Goodwill

In accordance with the authoritative guidance issued by the FASB on accounting and reporting for acquired goodwill and other intangible assets, the Company performs its annual impairment test of goodwill on October 1 of each year. The Company's goodwill balance of \$46.4 million was unchanged at September 30, 2012 when compared to the balance reported at the end of fiscal year 2011.

Intangibles

Other purchased intangible assets consist of the following (in thousands):

| | September 30, 2012 | | | December 31, 2011 | | |
|------------------------|--------------------------------------|-------------------------------------|------------------------------------|--------------------------------------|-------------------------------------|------------------------------------|
| | Gross Carrying Amount | Accumulated Amortization | Net Carrying Amount | Gross Carrying Amount | Accumulated Amortization | Net Carrying Amount |
| Customer lists | \$ 22,030 | \$ (17,060) | \$ 4,970 | \$ 22,030 | \$ (16,199) | \$ 5,831 |
| Purchased technologies | 15,659 | (10,920) | 4,739 | 15,659 | (10,099) | 5,560 |
| Leases | 47 | (23) | 24 | 47 | (17) | 30 |

Edgar Filing: ACTUATE CORP - Form 10-Q

\$ 37,736 \$ (28,003) \$ 9,733 \$ 37,736 \$ (26,315) \$ 11,421

Amortization expense of purchased technology and other intangible assets remained at approximately \$562,000 for each of the three months ended September 30, 2012 and 2011, respectively. Of this total, approximately \$273,000 was related to the amortization of purchased technology for each of the two quarters ended September 30, 2012 and 2011, respectively. Amortization expense of purchased intangible assets was approximately \$1.7 million and \$1.8 million for the nine months ended September 30, 2012 and 2011, respectively. Of this total, approximately \$820,000 was related to the amortization of purchased technologies for each of the nine months ended September 30, 2012 and 2011. Purchased identifiable intangible assets are amortized on a straight-line basis over their useful lives. The estimated useful economic lives of the acquired customer lists and purchased technologies are seven years. The estimated economic useful life of favorable leases is five years. Amortization of purchased technology is included in cost of license fees in the accompanying condensed consolidated statements of income. The expected remaining annual amortization expense is summarized as follows (in thousands):

Table of Contents

| Fiscal Year | Purchased Technology and Intangibles |
|--------------------------|--|
| 2012 (remainder of year) | \$ 562 |
| 2013 | 2,250 |
| 2014 | 2,250 |
| 2015 | 2,244 |
| 2016 and thereafter | 2,427 |
| | \$ 9,733 |

7. Commitments and Contingencies**General**

The Company is engaged in certain legal actions arising in the ordinary course of business. Although there can be no assurance as to the outcome of such litigation, the Company believes it has adequate legal defenses and it believes that the ultimate outcome of any of these actions will not have a material effect on the Company's consolidated financial position or results of operations.

In the normal course of business, we provide customers with indemnification provisions of varying scope against claims of intellectual property infringement by third parties arising from the use of our products. Historically, costs related to these indemnification provisions have not been significant and we are unable to estimate the maximum potential impact of these indemnification provisions on our future results of operations.

One employee of the Company's French subsidiary was terminated in June of 2011. That employee made a claim against the Company for approximately \$275,000, which was discussed at a meeting convocation with the French authorities on August 23, 2011. A hearing date was set for April 4, 2012 but has now been postponed to January 13, 2013. At this point in time it is unclear whether the basis of the claim is valid or whether a payout is probable or estimable. Therefore, we have not reflected an accrual for this item on our Consolidated Balance Sheet. However, if and when a payout for this claim becomes probable and estimable we will record the corresponding expense.

The operating lease underlying the Company's headquarters facility expired in July of 2012. Therefore, the Company secured a nearby alternative location and signed a lease before the end of fiscal 2011 on that new facility. Under the terms of its previous headquarters facility lease, if the Company's landlord formally requests it, the Company would be required to restore the facility to its original condition before it turns it back over to the landlord. In June 2012, the landlord formally requested that we restore some of the facility to its original condition and requested that we pay approximately \$185,000 in restoration charges. These restoration charges were fully expensed in the second quarter of 2012.

Revolving credit line

In early November of 2008, the Company entered into a revolving Credit Agreement with Wells Fargo Foothill (WFF) and secured a revolving line of credit in the principal amount of up to \$50 million. During the fourth quarter of fiscal 2008, the Company used \$30 million of its cash along with \$30 million of funds available through this credit facility to complete a \$60 million common stock buyback. During the first quarter of 2010, the Company borrowed an additional \$10 million of funds available through this credit facility to complete the acquisition of Xenos, which was completed on February 1, 2010. There are no minimum pay-down requirements under the terms of this credit facility so long as we remain in compliance with the terms of the Credit Agreement. Total costs associated with the facility, including legal and closing fees, amounted to approximately \$1.1 million and were fully paid as of September 30, 2012. These costs were capitalized and are being amortized over four years in the Company's Consolidated Financial Statements. Such assets are reflected as current assets if amortized within one year or non-current assets if amortized beyond one year. The Credit Agreement was originally for a period of four years and was originally scheduled to expire on November 3, 2012.

In May 2011, the Company paid down the outstanding balance on its revolving line of credit. The Company used \$40 million in cash and short-term investments in order to pay down this outstanding debt.

On December 29, 2011, the Company amended and re-negotiated its credit facility with Wells Fargo Capital Finance, LLC (WFCF). The amended credit facility provided for the following:

Edgar Filing: ACTUATE CORP - Form 10-Q

An extension of the original agreement entered in November 2008. The termination date was extended from November 3, 2012 to November 3, 2015,

Replacement of a \$125,000 commitment fee that was payable on November 3, 2011 with a closing fee of \$100,000 that was paid on December 29, 2011,

A 50% reduction in the applicable internal rate on the outstanding credit balance from 3.5% to 1.75%, and

A reduction in the unused line fee from 0.50% to 0.30% per year applied to the unutilized portion of the credit facility.

Table of Contents

The remaining unamortized costs associated with the credit facility will be amortized from the date of amendment over four years.

As of September 30, 2012, there was no balance owed on this credit facility and the balance available under the revolving credit facility was approximately \$50 million. Interest is based on a floating rate plus an applicable margin based on the outstanding balance of the amount drawn under the Credit Agreement. The floating rate is determined at the Company's election and may either be (i) London Interbank Offered Rate (LIBOR) or (ii) the greater of the Federal Funds Rate plus applicable margin and the Prime Rate. If the Company's usage of the credit line exceeds 80% of its trailing four quarters of recurring maintenance revenue, or if the sum of available funds under the Credit Agreement plus available cash is less than \$10 million, the Company is required to meet certain minimum income targets and be subject to a limit on annual capital expenditures. As of September 30, 2012, the Company was able to meet the 80% test as well as the \$10 million minimum cash threshold and was therefore not subject to the income or the capital expenditures covenants. The Company is required to make interest payments on any outstanding balances and pay an unused commitment fee on any unused portion of the credit line on a monthly basis.

The following table represents costs related to the Company's credit facility (in thousands):

| | Three Months Ended September 30, | | Nine months Ended September 30, | |
|-------------------------------------|-------------------------------------|--------|------------------------------------|--------|
| | 2012 | 2011 | 2012 | 2011 |
| Interest expense | \$ | \$ | \$ | \$ 441 |
| Amortization of debt issuance costs | 17 | 72 | 51 | 216 |
| Unused line fees | 38 | 64 | 114 | 122 |
| | \$ 55 | \$ 136 | \$ 165 | \$ 779 |

The Credit Agreement contains covenants, which, among other things, impose certain limitations with respect to lines of business, mergers, investments and acquisitions, additional indebtedness, distributions, guarantees, liens and encumbrances. In the event the Company does not meet the requirements specified above, a triggering event will be deemed to have occurred and the Company would be required to maintain the two financial covenants listed below:

achieve income before interest and taxes, measured on a quarter-end basis, of at least the required amount set forth per the Credit Agreement,

limit the amount of capital expenditures to an amount not exceeding that set forth per the Credit Agreement.

The Company's indebtedness under the Credit Agreement is secured by a lien on (i) substantially all of its assets and the assets of Actuate International Corporation and (ii) by a pledge of all of its stock and a portion of the stock of each of its subsidiaries.

Operating Lease Commitments

On November 28, 2011, the Company entered into a ten year lease agreement with a third party for approximately 58,000 square feet of office space in the BayCenter Campus in San Mateo, California. This lease is operating in nature and commenced on June 1, 2012 and will end on May 31, 2022. In addition, the lease provides for four months of free rent (rent holiday) and approximately \$2.6 million in landlord incentives to be applied towards construction of improvements. At September 30, 2012, the deferred rent liability balance related to the new lease totaled approximately \$3.1 million and this balance gradually declines every month through May 2022 when contractual cash payments eventually exceed the straight-line lease expense. This deferred rent liability balance was classified under the long term accrued liabilities section of the Company's Consolidated Balance Sheet at September 30, 2012. Actuate vacated its previous corporate headquarters located at the Bridgepointe Campus in July 2012 and is now using the BayCenter Campus as its corporate headquarters.

Upon the execution of the new lease, Actuate delivered to the new landlord two letters of credit totaling \$225,300. These letters of credit guarantee Actuate's contractual obligations related to the BayCenter Campus in San Mateo, California.

Edgar Filing: ACTUATE CORP - Form 10-Q

Actuate leases smaller office facilities in various locations in the United States and abroad. All facilities are leased under operating leases. Total rent expense was approximately \$1.2 million in the third quarter of fiscal year 2012 compared with approximately \$862,000 in third quarter of fiscal year 2011. The increase in rent expense during the third quarter of 2012 compared with third quarter of last year was partially offset by approximately \$142,000 of lower facilities related operating expenses.

Table of Contents***Stock Option Plans***

An individual who first joins the Board of Directors as a non-employee director is awarded an option to purchase 25,000 shares of the Company's Common Stock and a restricted stock unit award (RSU) covering 12,500 shares of the Company's Common Stock. These options and RSUs each have a four year vesting period tied to continued Board service. Each option has an exercise price equal to the closing price of the Company's Common Stock on the day of the grant, and 25% will vest upon the non-employee director's continued Board service through the first anniversary of the award date and on an equal, monthly basis over the next 3 years of service thereafter. The first 25% of each restricted stock unit award will vest 13 months following the award date and the remainder will vest in a series of three successive equal annual installments on each of the second, third and fourth anniversaries of the award date, provided that the non-employee director continues in Board service through each such vesting date. Each non-employee director receiving an initial 12,500-share RSU award is given the opportunity to elect to defer the receipt of the shares of Actuate Common Stock that vest and become issuable pursuant to the initial RSU award. If a non-employee director makes a timely deferral election, then the shares of Actuate Common Stock in which he or she vests under the initial RSU award will be issued upon his termination of Board service. In the absence of an effective deferral election, any shares of the Company's Common Stock in which the non-employee director vests under the initial RSU award will be issued as those shares vest.

Each continuing non-employee director is awarded an option to purchase 16,000 shares of the Company's Common Stock and a RSU award covering 8,000 shares of the Company's Common Stock at each annual stockholders meeting. Each option has an exercise price equal to the closing price of Actuate's Common Stock on the day of the grant, and will vest upon the non-employee director's continued Board service through the first anniversary of the award date. Each restricted stock unit award granted to a continuing non-employee director will vest upon the non-employee director's continued Board service through the first anniversary of the award date. Before the start of each calendar year, each of our non-employee directors is given the opportunity to elect to defer the receipt of any or all of the shares of Actuate Common Stock that vest and become issuable pursuant to the restricted stock unit award to be made to such non-employee director at the next annual stockholders meeting. If a non-employee director makes a timely deferral election, then the shares of Actuate Common Stock in which he or she vests under the RSU award will be issued upon his termination of Board service. In the absence of an effective deferral election, any shares of the Company's Common Stock in which the non-employee director vests under the RSU award will be issued as those shares vest.

Each restricted stock unit award and each option award granted to a new or continuing non-employee director will vest in full on an accelerated basis upon (i) an approved acquisition of the Company by merger or consolidation, (ii) a sale of all or substantially all of the Company's assets, (iii) the successful completion of a tender or exchange offer for securities possessing more than fifty percent (50%) of the total combined voting power of the Company's outstanding securities, or (iv) the death or disability of the optionee while serving as a member of the Board of Directors. Each restricted stock unit that vests will entitle the recipient to one share of the Company's common stock on the designated issuance date for that share. All grants are made under the 1998 Plan.

The Board of Directors may authorize the issuance of performance stock units (PSUs) from the Company's 1998 Equity Incentive Plan. PSUs are awards that vest either through a performance condition or market condition. In May 2012 the Board granted PSUs with a market condition (MSUs) to the Chief Executive Officer and Chief Financial Officer. Each MSU represents the right to one share of Actuate's common stock. The actual number of MSUs which will be eligible to vest will be based on the performance of Actuate's stock price relative to the performance of the S&P Small Cap 600 Index over a two-year vesting period, up to 200% of the MSUs initially granted. After the initial performance period, 50% of the earned award vests immediately and the remaining 50% is subject to an additional one year service period. MSUs are valued using the Monte Carlo simulation model and the compensation expense is amortized over the three year performance and service period.

In connection with the Xenos acquisition, Actuate's Board of Directors duly authorized the issuance of stock options to eligible employees from the Company's 1998 Equity Incentive Plan. A total of 573,800 non-statutory stock options were issued in February of 2010 with the exercise price of \$5.31. Each grant shall fully vest in four years with 25% cliff vesting at the end of year one and the remaining balance to vest in thirty-six successive monthly installments.

As an employee retention incentive, Actuate also invited Xenos employees who were holders of Xenos Options to exchange any Options that they did not exercise in connection with the Offer for options to purchase shares of common stock of Actuate on a tax-free rollover basis (an Option Exchange). The replacement options issued by Actuate would have the same intrinsic value as the options given up by Xenos. On February 1, 2010, 30,750 Xenos options were exchanged for 19,025 Actuate options with exercise prices ranging from \$2.04 to \$3.54. These options were fully vested and exercisable at the date of exchange. All options, excluding RSUs and MSUs, are subject to the same vesting schedule (twenty-five percent of the option shares will vest on the one year anniversary of the option grant date and the remaining option shares will vest in thirty-six equal monthly installments over the thirty-six month period measured from the first anniversary of the option grant date, provided the optionee continues to provide services to the Corporation through each applicable vesting date) and all have ten year terms.

Shares issued as a result of the exercise of options under any of our plans would be fulfilled through shares currently in our existing pools. Total authorized but unissued shares were 25,679,264 as of September 30, 2012.

Table of Contents

| Plan Summary | Available for Grant | Outstanding | RSUs Released | Total Authorized But Unissued |
|--|----------------------------|--------------------|----------------------|--------------------------------------|
| Amended and Restated 1998 Equity Incentive Plan | 11,719,096 | 12,535,369 | | 24,254,465 |
| 2001 Supplemental Stock Plan | 695,880 | 108,919 | | 804,799 |
| 1998 Non-Employee Director Option Plan | 495,000 | 175,000 | | 670,000 |
| Total Stock Plans | 12,909,976 | 12,819,288 | | 25,729,264 |
| RSUs granted inception to date | 829,938 | (812,374) | | 17,564 |
| RSUs Shares released (2) | | | (17,564) | (17,564) |
| Total Options Balance at September 30, 2012 | 13,739,914 | 12,006,914 | (17,564) | 25,729,264 |
| Miscellaneous Stock Grant (1) | (50,000) | | | (50,000) |
| Total Stock Plans Balance at September 30, 2012 | 13,689,914 | 12,006,914 | (17,564) | 25,679,264 |

- (1) Board approved stock grant on February 17, 2011 to the beneficiary of a deceased senior executive in recognition of services performed.
(2) RSU with no deferral elections were released to grant recipients upon vesting.

The weighted average grant date fair value of options granted during the quarter ended September 30, 2012 was \$3.29 per option. Upon the exercise of options, the Company issues new common stock from its authorized shares. The total intrinsic value of options exercised during the quarter ended September 30, 2012 was \$1.8 million.

All vested stock options are exercisable. The following table summarizes information about stock options outstanding and exercisable as of September 30, 2012:

| Range of Exercise Prices | Options Outstanding | | | Options Exercisable | |
|---------------------------------|----------------------------|--|--|----------------------------|--|
| | Number of Shares | Weighted-Average Remaining Contractual Life | Weighted-Average Exercise Price | Number of Shares | Weighted-Average Exercise Price |
| \$1.39-\$2.99 | 1,830,709 | 1.51 years | \$ 2.34 | 1,830,397 | \$ 2.34 |
| \$3.03-\$3.59 | 1,659,223 | 4.94 years | \$ 3.56 | 1,544,040 | \$ 3.56 |
| \$3.65-\$4.80 | 2,048,917 | 5.47 years | \$ 4.45 | 1,564,742 | \$ 4.39 |
| \$4.84-\$5.31 | 1,430,990 | 5.16 years | \$ 5.15 | 1,266,497 | \$ 5.14 |
| \$5.32-\$6.08 | 1,677,370 | 7.83 years | \$ 5.52 | 679,023 | \$ 5.50 |
| \$6.10-\$6.25 | 1,280,326 | 5.46 years | \$ 6.11 | 1,207,746 | \$ 6.11 |
| \$6.27-\$7.02 | 1,985,979 | 8.33 years | \$ 6.43 | 306,947 | \$ 6.89 |
| \$7.04-\$8.39 | 93,400 | 7.62 years | \$ 7.42 | 40,500 | \$ 7.84 |
| \$1.39-\$8.39 | 12,006,914 | 5.57 years | \$ 4.77 | 8,439,892 | \$ 4.35 |

Table of Contents

| | September 30, 2012 | September 30, 2011 |
|---|-----------------------|-----------------------|
| Options Outstanding Vested and Expected to Vest | | |
| Vested and expected to vest, net of expected forfeitures | 11,919,426 | 13,370,846 |
| Aggregate intrinsic value (in thousands) | \$ 27,111 | \$ 19,565 |
| Weighted average exercise price per share | \$ 4.76 | \$ 4.16 |
| Weighted average remaining contractual term (in years) | 5.55 | 5.17 |
| Options Exercisable | | |
| Options currently exercisable | 8,439,892 | 10,002,680 |
| Aggregate intrinsic value of currently exercisable options (in thousands) | \$ 22,674 | \$ 17,701 |
| Weighted average exercise price per share | \$ 4.35 | \$ 3.88 |
| Weighted average remaining contractual term (in years) | 4.38 | 4.10 |

As of September 30, 2012, the number of shares reserved for future grants under all option plans was 12,859,976. The number of shares available for future purchase under the Purchase Plan was 2,577,479.

Summary of Restricted Stock Units

Restricted stock unit activity for the nine months ended September 30, 2012 and 2011:

| | September 30, 2012 | September 30, 2011 |
|-------------------------------|-----------------------|-----------------------|
| Beginning outstanding balance | 384,687 | 182,500 |
| Awarded | 205,000 | 232,500 |
| Released | (12,313) | (5,251) |
| Forfeited | | (25,062) |
| Ending outstanding balance | 577,374 | 384,687 |

The weighted average grant date fair value of restricted stock units granted during the quarter ended September 30, 2012 and 2011 were \$6.40 and \$5.48 per unit, respectively.

| | Number of Units | Weighted Average Remaining Contractual Life (years) | Aggregate Intrinsic Value (thousands) |
|--|--------------------|--|---|
| Restricted stock units outstanding | 577,374 | 1.38 | \$ 4,059 |
| Restricted stock units vested and expected to vest (1) | 566,150 | 1.36 | \$ 2,805 |
| Restricted stock units vested and deferred (2) | 167,125 | N/A | \$ 1,175 |

Summary of Market-Performance Based Restricted Stock Units (MSUs)

MSU activity for the nine months ended September 30, 2012:

| | September 30, 2012 |
|-----------------------------------|-----------------------|
| Beginning outstanding balance (3) | |
| Awarded | 235,000 |
| Released | |
| Forfeited | |
| Ending outstanding balance | 235,000 |

Table of Contents

The weighted average grant date fair value of MSUs granted during the nine months ended September 30, 2012 was \$8.01.

| | Number of Units | Weighted Average Remaining Contractual Life (years) | Aggregate Intrinsic Value (thousands) |
|--------------------------------------|--------------------|--|---|
| MSUs outstanding | 235,000 | 1.75 | \$ 1,652 |
| MSUs vested and expected to vest (1) | 226,857 | 1.74 | \$ 1,595 |
| MSUs vested and deferred (2) | | | \$ |

(1) Net of expected forfeitures.

(2) Awards earned but receipt of shares deferred until employee leaves the Company.

(3) There were no MSUs granted in fiscal 2011.

8. Deferred Revenue

Deferred revenue consists of the following (in thousands):

| | September 30, 2012 | December 31, 2011 |
|----------------------------|-----------------------|----------------------|
| Maintenance and support | \$ 35,282 | \$ 39,478 |
| Other | 3,096 | 5,284 |
| | \$ 38,378 | \$ 44,762 |
| Less: current portion | (37,073) | (43,045) |
| Long-term deferred revenue | \$ 1,305 | \$ 1,717 |

Maintenance and support consists of first year maintenance and support services associated with the initial purchase of Actuate's software, and the renewal of annual maintenance and support services from customers who purchased Actuate's software in prior periods. The maintenance and support period is generally 12 months and revenues are typically recognized on a straight-line basis over the term of the maintenance and support period.

Other deferred revenue consists of deferred license, training and consulting fees generated from arrangements, which did not meet some or all of the revenue recognition criteria of FASB's Accounting Standards Codification 985 Software, and are, therefore, deferred until all revenue recognition criteria have been met.

9. Subsequent Events

On October 22, 2012, the Company acquired Quiterian S.L., a privately held software company that provides visual data mining, social media analytics and predictive analytics for business and other non-technical users. Actuate acquired 100% of the outstanding shares held by the Quiterian shareholders for \$5.2 million in cash. This purchase price was entirely paid upon closing, net of a 10% holdback. There are \$3 million in potential additional payments which may be required over the next three year period. These payments are wholly dependent on the achievement of specific contingencies. The Company is currently evaluating the impact of this acquisition on the Company's future financial statements.

Actuate had pledged \$426,000 of restricted cash as collateral for standby letters of credit that guarantee its contractual obligations relating to its corporate headquarter facilities located at the Bridgepointe Campus in San Mateo, California. This restricted cash was classified as Other Deposits in the accompanying Consolidated Balance Sheet as of September 30, 2012. Actuate vacated its previous corporate headquarters located at the Bridgepointe Campus in July 2012 and is now using the BayCenter Campus as its corporate headquarters. As a result of this move, in early October 2012, the restricted cash balance was no longer required as the Company's contractual obligations relating to its previous corporate headquarter facilities ceased and the pledge of restricted cash as collateral for standby letters of credit were therefore released.

Edgar Filing: ACTUATE CORP - Form 10-Q

On August 2, 2012, the Board of Directors approved an ongoing extension of the Company's share repurchase program. This extension authorized management to make additional repurchases of Actuate common stock up to an aggregate of \$30 million. The share repurchase authorization does not have an expiration date and the pace and timing of repurchases will depend on factors such as cash generation from operations, the volume of employee stock plan activity, cash requirements for acquisitions, economic and market conditions, stock price and legal and regulatory requirements. Subsequent to September 30, 2012, through November 6, 2012, the Company has repurchased 236,000 shares totaling approximately \$1.2 million in the open market under this stock repurchase plan.

Table of Contents

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

The following information should be read in conjunction with the historical financial information and the notes thereto included in Item 1 of this Quarterly Report on Form 10-Q, the consolidated financial statements and notes thereto and the related Management's Discussion and Analysis of Financial Condition and Results of Operations contained in our Annual Report on Form 10-K for the year ended December 31, 2011 as filed with the Securities and Exchange Commission on March 9, 2012.

The statements contained in this Form 10-Q that are not purely historical are forward looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, including statements regarding Actuate's expectations, beliefs, hopes, intentions, plans or strategies regarding the future. All forward-looking statements in this Form 10-Q are based upon information available to Actuate as of the date hereof, and Actuate assumes no obligation to update any such forward-looking statements. Actual results could differ materially from Actuate's current expectations. Factors that could cause or contribute to such differences include, but are not limited to, the risks discussed in Part II, Item 1A Risk Factors of this Form 10-Q, Part I, Item 1A Risk Factors in our Annual Report for the year ended December 31, 2011 and in other filings made by the Company with the Securities and Exchange Commission.

Overview

Actuate Corporation (we , Actuate or the Company) was incorporated in November 1993 in the State of California and reincorporated in the State of Delaware in July 1998. Actuate provides software and services to develop and deploy custom Business Intelligence and information applications that deliver rich interactive content to improve customer loyalty and corporate performance. Applications built on Actuate's open source-based platform seek to provide all stakeholders inside and outside the firewall, including employees, customers, partners and citizens with information that they can easily access and understand to maximize revenue, cut costs, improve customer satisfaction, streamline operations, create competitive advantage and make better decisions. Our goal is to ensure that all users can use decision-making information in their day-to-day activities, opening up completely new avenues for improving corporate performance. Actuate's telephone number is 650-645-3000. Actuate maintains Web sites at www.actuate.com, www.birt-exchange.org and www.birt-exchange.com. The information posted on our Web sites is not incorporated into this quarterly report.

We began shipping our first product in January 1996. We sell software products through two primary means: (i) directly to end-user customers through our direct sales force and (ii) through indirect channel partners such as OEMs, resellers and system integrators. OEMs generally integrate our products with their applications and either provide hosting services or resell them with their products. Our other indirect channel partners resell our software products to end-user customers. Our total revenues are derived from license fees for software products and fees for services relating to such products, including software maintenance and support, professional services and training.

Despite the recent global recession, we have continued to achieve profitability and positive cash flows during the year. Nevertheless, our business model and longer-term financial results are not immune to a sustained economic downturn. For example, the recent domestic and global economic downturn resulted in reduced demand for information technology, including enterprise software and services. The direction and relative strength of the global economy continues to be uncertain and makes it difficult for us to forecast operating results and to make decisions about future investments. Information technology spending has historically declined as general economic and market conditions worsened. During challenging and uncertain economic times and in tight credit markets, many customers delay or reduce technology purchases. Contract negotiations may become more protracted or difficult if customers institute additional internal approvals for technology purchases or require more negotiation of contract terms and conditions. Such economic conditions could result in reductions in sales of our products, longer sales cycles, difficulties in collection of accounts receivable or delayed payments, slower adoption of new technologies, increased price competition and reductions in the rate at which our customers renew their maintenance agreements and procure consulting services. Furthermore, a significant portion of our revenues have historically been derived from customers in the financial services industry. The Company expects that it will continue to derive a significant portion of its revenues from these financial services customers for the foreseeable future. Unfavorable economic conditions have adversely impacted the financial services industry over the past several years. If this adverse trend were to continue, it would likely have a material adverse effect on the Company's business, financial condition and results of operations.

We intend to continue to invest significant resources to expand our sales and engineering operations. In order to expand sales, we must establish additional foreign operations, expand our channel management and support organizations, hire additional personnel, recruit additional resellers and/or increase the productivity of existing resellers. Factors that may affect our operating results include the possibility of a prolonged period of limited economic growth or possible economic decline in and adverse effects of the ongoing sovereign debt crisis in Europe, including its expected negative impact on European economic growth versus the rest of the world; disruptions to the credit and financial markets in Europe, the U.S., and elsewhere; contractions or limited growth in corporate spending and adverse economic conditions that may be specific to information technology and the software industry.

Table of Contents

We continue to monitor market conditions and may make adjustments to our business in order to reduce the adverse impact that changes to the economic environment could have on our business. We expect to continue to explore both organic and strategic growth opportunities. In particular, we may acquire companies or technology that can contribute to the strategic, operational and financial performance of our business.

For the remainder of fiscal 2012, we expect three additional trends to continue that would have a significant impact on the results of our operations. We currently believe that corporate IT budgets will grow only modestly if at all in the fiscal year 2012, particularly among financial services companies in the United States and Western Europe. Second, corporations are reluctant to buy software from new vendors and we continue to witness corporations consolidating their Business Intelligence, Analytics, Performance Management, Print Stream/Document Transformation and Output Management software purchases among fewer suppliers. Finally, we expect to experience vigorous competition in the BI market. Several of our competitors have released products that are marketed to be directly competitive with our offerings. As one of the few independent BI vendors remaining, Actuate faces competition from large and well-established vendors including Microsoft, SAP, Oracle and IBM all of which have acquired BI competitors. The existence of these competitive products may require additional engineering, sales and marketing efforts to differentiate our products. We believe that competition in the BI and information applications market will be vigorous in the near future.

For fiscal year 2012, we will continue to pursue the strategic initiatives to improve revenue growth driven by BIRT, initiatives related to Performance Management, and pursuing opportunities related to traditional Xenos markets. These initiatives are as follows:

Investing in BIRT We are continuing to make a significant investment in BIRT. BIRT has become widely adopted by developers and continues to drive demand for our BIRT-based commercially available products, including ActuateOne. The BIRT project is a core, long-term initiative.

Selling to IT Management We are re-focusing our sales efforts on selling our products to IT managers who we believe generally recognize the technical advantages of our products.

Selling to Line-of-Business Management We are creating applications and software solutions to sell to line-of-business managers in the areas of performance management and customer self-service and statementing.

Selling to Global 9000 Corporations particularly to Financial Services Companies We continue to focus on selling our products to Global 9000 financial services companies in an effort to increase our substantive market share in this sector. We believe that as conditions in Financial Services Sector improve, the industry will once again lead in the adoption of BI and information applications both inside and outside the firewall.

Building out and delivering on our roadmap of applying BIRT to additional data sources including hard to reach print stream data by investing in the development of BIRT based Xenos offerings.

We have a limited ability to forecast future revenues and expenses, thus the prediction of future operating results is difficult. In addition, historical growth rates in our revenues and earnings should not be considered indicative of future revenue or earnings growth rates or operating results. There can be no assurance that any of our business strategies will be successful or that we will be able to achieve and maintain profitability on a quarterly or annual basis. It is possible that in some future quarter our operating results will be below the expectations of public market analysts and investors, and in such event the price of our common stock could decline.

| | Three Months Ended September 30, (in thousands except per share data) | | | |
|--------------------------|--|-------------|------------------|-----------------|
| | 2012 | 2011 | \$ Change | % Change |
| Financial Summary | | | | |
| Total revenues | \$ 32,179 | \$ 33,809 | \$ (1,630) | (5)% |

Edgar Filing: ACTUATE CORP - Form 10-Q

| | | | | |
|--|---------|----------|------------|-------|
| Total operating expenses | 29,466 | 27,007 | 2,459 | 9% |
| Income from operations | 2,713 | 6,802 | (4,089) | (60)% |
| Operating margins | 8% | 20% | (12)% | (60)% |
| Net income | \$ 107 | \$ 4,722 | \$ (4,615) | (98)% |
| Diluted net income per share | \$ 0.00 | \$ 0.09 | \$ (0.09) | |
| Shares used in diluted per share calculation | 52,794 | 52,285 | | |

Financial Performance Summary for the quarter ended September 30, 2012 compared to September 30, 2011:

Increase in license revenues of 13%, or approximately \$1.5 million. This increase was primarily the result of improved license sales in North America and Asia.

Decrease in services revenues of 14%, or approximately \$3.1 million. This decrease was mainly driven by lower maintenance and support revenues as we experienced higher customer decline rates.

Table of Contents

Decrease in operating margins driven by lower revenues and higher operating expenses. The increase in operating expense was mainly attributed to employee compensation cost as our overall average headcount increased by 7% during the third quarter of 2012 compared to the same period in 2011. Most of this increase was concentrated in sales and marketing as we increased the number of field sales reps. The increase in employee compensation was also driven by stock-based compensation due to a lower forfeiture rate which resulted in higher operating expenses.

Lower net income due to a higher effective tax rate. Following the Company's evaluation of likely use of research and development (R & D) credits, a valuation allowance was recorded against California R & D credits in the third quarter of fiscal 2012 which significantly increased the effective tax rate as compared to the same quarter of the prior year.

Critical Accounting Policies, Judgments and Estimates

The discussion and analysis of our financial condition and results of operations are based upon our Consolidated Financial Statements, which have been prepared in accordance with generally accepted accounting principles in the United States of America. The preparation of these financial statements requires us to make estimates, assumptions and judgments that can have a significant impact on the reported amounts of assets and liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities at the date of our financial statements. We base our estimates, assumptions and judgments on historical experience and various other factors that we believe to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. On a regular basis we evaluate our estimates, assumptions and judgments and make changes accordingly. We believe that the estimates, assumptions and judgments involved in revenue recognition, allowances for doubtful accounts, stock-based compensation, accounting for income taxes, restructuring and integration costs, allocation of purchase price of acquisitions, and the impairment of goodwill, have the greatest potential impact on our Consolidated Financial Statements, so we consider these to be our critical accounting policies.

For further information about our significant accounting policies, see the discussion under Item 7 to the annual consolidated financial statements as of and for the year ended December 31, 2011, as filed with the SEC on Form 10-K on March 9, 2012.

Results of Operations

The following table sets forth certain consolidated statement of income data as a percentage of total revenues for the periods indicated.

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|-------------------------------------|------|------------------------------------|------|
| | 2012 | 2011 | 2012 | 2011 |
| Revenues: | | | | |
| License fees | 41% | 35% | 41% | 36% |
| Services | 59 | 65 | 59 | 64 |
| Total revenues | 100 | 100 | 100 | 100 |
| Costs and expenses: | | | | |
| Cost of license fees | 1 | 1 | 1 | 1 |
| Cost of services | 16 | 15 | 15 | 16 |
| Sales and marketing | 38 | 31 | 35 | 32 |
| Research and development | 19 | 17 | 17 | 19 |
| General and administrative | 17 | 14 | 16 | 16 |
| Amortization of other purchased intangibles | 1 | 1 | 1 | 1 |
| Asset impairment | | | | 2 |
| Restructuring charges | | 1 | | |
| Total costs and expenses | 92 | 80 | 85 | 87 |
| Income from operations | 8 | 20 | 15 | 13 |
| Interest income and other income/(expense), net | 1 | 3 | 1 | (1) |
| Interest expense | | | (1) | (1) |

Edgar Filing: ACTUATE CORP - Form 10-Q

| | | | | |
|----------------------------|---|-----|----|----|
| Income before income taxes | 9 | 23 | 15 | 11 |
| Provision for income taxes | 9 | 9 | 6 | 4 |
| Net income | % | 14% | 9% | 7% |

Table of Contents*Revenues*

| | Three Months Ended (In thousands) | | | | Nine Months Ended (In thousands) | | | |
|-----------------------|--------------------------------------|------------------|-------------------|---------------|-------------------------------------|------------------|------------------|---------------|
| | September 30, | | Variance \$ s | Variance % | September 30, | | Variance \$ s | Variance % |
| | 2012 | 2011 | | | 2012 | 2011 | | |
| Revenues | | | | | | | | |
| License fees | \$ 13,304 | \$ 11,815 | \$ 1,489 | 13% | \$ 42,389 | \$ 35,914 | \$ 6,475 | 18% |
| Services | 18,875 | 21,994 | (3,119) | (14)% | 60,854 | 63,721 | (2,867) | (4)% |
| Total Revenues | \$ 32,179 | \$ 33,809 | \$ (1,630) | (5)% | \$ 103,243 | \$ 99,635 | \$ 3,608 | 4% |
| % of Revenue | | | | | | | | |
| License fees | 41% | 35% | | | 41% | 36% | | |
| Services | 59% | 65% | | | 59% | 64% | | |
| Total Revenues | 100% | 100% | | | 100% | 100% | | |

Our revenues are derived from license fees and services. Our services revenues include software maintenance and support, professional consulting and training. Our total revenues decreased 5% from \$33.8 million for the quarter ended September 30, 2011 to \$32.2 million for the quarter ended September 30, 2012. This decrease was primarily experienced in Europe and North America, where total revenues decreased by approximately \$2.5 million compared to the third quarter of 2011. Partially offsetting these negative results was approximately \$900,000 increase in revenues in Asia Pacific.

Our services revenue decreased 14% or approximately \$3.1 million over the same quarter last year due largely to lower maintenance revenues. This decrease in maintenance revenues was primarily caused by maintenance renewal declines, and adverse currency exchange impacts. The weak economic environment, mainly in Europe also contributed to the decline in maintenance revenues during the quarter. It is important to note that we are currently transitioning from our legacy e.Reports product suite to our new BIRT based product offering. As our legacy products age, we have experienced higher than normal decline rates which may continue for the foreseeable future. In the mean time, BIRT is expected to become the dominant contributor to license and maintenance revenues. As this transition progresses, we expect to see our decline rate improve, consequently resulting in stronger maintenance growth rates in the future.

Professional services revenues also decreased during the third quarter of 2012 as a result of a weak macro environment. Additionally, we continue to experience an increase in the adoption of BIRT-based projects by our customers in 2012 compared to last year. These BIRT-based projects do not require professional service to the same extent as the Company's traditional designer products.

Sales outside of North America were \$7.1 million or 22% of total revenues for the third quarter of fiscal 2012, compared to \$7.8 million, or 23% of total revenues for the third quarter of fiscal 2011. As a result of fluctuations in foreign currency exchange rates, our total revenues were negatively impacted by approximately \$700,000 during the third quarter of fiscal 2012 compared to approximately \$780,000 of exchange gains reported during the same period in the prior year.

For the first nine months of fiscal year 2012, the underlying reasons for the fluctuations in the various components of our revenues were similar to those experienced during the quarter as noted above. Revenues outside of North America increased by 17% from \$22.3 million in the first nine months of fiscal 2011 to approximately \$26 million in the first nine months of fiscal 2012. We completed two transactions in Asia which resulted in combined license revenues in excess of \$1 million. Our license sales also increased in Europe during the first nine months of 2012 and included one transaction with license revenue in excess of \$1 million while North America revenues remained relatively unchanged. The international revenues represented 25% of our total revenues versus 22% in the same period last year. As a result of fluctuations in foreign currency exchange rates, our total revenues were negatively impacted by approximately \$1.3 million during the first nine months of fiscal 2012.

License fees. The increase in license revenues for the third quarter of fiscal 2012 over the same period in the prior year was due to improved product demand in North America and Asia. North America license sales increased 13% or approximately \$1.2 million. Our license sales also increased in Asia by 237% or approximately \$922,000 during the third quarter of 2012. These increases were partially offset by lower license revenues in Europe.

Edgar Filing: ACTUATE CORP - Form 10-Q

For the first nine months of fiscal 2012, the underlying reasons for the increase in the various components of our license revenues were similar to those experienced during the quarter as noted above. International license sales increased 52% or by approximately \$3.5 million during the first nine months of 2012 compared to the first nine months of 2011. Our license sales increased in Europe by 43% or approximately \$2 million and in Asia by 72% or approximately \$1.5 million during the first nine months of 2012. North America license growth remained strong at approximately 10% or \$2.9 million over the same period last year. As a result of fluctuations in foreign currency exchange rates, our license revenues were negatively impacted by approximately \$400,000 during the first nine months of fiscal 2012.

Table of Contents

During the third quarter of fiscal 2012, we completed two license transactions greater than \$1 million and closed transactions greater than \$100,000 with 66 customers. During the same period last year we completed two license transactions greater than \$1 million and closed transactions greater than \$100,000 with 57 customers.

The following table represents our license revenues by region (in thousands):

| | Three Months Ended (In thousands) | | | | Nine Months Ended (In thousands) | | | |
|---------------------------------------|--------------------------------------|------------------|------------------|---------------|-------------------------------------|------------------|------------------|---------------|
| | September 30, | | Variance \$ s | Variance % | September 30, | | Variance \$ s | Variance % |
| | 2012 | 2011 | | | 2012 | 2011 | | |
| License Revenues | | | | | | | | |
| North America | \$ 10,640 | \$ 9,426 | \$ 1,214 | 13% | \$ 32,067 | \$ 29,133 | \$ 2,934 | 10% |
| Europe Middle East, and Africa (EMEA) | 1,353 | 2,000 | (647) | (32)% | 6,656 | 4,646 | 2,010 | 43% |
| Asia Pacific and others | 1,311 | 389 | 922 | 237% | 3,666 | 2,135 | 1,531 | 72% |
| Total | \$ 13,304 | \$ 11,815 | \$ 1,489 | 13% | \$ 42,389 | \$ 35,914 | \$ 6,475 | 18% |

% of total revenue 41% 35% 41% 36%

Services. Services revenues are comprised of maintenance and support, professional services, and training. The 14% overall decrease in services revenues was driven primarily by lower maintenance renewal revenues driven by higher maintenance renewal declines during fiscal 2011 and the first nine months of 2012. Maintenance revenues decreased 13% or by approximately \$2.5 million in the third quarter of 2012 compared to the third quarter of 2011. This decrease in maintenance revenues was primarily caused by maintenance renewal declines, and adverse currency exchange impacts. The weak economic environment, mainly in Europe also contributed to the decline in maintenance revenues during the quarter. It is important to note that we are currently transitioning from our legacy e.Reports product suite to our new BIRT based product offering. As our legacy products age, we have experienced higher than normal decline rates which may continue for the foreseeable future. In the mean time, BIRT is expected to become the dominant contributor to license and maintenance revenues. As this transition progresses, we expect to see our decline rate improve.

Foreign currency exchange losses attributed to international maintenance revenues were approximately \$530,000 during the third quarter of fiscal 2012 compared to approximately \$540,000 of exchange gains reported during the same period in the prior year.

For the first nine months of fiscal year 2012, the underlying reasons for the changes in the various components of our services revenues were similar to those experienced during the quarter as noted above. The increase in services revenues in Asia for the first nine months of 2012 was mostly due to a large compliance transaction that included back maintenance in the first quarter, which consequently resulted in high services revenues for this region.

The following table represents our total services revenues by region (in thousands):

| | Three Months Ended (In thousands) | | | | Nine Months Ended (In thousands) | | | |
|---------------------------------------|--------------------------------------|------------------|-------------------|---------------|-------------------------------------|------------------|-------------------|---------------|
| | September 30, | | Variance \$ s | Variance % | September 30, | | Variance \$ s | Variance % |
| | 2012 | 2011 | | | 2012 | 2011 | | |
| Services Revenues | | | | | | | | |
| North America | \$ 14,424 | \$ 16,596 | \$ (2,172) | (13)% | \$ 45,144 | \$ 48,247 | \$ (3,103) | (6)% |
| Europe Middle East, and Africa (EMEA) | 3,446 | 4,368 | (922) | (21)% | 12,161 | 12,522 | (361) | (3)% |
| Asia Pacific and others | 1,005 | 1,030 | (25) | (2)% | 3,549 | 2,952 | 597 | 20% |
| Total Services | \$ 18,875 | \$ 21,994 | \$ (3,119) | (14)% | \$ 60,854 | \$ 63,721 | \$ (2,867) | (4)% |

Edgar Filing: ACTUATE CORP - Form 10-Q

% of total revenue

59%

65%

59%

64%

By region, North America accounted for approximately 76% of the total services revenues in the third quarter of fiscal 2012 while Europe and Asia Pacific accounted for 18% and 6% of the total services revenues, respectively. For the same period last year, North America accounted for approximately 75% of the total services revenues while the Europe and Asia Pacific regions accounted for 20% and 5% of the total services revenues, respectively. Foreign currency exchange losses attributed to international services revenues were approximately \$560,000 during the third quarter of fiscal 2012 compared to approximately \$570,000 of exchange gains reported during the same period in the prior year.

Table of Contents**Costs and Expenses***Cost of license fees*

| | Three Months Ended (In thousands) | | | | Nine Months Ended (In thousands) | | | |
|----------------------|--------------------------------------|--------|----------|----------|-------------------------------------|----------|----------|----------|
| | September 30, | | Variance | Variance | September 30, | | Variance | Variance |
| | 2012 | 2011 | \$ s | % | 2012 | 2011 | \$ s | % |
| Cost of license fees | \$ 482 | \$ 424 | \$ 58 | 14% | \$ 1,439 | \$ 1,366 | \$ 73 | 5% |
| % of license revenue | 4% | 4% | | | 3% | 4% | | |

Cost of license fees consists primarily of product packaging, documentation, production costs and the amortization of purchased technology. The increase in cost of license fees in absolute dollars for the third quarter and the first nine months of fiscal 2012, compared to the corresponding period was not significant. We expect our cost of license fees, as a percentage of revenues from license fees, to increase as a result of our acquisition of Quiterian which will result in additional amortization of purchased technology in the fourth quarter of 2012.

Cost of services

| | Three Months Ended (In thousands) | | | | Nine Months Ended (In thousands) | | | |
|-----------------------|--------------------------------------|----------|----------|----------|-------------------------------------|-----------|----------|----------|
| | September 30, | | Variance | Variance | September 30, | | Variance | Variance |
| | 2012 | 2011 | \$ s | % | 2012 | 2011 | \$ s | % |
| Cost of services | \$ 5,187 | \$ 4,998 | \$ 189 | 4% | \$ 15,267 | \$ 15,653 | \$ (386) | (2)% |
| % of services revenue | 27% | 23% | | | 25% | 25% | | |

Cost of services consists primarily of personnel and related costs, share-based compensation, facilities costs incurred in providing software maintenance and support, training and consulting services, as well as third-party costs incurred in providing training and consulting services. The increase in cost of services for the third quarter of 2012, compared to the same period last year was driven by higher stock based compensation due to a lower annualized forfeiture rate and merit increases which were effective July 1 of this year. Facilities related expenses also increased due to higher depreciation related to our new headquarter facility which we occupied in the third quarter of 2012. Partially offsetting these increases were lower commissions and third party consulting fees due to a decrease in professional services revenues.

For the nine months ended September 30, 2012, the underlying reasons for the changes in the various components of our cost of services were similar to those experienced during the quarter as noted above. Currently we expect our cost of services expenses as a percentage of total services revenues to remain at the current levels for the remainder of fiscal 2012.

Sales and marketing

| | Three Months Ended (In thousands) | | | | Nine Months Ended (In thousands) | | | |
|---------------------|--------------------------------------|-----------|----------|----------|-------------------------------------|-----------|----------|----------|
| | September 30, | | Variance | Variance | September 30, | | Variance | Variance |
| | 2012 | 2011 | \$ s | % | 2012 | 2011 | \$ s | % |
| Sales and marketing | \$ 12,067 | \$ 10,423 | \$ 1,644 | 16% | \$ 35,811 | \$ 31,819 | \$ 3,992 | 13% |
| % of total revenue | 38% | 31% | | | 35% | 32% | | |

Sales and marketing expenses consist primarily of salaries, commissions, share-based compensation and bonuses earned by sales and marketing personnel, promotional expenses, travel, entertainment and facility costs. Our overall sales and marketing expenses increased in the third quarter of 2012 compared to the corresponding period in the prior year due to approximately \$1.3 million increase in employee compensation and related benefits. This increase was driven primarily by higher average sales headcount which increased by 19% or 30 employees between the

Edgar Filing: ACTUATE CORP - Form 10-Q

third quarter of 2012 and the third quarter of 2011 as well as by higher stock based compensation due to a lower annualized forfeiture rate and merit increases which were effective July 1 of this year. Employee training and business travel increased during the third quarter of 2012 compared to the third quarter of 2011 due to our annual sales kickoff, which did not occur in 2011. We also experienced increases in marketing related expenses driven mainly by BIRT road shows and depreciation expense related to our new headquarter facility which we occupied in the third quarter of 2012. These increases were partially offset by lower third party commissions earned by our business partners in EMEA as license sales decreased in this region during the third quarter of 2012.

Table of Contents

For the nine months ended September 30, 2012, the underlying reasons for the changes in the various components of our sales and marketing expense were similar to those experienced during the quarter as noted above. We currently expect our sales and marketing expenses as a percentage of total revenues to remain at the current levels for the remainder of fiscal 2012.

Research and development

| | Three Months Ended (In thousands) | | | | Nine Months Ended (In thousands) | | | |
|--------------------------|--------------------------------------|----------|------------------|---------------|-------------------------------------|-----------|------------------|---------------|
| | September 30, | | Variance \$ s | Variance % | September 30, | | Variance \$ s | Variance % |
| | 2012 | 2011 | | | 2012 | 2011 | | |
| Research and development | \$ 6,060 | \$ 5,830 | \$ 230 | 4% | \$ 17,668 | \$ 18,480 | \$ (812) | (4)% |
| % of total revenue | 19% | 17% | | | 17% | 19% | | |

Research and development costs consist primarily of personnel and related costs associated with the development of new products, share-based compensation costs, enhancement of existing products, quality assurance and testing. Our overall research and development expense increased compared to the corresponding period in the prior year due to stock based compensation as a result of a lower annualized forfeiture rate and depreciation expense related to our new headquarter facility which we occupied in the third quarter of 2012.

For the nine months ended September 30, 2012, the decrease in research and development expense compared to the corresponding period in the prior year was primarily due to lower employee compensation and related benefits of approximately \$1 million. This decrease was mainly driven by lower salaries as our average headcount decreased by 6% or 10 employees during fiscal 2012 compared to the corresponding period in the prior year. We believe that continued investments in technology and product development costs are essential for us to remain competitive in the markets we serve, and we expect our research and development expenses as a percentage of total revenues to remain at the current levels for the remainder of fiscal 2012.

General and administrative

| | Three Months Ended (In thousands) | | | | Nine Months Ended (In thousands) | | | |
|----------------------------|--------------------------------------|----------|------------------|---------------|-------------------------------------|-----------|------------------|---------------|
| | September 30, | | Variance \$ s | Variance % | September 30, | | Variance \$ s | Variance % |
| | 2012 | 2011 | | | 2012 | 2011 | | |
| General and administrative | \$ 5,360 | \$ 4,885 | \$ 475 | 10% | \$ 16,918 | \$ 15,623 | \$ 1,295 | 8% |
| % of total revenue | 17% | 14% | | | 16% | 16% | | |

General and administrative expenses consist primarily of personnel costs, share-based compensation costs and related costs for finance, human resources, information systems and general management, as well as legal, bad debt and accounting expenses. The increase in general and administrative expenses in the third quarter of 2012 compared to the corresponding period in the prior year was driven mainly by approximately \$550,000 of higher stock based compensation resulting from a lower annualized forfeiture rate, higher depreciation expense related to our new headquarter facility which we occupied in the third quarter of 2012, an increase in bad debt expense and approximately \$168,000 of expenses related to our acquisition of Quiterian, which was announced on October 22, 2012. These increases were offset partially by lower litigation and audit related expenses incurred during the third quarter of 2012.

For the nine months ended September 30, 2012, the increase in general and administrative expenses compared to the corresponding period in the prior year was primarily due to higher stock base compensation and legal fees related to contract compliance matters pursued during the year. We expect our general and administrative expenses as a percentage of total revenues to remain at the current levels for the remainder of fiscal 2012.

Asset impairment

During the second quarter of fiscal 2011, the Company recorded \$1.7 million of in-process research and development (IPR&D) impairment charges. The Company had previously recorded IPR&D representing the fair value of a project that was underway at Xenos at the time of acquisition. The product underlying this IPR&D item was released on June 28, 2010 and the fair value of this intangible asset was amortized on a straight-line basis over the respective estimated useful life of seven years beginning July 2010. During the second quarter of 2011, the

Edgar Filing: ACTUATE CORP - Form 10-Q

Company deemed that it was necessary to impair this IPR&D due to the fact that changes in circumstances indicated to management that the carrying value of the IPR&D was not recoverable. Based on an analysis of historical sales of the product since its release in the second quarter of fiscal 2010, as well as the calculation of a discounted cash flow analysis projecting expected cash flows through the remaining useful life of the product, it was determined that the IPR&D balance should be impaired down to zero.

Table of Contents*Amortization of other purchased intangibles*

| | Three Months Ended (In thousands) | | | | Nine Months Ended (In thousands) | | | |
|---|--------------------------------------|--------|------------------|---------------|-------------------------------------|----------|------------------|---------------|
| | September 30, | | Variance \$ s | Variance % | September 30, | | Variance \$ s | Variance % |
| | 2012 | 2011 | | | 2012 | 2011 | | |
| Amortization of other purchased intangibles | \$ 289 | \$ 289 | \$ | % | \$ 867 | \$ 1,007 | \$ (140) | (14)% |
| % of total revenue | 1% | 1% | | | 1% | 1% | | |

Amortization expense decreased during the first nine months of 2012 as compared to the same period in 2011 due to the impairment of in-process research and development (IPR&D) related to our acquisition of Xenos. This IPR&D was amortized prior to impairment which occurred in June 2011. We continue to amortize the intangible assets purchased through the acquisition of Xenos on a straight-line basis over their estimated useful lives of seven years. For the remainder of fiscal 2012, we expect amortization expense related to other purchased intangible assets to as a result of our acquisition of Quiterian in the fourth quarter of 2012.

Restructuring charges

| | Three Months Ended (In thousands) | | | | Nine Months Ended (In thousands) | | | |
|--------------------|--------------------------------------|--------|------------------|---------------|-------------------------------------|--------|------------------|---------------|
| | September 30, | | Variance \$ s | Variance % | September 30, | | Variance \$ s | Variance % |
| | 2012 | 2011 | | | 2012 | 2011 | | |
| Restructuring | \$ 21 | \$ 158 | \$ (137) | (87)% | \$ 54 | \$ 889 | \$ (835) | (94)% |
| % of total revenue | % | 1% | | | % | % | | |

Our restructuring expense decreased significantly in the third quarter and the first nine months of 2012 compared to the same periods last year due to the fact that in mid 2011 we implemented a plan to restructure parts of our North America product development and global sales and marketing operations in order to align our cost structure with our business plan. As a result of the restructuring program, we reduced our global workforce by 26 positions and recorded approximately \$1.2 million of restructuring charges related to employee severance arrangements and idle facilities in North America and Europe. In addition to these charges, we reversed approximately \$283,000 of a previously accrued severance liability in 2011. This severance liability was initially recorded in December 2004 in connection with litigation related to a previous reduction in work force in Europe.

Historically, restructuring charges have included costs associated with reductions in workforce, exits of idle facilities and disposals of fixed assets. These restructuring charges were based on actual and estimated costs incurred including estimates of sublease income on portions of our idle facilities that we periodically update based on market conditions and in accordance with our restructuring plans. These estimates were impacted by the rules governing the termination of employees, especially those in foreign countries.

Interest and other income, net

| | Three Months Ended (In thousands) | | | | Nine Months Ended (In thousands) | | | |
|---|--------------------------------------|----------|------------------|---------------|-------------------------------------|----------|------------------|---------------|
| | September 30, | | Variance \$ s | Variance % | September 30, | | Variance \$ s | Variance % |
| | 2012 | 2011 | | | 2012 | 2011 | | |
| Interest and other income, net | \$ 102 | \$ 170 | \$ (68) | (40)% | \$ 258 | \$ 474 | \$ (216) | (46)% |
| Foreign exchange gain/(loss) | 72 | 812 | (740) | (91)% | 505 | (1,314) | 1,819 | (138)% |
| Total interest income and other income (expense), net | \$ 174 | \$ 982 | \$ (808) | (82)% | \$ 763 | \$ (840) | \$ 1,603 | (191)% |
| Interest expense | \$ (55) | \$ (136) | \$ 81 | (60)% | \$ (255) | \$ (781) | \$ 526 | (67)% |

Edgar Filing: ACTUATE CORP - Form 10-Q

During the third quarter of 2012, we experienced currency exchange gains as a result of favorable revaluation of net monetary assets held by our subsidiaries in North America, partially offset by losses in Europe and Asia. In North America we experienced exchange gains as Canadian based net assets revalued positively against the U.S. Dollar while in Europe and Asia, net monetary assets held by our subsidiaries in U.S. Dollars revalued negatively as the U.S. Dollar became weaker against the Swiss Franc and the Singaporean Dollar. The revaluation of these currency amounts held by our subsidiaries is a required procedure in consolidating and reporting the financial results of our global operations. We also incurred lower interest expense as we fully paid-down the outstanding balance on our credit facility in early part of May 2011.

Table of Contents

For the nine months ended September 30, 2012, the underlying reasons for the changes in the various components of interest and other income, net were similar to those experienced during the quarter as noted above.

Provision for income taxes

| | Three Months Ended (In thousands) | | | | Nine Months Ended (In thousands) | | | |
|----------------------------|--------------------------------------|----------|----------|------|-------------------------------------|----------|----------|-----|
| | September 30, | | Variance | | September 30, | | Variance | |
| | 2012 | 2011 | \$ s | % | 2012 | 2011 | \$ s | % |
| Provision for income taxes | \$ 2,725 | \$ 2,926 | \$ (201) | (7)% | \$ 6,182 | \$ 4,514 | \$ 1,668 | 37% |
| Effective tax rate | 96% | 38% | | | 39% | 39% | | |

For the three months ended September 30, 2012, we recorded an income tax provision of \$2.7 million, as compared to an income tax provision of \$2.9 million for the same period last year. The decrease in the income tax provision for the third quarter of fiscal 2012 as compared to the third quarter of fiscal 2011 is due to significantly lower profit before tax for the quarter. In addition, the expense for valuation allowance of \$1.8 million recorded against California R & D credits in the third quarter of fiscal 2012 significantly increased the effective tax rate compared to the same quarter of the prior year.

For the nine months ended September 30, 2012, we recorded an income tax provision of \$6.2 million, as compared to an income tax provision of \$4.5 million for the same period last year. The increase in the income tax provision for the nine months of fiscal 2012 as compared to the nine months of fiscal 2011 is mainly due a valuation allowance of \$1.8 million recorded against California R & D credits in the third quarter of fiscal 2012 which significantly increased the effective tax rate compared to the same period of the prior year. The effective rate before discrete items for both the three and the nine months ended September 30, 2012 was lower due to the increased mix of foreign earnings in lower tax jurisdictions as compared to the same period in the prior year.

We believe that it is more likely than not that the benefit from certain state R & D credit carryforwards will not be realized. In recognition of this risk, we have provided a valuation allowance of \$1.8 million on the deferred tax assets relating to these state R & D credit carryforwards. If our assumptions change and we determine we will be able to realize these R & D credits, the tax benefits relating to any reversal of the valuation allowance on deferred tax assets as of September 30, 2012, will be accounted for as a reduction of income tax expense.

During the three months ended September 30, 2012, the Company reduced its reserve for uncertain tax positions by approximately \$323,000 due to the expiration of the statute of limitations on U.S. Federal R & D tax credits. The Company recognizes interest and penalties accrued related to unrecognized tax benefits as a component of income tax expense. The Company does not believe it is reasonably possible that its reserve for uncertain tax positions would materially change in the next 12 months.

Liquidity and Capital Resources

Our sources of cash, cash equivalents and short-term investments are funds generated from our business operations and funds that may be drawn down under our credit facility. The following sections discuss changes in our balance sheet and cash flows, and other commitments on our liquidity and capital resources during the first nine months of 2012. This data should be read in conjunction with the Consolidated Statements of Cash Flows.

| (dollars in thousands) | As of September 30, 2012 | As of September 30, 2011 | Change \$ | Change % |
|---|--------------------------------|--------------------------------|--------------|----------|
| Cash, cash equivalents and short-term investments | \$ 74,600 | \$ 63,514 | \$ 11,086 | 17% |
| Working capital | \$ 56,259 | \$ 39,391 | \$ 16,868 | 43% |
| Stockholders' equity and non-controlling interest | \$ 128,277 | \$ 113,483 | \$ 14,794 | 13% |

We hold our cash, cash equivalents and investments primarily in the United States, Switzerland, and Singapore. As of September 30, 2012, approximately \$30 million of the total \$74.6 million of cash, cash equivalents and short term investments was held by our foreign subsidiaries. Currently, the foreign cash is not available to fund the U.S. operations. If these funds are needed for our operations in the U.S., we would be required to accrue and pay U.S. taxes to repatriate these funds. However, our intent is to indefinitely reinvest these funds outside of the U.S. and our current plans or cash requirements do not demonstrate a need to repatriate them to fund our U.S. operations.

Edgar Filing: ACTUATE CORP - Form 10-Q

Cash flows from operating activities: Net cash provided by operating activities was \$16.6 million, resulting from net income of \$9.5 million, adjusted for \$8.4 million in non-cash charges and \$1.3 million in net change in operating assets and liabilities. The non-cash charges included depreciation and amortization, stock-based compensation, impairment of fixed assets, tax benefits related to stock benefit plans and other non-cash adjustments, and the change in valuation allowance on deferred income tax assets. Net change in operating assets and liabilities included a decrease in accounts receivables, accrued compensation and other liabilities primarily

Table of Contents

associated with payments of bonuses and commissions, payments of annual 401(k) Plan match for fiscal 2011, and payments of accrued audit and legal fees. Days sales outstanding (DSO) which is calculated based on revenue for the most recent quarter and accounts receivable as of the balance sheet date decreased by 2 days from 60 days at September 30, 2011 to 58 days at September 30, 2012. Approximately 40% or \$6.7 million of the net cash provided from operations was from a reduction in accounts receivable during the year. We continue to closely monitor the credit quality and payment history of our existing and new customers to better identify and minimize, in advance, the risk of our customers potential inability to make required payments.

Our primary source of operating cash flows is the collection of accounts receivable from our customers, including maintenance which is typically billed annually in advance. Our overall maintenance revenues comprised 54% of our total revenues in the first nine months of fiscal 2012 and we believe that future proceeds from maintenance renewals will be one of primary sources of our operating cash flows. It is important to note that we are currently transitioning from our legacy e.Reports product suite to our new BIRT based product offering. As our legacy products age, we have experienced higher than normal decline rates. We expect this trend to continue. In the mean time, BIRT is expected to become the dominant contributor to license and maintenance revenues. As this transition progresses, we expect to see our decline rate improve.

Our operating cash flows are also impacted by the timing of payments to our vendors for accounts payable and other liabilities. We generally pay our vendors and service providers in accordance with the invoice terms and conditions. The timing of cash payments in future periods will be impacted by the terms of accounts payable arrangements.

Cash flows from investing activities: The changes in cash flows from investing activities primarily relate to the timing of purchases, maturities and sales of our investments in marketable securities. We also use cash to invest in capital and other assets to support our growth. Cash used in investing activities for the nine months ended September 30, 2012 was approximately \$11.7 million compared with cash provided of \$25.8 million for the same period in fiscal 2011. The decrease in cash used in the first nine months of this year was mainly due to leasehold improvements associated with our new headquarters facility located at the BayCenter Campus in San Mateo, California which became available for occupancy in July 2012. The remaining change in cash used primarily relates to the timing of purchases and maturities of marketable securities. During the first nine months of 2011, we liquidated a large portion of our short-term investments in order to fully pay down the outstanding balance on our revolving line of credit with WFF. As a result of this liquidation which resulted in an increase in cash provided from investing activities for the nine months ended September 30, 2011.

Cash flows from financing activities: Cash used in financing activities was \$4.4 million for the nine months ended September 30, 2012 compared to \$30.6 million used during the same period in fiscal 2011. During the first nine months of 2012, we used approximately \$16 million to repurchase 2,371,604 shares of our common stock compared with \$5 million to repurchase 810,800 shares during the same period last year. The cash used for the repurchases were partially offset by proceeds from the exercise of employee stock options and related tax benefits during the first nine months of 2012 and 2011. During the first nine months of 2011, we used \$40 million to fully pay down the outstanding balance on our revolving line of credit with WFF. This pay down was partially offset by proceeds from the exercise of employee stock options and related tax benefits during the first nine months of 2011.

We believe that our current cash balances, funds available under our credit facility, and cash generated from operations will be sufficient to meet our working capital and capital expenditure requirements for at least the next twelve months. Thereafter, if cash generated from operations is insufficient to satisfy our liquidity requirements, we may find it necessary to sell additional equity, or obtain additional credit facilities. The sale of additional equity could result in additional dilution to our current stockholders. A portion of our cash may be used to acquire or invest in complementary businesses or complementary products or to obtain the right to use complementary technologies.

Contractual Obligations and Commercial Commitments

General

The Company is engaged in certain legal actions arising in the ordinary course of business. Although there can be no assurance as to the outcome of such litigation, the Company believes it has adequate legal defenses and it believes that the ultimate outcome of any of these actions will not have a material effect on the Company's consolidated financial position or results of operations. However, expenses associated with certain of these legal actions could result in increased operating expenses that may adversely impact the Company's future operating results and cash flows.

Revolving credit line

In early November of 2008, the Company entered into a revolving Credit Agreement with Wells Fargo Foothill (WFF) and secured a revolving line of credit in the principal amount of up to \$50 million. During the fourth quarter of fiscal 2008, the Company used \$30 million of its cash

Edgar Filing: ACTUATE CORP - Form 10-Q

along with \$30 million of funds available through this credit facility to complete a \$60 million common stock buyback. During the first quarter of 2010, the Company borrowed an additional \$10 million of funds available through this credit facility to complete the acquisition of Xenos, which was completed on February 1, 2010. There are no minimum pay-down requirements under the terms of this credit facility so long as we remain in compliance with the terms of the Credit Agreement. Total

Table of Contents

costs associated with the facility, including legal and closing fees, amounted to approximately \$1.1 million and were fully paid as of September 30, 2012. These costs were capitalized and are being amortized over four years in the Company's Consolidated Financial Statements. Such assets are reflected as current assets if amortized within one year or non-current assets if amortized beyond one year. The Credit Agreement was originally for a period of four years and was originally scheduled to expire on November 3, 2012.

In May 2011, the Company paid down the outstanding balance on its revolving line of credit. The Company used \$40 million in cash and short-term investments in order to pay down this outstanding debt.

On December 29, 2011, the Company amended and re-negotiated its credit facility with Wells Fargo Capital Finance, LLC ("WFCF"). The amended credit facility provided for the following:

An extension of the original agreement entered in November 2008. The termination date was extended from November 3, 2012 to November 3, 2015,

Replacement of a \$125,000 commitment fee that was payable on November 3, 2011 with a closing fee of \$100,000 that was paid on December 29, 2011,

A 50% reduction in the applicable internal rate on the outstanding credit balance from 3.5% to 1.75%, and

A reduction in the unused line fee from 0.50% to 0.30% per year applied to the unutilized portion of the credit facility. The remaining unamortized costs associated with the credit facility will be amortized from the date of amendment over four years.

As of September 30, 2012, there was no balance owed on this credit facility and the balance available under the revolving credit facility was approximately \$50 million. Interest is based on a floating rate plus an applicable margin based on the outstanding balance of the amount drawn under the Credit Agreement. The floating rate is determined at the Company's election and may either be (i) London Interbank Offered Rate ("LIBOR") or (ii) the greater of the Federal Funds Rate plus applicable margin and the Prime Rate. If the Company's usage of the credit line exceeds 80% of its trailing four quarters of recurring maintenance revenue, or if the sum of available funds under the Credit Agreement plus available cash is less than \$10 million, the Company is required to meet certain minimum income targets and be subject to a limit on annual capital expenditures. As of September 30, 2012, the Company was able to meet the 80% test as well as the \$10 million minimum cash threshold and was therefore not subject to the income or the capital expenditures covenants. The Company is required to make interest payments on any outstanding balances and pay an unused commitment fee on any unused portion of the credit line on a monthly basis.

The following table represents costs related to the Company's credit facility (in thousands):

| | Three Months Ended | | Nine months Ended | |
|-------------------------------------|--------------------|--------------------|--------------------|--------------------|
| | September 30, 2012 | September 30, 2011 | September 30, 2012 | September 30, 2011 |
| Interest expense | \$ | \$ | \$ | \$ 441 |
| Amortization of debt issuance costs | 17 | 72 | 51 | 216 |
| Unused line fees | 38 | 64 | 114 | 122 |
| | \$ 55 | \$ 136 | \$ 165 | \$ 779 |

The Credit Agreement contains covenants, which, among other things, impose certain limitations with respect to lines of business, mergers, investments and acquisitions, additional indebtedness, distributions, guarantees, liens and encumbrances. In the event the Company does not meet the requirements specified above, a triggering event will be deemed to have occurred and the Company would be required to maintain the two financial covenants listed below:

achieve income before interest and taxes, measured on a quarter-end basis, of at least the required amount set forth per the Credit Agreement,

limit the amount of capital expenditures to an amount not exceeding that set forth per the Credit Agreement.

The Company's indebtedness under the Credit Agreement is secured by a lien on (i) substantially all of its assets and the assets of Actuate International Corporation and (ii) by a pledge of all of its stock and a portion of the stock of each of its subsidiaries.

Operating Lease Commitments

On November 28, 2011, the Company entered into a ten year lease agreement with a third party for approximately 58,000 square feet of office space in the BayCenter Campus in San Mateo, California. This lease is operating in nature and commenced on June 1, 2012 and will end on May 31, 2022. In addition, the lease provides for four months of free rent (rent holiday) and approximately \$2.6 million in landlord incentives to be applied towards construction of improvements. At September 30, 2012, the deferred rent liability balance related to the new lease totaled approximately \$3.1 million and this balance gradually declines every

Table of Contents

month through May 2022 when contractual cash payments eventually exceed the straight-line lease expense. This deferred rent liability balance was classified under the long term accrued liabilities section of the Company's Consolidated Balance Sheet at September 30, 2012. Actuate vacated its previous corporate headquarters located at the Bridgepointe Campus in July 2012 and is now using the BayCenter Campus as its corporate headquarters.

Upon the execution of the new lease, Actuate delivered to the new landlord two letters of credit totaling \$225,300. These letters of credit guarantee Actuate's contractual obligations related to the BayCenter Campus in San Mateo, California.

Actuate leases smaller office facilities in various locations in the United States and abroad. All facilities are leased under operating leases. Total rent expense was approximately \$1.2 million in the third quarter of fiscal year 2012 compared with approximately \$862,000 in third quarter of fiscal year 2011. The increase in rent expense during the third quarter of 2012 compared with third quarter of last year was partially offset by approximately \$142,000 of lower facilities related operating expenses.

| | Total | Less than 1 year | 1 - 3 years | 3 - 5 years | Thereafter |
|---|------------------|-----------------------------|------------------------|------------------------|-------------------|
| Obligations: | | | | | |
| Operating leases (1) | \$ 30,779 | \$ 4,235 | \$ 7,264 | \$ 5,632 | \$ 13,648 |
| Interest and loan obligations (2) | 470 | 152 | 305 | 13 | |
| Obligations for uncertain tax positions (3) | 1,344 | | 1,344 | | |
| Total | \$ 32,593 | \$ 4,387 | \$ 8,913 | \$ 5,645 | \$ 13,648 |

- (1) Our future contractual obligations include minimum lease payments under operating leases at September 30, 2012.
- (2) Includes estimated interest and commitment fees related to the revolving line of Credit Agreement with WFCF.
- (3) Represents the tax liability associated with uncertain tax positions. See discussion on obligations for uncertain tax positions in Note 12 of our Notes to the Consolidated Financial Statements of our Form 10-K for fiscal year 2011 filed with the SEC on March 9, 2012.

Table of Contents**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Market Risk. Market risk represents the risk of loss that may impact our financial position due to adverse changes in financial market prices and rates. Our market risk exposure is primarily a result of credit risk, fluctuations in interest rates and foreign exchange rates.

Foreign Currency Exchange Risk. During the first nine months of fiscal years 2012 and 2011 we derived 27% and 22% of our total revenues from sales outside of North America, respectively. We face exposure to market risk on these receivables with respect to fluctuations in the relative value of currencies. Our international revenues and expenses are denominated in foreign currencies, principally the Euro and the British Pound Sterling. The functional currency of each of our foreign subsidiaries is the local currency. We are also exposed to foreign exchange rate fluctuations as the financial results of foreign subsidiaries are translated into U.S. dollars in consolidation. As exchange rates vary, transaction gains and losses may vary from expectations and adversely impact overall expected profitability. Our realized gains due to foreign exchange rate fluctuations was approximately \$505,000 during the first nine months of fiscal 2012 compared to losses of approximately \$1.3 million for the first nine months of fiscal 2011. During the first nine months of fiscal 2012, exchange rate fluctuations on foreign revenue transactions negatively impacted our total revenues by approximately \$1.3 million when compared to the same period in the prior year while expenses were positively impacted by approximately \$890,000.

We performed a sensitivity analysis on the net monetary accounts subject to revaluation that are held primarily by our international subsidiaries. We used the following steps to determine the approximate impact of currency exchange rate fluctuations:

Identified material net monetary assets held in non-functional currencies. These primarily consist of the Euro, British Pound, Canadian Dollar, and the U.S. Dollar-based net assets held by our international subsidiaries.

Applied hypothetical changes in exchange rates to these net monetary balances held by each subsidiary as identified above. The result was a hypothetical revaluation gain or (loss) in the subsidiary's functional currency.

We then translated the revaluation result as described above to U.S. Dollars using the latest quarter average exchange rate. This resulted in hypothetical revaluation gains or (losses) before income taxes. These hypothetical results are summarized in the table below as of September 30, 2012:

| Estimated annual changes in currency exchange (in millions) | | | | | |
|---|----------|----------|--------|--------|--------|
| -15% | -10% | -5% | +5% | +10% | +15% |
| \$ (4.8) | \$ (3.2) | \$ (1.6) | \$ 1.6 | \$ 3.2 | \$ 4.8 |

Interest Rate Risk. The primary objective of our investment activities is to preserve principal while at the same time maximizing yields without significantly increasing risk. To achieve this objective, we invest in highly liquid and high quality debt securities. Due to the nature of our investments, we believe that there is limited risk exposure.

Credit Risk. Financial instruments that potentially subject us to concentrations of credit risk consist primarily of cash and cash equivalents, investments in marketable securities, and trade accounts receivable. We have policies that limit investments in investment grade securities and the amount of credit exposure to any one issuer.

We sell primarily to customers in the financial services industry, predominantly in the United States and Europe. Accordingly, unfavorable economic conditions adversely impacting the financial services industry has had a material adverse effect on the Company's business, financial condition and results of operations. For example, the financial services industry has experienced and may continue to experience cyclical fluctuations in profitability, which may affect timing of, or actual purchases of, our products which would have a material adverse effect on the our business, financial condition and results of operations. There were no customers that accounted for more than 10% of total revenues in the twelve months ended September 30, 2012 or 2011.

We perform ongoing credit evaluations of our customers and maintain an allowance for potential credit losses. We do not require collateral or other security to support customer receivables. Our credit risk is also mitigated because our customer base is diversified by geography. We generally do not use foreign exchange contracts to hedge the risk in receivables denominated in foreign currencies. We do not hold or issue derivative financial instruments for trading or speculative purposes.

Edgar Filing: ACTUATE CORP - Form 10-Q

We do not believe that future market equity or interest rate risks related to our marketable investments or debt obligations will have a material impact on our results of operations. The Company is not currently invested in any derivative securities.

Table of Contents**ITEM 4. CONTROLS AND PROCEDURES****a) Evaluation of Disclosure Controls and Procedures**

As of September 30, 2012 (the Evaluation Date), Actuate Corporation carried out an evaluation under the supervision and with the participation of Actuate management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of Actuate disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act). There are inherent limitations to the effectiveness of any system of disclosure controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable, not absolute, assurance of achieving their control objectives. Our Chief Executive Officer and Chief Financial Officer have concluded that, as of September 30, 2012, (1) Actuate disclosure controls and procedures were designed to provide reasonable assurance of achieving their objectives, and (2) Actuate disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed in the reports Actuate files and submits under the Exchange Act is recorded, processed, summarized and reported as and when required, and that such information is accumulated and communicated to Actuate management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding its required disclosure.

(b) Changes in Internal Control over Financial Reporting

There were no changes in Actuate internal control over financial reporting during the three months ended September 30, 2012, that have materially affected, or are reasonably likely to materially affect, Actuate internal control over financial reporting.

Part II. Other Information**Item 1. Legal Proceedings**

The Company is engaged in certain legal actions arising in the ordinary course of business, including international employment litigation arising out of restructuring activities. Although there can be no assurance as to the outcome of such litigation, the Company believes that it has adequate legal defenses and that the ultimate outcome of any of these actions will not have a material effect on the Company's financial position or results of operations. However, expenses associated with certain of these legal actions could result in increased operating expenses that may adversely impact the Company's future operating results and cash flows.

Item 1A. Risk Factors

Investors should carefully consider the following risk factors and warnings before making an investment decision. The risks described below are not the only ones facing Actuate. Additional risks that we do not yet know of or that we currently think are immaterial may also impair our business operations. If any of the following risks, or the additional risks described in the preceding sentence, actually occurs, our business, operating results or financial condition could be materially harmed. In such case, the trading price of our common stock could decline and you may lose all or part of your investment. Investors should also refer to the other information set forth in this Report on Form 10-K, including the financial statements and the notes thereto.

THE COMPANY'S OPERATING RESULTS MAY BE VOLATILE AND DIFFICULT TO PREDICT. IF IT FAILS TO MEET ITS ESTIMATES OF FUTURE OPERATING RESULTS OR IT FAILS TO MEET THE EXPECTATIONS OF PUBLIC MARKET ANALYSTS AND INVESTORS, THE MARKET PRICE OF ITS STOCK MAY DECREASE SIGNIFICANTLY.

The susceptibility of the Company's operating results to significant fluctuations makes any prediction, including the Company's estimates of future operating results, difficult. In addition, the Company believes that period-to-period comparisons of its operating results are not necessarily meaningful and investors should not rely on them as indications of the Company's future performance. The Company's operating results have in the past varied, and may in the future vary significantly due to factors such as the following:

Demand for its products;

Edgar Filing: ACTUATE CORP - Form 10-Q

The size and timing of significant orders for its products;

A slowdown or a decrease in spending on information technology by its current and/or prospective customers;

Competition from products that are directly competitive with its products;

Lost revenue from introduction or market acceptance of open source products that are directly competitive with its products;

The management, performance and expansion of its international operations;

Foreign currency exchange rate fluctuations;

Customers' desire to consolidate their purchases of Rich Information Applications, Performance Management, Business Intelligence or Enterprise Output Management software to one or a very small number of vendors from which a customer has already purchased software;

Table of Contents

General domestic and international economic and political conditions, including war, terrorism, and the threat of war or terrorism;

Sales cycles and sales performance of its indirect channel partners;

Changes in the way it and its competitors price their respective products and services, including maintenance and transfer fees;

Continued successful relationships and the establishment of new relationships with OEMs;

Changes in its level of operating expenses and its ability to control costs;

The cost, outcome or publicity surrounding any pending or threatened lawsuits;

Ability to make new products and product enhancements commercially available in a timely manner;

Ability to effectively launch new or enhanced products, including the timely education of the Company's sales, marketing and consulting personnel with respect to such new or enhanced products;

Customers delaying purchasing decisions in anticipation of new products or product enhancements;

Budgeting cycles of its customers;

Failure to successfully manage acquisitions and integrate acquired companies;

Defects in products and other product quality problems;

Failure to successfully meet hiring needs including for qualified professional services employees and unexpected personnel changes;

Changes in the market segments and types of customers where it focuses sales and marketing efforts;

Changes in perpetual licensing models to term-or subscription-based models with respect to which license revenue is not fully recognizable at the time of initial sale;

Changes in service models with respect to which consulting services are performed on a fixed-fee, rather than variable fee, basis; and

Potential impairments of goodwill, intangibles and other investments.

Edgar Filing: ACTUATE CORP - Form 10-Q

Because the Company's software products are typically shipped shortly after orders are received, total revenues in any quarter are substantially dependent on orders booked and shipped throughout that quarter. Furthermore, several factors may require the Company, in accordance with accounting principles generally accepted in the United States, to defer recognition of license fee revenue for a significant period of time after entering into a license agreement, including:

Whether the license agreement includes both software products that are then currently available and software products or other enhancements that are still under development;

Whether the license agreement relates entirely or partly to software products that are currently not available;

Whether the license agreement requires the performance of services that may preclude revenue recognition until successful completion of such services;

Whether the license agreement includes acceptance criteria that may preclude revenue recognition prior to customer acceptance;

Whether the license agreement includes undelivered elements (including limited terms or durations) that may preclude revenue recognition prior to customer acceptance; and

Whether the license agreement includes extended payment terms that may delay revenue recognition until the payment becomes due. In addition, the Company may in the future experience fluctuations in its gross and operating margins due to changes in the mix of its domestic and international revenues, changes in the mix of its direct sales and indirect sales and changes in the mix of license revenues and service revenues, as well as changes in the mix among the indirect channels through which its products are offered.

A significant portion of the Company's total revenues in any given quarter is derived from existing customers. The Company's ability to achieve future revenue growth, if any, will be substantially dependent upon its ability to increase revenues from license fees and services from existing customers, to expand its customer base and to increase the average size of its orders. To the extent that such increases do not occur in a timely manner, the Company's business, operating results and financial condition would be harmed.

Table of Contents

The Company's expense levels and any plans for expansion are based in significant part on its expectations of future revenues and are relatively fixed in the short-term. If revenues fall below expectations and the Company is unable to respond quickly by reducing its spending, the Company's business, operating results, and financial condition could be harmed.

The Company often implements changes to its license pricing structure for all of its products including increased prices and modified licensing parameters. If these changes are not accepted by the Company's current customers or future customers, its business, operating results, and financial condition could be harmed.

Based upon all of the factors described above, the Company has a limited ability to forecast the amount and mix of future revenues and expenses and, the Company's actual operating results may from time to time fall below its estimates or the expectations of public market analysts and investors which is likely to cause the price of the Company's common stock to decline.

OUR DEBT COVENANTS IN OUR CREDIT AGREEMENT RESTRICT OUR FINANCIAL AND OPERATIONAL FLEXIBILITY.

Our Credit Agreement contains a number of financial covenants, which, among other things, may require us to maintain specified financial ratios and impose certain limitations on us with respect to lines of business, mergers, investments and acquisitions, additional indebtedness, distributions, guarantees, liens and encumbrances. Our ability to meet the financial ratios can be affected by operating performance or other events beyond our control, and we cannot assure you that we will meet those ratios and failure to do so may cause an event of default under the Credit Agreement. Our indebtedness under the Credit Agreement is secured by a lien on substantially all of our assets and of our subsidiaries, by a pledge of our operating and license subsidiaries' stock and by a guarantee of our subsidiaries. If the amounts outstanding under the Credit Agreement were accelerated due to an event of default, the lenders could proceed against such available collateral by forcing the sales of these assets.

THE COMPANY HAS MADE, AND MAY IN THE FUTURE MAKE, ACQUISITIONS, WHICH INVOLVE NUMEROUS RISKS.

The Company's business is highly competitive, and as such, its growth is dependent upon its ability to expand its market, enhance its existing products, introduce new products on a timely basis and expand its distribution channels and professional services organizations. In order to achieve these objectives, the Company had pursued and will continue to pursue acquisitions of other companies.

Generally, acquisitions involve numerous risks, including the following:

The benefits of the acquisition not materializing as planned or not materializing within the time periods or to the extent anticipated;

The Company's ability to manage acquired entities' people and processes that are headquartered in separate geographical locations from the Company's headquarters;

The possibility that the Company will pay more than the value it derives from the acquisition;

Difficulties in integration of the operations, technologies, and products of the acquired companies;

The assumption of certain known and unknown liabilities of the acquired companies;

Difficulties in retaining key relationships with customers, partners and suppliers of the acquired company, the loss of recurring revenue from multiple subsidiaries of one large multi-national organization or the ability to sell and support certain third party software.

Edgar Filing: ACTUATE CORP - Form 10-Q

The risk of diverting management's attention from normal daily operations of the business;

The Company's ability to issue new releases of the acquired company's products on existing or other platforms;

Negative impact to the Company's financial condition and results of operations and the potential write down of impaired goodwill and intangible assets resulting from the consolidation of financial statements;

Risks of entering markets in which the Company has no or limited direct prior experience; and

The potential loss of key employees of the acquired company.

Mergers and acquisitions of high-technology companies are inherently risky, and the Company cannot be certain that any acquisition will be successful and will not materially harm the Company's business, operating results or financial condition.

Table of Contents

INTELLECTUAL PROPERTY CLAIMS AGAINST THE COMPANY CAN BE COSTLY AND COULD RESULT IN THE LOSS OF SIGNIFICANT RIGHTS.

Third parties may claim that the Company's current or future products infringe their intellectual property rights. The Company has been subject to infringement claims in the past and it expects that companies in the Business Intelligence, Rich Information Applications, Enterprise Output Management or Performance Management software market will increasingly be subject to infringement claims as the number of products and/or competitors in its industry segment grows and the functionality of products in different industry segments overlaps. Any such claims, with or without merit, could be time-consuming to defend, result in significant litigation and other expenses, divert management's attention and resources, cause product shipment delays or require the Company to enter into royalty or licensing agreements. Such royalty or licensing agreements, if required, may not be available on terms acceptable to the Company or at all. A successful claim of product infringement against the Company and its failure or inability to license the infringed or similar technology could materially harm the Company's business, operating results and financial condition.

COMPUTER HACKERS MAY DAMAGE OUR SYSTEMS, SERVICES AND PRODUCTS, AND BREACHES OF DATA PROTECTION COULD IMPACT OUR BUSINESS.

Computer programmers and hackers may be able to penetrate our network security and misappropriate our confidential information or that of third parties, create system disruptions or cause interruptions or shutdowns of our internal systems and services. If successful, any of these events could damage our computer systems or those of our customers and could disrupt or prevent us from providing timely maintenance and support for our software platform. Computer programmers and hackers also may be able to develop and deploy viruses, worms and other malicious software programs that attack our products or otherwise exploit any security vulnerabilities of our products. The costs to us to eliminate or alleviate security problems, bugs, viruses, worms, malicious software programs and security vulnerabilities could be significant, and the efforts to address these problems could result in interruptions, delays, cessation of service and loss of existing or potential customers and may impede our sales, manufacturing, distribution and other critical functions.

In the course of our regular business operations and providing maintenance and support services to our customers, we process and transmit proprietary information and sensitive or confidential data, including personal information of employees, customers and others. Breaches in security could expose us, our customers or the individuals affected to a risk of loss or misuse of this information, which could result in potential regulatory actions, litigation and potential liability for us, as well as the loss of existing or potential customers and damage to our brand and reputation.

THE COMPANY MAY NOT BE ABLE TO PROTECT ITS SOURCE CODE FROM COPYING.

Source code, the detailed program commands for our operating systems and other software programs, is critical to our business. Although we take significant measures to protect the secrecy of large portions of our source code, unauthorized disclosure or reverse engineering of a significant portion of our source code could make it easier for third parties to compete with our products by copying functionality, which could adversely affect our revenue and operating margins.

IF THE COMPANY FAILS TO GROW REVENUE FROM INTERNATIONAL OPERATIONS AND EXPAND ITS INTERNATIONAL OPERATIONS ITS BUSINESS WOULD BE SERIOUSLY HARMED.

The Company's total revenues derived from sales outside North America were 25%, 22% and 19% for the first nine months of fiscal years 2012, 2011 and 2010, respectively. Its ability to achieve revenue growth in the future will depend in large part on its success in increasing revenues from international sales. The Company intends to continue to invest significant resources to expand its sales and support operations outside North America and to potentially enter additional international markets. In order to expand international sales, the Company must establish additional foreign operations, expand its international channel management and support organizations, hire additional personnel, recruit additional international resellers and increase the productivity of existing international resellers. The Company intends to continue to shift its focus from direct sales to indirect sales in certain of its international markets in 2012. If it is not successful in expanding international operations in a timely and cost-effective manner, the Company's business, operating results and financial condition could be materially harmed.

IF THE COMPANY DOES NOT SUCCESSFULLY EXPAND ITS DISTRIBUTION CHANNELS AND DEVELOP AND MAINTAIN RELATIONSHIPS WITH OEMs, ITS BUSINESS WOULD BE SERIOUSLY HARMED.

To date, the Company has sold its products principally through its direct sales force, as well as through indirect sales channels, such as its OEMs, resellers and systems integrators. The Company's revenues from license fees resulting from sales through indirect channel partners were approximately 36%, 32%, and 58% of total revenues from license fees for the first nine months of fiscal years 2012, 2011 and 2010,

Edgar Filing: ACTUATE CORP - Form 10-Q

respectively. The higher ratio of license fees through indirect channel partners experienced in fiscal 2010 was primarily attributed to the IBM transaction. The Company's ability to achieve significant revenue growth in the future will depend in large part on the success of its sales force in further establishing and maintaining relationships with indirect channel partners. In particular, a significant element of the Company's strategy is to embed its technology in products offered by OEMs for resale or as a

Table of Contents

hosted application to such OEMs' customers and end-users. Xenos Group's business in the United Kingdom relies on the sale and support of third party software as a significant component of its business. The Company also intends to establish and expand its relationships with resellers and systems integrators so that such resellers and systems integrators will increasingly recommend its products to their clients. The Company's future success will depend on the ability of its indirect channel partners to sell and support its products. If the sales and implementation cycles of its indirect channel partners are lengthy or variable or its OEMs experience difficulties embedding the Company's technology into their products, or if it fails to train the sales and customer support personnel of such indirect channel partners in a timely or effective fashion, the Company's business, operating results and financial condition would be materially harmed.

Although the Company is currently investing, and plans to continue to invest, significant resources to expand and develop relationships with OEMs and resellers, it has at times experienced and continues to experience difficulty in establishing and maintaining these relationships. If the Company is unable to successfully expand this distribution channel and secure license agreements with additional OEMs and resellers on commercially reasonable terms, including significant up-front payments of minimum license fees, and extend existing license agreements with existing OEMs on commercially reasonable terms, the Company's operating results would be adversely affected. Any inability by the Company to maintain existing or establish new relationships with indirect channel partners, including systems integrators and resellers, or, if such efforts are successful, a failure of the Company's revenues to increase correspondingly with expenses incurred in pursuing such relationships, would materially harm the Company's business, operating results and financial condition.

THE COMPANY MAY NOT BE ABLE TO COMPETE SUCCESSFULLY AGAINST ITS CURRENT AND FUTURE COMPETITORS.

The Company's market is intensely competitive and characterized by rapidly changing technology, evolving standards and product releases by the Company's competitors that are marketed to compete directly with the Company's products. The Company's competition comes in five principal forms:

Competition from current or future Business Intelligence software vendors such as Information Builders, Qlik Tech, Pentaho, Jaspersoft and MicroStrategy, each of which offers reporting products;

Competition from other large software vendors such as IBM, Microsoft, Oracle and SAP, to the extent they sell Rich Information Applications, Enterprise Output Management and Performance Management as separate products or include similar functionality with their applications or databases;

Competition from other software vendors and software development tool vendors including providers of open-source software products that may develop scalable Business Intelligence, Performance Management, Enterprise Output Management and Rich Information Applications products;

Competition from the IT departments of current or potential customers that may develop scalable Business Intelligence, Performance Management, Enterprise Output Management and Rich Information Applications products internally, which may be cheaper and more customized than the Company's products; and

Competition from Eclipse BIRT. The Company expects that Eclipse BIRT, which is free, may in the short term cannibalize some smaller sales of its Business Intelligence and Rich Information Applications products.

Many of the Company's current and potential competitors have significantly greater financial, technical, marketing and other resources. These competitors may be able to respond more quickly to new or emerging technologies and changes in customer requirements or devote greater resources to the development, promotion and sales of their products than the Company. Also, most current and potential competitors have greater name recognition and the ability to leverage a significant installed customer base. These companies have released and can continue to release competing Business Intelligence, Performance Management, Enterprise Output Management and Rich Information Applications software products or significantly increase the functionality of their existing software products, either of which could result in a loss of market share for the Company. The Company expects additional competition as other established and emerging companies enter the Business Intelligence, Performance Management, Enterprise Output Management and Rich Information Applications software market and new products and technologies are introduced. Increased competition could result in price reductions, fewer customer orders, reduced gross margins, longer

Edgar Filing: ACTUATE CORP - Form 10-Q

sales cycles and loss of market share, any of which would harm the Company's business, operating results and financial condition.

Current and potential competitors may make strategic acquisitions or establish cooperative relationships among themselves or with third parties, thereby increasing their ability to address the needs of the Company's customers. Also, the Company's current or future channel partners may have established in the past, or may in the future, establish cooperative relationships with the Company's current or potential competitors, thereby limiting the Company's ability to sell its products through particular distribution channels. It is possible that new competitors or alliances among current and new competitors may emerge and rapidly gain significant market share. Such competition could reduce the Company's revenues from license fees and services from new or existing customers on terms favorable to us. If the Company is unable to compete successfully against current and future competitors, the Company's business, operating results and financial condition would be materially harmed.

Table of Contents

IF THE MARKET FOR BUSINESS INTELLIGENCE, RICH INFORMATION APPLICATIONS, ENTERPRISE OUTPUT MANAGEMENT AND PERFORMANCE MANAGEMENT SOFTWARE DOES NOT GROW AS THE COMPANY EXPECTS, ITS BUSINESS WOULD BE SERIOUSLY HARMED.

The Company cannot be certain that the market for Business Intelligence and Rich Information Applications, Enterprise Output Management and Performance Management software products will continue to grow or that, even if the market does grow, businesses will purchase the Company's products. If the market for Business Intelligence, Rich Information Applications, Enterprise Output Management and Performance Management software products declines, fails to grow or grows more slowly than the Company expects, its business, operating results and financial condition would be harmed. To date, all of the Company's revenues have been derived from licenses for its Business Intelligence, Rich Information Applications, Enterprise Output Management and Performance Management related products and services, and it expects this to continue for the foreseeable future. The Company has spent, and intends to continue to spend, considerable resources educating potential customers and indirect channel partners about Business Intelligence, Rich Information Applications, Enterprise Output Management and Performance Management software and products. However, if such expenditures do not enable its products to achieve any significant degree of market acceptance, the Company's business, operating results and financial condition would be materially harmed.

BECAUSE THE SALES CYCLES OF THE COMPANY'S PRODUCTS ARE LENGTHY AND VARIABLE, ITS QUARTERLY RESULTS MAY FLUCTUATE.

The purchase of the Company's products by its end-user customers for deployment within the customer's organization typically involves a significant commitment of capital and other resources, and is therefore subject to delays that are beyond the Company's control. These delays can arise from a customer's internal procedures to approve large capital expenditures, budgetary constraints, the testing and acceptance of new technologies that affect key operations and general economic and political events. The sales cycle for initial orders and larger follow-on orders for the Company's products can be lengthy and variable. Additionally, sales cycles for sales of the Company's products to OEMs tend to be longer, ranging from 6 to 24 months or more, and may involve convincing the OEMs' entire organization that the Company's products are the appropriate software for their applications. This time period does not include the sales and implementation cycles of such OEMs' own products, which can be longer than the Company's sales and implementation cycles. Certain of the Company's customers have in the past, or may in the future, experience difficulty completing the initial implementation of the Company's products. Any difficulties or delays in the initial implementation by the Company's end-user customers or indirect channel partners could cause such customers or partners to reject the Company's software or lead to the delay or non-receipt of future orders for the large-scale deployment of its products, in which case the Company's business, operating results and financial condition would be materially harmed.

ADVANCES IN HARDWARE AND SOFTWARE TECHNOLOGY MAY CAUSE OUR SOFTWARE REVENUE TO DECLINE.

In the past, the Company has licensed software for a certain number of processors or CPUs to many of its customers. Advances in hardware technology, including, but not limited to, greater CPU clock speeds, multiple-core processors and virtualization, have afforded software performance gains to some customers, causing them to defer additional software purchases from the Company. The occurrence of any of these events, and other future advances, could seriously harm the Company's business, operating results and financial condition. Use of the Company's software on more advanced hardware than the hardware on which the software was originally installed, without payment of a fee, is prohibited by the terms of applicable license agreements or Company policies. The Company intends to require compliance with such terms. As a result of its enforcement efforts, customers may defer or cease purchasing additional software or maintenance and support. The occurrence of any of these events could materially harm the Company's business, operating results and financial condition.

DECLINING RENEWAL OF MAINTENANCE SERVICES ON OUR OLDER SOFTWARE SALES PRODUCTS

The Company has historically experienced a high maintenance renewal rate across its various product lines. However, the Company is currently transitioning from its legacy e.Reports product suite, to a new BIRT based product offering. As its legacy products age, the Company expects to experience higher than normal decline rates. In the meantime, BIRT is expected to become the dominant contributor to license and maintenance revenues. As this transition progresses the Company expects to see its maintenance renewal rate and maintenance revenues improve. If this transition does not materialize, the Company's business, operating results and financial condition could be materially harmed.

Table of Contents

IF THE COMPANY IS UNABLE TO FAVORABLY ASSESS THE EFFECTIVENESS OF ITS INTERNAL CONTROL OVER FINANCIAL REPORTING IN FUTURE PERIODS OR IF THE COMPANY'S INDEPENDENT AUDITORS ARE UNABLE TO PROVIDE AN UNQUALIFIED ATTESTATION REPORT ON SUCH ASSESSMENT, THE COMPANY'S STOCK PRICE COULD BE ADVERSELY AFFECTED.

Pursuant to Section 404 of the Sarbanes-Oxley Act of 2002 (Section 404), the Company's management is required to report on, and its independent auditors are required to attest to, the effectiveness of the Company's internal controls over financial reporting on an annual basis. The Company's assessment, testing and evaluation of the design and operating effectiveness of its internal control over financial reporting are ongoing. The Company cannot predict the outcome of its testing in future periods. If in future periods the Company concludes that its internal control over financial reporting is not effective, it may be required to change its internal control over financial reporting to remediate deficiencies, and investors may lose confidence in the reliability of its financial statements, causing the Company's stock price to decline significantly.

SECTION 404 AND REGULATORY CHANGES HAVE CAUSED THE COMPANY TO INCUR INCREASED COSTS AND OPERATING EXPENSES, INCLUDING ADDITIONAL COST AND EXPENSES ASSOCIATED WITH HIRING QUALIFIED PERSONNEL TO COMPLY WITH SUCH REGULATORY REQUIREMENT.

The Sarbanes-Oxley Act of 2002 and regulatory changes by the SEC and Nasdaq have caused the Company to incur significant increased costs. In particular, the rules governing the standards that must be met for management to assess its internal controls over financial reporting under Section 404 are complex, and require significant documentation, testing and possible remediation. This ongoing process of reviewing, documenting and testing the Company's internal controls over financial reporting has resulted in, and will likely continue to result in ongoing cost to the Company. Furthermore, achieving and maintaining compliance with Sarbanes-Oxley and other new rules and regulations has and will continue to require the Company to hire additional personnel and to use additional outside legal, accounting and advisory services.

In addition, any acquisitions made by the Company will also put a significant strain on its management, information systems and resources. Any expansion of the Company's international operations will lead to increased financial and administrative demands associated with managing its international operations and managing an increasing number of relationships with foreign partners and customers and expanded treasury functions to manage foreign currency risks, all of which will require the Company to incur additional cost to implement necessary changes to maintain effective internal controls over financial reporting.

IF THE COMPANY DOES NOT RESPOND TO RAPID TECHNOLOGICAL CHANGES, ITS PRODUCTS COULD BECOME OBSOLETE.

The market for the Company's products is characterized by rapid technological changes, frequent new product introductions and enhancements, changing customer demands, and evolving industry standards. Any of these factors can render existing products obsolete and unmarketable. The Company believes that its future success will depend in large part on its ability to support current and future releases of popular operating systems and computer programming languages, databases and software applications, to timely develop new products that achieve market acceptance and to meet an expanding range of customer requirements. If the announcement or introduction of new products by the Company or its competitors or any change in industry standards causes customers to defer or cancel purchases of existing products, the Company's business, operating results and financial condition would be harmed.

As a result of the complexities inherent in Business Intelligence, Rich Information Applications, Enterprise Output Management and Performance Management software, major new products and product enhancements can require long development and testing periods. In addition, customers may delay their purchasing decisions in anticipation of the general availability of new or enhanced versions of the Company's products. As a result, significant delays in the general availability of such new releases or significant problems in the installation or implementation of such new releases could harm the Company's business, operating results and financial condition. If the Company fails to successfully develop, on a timely and cost effective basis, product enhancements or new products that respond to technological change, evolving industry standards or customer requirements or such new products and product enhancements fail to achieve market acceptance, the Company's business, operating results and financial condition would be harmed.

IF THE COMPANY DOES NOT RELEASE NEW PRODUCTS AND ENHANCEMENTS TO EXISTING PRODUCTS IN A TIMELY MANNER OR IF SUCH NEW PRODUCTS AND ENHANCEMENTS, INCLUDING THE COMPANY'S OPEN SOURCE PROJECT, FAIL TO ACHIEVE MARKET ACCEPTANCE, THE COMPANY'S BUSINESS COULD BE SERIOUSLY HARMED.

The Company believes that its future success will depend in large part on the success of new products and enhancements to its products that it makes generally available. Prior to the release of any new products or enhancements, the products must undergo a long development and testing

Edgar Filing: ACTUATE CORP - Form 10-Q

period. To date, the development and testing of new products and enhancements have taken longer than expected. In the event the development and testing of new products and enhancements continue to take longer than expected, the

Table of Contents

release of new products and enhancements will be delayed. If the Company fails to release new products and enhancements in a timely manner, its business, operating results and financial condition would be harmed. In addition, if such new products and enhancements do not achieve market acceptance, the Company's business, operating results and financial condition would be harmed.

The Company has developed a BIRT open source product through its involvement in the Eclipse Foundation. The Company hopes that BIRT and a commercial version of BIRT will be widely adopted by Java developers and will result in such developers recommending to their employees and customers that they license the Company's commercially available products. If BIRT does not achieve market acceptance and result in promoting sales of commercial products, the Company's business, operating results and financial condition may be harmed.

THE SUCCESS OF THE COMPANY'S OPEN-SOURCE BIRT INITIATIVE IS DEPENDENT ON BUILDING A DEVELOPER COMMUNITY AROUND BIRT.

The success of the Company's BIRT initiative is dependent on the open source contributions of third-party programmers and corporations, and if they cease to make these contributions to the Eclipse open source project, the BIRT project, or the general open source movement, the Company's BIRT product strategy could be adversely affected. If key members, or a significant percentage, of this group of developers or corporations decides to cease development of Eclipse, BIRT or other open source applications, the Company would have to either rely on another party (or parties) to develop these technologies, develop them itself or adapt its open source product strategy accordingly. This could increase the Company's development expenses, delay its product releases and upgrades or adversely impact customer acceptance of open source offerings.

IF SECURITY MEASURES REGARDING OUR BIRT ONDEMAND AND PERFORMANCE MANAGEMENT ONDEMAND SERVICES ARE BREACHED AND UNAUTHORIZED ACCESS IS OBTAINED TO A CUSTOMER'S DATA OR OUR DATA OR OUR INFORMATION TECHNOLOGY SYSTEMS, WE MAY INCUR SIGNIFICANT LEGAL AND FINANCIAL EXPOSURE AND LIABILITIES.

Our BIRT onDemand and Performance Management onDemand services involve the storage and transmission of customers' proprietary information, and security breaches could expose us to a risk of loss of this information, litigation and possible liability. These security measures may be breached as a result of third-party action, including intentional misconduct by computer hackers, employee error, malfeasance or otherwise, during transfer of data to additional data centers or at any time, and result in someone obtaining unauthorized access to our customers data or our data, including our intellectual property and other confidential business information, or our information technology systems. Additionally, third parties may attempt to fraudulently induce employees or customers into disclosing sensitive information such as user names, passwords or other information in order to gain access to our customers' data or our data, including our intellectual property and other confidential business information, or our information technology systems. Because the techniques used to obtain unauthorized access, or to sabotage systems, change frequently and generally are not recognized until launched against a target, we may be unable to anticipate these techniques or to implement adequate preventative measures. Any security breach could lead to legal liability.

FROM TIME TO TIME, WE MAY BE INVOLVED IN LEGAL PROCEEDINGS ABOUT WHICH WE ARE UNABLE TO ASSESS OUR EXPOSURE AND WHICH COULD BECOME SIGNIFICANT LIABILITIES UPON JUDGMENT.

We are involved in legal proceedings from time to time. Companies in our industry have been subject to claims related to patent infringement, as well as contract and employment-related claims. At times, including now, we are also plaintiffs in litigation involving the Company's intellectual property. We may not be able to accurately assess risk related to these suits including expenses and other potential liabilities.

THE COMPANY'S INTERNATIONAL OPERATIONS ARE SUBJECT TO SIGNIFICANT RISKS.

A substantial portion of the Company's revenues are derived from international sales. International operations and sales are subject to a number of risks, any of which could harm the Company's business, operating results and financial conditions. These risks include the following:

Economic and political volatility and instability, including world-wide or regional recessions, war and terrorism or the threat of war and terrorism;

Difficulty of managing an organization spread across many countries;

Multiple and conflicting tax laws and regulations;

Costs of localizing products for foreign countries;

Difficulty in hiring employees and difficulties and high costs associated with terminating employees and restructuring operations in foreign countries;

Trade laws and business practices favoring local competition;

Table of Contents

Dependence on local vendors;

Increasing dependence on resellers in certain geographies;

Compliance with multiple, conflicting and changing government laws and regulations;

Weaker intellectual property protection in foreign countries and potential loss of proprietary information due to piracy or misappropriation;

Longer sales cycles;

Import and export restrictions and tariffs;

Difficulties in staffing and managing foreign operations;

The significant presence of some of our competitors in certain international markets;

Greater difficulty or delay in accounts receivable collection; and

Foreign currency exchange rate fluctuations.

The Company hopes that, over time, an increasing portion of its revenues and costs will be denominated in foreign currencies. To the extent such denomination in foreign currencies does occur, gains and losses on the conversion to U.S. dollars of accounts receivable, accounts payable and other monetary assets and liabilities arising from international operations may contribute to fluctuations in the Company's results of operations. Although the Company may in the future decide to undertake foreign exchange hedging transactions to cover a portion of its foreign currency transaction exposure, it currently does not attempt to cover any foreign currency exposure. If it is not effective in any future foreign exchange hedging transactions in which it engages, the Company's business, operating results and financial condition could be materially harmed.

THE COMPANY'S EXECUTIVE OFFICERS AND CERTAIN KEY PERSONNEL ARE CRITICAL TO ITS BUSINESS AND IT MAY NOT BE ABLE TO RECRUIT AND RETAIN THE PERSONNEL IT NEEDS.

The Company's future success depends upon the continued service of its executive officers and other key engineering, sales, marketing and customer support personnel. None of its executive officers or key employees is bound by an employment agreement for any specific term. If the Company loses the service of one or more of its executive officers or key employees, or if one or more of its executive officers or key employees decide to join a competitor or otherwise compete directly or indirectly with it, it could have a significant adverse effect on the Company's business.

In addition, because experienced personnel in the Company's industry are in high demand and competition for their talents is intense, the Company has relied on its ability to grant stock options as one mechanism for recruiting and retaining this highly skilled talent. Accounting standards require the expensing of stock options, which impairs the Company's ability to provide these incentives without incurring significant compensation costs. There can be no assurance that the Company will continue to successfully attract and retain key personnel in the future.

CHANGES IN ACCOUNTING PRINCIPLES OR STANDARDS, OR IN THE WAY THEY ARE APPLIED, COULD RESULT IN UNFAVORABLE ACCOUNTING CHARGES OR EFFECTS AND UNEXPECTED FINANCIAL REPORTING FLUCTUATIONS, AND COULD ADVERSELY AFFECT OUR REPORTED OPERATING RESULTS.

Edgar Filing: ACTUATE CORP - Form 10-Q

We prepare our consolidated financial statements in conformity with U.S. Generally Accepted Accounting Principles (GAAP). These principles are subject to interpretation by the SEC and various bodies formed to interpret and create appropriate accounting principles and guidance. A change in existing principles or guidance can have a significant effect on our reported results and may retroactively affect previously reported results. Additionally, proposed accounting standards could have a significant impact on our operational processes, revenues and expenses, and could cause unexpected financial reporting fluctuations.

For example, the Financial Accounting Standards Board (FASB) is currently working together with the International Accounting Standards Board (IASB) to converge certain accounting principles and facilitate more comparable financial reporting between companies who are required to follow GAAP and those who are required to follow International Financial Reporting Standards (IFRS). These efforts may result in different accounting principles under GAAP, which may have a material impact on the way in which we report financial results in areas including, but not limited to, revenue recognition, lease accounting, and financial statement presentation. We expect the SEC to make a determination in the near future regarding the incorporation of IFRS into the financial reporting system for U.S. companies. A change in accounting principles from GAAP to IFRS may have a material impact on our financial statements and may retroactively adversely affect previously reported transactions.

Table of Contents

THE COMPANY MAY BE UNABLE TO SUSTAIN OR INCREASE ITS PROFITABILITY.

While the Company was profitable in its last eight fiscal years, it incurred net losses during fiscal year 2003 and 2002. Its ability to sustain or increase profitability on a quarterly or annual basis will be affected by changes in its business. It expects its operating expenses to increase as its business grows, and it anticipates that it will make investments in its business. Therefore, the Company's results of operations will be harmed if its revenues do not increase at a rate equal to or greater than increases in its expenses or are insufficient for it to sustain profitability.

IF THE COMPANY OVERESTIMATES REVENUES, IT MAY BE UNABLE TO REDUCE ITS EXPENSES TO AVOID OR MINIMIZE A NEGATIVE IMPACT ON ITS RESULTS OF OPERATIONS.

The Company's revenues are difficult to forecast and are likely to fluctuate significantly from period to period. The Company bases its operating expense budgets on expected revenue trends. The Company's estimates of sales trends may not correlate with actual revenues in a particular quarter or over a longer period of time. Variations in the rate and timing of conversion of the Company's sales prospects into actual licensing revenues could cause it to plan or budget inaccurately and those variations could adversely affect the Company's financial results. In particular, delays, reductions in amount or cancellation of customers' purchases would adversely affect the overall level and timing of the Company's revenues and its business, results of operations and financial condition could be harmed. In addition, many of its expenses, such as office and equipment leases and certain personnel costs, are relatively fixed. It may be unable to adjust spending quickly enough to offset any unexpected revenue shortfall. Accordingly, any shortfall in revenue may cause a material variation in operating results in any period.

IF THE COMPANY'S PRODUCTS CONTAIN MATERIAL DEFECTS, ITS REVENUES MAY DECLINE.

Software products as complex as those offered by the Company often contain errors or defects, particularly when first introduced, when new versions or enhancements are released and when configured to individual customer computing systems. The Company currently has known errors and defects in its products. Despite testing conducted by the Company, if additional defects and errors are found in current versions, new versions or enhancements of its products after commencement of commercial shipment, or if such errors or defects cannot be cured or repaired timely, it could result in the loss of revenues or a delay in market acceptance or an increase in the rate of return of the Company's products. The occurrence of any of these events could materially harm the Company's business, operating results and financial condition.

THE COMPANY MAY BE SUBJECT TO PRODUCT LIABILITY CLAIMS.

Although license agreements with its customers typically contain provisions designed to limit the Company's exposure to potential product liability claims, it is possible that such limitation of liability provisions may not be effective as a result of existing or future laws or unfavorable judicial decisions. The sale and support of the Company's products may entail the risk of such claims, which are likely to be substantial in light of the use of its products in business-critical applications. A product liability claim brought against the Company could materially harm its business, operating results and financial condition.

THE PROTECTION OF OUR PROPRIETARY RIGHTS MAY BE INADEQUATE.

The Company has a small number of issued and pending U.S. patents expiring at varying times ranging from 2015 to 2024. The Company relies primarily on a combination of copyright and trademark laws, trade secrets, confidentiality procedures, contractual provisions and license keys to protect its proprietary technology. For example, the Company licenses its software pursuant to click-wrap or signed license agreements that impose certain restrictions on licensees' ability to utilize the software. In addition, the Company seeks to avoid disclosure of its intellectual property, including by requiring those persons with access to its proprietary information to execute confidentiality agreements with the Company and by restricting access to its source code. The Company takes precautions to protect our software, certain documentation, and other written materials under trade secret and copyright laws, which afford only limited protection.

Despite the Company's efforts to protect its proprietary rights, unauthorized parties may attempt to copy aspects of its products or to obtain and use information that the Company regards as proprietary. Policing unauthorized use of the Company's products is difficult, and while it is unable to determine the extent to which piracy of its software products exists, software piracy can be expected to be a persistent problem. In addition, the laws of many countries do not protect the Company's proprietary rights to the same extent as the laws of the United States. If the Company's means of protecting its proprietary rights is not adequate or its competitors independently develop similar technology, the Company's business could be materially harmed.

Table of Contents

IF SECURITIES OR INDUSTRY ANALYSTS DO NOT PUBLISH RESEARCH OR REPORTS OR PUBLISH UNFAVORABLE RESEARCH OR REPORTS ABOUT OUR BUSINESS, OUR STOCK PRICE AND TRADING VOLUME COULD DECLINE.

The trading market for our common stock will be influenced by the research and reports that securities or industry analysts may publish about us, our business, our market or our competitors. If any of the analysts who may cover us adversely change their recommendation regarding our stock, or provide more favorable relative recommendations about our competitors, our stock price would likely decline. If any analyst who may cover us were to cease coverage of our company or fail to regularly publish reports on us, interest in our stock could decrease, which could cause our stock price or trading volume to decline.

THE COMPANY'S COMMON STOCK PRICE MAY BE VOLATILE, WHICH COULD RESULT IN SUBSTANTIAL LOSSES FOR STOCKHOLDERS.

The market price of shares of the Company's common stock has been and is likely to continue to be highly volatile and may be significantly affected by factors such as the following:

Actual or anticipated fluctuations in its operating results;

Changes in the economic and political conditions in the United States and abroad;

Terrorist attacks, war or the threat of terrorist attacks and war;

The announcement of mergers or acquisitions by the Company or its competitors;

Developments in ongoing or threatened litigation;

Announcements of technological innovations;

Failure to comply with the requirements of Section 404 of the Sarbanes-Oxley Act;

New products, including open source products, or new contracts announced by it or its competitors;

Developments with respect to copyrights or proprietary rights;

Price and volume fluctuations in the stock market;

Changes in corporate purchasing of Business Intelligence, Rich Information Applications and Performance Management software;

Adoption of new accounting standards affecting the software industry; and

Edgar Filing: ACTUATE CORP - Form 10-Q

Changes in financial estimates by securities analysts.

In addition, following periods of volatility in the market price of a particular company's securities, securities class action litigation has often been brought against such companies. If the Company is involved in such litigation, it could result in substantial costs and a diversion of management's attention and resources and could materially harm the Company's business, operating results and financial condition.

WE CURRENTLY DO NOT INTEND TO PAY DIVIDENDS ON OUR COMMON STOCK, AND CONSEQUENTLY, YOUR ONLY OPPORTUNITY TO ACHIEVE A RETURN ON YOUR INVESTMENT IS IF THE PRICE OF OUR COMMON STOCK APPRECIATES AND YOU SELL YOUR SHARES AT A PRICE ABOVE YOUR COST.

We currently do not intend to declare or pay dividends on shares of our common stock in the foreseeable future. Consequently, your only opportunity to achieve a return on your investment in our company will be if the market price of our common stock appreciates and you sell your shares at a price above your cost. There is no guarantee that the price of our common stock will ever exceed the price that you pay. Investors seeking cash dividends should not purchase our common stock.

CHANGES IN CORPORATE INCOME TAX LAWS, INCOME TAX RATES OR NEGATIVE INCOME TAX RULINGS COULD ADVERSELY IMPACT THE COMPANY'S FINANCIAL RESULTS.

The Company is taxable principally in the United States, Canada and certain jurisdictions in Europe and Asia/Pacific. All of these jurisdictions have in the past and may in the future make changes to their corporate income tax laws and/or corporate income tax rates, which could increase or decrease the Company's future income tax provision. While the Company believes that all material income tax liabilities are reflected properly in its Consolidated Balance Sheet, it has no assurance that it will prevail in all cases in the event the taxing authorities disagree with its interpretations of the tax law. Future levels of research and development spending will impact the Company's entitlement to related tax credits, which generally lower its effective income tax rate. Future effective income tax rates could be adversely affected if tax laws are enacted that are targeted to eliminate the benefits of the Company's tax structure and if its earnings are lower than anticipated in jurisdictions where the Company has statutory tax rates lower than tax rates in the United States or other higher tax jurisdictions.

Table of Contents***CERTAIN OF THE COMPANY'S CHARTER PROVISIONS AND DELAWARE LAW MAY PREVENT OR DETER A CHANGE IN CONTROL OF THE COMPANY.***

The Company's Certificate of Incorporation, as amended and restated (the "Certificate of Incorporation"), and Bylaws, as amended and restated ("Bylaws"), contain certain provisions that may have the effect of discouraging, delaying or preventing a change in control of the Company or unsolicited acquisition proposals that a stockholder might consider favorable, including provisions authorizing the issuance of blank check preferred stock, eliminating the ability of stockholder to act by written consent and requiring stockholders to provide advance notice for proposals and nomination of directors at the Annual Meeting of Stockholder. In addition, certain provisions of Delaware law and the Company's stock option plans may also have the effect of discouraging, delaying or preventing a change in control or unsolicited acquisition proposals. The Company has also entered into change of control agreements with its executive officers, which agreements require payment to an executive upon termination of employment within 12 months after acquisition. The anti-takeover effect of these provisions may also have an adverse effect on the public trading price of the Company's common stock.

DEPENDENCE ON THE FINANCIAL SERVICES INDUSTRY COULD SIGNIFICANTLY AFFECT THE COMPANY'S REVENUES.

A significant portion of the Company's revenues are derived from customers in the financial services industry and the Company expects it will continue to derive a significant portion of its revenues from these customers for the foreseeable future. Accordingly, unfavorable economic conditions adversely impacting the financial services industry has had a material adverse effect on the Company's business, financial condition and results of operations. For example, the financial services industry has experienced and may continue to experience cyclical fluctuations in profitability, which may affect timing of, or actual purchases of, the Company's products which would have a material adverse effect on the Company's business, financial condition and results of operations.

CATASTROPHIC EVENTS MAY DISRUPT OUR BUSINESS.

We rely on our network infrastructure and enterprise applications, internal technology systems and our Website for our development, marketing, operational, support, hosted services and sales activities. A disruption, infiltration or failure of these systems in the event of a major earthquake, fire, power loss, telecommunications failure, software or hardware malfunctions, cyber attack, war, terrorist attack, or other catastrophic event could cause system interruptions, reputational harm, loss of intellectual property, delays in our product development, lengthy interruptions in our services, breaches of data security and loss of critical data and could prevent us from fulfilling our customers' orders. Our corporate headquarters, a significant portion of our research and development activities, certain of our data centers, and certain other critical business operations are located in the San Francisco Bay Area, which is near major earthquake faults. We have developed certain disaster recovery plans and certain backup systems to reduce the potentially adverse effect of such events, but a catastrophic event that results in the destruction or disruption of any of our data centers or our critical business or information technology systems could severely affect our ability to conduct normal business operations and, as a result, our future operating results could be adversely affected.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

The table below sets forth information regarding repurchases of Actuate common stock by Actuate during the three months ended September 30, 2012.

Issuer Purchases of Equity Securities

| Period | Total Number of Shares Purchased | Average price paid per share | Total number of shares purchased as part of publicly announced programs (1) | Maximum dollar value of shares that may yet be purchased under the program (1) |
|--|----------------------------------|------------------------------|---|--|
| <u>Month #1</u> | | | | |
| July 1, 2012 through July 31, 2012 | | \$ | | |
| <u>Month #2</u> | | | | |
| August 1, 2012 through August 31, 2012 | 577,642 | \$ 6.90 | 577,642 | |
| <u>Month #3</u> | | | | |

Edgar Filing: ACTUATE CORP - Form 10-Q

| | | | | |
|--|----------------|----------------|----------------|----------------------|
| September 1, 2012 through September 30, 2012 | 285,100 | \$ 7.10 | 285,100 | |
| Total | 862,742 | \$ 6.95 | 862,742 | \$ 24,000,000 |

- (1) The Company's stock repurchase program was originally announced in September 2001 and has been extended from time to time by Actuate's Board of Directors.

Table of Contents

On August 2, 2012, the Board of Directors approved an ongoing extension of the Company's share repurchase program. This extension authorized management to make additional repurchases of Actuate common stock up to an aggregate of \$30 million. The share repurchase authorization does not have an expiration date and the pace and timing of repurchases will depend on factors such as cash generation from operations, the volume of employee stock plan activity, cash requirements for acquisitions, economic and market conditions, stock price and legal and regulatory requirements.

These repurchased shares were recorded as treasury stock and were accounted for under the cost method. No repurchased shares have been retired.

Item 6. Exhibits

- 31.1 Rule 13a-14(a)/15d-14(a) Certification of the Chief Executive Officer
- 31.2 Rule 13a-14(a)/15d-14(a) Certification of the Chief Financial Officer
- 32.1 Section 1350 Certifications
- 101 The following materials from the Quarterly Report on Form 10-Q of Actuate Corporation for the quarter ended June 30, 2012, formatted in XBRL (eXtensible Business Reporting Language); (i) Condensed Consolidated Balance Sheets, (ii) Condensed Consolidated Statements of Income, (iii) Condensed Consolidated Statements of Cash Flows, (iv) Condensed Consolidated Statements of Comprehensive Income, and (v) Notes to Consolidated Financial Statements*.

* Pursuant to Rule 406T of Regulation S-T, these interactive data files are furnished and not filed or a part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, as amended; are deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, as amended; and otherwise are not subject to liability under these sections.

Table of Contents

Signature

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

Actuate Corporation

(Registrant)

Dated: November 7, 2012

By:

/s/ DANIEL A. GAUDREAU

Daniel A. Gaudreau
Senior Vice President,

Operations and Chief Financial Officer

(Principal Financial and Accounting Officer)