

CHORDIANT SOFTWARE INC
Form 10-Q
May 06, 2008

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 March 31, 2008

OR

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

For the transition period from _____ to _____

Commission File Number 000-29357

Chordiant Software, Inc.
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

93-1051328
(I.R.S. Employer
Identification No.)

20400 Stevens Creek Boulevard, Suite 400
Cupertino, CA 95014
(Address of principal executive offices) (Zip Code)

(408) 517-6100
(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year if changed since last report)

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 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):

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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

As of April 30, 2008, there were 30,043,988 shares of the registrant's common stock outstanding.

Table of Contents

CHORDIANT SOFTWARE, INC.
 QUARTERLY REPORT ON FORM 10-Q FOR THE PERIOD ENDED MARCH 31, 2008
 TABLE OF CONTENTS

		Page No.
PART I. FINANCIAL INFORMATION		
Item 1.	<u>Financial Statements (Unaudited)</u>	3
	<u>Condensed Consolidated Balance Sheets as of March 31, 2008 and September 30, 2007</u>	3
	<u>Condensed Consolidated Statements of Operations for the Three and Six Months Ended March 31, 2008 and 2007</u>	4
	<u>Condensed Consolidated Statements of Cash Flows for the Six Months Ended March 31, 2008 and 2007</u>	5
	<u>Notes to Condensed Consolidated Financial Statements</u>	6
Item 2.	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	27
Item 3.	<u>Quantitative and Qualitative Disclosures about Market Risk</u>	43
Item 4.	<u>Controls and Procedures</u>	44
PART II. OTHER INFORMATION		
Item 1.	<u>Legal Proceedings</u>	45
Item 1A.	<u>Risk Factors</u>	45
Item 2.	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	55
Item 4.	<u>Submission of Matters to a Vote of Security Holders</u>	56
Item 5.	<u>Other Information</u>	57
Item 6.	<u>Exhibits</u>	58
	<u>Signatures</u>	58

Table of Contents

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)

CHORDIANT SOFTWARE, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except per share data)
(Unaudited)

	March 31, 2008	September 30, 2007
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 68,956	\$ 77,987
Marketable securities	751	12,159
Accounts receivable, net including \$255 due from related parties at September 31, 2007	25,883	27,381
Prepaid expenses and other current assets	7,617	5,352
Total current assets	103,207	122,879
Property and equipment, net	3,751	3,638
Goodwill	32,044	32,044
Intangible assets, net	2,120	2,725
Other assets	2,451	3,529
Total assets	\$ 143,573	\$ 164,815
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 9,174	\$ 8,080
Accrued expenses	11,031	13,804
Deferred revenue, including related party balances of nil and \$116 at March 31, 2008 and September 30, 2007, respectively	38,213	44,548
Total current liabilities	58,418	66,432
Deferred revenue—long-term	16,925	23,434
Restructuring costs, net of current portion	733	942
Other long-term liabilities	894	646
Total liabilities	76,970	91,454
Commitments and contingencies (Notes 8, 9 and 10)		
Stockholders' equity:		
Preferred stock, \$0.001 par value; 51,000 shares authorized; none issued and outstanding at March 31, 2008 and September 30, 2007	—	—
Common stock, \$0.001 par value; 300,000 shares authorized; 31,866 and 33,221 shares issued and outstanding at March 31, 2008 and September 30, 2007, respectively	32	33
Additional paid-in capital	289,138	295,650
Accumulated deficit	(227,869)	(226,915)

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Accumulated other comprehensive income	5,302	4,593
Total stockholders' equity	66,603	73,361
Total liabilities and stockholders' equity	\$ 143,573	\$ 164,815

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

3

Table of Contents

CHORDIANT SOFTWARE, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)
(Unaudited)

	Three Months Ended March 31,		Six Months Ended March 31,	
	2008	2007	2008	2007
Revenues:				
License	\$ 4,807	\$ 18,882	\$ 13,614	\$ 26,044
Service, including related party items aggregating \$52 and \$61 for the three months ended March 31, 2008 and 2007, respectively, and \$116 and \$124 for the six months ended March 31, 2008 and 2007, respectively	19,909	13,883	40,236	29,660
Total revenues	24,716	32,765	53,850	55,704
Cost of revenues:				
License	283	583	617	1,037
Service	8,532	5,622	17,010	13,088
Amortization of intangible assets	303	303	606	606
Total cost of revenues	9,118	6,508	18,233	14,731
Gross profit	15,598	26,257	35,617	40,973
Operating expenses:				
Sales and marketing	7,400	8,314	16,303	15,578
Research and development	6,381	7,296	13,106	13,592
General and administrative	4,019	5,295	9,022	10,906
Restructuring expense	—	255	—	6,727
Total operating expenses	17,800	21,160	38,431	46,803
Income (loss) from operations	(2,202)	5,097	(2,814)	(5,830)
Interest income, net	613	492	1,448	796
Other income, net	350	180	485	165
Income (loss) before income taxes	(1,239)	5,769	(881)	(4,869)
Provision for (benefit from) income taxes	(80)	794	73	905
Net income (loss)	\$ (1,159)	\$ 4,975	\$ (954)	\$ (5,774)
Net income (loss) per share:				
Basic	\$ (0.04)	\$ 0.15	\$ (0.03)	\$ (0.18)
Diluted	\$ (0.04)	\$ 0.15	\$ (0.03)	\$ (0.18)
Weighted average shares used in computing net income (loss) per share:				
Basic	33,066	32,153	33,181	31,939
Diluted	33,066	33,216	33,181	31,939

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

Table of Contents

CHORDIANT SOFTWARE, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Six Months Ended March 31,	
	2008	2007
Cash flows from operating activities:		
Net loss	\$ (954)	\$ (5,774)
Adjustments to reconcile net loss to net cash provided by (used for) operating activities:		
Depreciation and amortization	864	724
Amortization of intangibles and capitalized software	1,140	1,056
Non-cash stock-based compensation expense	2,157	1,869
Provision for doubtful accounts and sales returns	175	78
Loss on disposal of assets	—	663
Realized gain on sale of marketable securities	(8)	—
Accretion of discounts on marketable securities	(51)	—
Other non-cash charges	—	445
Changes in assets and liabilities:		
Accounts receivable	1,856	(9,331)
Prepaid expenses and other current assets	(2,047)	(4,357)
Other assets	702	780
Accounts payable	1,067	(539)
Accrued expenses, other long-term liabilities and restructuring	(4,076)	2,992
Deferred revenue	(13,430)	34,864
Net cash provided by (used for) operating activities	(12,605)	23,470
Cash flows from investing activities:		
Purchases of property, equipment, and leasehold improvements	(950)	(1,506)
Capitalized product development costs	(111)	—
Proceeds from release of (increase in) restricted cash	(3)	167
Purchases of marketable securities and short-term investments	(5,099)	—
Proceeds from maturities of marketable securities and short-term investments	16,566	—
Net cash provided by (used for) investing activities	10,403	(1,339)
Cash flows from financing activities:		
Proceeds from exercise of stock options	614	3,235
Payment on capital leases	—	(96)
Excess tax benefits from stock-based compensation	17	—
Repurchase of common stock	(8,086)	—
Net cash provided by (used for) financing activities	(7,455)	3,139
Effect of exchange rate changes	626	773
Net increase (decrease) in cash and cash equivalents	(9,031)	26,043
Cash and cash equivalents at beginning of period	77,987	45,278
Cash and cash equivalents at end of period	\$ 68,956	\$ 71,321

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 1—THE COMPANY

Chordiant Software, Inc., or the Company, or Chordiant is an enterprise software vendor that offers software solutions for global business-to-consumer companies that seek to improve the quality of their customer interactions and to reduce costs through increased employee productivity and process efficiencies. The Company concentrates on serving global customers in banking, insurance, healthcare, communications, retail and other consumer direct industries.

NOTE 2—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying Condensed Consolidated Financial Statements have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission, or SEC. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to such rules and regulations. The September 30, 2007 Condensed Consolidated Balance Sheet was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States. However, the Company believes that the disclosures are adequate to make the information presented not misleading. These unaudited Condensed Consolidated Financial Statements should be read in conjunction with the audited Consolidated Financial Statements and related Notes included in the Company's Annual Report on Form 10-K for the year ended September 30, 2007, or 2007 Form 10-K, filed with the SEC.

All adjustments, consisting of only normal recurring adjustments, which in the opinion of management, are necessary to state fairly the financial position, results of operations and cash flows for the interim periods presented have been made. The results of operations for interim periods are not necessarily indicative of the results expected for the full fiscal year or for any future period.

Reclassifications

Certain reclassifications have been made to prior period balances to conform to the current period's presentation.

Principles of Consolidation

The accompanying unaudited Condensed Consolidated Financial Statements include the accounts of the Company and its wholly-owned subsidiaries. All significant intercompany transactions and balances have been eliminated in consolidation.

Use of estimates

The preparation of Condensed Consolidated Financial Statements in conformity with accounting principles generally accepted in the United States of America requires the Company to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods.

On an on-going basis, the Company evaluates the estimates, including those related to the allowance for doubtful accounts, valuation of stock-based compensation, valuation of goodwill and intangible assets, valuation of deferred tax assets, restructuring expenses, contingencies, Vendor Specific Objective Evidence, or VSOE, of fair value in multiple element arrangements and the estimates associated with the percentage-of-completion method of accounting for certain of our revenue contracts. The Company bases these estimates on historical experience and on various other assumptions that are believed to be reasonable. Actual results may differ from these estimates under different assumptions or conditions.

Revenue recognition

The Company derives revenue from licensing software and related services, which include assistance in implementation, customization and integration, post-contract customer support, or PCS, training and consulting. All revenue amounts are presented net of sales taxes in the Company's Condensed Consolidated Statements of Operations. The amount and timing of revenue is difficult to predict and any shortfall in revenue or delay in recognizing revenue could cause operating results to vary significantly from period to period and could result in operating losses. The accounting rules related to revenue recognition are complex and are affected by the interpretation of the rules and an understanding of industry practices, both of which are subject to change. Consequently, the revenue recognition accounting rules require management to make significant estimates based on judgment.

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

Software license revenue is recognized in accordance with the AICPA's Statement of Position No. 97-2 "Software Revenue Recognition," as amended by Statement of Position No. 98-9 "Software Revenue Recognition with Respect to Certain Arrangements" (collectively "SOP 97-2").

For arrangements with multiple elements, the Company recognizes revenue for services and post-contract customer support based upon the fair value VSOE of the respective elements. The fair value VSOE of the services element is based upon the standard hourly rates charged for the services when such services are sold separately. The fair value VSOE for annual post-contract customer support is generally established with the contractual future renewal rates included in the contracts, when the renewal rate is substantive and consistent with the fees when support services are sold separately. When contracts contain multiple elements and fair value VSOE exists for all undelivered elements, the Company accounts for the delivered elements, principally the license portion, based upon the "residual method" as prescribed by SOP 97-2. In multiple element transactions where VSOE is not established for an undelivered element, revenue is recognized upon the establishment of VSOE for that element or when the element is delivered.

At the time a transaction is entered into, the Company assesses whether any services included within the arrangement relate to significant implementation or customization essential to the functionality of our products. For contracts for products that do not involve significant implementation or customization that is essential to the product functionality, the Company recognizes license revenue when there is persuasive evidence of an arrangement, the fee is fixed or determinable, collection of the fee is probable and delivery has occurred as prescribed by SOP 97-2. For contracts that involve significant implementation or customization services essential to the functionality of our products, the license and professional consulting services revenue is recognized using either the percentage-of-completion method or the completed contract method as prescribed by Statement of Position No. 81-1, "Accounting for Performance of Construction-Type and Certain Product-Type Contracts", or SOP 81-1.

The percentage-of-completion method is applied when the Company has the ability to make reasonably dependable estimates of the total effort required for completion using labor hours incurred as the measure of progress towards completion. The progress toward completion is measured based on the "go-live" date. The "go-live" date is defined as the date the essential product functionality has been delivered or the application enters into a production environment or the point at which no significant additional Chordiant supplied professional service resources are required. Estimates are subject to revisions as the contract progresses to completion and these changes are accounted for as changes in accounting estimates when the information becomes known. Information impacting estimates obtained after the balance sheet date but before the issuance of the financial statements is used to update the estimates. Provisions for estimated contract losses, if any, are recognized in the period in which the loss becomes probable and can be reasonably estimated. When additional licenses are sold related to the original licensing agreement, revenue is recognized upon delivery if the project has reached the go-live date, or if the project has not reached the go-live date, revenue is recognized under the percentage-of-completion method. Revenue from these arrangements is classified as license and service revenue based upon the estimated fair value of each element using the residual method.

The completed contract method is applied when the Company is unable to obtain reasonably dependable estimates of the total effort required for completion. Under the completed contract method, all revenue and related costs of revenue are deferred and recognized upon completion.

For product co-development arrangements relating to software products in development prior to the consummation of the individual arrangements, where the Company retains the intellectual property being developed, and intends to sell the resulting products to other customers, license revenue is deferred until the delivery of the final product, provided

all other requirements of SOP 97-2 are met. Expenses associated with these co-development arrangements are accounted for under SFAS No. 86, "Accounting for the Costs of Computer Software to Be Sold, Leased, or Otherwise Marketed" and are normally expensed as incurred as they are considered to be research and development costs that do not qualify for capitalization or deferral.

Revenue from subscription or term license agreements, which include software and rights to unspecified future products or maintenance, is recognized ratably over the term of the subscription period. Revenue from subscription or term license agreements, which include software, but exclude rights to unspecified future products and maintenance, is recognized upon delivery of the software if all conditions of recognizing revenue have been met including that the related agreement is non-cancelable, non-refundable and provided on an unsupported basis.

For transactions involving extended payment terms, the Company deems these fees not to be fixed or determinable for revenue recognition purposes and revenue is deferred until the fees become due and payable.

For arrangements with multiple elements accounted for under SOP 97-2 where the Company determines it can account for the elements separately and the fees are not fixed or determinable due to extended payment terms, revenue is recognized in the following manner. If the undelivered element is PCS, or other services, an amount equal to the estimated value of the services to be rendered prior to the next payment becoming due is allocated to the undelivered services. The residual of the payment is allocated to the delivered elements of the arrangement.

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

For arrangements with multiple elements accounted for under SOP 81-1 where the Company determines it can account for the elements separately and the fees are not fixed or determinable due to extended payment terms, revenue is recognized in the following manner. Amounts are first allocated to the undelivered elements included in the arrangement, as payments become due or are received, the residual is allocated to the delivered elements.

Revenue for PCS is recognized ratably over the support period which ranges from one to five years.

Training and consulting services revenue is recognized as such services are performed on an hourly or daily basis for time and material contracts. For consulting services arrangements with a fixed fee, revenue is recognized on a percentage-of-completion basis.

For all sales, either a signed license agreement or a binding purchase order with an underlying master license agreement is used as evidence of an arrangement. Sales through third party systems integrators are evidenced by a master agreement governing the relationship together with binding purchase orders or order forms on a transaction-by-transaction basis. Revenues from reseller arrangements are recognized on the "sell-through" method, when the reseller reports to the Company the sale of software products to end-users. The Company's agreements with customers and resellers do not contain product return rights.

Collectibility is assessed based on a number of factors, including past transaction history with the customer and the credit-worthiness of the customer. Collateral is generally not requested from customers. If it is determined that the collection of a fee is not probable, the revenue is recognized at the time the collection becomes probable, which is generally upon the receipt of cash.

Restricted Cash

At March 31, 2008 and September 30, 2007, restricted cash included interest-bearing certificates of deposit. These restricted cash balances serve as collateral for letters of credit securing certain lease obligations. These restricted cash balances are classified in Prepaid Expenses and Other Current Assets and in Other Assets in the Condensed Consolidated Balance Sheets. See Note 3 for restricted cash balances at each balance sheet date.

Concentrations of Credit Risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist of cash, cash equivalents, restricted cash, marketable securities and accounts receivable. To date, the Company has invested excess funds in money market accounts, commercial paper, corporate bonds, certificates-of-deposit, and marketable securities with maturities of less than one year. The Company's marketable securities are composed of investment instruments that are highly rated. As of the date of the filing of this Form 10-Q, the Company has sold all of its marketable securities, converting the funds to cash and cash equivalents.

The Company's accounts receivable are derived from sales to customers located in North America, Europe, and elsewhere in the world. The Company performs ongoing credit evaluations of customers' financial condition and, generally, requires no collateral from customers. The Company maintains an allowance for doubtful accounts when deemed necessary. The Company estimates its allowance for doubtful accounts by analyzing accounts receivable for specific risk accounts as well as providing for a general allowance amount based on historical bad debt and billing dispute percentages. The estimate considers historical bad debts, customer concentrations, customer credit-worthiness

and current economic trends. To date, bad debts have not been material and have been within management expectations.

Some of our current or prospective customers, especially those in the banking and insurance industries are in businesses that have or could have exposure, directly or indirectly, to the residential mortgage sector or homebuilder sector which has recently been facing financial difficulties. Customers that have accounted for significant revenues in the past may not generate revenues in any future period, causing our failure to obtain new significant customers or additional orders from existing customers to materially affect our operating result. The following table summarizes the revenues from customers and resellers that accounted for 10% or more of total revenues:

	Three Months Ended March 31,		Six Months Ended March 31,	
	2008	2007	2008	2007
Citicorp Credit Services, Inc.	25%	*	23%	*
Wellpoint, Inc.	11%	*	11%	*
International Business Machines ("IBM")	*	40%	10%	28%
Lloyds TSB Bank plc	*	12%	*	11%
Sky Subscribers Services Limited	*	10%	*	*

* Represents less than 10% of total revenues.

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

As previously announced, the Company agreed to license certain of its software to IBM's customers.

At March 31, 2008, Citicorp Credit Services, Inc., Akbank T.A.S., and Wellpoint, Inc. accounted for 15%, 13% and 12%, of our accounts receivable, respectively. At September 30, 2007, Wellpoint, Inc., IBM and Citicorp Credit Services, Inc. accounted for approximately 28%, 17% and 15% of our accounts receivable, respectively.

Research and Development

Software development costs are expensed as incurred until technological feasibility of the underlying software product is achieved. After technological feasibility is established, software development costs are capitalized until general availability of the product. Capitalized costs are then amortized at the greater of a straight line basis over the estimated product life, or the ratio of current revenue to total projected product revenue.

During fiscal year 2008, technological feasibility to port existing products to new platforms was established through the completion of detailed program designs. Costs aggregating \$0.1 million associated with these products have been capitalized and included in Other Assets as of March 31, 2008. These products were not available for general release as of March 31, 2008, accordingly the costs capitalized have not been amortized.

During the quarter ended September 30, 2006, technological feasibility to port an existing product to a new platform was established through the completion of a detailed program design. Costs aggregating \$0.5 million associated with this product have been capitalized and included in Other Assets as of September 30, 2007. This product was completed and became available for general release in July 2007, accordingly, the capitalized costs are being amortized using the straight-line method over the estimated economic life of the product which is 36 months. For the three and six months ended March 31, 2008, amortization expense, included in cost of revenue for licenses related to this product was both less than \$0.1 million. As of March 31, 2008, the unamortized expense was \$0.4 million.

During the quarter ended September 30, 2004, technological feasibility for an acquired banking product was established through the completion of a detailed program design. Costs aggregating \$2.7 million associated with this product have been capitalized and included in Other Assets as of September 30, 2005. During the quarter ended September 30, 2005, the product became available for general release and, accordingly, the costs capitalized commenced to be amortized. The capitalized costs are being amortized using the straight-line method over the estimated economic life of the product which is 36 months. For the three and six months ended March 31, 2008 and 2007, amortization expense, included in cost of revenue for licenses, related to this product was \$0.2 million and \$0.5 million, respectively. As of March 31, 2008, the unamortized expense was \$0.3 million.

Income Taxes

Income taxes are accounted for using an asset and liability approach, which requires the recognition of taxes payable or refundable for the current period and deferred tax liabilities and assets for the future tax consequences of events that have been recognized in our financial statements or tax returns. The measurement of current and deferred tax liabilities and assets is based on provisions of the enacted tax law; the effects of future changes in tax laws or rates are not anticipated. The measurement of deferred tax assets is reduced, if necessary, by the amount of any tax benefits that, based on available evidence, are not expected to be realized.

Effective October 1, 2007, the Company adopted Financial Accounting Standards Interpretation, No. 48 “Accounting for Uncertainty in Income Taxes — an interpretation of Financial Accounting Standards Board or FASB Statement No. 109” or FIN 48. FIN 48 prescribes a recognition threshold and measurement guidance for the financial statement reporting of uncertain tax positions taken or expected to be taken in a company’s income tax return. The application of FIN 48 is discussed in Note 11 to the Condensed Consolidated Financial Statements.

Net Income (Loss) Per Share

The Company computes net income (loss) per share in accordance with Statement of Financial Accounting Standard, or SFAS, No. 128, “Earnings per Share”, or SFAS 128. Under the provisions of SFAS 128, basic net income (loss) per share is computed by dividing the net income (loss) by the weighted average number of common shares outstanding during the period. Diluted net income (loss) per share is computed by dividing the net income (loss) for the period by the weighted average number of common and potentially dilutive shares outstanding during the period. Potentially dilutive shares, which consist of incremental shares issuable upon the exercise of stock options and unvested restricted stock (using the treasury stock method), are included in the calculation of diluted net income per share, in periods in which net income is reported, to the extent such shares are dilutive. In accordance with SFAS 123(R), unvested performance based restricted stock units are not included in the computation of earnings

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

per share as they are considered contingently issuable shares. The calculation of diluted net loss per share excludes potential common shares as their effect is anti-dilutive for the three and six months ended March 31, 2008 and six months ended March 31, 2007.

The following table sets forth the computation of basic and diluted net income (loss) per share for the periods indicated (in thousands, except for per share data):

	Three Months Ended March 31,		Six Months Ended March 31,	
	2008	2007	2008	2007
Net income (loss) available to common stockholders	\$ (1,159)	\$ 4,975	\$ (954)	\$ (5,774)
Denominator:				
Weighted average common stock outstanding	33,137	32,276	33,252	32,102
Common stock subject to repurchase	(71)	(123)	(71)	(163)
Denominator for basic calculation	33,066	32,153	33,181	31,939
Effect of dilutive potential common shares	—(*)	984	—(*)	—(*)
Effect of dilutive common stock subject to repurchase	—(*)	79	—(*)	—(*)
Denominator for diluted calculation	33,066	33,216	33,181	31,939
Net income (loss) per share – basic	\$ (0.04)	\$ 0.15	\$ (0.03)	\$ (0.18)
Net income (loss) per share – diluted	\$ (0.04)	\$ 0.15	\$ (0.03)	\$ (0.18)

(*) – Dilutive potential common shares are excluded from the calculation of diluted net loss per share.

The following table sets forth the potential total common shares that are excluded from the calculation of diluted net loss per share as their effect is anti-dilutive as of the date indicated (in thousands)

	March 31, 2008	March 31, 2007
Employee stock options	4,015	2,659
Restricted stock awards	71	—
	4,086	2,659

Recent Accounting Pronouncements

In March 2008, the FASB issued SFAS No. 161, “Disclosures about Derivative Instruments and Hedging Activities — an amendment of FASB Statement No. 133” or SFAS 161. SFAS 161 requires enhanced disclosures about how and why an entity uses derivative instruments, how derivative instruments and related hedge items are accounted for under Statement 133 and its related interpretations, and how derivative instruments and related hedged items affected an entity’s financial position, financial performance, and cash flows. SFAS No. 161 is effective for fiscal years beginning after November 15, 2008, with early application encouraged. The Company is currently evaluating the effects of

implementing this new standard.

In February 2008, the Financial Accounting Standards Board issued FASB Staff Position (FSP) No. FAS 157-1 and FSP No. FAS 157-2. FSP No. 157-1 amends SFAS No. 157, "Fair Value Measurements," to exclude SFAS No. 13, "Accounting for Leases," and other accounting pronouncements that address fair value measurements for purposes of lease classification or measurement under Statement 13. FSP No. 157-2 delays the effective date of SFAS No. 157 for nonfinancial assets and non-financial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis. The Company has evaluated the new FSPs and has determined that it will not have a significant impact on the determination or reporting of our financial results.

In December 2007, the Securities and Exchange Commission, or SEC, issued Staff Accounting Bulletin, or SAB No. 110, "Share-Based Payment". SAB 110 allows for the continued use of the "simplified method" allowed under SAB 107 in developing an estimate of expected term "plain vanilla" share options in accordance with SFAS 123(R). The guidance is applicable after December 31, 2007. The Company has evaluated the new standard and has determined that it will not have a significant impact on the determination or reporting of our financial results.

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

In December 2007, the FASB, issued SFAS No.141(R), “Business Combinations”, or SFAS 141(R). SFAS 141(R) replaces SFAS No. 141. SFAS 141(R) establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, any non controlling interest in the acquiree and the goodwill acquired. The Statement also establishes disclosure requirements which will enable users to evaluate the nature and financial effects of the business combination. SFAS 141(R) is effective for fiscal years beginning after December 15, 2008. The Company is currently evaluating the effects of implementing this new standard.

In December 2007, the FASB issued SFAS No. 160, “Noncontrolling Interests in Consolidated Financial Statements — an amendment of Accounting Research Bulletin No. 51”, or SFAS 160. SFAS 160 establishes accounting and reporting standards for ownership interests in subsidiaries held by parties other than the parent, the amount of consolidated net income attributable to the parent and to the noncontrolling interest, changes in a parent’s ownership interest and the valuation of retained noncontrolling equity investments when a subsidiary is deconsolidated. The Statement also establishes reporting requirements that provide sufficient disclosures that clearly identify and distinguish between the interests of the parent and the interests of the noncontrolling owners. SFAS No. 160 is effective for fiscal years beginning after December 15, 2008. The Company is currently evaluating the effects of implementing this new standard.

In November 2007, the SEC, issued SAB, No. 109, “Written Loan Commitments Recorded at Fair Value Through Earnings”. SAB 109 provides guidance on written loan commitments that the expected net future cash flows related to the associated servicing of the loan should be included in the measurement of all written loan commitments that are accounted for at fair value through earnings. The guidance is applicable for fiscal years beginning after December 15, 2007. The Company has evaluated the new standard and has determined that it will not have a significant impact on the determination or reporting of our financial results.

NOTE 3—BALANCE SHEET COMPONENTS

Accounts Receivable, Net

Accounts receivable, net consists of the following (in thousands):

	March 31, 2008	September 30, 2007
Accounts receivable, net:		
Accounts receivable	\$ 26,095	\$ 27,546
Less: allowance for doubtful accounts	(212)	(165)
	\$ 25,883	\$ 27,381

Prepaid Expenses and Other Current Assets

Prepaid expense and other current assets consist of the following (in thousands):

March 31, 2008	September 30,
-------------------	------------------

2007

Prepaid expense and other current assets:

Prepaid commissions and royalties	\$	4,071	\$	3,104
Restricted cash		49		46
Other prepaid expenses and current assets		3,497		2,202
	\$	7,617	\$	5,352

11

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

Property and Equipment, Net

Property and equipment, net consists of the following (in thousands):

	March 31, 2008	September 30, 2007
Property and equipment, net:		
Computer hardware (useful lives of 3 years)	\$ 4,665	\$ 4,167
Purchased internal-use software (useful lives of 3 years)	3,070	2,685
Furniture and equipment (useful lives of 3 to 7 years)	756	739
Leasehold improvements (shorter of 7 years or the term of the lease)	2,921	2,883
	11,412	10,474
Accumulated depreciation and amortization	(7,661)	(6,836)
	\$ 3,751	\$ 3,638

Intangible Assets, Net

Intangible assets, net consist of the following (in thousands):

	March 31, 2008			September 30, 2007		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Intangible assets:						
Developed technologies	\$ 6,904	\$ (5,317)	\$ 1,587	\$ 6,904	\$ (4,869)	\$ 2,035
Customer list and trade-names	2,731	(2,198)	533	2,731	(2,041)	690
	\$ 9,635	\$ (7,515)	\$ 2,120	\$ 9,635	\$ (6,910)	\$ 2,725

All of the Company's acquired intangible assets are subject to amortization and are carried at cost less accumulated amortization. Amortization is computed on a straight line basis over the estimated useful lives which are as follows: Developed technologies—one and one half to five years; trade-names—three to five years; customer list—three to five years. Aggregate amortization expense for intangible assets totaled \$0.3 million and \$0.6 million for each of the three and six month periods ended March 31, 2008 and 2007, respectively. The Company expects amortization expense on acquired intangible assets to be \$0.6 million for the remainder of fiscal year 2008, \$1.2 million in fiscal year 2009, and \$0.3 million in fiscal year 2010.

Other Assets

Other assets consist of the following (in thousands):

March 31,

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	2008	September 30, 2007
Other assets:		
Long-term accounts receivable	\$ 118	\$ 984
Long-term restricted cash	274	265
Other assets	2,059	2,280
	\$ 2,451	\$ 3,529

The long-term accounts receivable balance at September 30, 2007 represented a receivable from a single customer related to a sale transaction that occurred during the quarter ended December 31, 2006. This amount represents the third and final payment which is due in the quarter ending December 2008. All revenue associated with this receivable has been deferred and will not be recognized until the payment becomes due. As of March 31, 2008, this receivable has been recorded as a current accounts receivable.

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

Accrued Expenses

Accrued expenses consist of the following (in thousands):

	March 31, 2008	September 30, 2007
Accrued expenses:		
Accrued payroll, payroll taxes and related expenses	\$ 5,451	\$ 6,781
Accrued restructuring expenses, current portion (Note 5)	554	3,044
Accrued third party consulting fees	1,223	1,264
Accrued income, sales and other taxes	1,358	1,143
Stock repurchase settlement (Note 14)	1,215	—
Other accrued liabilities	1,230	1,572
	\$ 11,031	\$ 13,804

Deferred Revenue

Deferred revenue consists of the following (in thousands):

	March 31, 2008	September 30, 2007
Deferred revenue:		
License	\$ 19,110	\$ 27,409
Support and maintenance	34,375	39,292
Other	1,653	1,281
	55,138	67,982
Less: current portion	(38,213)	(44,548)
Long-term deferred revenue	\$ 16,925	\$ 23,434

NOTE 4—MARKETABLE SECURITIES

The Company held the following marketable securities (in thousands):

	March 31, 2008				Fair Value
	Amortized Cost	Gross Unrealized Gain	Gross Unrealized Loss		
Marketable securities:					
Non-Taxable municipal bonds	\$ 756	\$ —	\$ (5)	\$ 751	
Total	\$ 756	\$ —	\$ (5)	\$ 751	

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	September 30, 2007			
	Amortized	Gross	Gross	Fair
	Cost	Unrealized	Unrealized	Value
		Gain	Loss	
Marketable securities:				
Commercial paper	\$ 3,008	\$ —	\$ (1)	\$ 3,007
Corporate bonds	9,153	3	(4)	9,152
Total	\$ 12,161	\$ 3	\$ (5)	\$ 12,159

As of March 31, 2008 and September 30, 2007, all marketable securities had maturity dates less than one year. For the three and six months ended March 31, 2008, less than \$0.1 million of gains were realized on the sale of marketable securities. For the three and six months ended March 31, 2007, no gains or losses were realized on the sale of marketable securities. Subsequent to March 31, 2008, all marketable securities were sold and converted to cash equivalents.

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 5—RESTRUCTURING

Restructuring Costs

Through March 31, 2008, the Company approved certain restructuring plans to, among other things, reduce its workforce and consolidate facilities. Restructuring and asset impairment expenses have been recorded to align the Company's cost structure with changing market conditions and to create a more efficient organization. The Company's restructuring expenses have been comprised primarily of: (i) severance and termination benefit costs related to reductions in our workforce; and (ii) lease termination costs and costs associated with permanently vacating certain facilities. The Company accounted for each of these costs in accordance with SFAS No. 146 or SFAS 146, "Accounting for Costs Associated with Exit or Disposal Activities" or previous guidance under Emerging Issues Task Force 94-3 or EITF 94-3.

Retroactive application of SFAS 146 to periods prior to January 1, 2003, was prohibited; accordingly, the accrual relating to facilities vacated prior to the effective date of SFAS 146 continues to be accounted for in accordance with the guidance of EITF 94-3. Accruals for facilities that were restructured prior to 2003 do not reflect any adjustments relating to the estimated net present value of cash flows associated with the facilities.

For each of the periods presented herein, restructuring expenses consist solely of:

• **Severance and Termination Benefits**—These costs represent severance and payroll taxes related to restructuring plans.

• **Excess Facilities**—These costs represent future minimum lease payments related to excess and abandoned office space under leases, the disposal of property and equipment including facility leasehold improvements, net of estimated sublease income.

As of March 31, 2008, the total restructuring accrual consisted of the following (in thousands):

	Current	Non-Current	Total
Severance and termination	\$ 135	\$ —	\$ 135
Excess facilities	419	733	1,152
Total	\$ 554	\$ 733	\$ 1,287

As of March 31, 2008 and September 30, 2007, \$0.6 million and \$3.0 million, respectively, of the restructuring reserve is included in the Accrued Expenses line item on the Condensed Consolidated Balance Sheets. The allocation between current portion and long term portion is based on the current lease agreements.

The Company expects the remaining severance and termination benefit accrual will be substantially paid by September 30, 2008.

The Company expects to pay the excess facilities amounts related to the restructured or vacated leased office space as follows (in thousands):

Fiscal Year Ended September 30,

	Total Future Minimum Lease Payments
2008 (remaining six months)	\$ 211
2009	412
2010	404
2011	125
Total	\$ 1,152

Included in the future minimum lease payments schedule above is an offset of \$0.8 million of contractually committed sublease rental income.

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

Fiscal Year 2007 Restructuring

In October 2006, the Company initiated a restructuring plan intended to align its resources and cost structure with expected future revenues. The restructuring plan included a balancing of service resources worldwide, elimination of duplicative functions internationally, and a shift in the U.S. field organization toward a focus on domain-based sales and pre-sales teams. As a result of the restructuring plan, management undertook a reduction of 33 positions or approximately 10% of the Company's workforce and consolidation of the European headquarters in the United Kingdom and the closure of the France office or 2007 Restructuring.

As part of the fiscal year 2007 Restructuring, the Company initially incurred a one-time restructuring expense of \$6.5 million for severance and termination benefits, and excess facilities expensed to Restructuring Expense in the Condensed Consolidated Statements of Operations. The Company accrued lease costs pertaining to the consolidation of excess facilities relating to lease terminations and non-cancelable lease costs in France and the United Kingdom. During the three months ended March 31, 2007, the Company incurred an additional charge of \$0.1 million for employee severance costs associated with the closure of the France office. In March 2007, the Company negotiated an early termination of the France office lease associated with its closure resulting in a \$0.2 million reduction in the restructure facility liability. This reduction was recorded as an offset to restructuring expense in the period. The Company was able to terminate the France facility lease during the year ended September 30, 2007. In the quarter ended December 31, 2007, the Company negotiated an early termination option for the United Kingdom lease which terminated the lease in January 2008. All termination payments have now been made.

The following table summarizes the activity related to the 2007 Restructuring (in thousands):

	Excess Facilities
Reserve balance as of September 30, 2007	\$ 2,526
Charge/adjustment	(36)
Non-cash	(62)
Cash paid	(2,428)
Reserve balance as of March 31, 2008	\$ —

Fiscal Year 2005 Restructuring

In May 2005, the Company appointed a task force to improve profitability and control expenses. The goal of the task force was to create a better alignment of functions within the Company, to make full utilization of the Company's India development center, to develop a closer relationship between the Company's field operations and customers, to review the sales and implementation models, as well adjust the organization model to flatten management levels, to review the Company's product line, and to enhance the Company's business model for profitability and operating leverage. This work resulted in an approximate 10% reduction in the Company's workforce, or 2005 Restructuring, and in July 2005 affected employees were notified. As part of the 2005 Restructuring, the Company incurred a one-time restructuring charge of \$1.1 million in the fourth quarter ended September 30, 2005 for severance and termination benefits.

During the six months ended March 31, 2007, the Company incurred an additional charge of less than \$0.1 million for additional severance expense for an employee located in France.

The following table summarizes the activity related to the 2005 Restructuring (in thousands):

	Severance and Termination Benefits
Reserve balance as of September 30, 2007	\$ 100
Charge/adjustment	38
Non-cash	(3)
Cash paid	—
Reserve balance as of March 31, 2008	\$ 135

Prior Restructurings

During fiscal year 2002, based upon the Company's continued evaluation of economic conditions in the information technology industry and our expectations regarding revenue levels, the Company restructured several areas so as to reduce

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

expenses and improve revenue per employee, or 2002 Restructuring. As part of the 2002 Restructuring, the Company recorded a total workforce reduction expense relating to severance and termination benefits of approximately \$2.0 million and \$3.8 million for years ended December 31, 2003 and 2002, respectively. In addition to these costs, the Company accrued lease costs related to excess facilities of \$0.2 million and \$2.8 million during the years ended December 31, 2003 and 2002, respectively, pertaining to the consolidation of excess facilities relating to lease terminations and non-cancelable lease costs. This expense was net of estimated sublease income based on current comparable rates for leases in the respective markets.

During the year ended September 30, 2007, the Company entered into a new sublease for the last remaining facility lease associated with the 2002 Restructuring. As a result of this sublease rental income being lower than previously estimated as part of the restructure facility reserve, the Company recorded an additional \$0.3 million of restructuring expense during the year ended September 30, 2007. The sublease term is through the entire remaining term of the Company's lease obligation for the facility.

The following table summarizes the activity related to the 2002 Restructuring (in thousands):

	Excess Facilities
Reserve balance as of September 30, 2007	\$ 1,360
Non-cash	—
Cash paid	(208)
Reserve balance as of March 31, 2008	\$ 1,152

NOTE 6—COMPREHENSIVE INCOME (LOSS)

The components of comprehensive income (loss) are as follows (in thousands):

	Three Months Ended March 31,		Six Months Ended March 31,	
	2008	2007	2008	2007
Net income (loss)	\$ (1,159)	\$ 4,975	\$ (954)	\$ (5,774)
Other comprehensive income (loss):				
Foreign currency translation gain	685	79	713	531
Net change in unrealized gain from investments	(9)	—	(4)	—
Comprehensive income (loss)	\$ (483)	\$ 5,054	\$ (245)	\$ (5,243)

NOTE 7—RELATED PARTY TRANSACTIONS

Charles E. Hoffman, a director of the Company, is the President and Chief Executive Officer of Covad Communications Group, Inc., or Covad, a customer of ours. Pursuant to software and services agreements, revenue from Covad was approximately \$0.1 million for the three and six months ended March 31, 2008 and 2007, respectively. Accounts receivable from Covad was nil and \$0.3 million as of March 31, 2008 and September 30, 2007, respectively. Deferred revenue from Covad was nil and \$0.1 million as of March 31, 2008 and September 30, 2007,

respectively.

NOTE 8—BORROWINGS

Revolving line of credit

The Company's revolving line of credit with Comerica Bank was amended and restated on March 8, 2006, subsequently amended and extended to March 7, 2008 and extended three additional months to June 7, 2008. The terms of the agreement include a \$5.0 million line of credit, available on a non-formula basis, and requires the Company to maintain (i) at least a \$5.0 million cash balance in Comerica Bank accounts, (ii) a minimum quick ratio of 2 to 1, (iii) a liquidity ratio of at least 1 to 1 at all times, and (iv) subordinate any debt issuances subsequent to the effective date of the agreement, and certain other covenants. All assets of the Company have been pledged as collateral on the credit facility.

16

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

The revolving line of credit contains a provision for a sub-limit of up to \$5.0 million for issuances of standby commercial letters of credit. As of March 31, 2008, the Company had utilized \$0.2 million of the standby commercial letters of credit limit of which \$0.2 million serves as collateral for computer equipment leases for Ness (see Note 9). The revolving line of credit also contains a provision for a sub-limit of up to \$3.0 million for issuances of foreign exchange forward contracts. As of March 31, 2008, the Company had not entered into any foreign exchange forward contracts. Pursuant to the amendment in March 2006, the Company is required to secure the standby commercial letters of credit and foreign exchange forward contracts through June 7, 2008. If these have not been secured to Comerica Bank's satisfaction, the Company's cash and cash equivalent balances held by Comerica Bank automatically secure such obligations to the extent of the then continuing or outstanding and undrawn letters of credit or foreign exchange contracts.

Borrowings under the revolving line of credit bear interest at the lending bank's prime rate. Except for the standby commercial letters of credit, as of March 31, 2008, there were no outstanding balances on the revolving line of credit.

NOTE 9—COMMITMENTS AND CONTINGENCIES

Lease Commitments

The Company leases its facilities and certain equipment under non-cancelable operating leases that expire on various dates through 2013. Rent expense is recognized on a straight line basis over the lease term.

Future minimum lease payments as of March 31, 2008 are as follows (in thousands):

	Operating Leases	Operating Sublease Income	Net Operating Leases
Fiscal year ended September 30:			
2008 (remaining six months)	\$ 1,610	\$ (139)	\$ 1,471
2009	2,586	(283)	2,303
2010	2,377	(293)	2,084
2011	1,781	(86)	1,695
2012	916	—	916
Thereafter	660	—	660
Total minimum payments	\$ 9,930	\$ (801)	\$ 9,129

Operating lease obligations in the table above include approximately \$1.9 million for our Boston, Massachusetts facility operating lease commitment that is included in Restructuring Expense. As of March 31, 2008, the Company has \$0.8 million in sublease income contractually committed for future periods relating to this facility. See Note 5 for further discussion.

The office lease for our Cupertino headquarters expires on December 31, 2008. In April 2008, the Company has exercised an option to renew our lease for an additional five years at ninety-five percent of the fair market value on December 31, 2008. While market rates can not be determined at this time, the Company expects our operating lease expense for this facility to increase effective January 1, 2009.

Asset Retirement Obligations

As required by SFAS No.143 “Accounting for Asset Retirement Obligations”, or SFAS 143, and Interpretation No. 47, “Accounting for Conditional Asset Retirement Obligations, an interpretation of FASB Statement No. 143”, or FIN 47, the Company recorded an Asset Retirement Obligation (ARO) of approximately \$0.3 million and a corresponding increase in leasehold improvements in the fiscal year 2007. SFAS 143 and FIN 47 requires the recognition of a liability for the fair value of a legally required conditional asset retirement obligation when incurred, if the liability’s fair value can be reasonably estimated. The fair value of the liability is added to the carrying amount of the associated asset and this additional carrying amount is amortized over the life of the asset.

The Company’s asset retirement obligations are associated with commitments to return property subject to operating leases to original condition upon lease termination. As of March 31, 2008, the Company estimated that gross expected cash flows of approximately \$0.4 million will be required to fulfill these obligations.

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

Asset retirement obligation payments as of March 31, 2008 are included in Other Long-term Liabilities and are estimated as follows (in thousands):

Fiscal year ended September 30:	Payments
2008 (remaining six months)	\$ —
2009	—
2010	—
2011	159
2012	206
Total	\$ 365

Other Obligations

The Company entered into an agreement with Ness Technologies Inc., Ness USA, Inc. (formerly Ness Global Services, Inc.) and Ness Technologies India, Ltd. (collectively, “Ness”), effective December 15, 2003, pursuant to which Ness provides the Company’s customers with technical product support through a worldwide help desk facility, a sustaining engineering function that serves as the interface between technical product support and internal engineering organization, product testing services and product development services (collectively, the “Services”). The agreement had an initial term of three years and was extended for two additional one year terms. Under the terms of the agreement, the Company pays for services rendered on a monthly fee basis, including the requirement to reimburse Ness for approved out-of-pocket expenses. The agreement may be terminated for convenience by the Company, subject to the payment of a termination fee. In 2004, 2005, 2006 and 2007 the Company further expanded its agreement with Ness whereby Ness is providing certain additional technical and consulting services. The additional agreements can be cancelled at the option of the Company without the payment of a termination fee. The remaining minimum purchase commitment under these agreements, if Chordiant was to cancel the contracts, was approximately \$0.7 million at March 31, 2008. In addition to service agreements, the Company has also guaranteed certain equipment lease obligations of Ness (see Note 8). Ness may procure equipment to be used in performance of the Services, either through leasing arrangements or direct cash purchases, for which the Company is obligated under the agreement to reimburse them. In connection with the procurement of equipment, Ness has entered into a 36 month equipment lease agreement with IBM India and, in connection with the lease agreement the Company has an outstanding standby letter of credit in the amount of \$0.2 million in guarantee of Ness’ financial commitments under the lease. Over the term of the lease, the Company’s obligation to reimburse Ness is approximately equal to the amount of the guarantee.

Indemnification

As permitted under Delaware law, the Company has agreements whereby the Company has indemnified our officers, directors and certain employees for certain events or occurrences while the employee, officer or director is, or was serving, at the Company’s request in such capacity. The term of the indemnification period is for the officer’s or director’s lifetime. The maximum potential amount of future payments the Company could be required to make under these indemnification agreements is unlimited; however, the Company has a Director and Officer insurance policy that limits the Company’s exposure and may enable the Company to recover a portion of any future amounts paid. Future payments may be required to defend current and former directors in the derivative class action lawsuit described in Note 10. As a result of insurance policy coverage, the Company believes the estimated fair value of these

indemnification agreements is minimal. Accordingly, the Company has no liabilities recorded for these agreements as of March 31, 2008.

The Company enters into standard indemnification agreements in our ordinary course of business. Pursuant to these agreements, the Company agrees to indemnify, defend, hold harmless, and to reimburse the indemnified party for losses suffered or incurred by the indemnified party, generally the Company's business partners or customers, in connection with any patent, copyright or other intellectual property infringement claim by any third party with respect to the Company's products. The term of these indemnification agreements is generally perpetual after execution of the agreement. The maximum potential amount of future payments the Company could be required to make under these indemnification agreements is unlimited. The Company has not incurred significant costs to defend lawsuits or settle claims related to these indemnification agreements. The Company believes the estimated fair value of these agreements is minimal. Accordingly, the Company has no liabilities recorded for these agreements as of March 31, 2008.

The Company enters into arrangements with our business partners, whereby the business partners agree to provide services as subcontractors for the Company's implementations. The Company may, at its discretion and in the ordinary course of business, subcontract the performance of any of these services. Accordingly, the Company enters into standard indemnification

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

agreements with its customers, whereby the Company indemnifies them for other acts, such as personal property damage by its subcontractors. The maximum potential amount of future payments the Company could be required to make under these indemnification agreements is unlimited; however, the Company has general and umbrella insurance policies that may enable the Company to recover a portion of any amounts paid. The Company has not incurred significant costs to defend lawsuits or settle claims related to these indemnification agreements. As a result, the Company believes the estimated fair value of these agreements is minimal. Accordingly, the Company has no liabilities recorded for these agreements as of March 31, 2008.

When, as part of an acquisition, the Company acquires all of the stock or all of the assets and liabilities of a company, the Company may assume the liability for certain events or occurrences that took place prior to the date of acquisition. The maximum potential amount of future payments, if any, the Company could be required to make for such obligations is undeterminable at this time. Accordingly, the Company has no amounts recorded for these contingent liabilities as of March 31, 2008.

The Company warrants that software products will perform in all material respects in accordance with standard published specifications and documentation in effect at the time of delivery of the licensed products to the customer for a specified period of time. Additionally, the Company warrants that maintenance and consulting services will be performed consistent with generally accepted industry standards. If necessary, the Company would provide for the estimated cost of product and service warranties based on specific warranty claims and claim history, however, the Company has not incurred significant expense under product or services warranties to date. As a result, the Company believes the estimated fair value on these warranties is minimal. Accordingly, the Company has no amounts recorded for these contingent liabilities as of March 31, 2008.

NOTE 10—LITIGATION

IPO Laddering

Beginning in July 2001, the Company and certain of its officers and directors, or Individuals, were named as defendants in a series of class action stockholder complaints filed in the United States District Court for the Southern District of New York, now consolidated under the caption, “In re Chordiant Software, Inc. Initial Public Offering Securities Litigation, Case No. 01-CV-6222”. In the amended complaint, filed in April 2002, the plaintiffs allege that the Company, the Individuals, and the underwriters of the Company’s initial public offering, or IPO, violated section 11 of the Securities Act of 1933 and section 10(b) of the Exchange Act of 1934 based on allegations that the Company’s registration statement and prospectus failed to disclose material facts regarding the compensation to be received by, and the stock allocation practices of, the Company’s IPO underwriters. The complaint also contains claims against the Individuals for control person liability under Securities Act section 15 and Exchange Act section 20. The plaintiffs seek unspecified monetary damages and other relief. Similar complaints were filed in the same court against hundreds of other public companies, or Issuers, that conducted IPO’s of their common stock in the late 1990’s or in the year 2000 (collectively, the “IPO Lawsuits”).

In August 2001, all of the IPO Lawsuits were consolidated for pretrial purposes before United States Judge Shira Scheindlin of the Southern District of New York. In July 2002, the Company joined in a global motion to dismiss the IPO Lawsuits filed by all of the Issuers (among others). In October 2002, the Court entered an order dismissing the Individuals from the IPO Lawsuits without prejudice, pursuant to an agreement tolling the statute of limitations with respect to the Individuals. In February 2003, the court issued a decision denying the motion to dismiss against

Chordiant and many of the other Issuers.

In June 2003, Issuers and plaintiffs reached a tentative settlement agreement that would, among other things, result in the dismissal with prejudice of all claims against the Issuers and Individuals in the IPO Lawsuits, and the assignment to plaintiffs of certain potential claims that the Issuers may have against the underwriters. The tentative settlement also provides that, in the event that plaintiffs ultimately recover less than a guaranteed sum of \$1 billion from the IPO underwriters, plaintiffs would be entitled to payment by each participating Issuer's insurer of a pro rata share of any shortfall in the plaintiffs' guaranteed recovery. In September 2003, in connection with the possible settlement, those Individuals who had entered tolling agreements with plaintiffs (described above) agreed to extend those agreements so that they would not expire prior to any settlement being finalized. In June 2004, Chordiant and almost all of the other Issuers entered into a formal settlement agreement with the plaintiffs. On February 15, 2005, the Court issued a decision certifying a class action for settlement purposes, and granting preliminary approval of the settlement subject to modification of certain bar orders contemplated by the settlement. On August 31, 2005, the Court reaffirmed class certification and preliminary approval of the modified settlement in a comprehensive Order, and directed that Notice of the settlement be published and mailed to class members beginning November 15, 2005. On February 24, 2006, the Court dismissed litigation filed against certain underwriters in connection with the claims to be assigned to the plaintiffs under the settlement. On April 24, 2006, the Court held a Final Fairness Hearing to determine whether to grant final approval of the settlement. On December 5, 2006, the Second Circuit Court of Appeals vacated the lower Court's earlier decision certifying as class actions the six IPO Lawsuits designated as "focus cases." Thereafter, the District Court ordered a stay of all proceedings in all of the IPO Cases pending the outcome of plaintiffs' petition to the Second Circuit for rehearing en banc. On April 6, 2007, the Second Circuit

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

denied plaintiffs' rehearing petition, but clarified that the plaintiffs may seek to certify a more limited class in the district court. Accordingly, the settlement will not be finally approved. Plaintiffs filed amended complaints in six "focus cases" on or about August 14, 2007. The Company is not a focus case. In September 2007, the Company's named officers and directors again extended the tolling agreement with plaintiffs. On or about September 27, 2007, plaintiffs moved to certify the classes alleged in the focus cases and to appoint class representatives and class counsel in those cases. The focus case issuers filed motions to dismiss the claims against them on or about November 9, 2007 and an opposition to plaintiffs' motion for class certification on December 21, 2007. On March 16, 2008, the court denied the motions to dismiss in the focus cases. This action may divert the efforts and attention of our management and, if determined adversely to us, could have a material impact on our business, results of operations, financial condition or cash flows.

Derivative Class Action

On August 1, 2006, a stockholder derivative complaint was filed in the United States District Court for the Northern District of California by Jesse Brown under the caption *Brown v. Kelly, et al.* Case No. C06-04671 JW (N.D. Cal.). On September 13, 2006, a second stockholder derivative complaint was filed in the United States District Court for the Northern District of California by Louis Suba under the caption *Suba v. Kelly et al.*, Case No. C06-05603 JW (N.D. Cal.). Both complaints were brought purportedly on behalf of the Company against certain current and former officers and directors. On November 27, 2006, the court entered an order consolidating these actions and requiring the plaintiffs to file a consolidated complaint. The consolidated complaint was filed on January 11, 2007. The consolidated complaint alleges, among other things, that the named officers and directors: (a) breached their fiduciary duties as they colluded with each other to backdate stock options, (b) violated section 10(b), 14(a) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder through their alleged actions, and (c) were unjustly enriched by their receipt and retention of such stock options. On May 21, 2007, the Company filed a motion to dismiss the entire action on the grounds that the plaintiffs failed to take the steps necessary to bring a derivative action. Instead of opposing the motion to dismiss on November 14, 2007, the plaintiffs filed an Amended Complaint adding new allegations against five more current and former officer and directors. The substantive allegations in the Amended Complaint are similar to those in the previous complaint. On December 14, 2007, the Company again filed a motion to dismiss the entire action on the grounds that the plaintiffs failed to take the steps necessary to bring a derivative action. The individual defendants also filed a motion to dismiss. On January 22, 2008, the parties reached a tentative non-binding agreement in principle on the settlement of this lawsuit. The parties are working to finalize and memorialize the terms of that settlement and will then seek court approval of the settlement. Under the tentative proposal the Company's cash contribution toward the settlement would not be material to the financial statements.

Patent Claim

In September 2006, the Company received a letter from Acacia Technologies Group, a patent holding company, suggesting that the Company may be infringing on two patents, designated by United States Patent Numbers 5,537,590 and 5,701,400, which are held by one of their patent licensing and enforcement subsidiaries. The Company is currently reviewing the validity of these patents and whether the Company's products may infringe upon them. The Company has not formed a view of whether the Company may have liability for infringement of these patents. Any related claims, whether or not they have merit, could be costly and time-consuming to defend, divert management's attention or cause product delays. If any of the Company's products were found to infringe such patents, the patent holder could seek an injunction to enjoin use of the infringing product. If the Company was required to settle such a claim, it could have a material impact on our business, results of operations, financial condition or cash flows.

Yue vs Chordiant Software, Inc.

On January 2, 2008, the Company and certain of our officers and one other employee were named in a complaint filed in the United States District Court for the Northern District of California by Dongxiao Yue under the caption Dongxiao Yue v. Chordiant Software, Inc. et al. Case No. CV 08-0019 BZ (N.D. Cal.). The complaint alleges that the Company's Marketing Director software product infringed copyrights in certain software referred to as the "PowerRPC software," copyrights which had been owned by Netbula LLC and assigned to Mr. Yue, the sole employee and owner of Netbula. The alleged infringement includes (a) distributing more copies of the PowerRPC software than had originally been authorized in a run time license Netbula granted to Chordiant Software, Intl., (b) infringement of a software developer kit ("SDK") by making copies of the SDK in excess of those that had been licensed by Netbula, (c) making unauthorized derivative works of the SDK, (d) unauthorized distribution of PowerRPC for products operating on the Windows Vista platform, (e) unauthorized distribution of PowerRPC for server based products. Plaintiff also claims that the license Netbula granted to Chordiant Software, Int'l Ltd. should not be construed to authorize uses by its parent company, Chordiant Software, Inc. The plaintiff seeks monetary damages, disgorgement of profits, and injunctive relief according to proof. The Company and its officers and employees have filed a motion to dismiss the complaint for failure to state a claim upon which relief could be granted, and as to lack of personal jurisdiction as to one employee. These motions are presently scheduled for hearing in June 2008.

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

The Company, from time to time, is also subject to various other claims and legal actions arising in the ordinary course of business. The ultimate disposition of these various other claims and legal actions is not expected to have a material effect on our business, financial condition, results of operations or cash flows. However, litigation is subject to inherent uncertainties.

NOTE 11—INCOME TAXES

Effective October 1, 2007, the Company adopted FIN No. 48 “Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109”. FIN 48 prescribes a recognition threshold and measurement guidance for the financial statement reporting of uncertain tax positions taken or expected to be taken in a company’s income tax return. FIN 48 also provides guidance related to recognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition matters related to uncertain tax positions. FIN 48 utilizes a two-step approach for evaluating uncertain tax positions accounted for in accordance with SFAS 109. Step one, recognition, requires a company to determine if the weight of available evidence indicates that a tax position is more likely than not to be sustained upon audit, including the resolution of related appeals or litigation processes, if any. Step two, measurement, is based on the largest amount of benefit, which is more likely than not to be realized on ultimate settlement. The cumulative effect of adopting FIN 48, if any, is recorded as an adjustment to the opening balance of retained earnings as of the adoption date.

The net income tax liabilities recognized under FIN 48 did not materially differ from the net assets recognized before adoption, and, therefore, the Company did not record an adjustment to retained earnings related to the adoption of FIN 48. At the adoption date of October 1, 2007, the Company had \$0.8 million of unrecognized tax benefits related to tax positions taken in prior periods, \$0.2 million of which would affect our effective tax rate if recognized. There were no material changes to the amount of unrecognized tax benefits during the first six months of fiscal 2008.

The Company recognized accrued interest and penalties related to unrecognized tax benefits in the Provision for Income Taxes. The Company had less than \$0.1 million accrued for interest and penalties as of March 31, 2008.

The Company files income tax returns in the U.S. federal jurisdiction and various state and foreign jurisdictions. With few exceptions, all U.S. federal, state and United Kingdom tax years between 1995 and 2007 remain open to examination due to net operating loss carryforwards and credit carryforwards. Tax years 2002 and later remain open to examination in the Netherlands, tax years 2003 and later remain open to examination in Canada and years 2004 and later remain open to examination in Germany.

An audit of the 2005 tax year is currently in process in the Netherlands. The Company does not expect resolution of this audit to have a material impact on our financial statements and the Company does not expect a significant increase or decrease in unrecognized tax benefits over the next 12 months.

The Company provides a valuation allowance for deferred tax assets when it is more likely than not that the net deferred tax assets will not be realized. Based on a number of factors, including the lack of a history of profits prior to 2007 and the fact that the market in which we compete is intensely competitive and characterized by rapidly changing technology, the Company believes that there is sufficient uncertainty regarding the realization of deferred tax assets such that a full valuation allowance has been provided. At March 31, 2008, the Company had approximately \$127.6 million and \$18.9 million of net operating loss carryforwards for federal and state purposes, respectively, and net operating loss carryforwards of approximately \$34.5 million in the United Kingdom. As a result of an IRC Section

382 study completed during fiscal 2008, it was determined that \$19.6 million of net operating loss carryforwards resulting from the acquisition of Prime Response will expire unutilized. The \$127.6 million in total federal net operating loss carryforwards is presented net of these Section 382 limitations. Upon being realized, the remaining \$13.8 million of the Prime Response federal net operating loss carryforwards would reduce goodwill and intangibles recorded at the date of acquisition before reducing the tax provision. Approximately \$3.5 million of additional net operating loss carryforwards are related to stock option deductions which, if utilized, would be accounted for as an addition to equity rather than as a reduction of the provision for income taxes. The net operating loss carryforwards are available to offset future federal and state taxable income and expire in years from 2008 through 2026. At March 31, 2008, there are approximately \$3.5 million of federal research and development credits and alternative minimum tax credits that expire in years 2011 through 2027. At March 31, 2008, there were also California state credits of approximately \$3.5 million that do not expire.

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 12—EMPLOYEE BENEFIT PLANS

2005 Equity Incentive Plan

As of March 31, 2008, there were approximately 2.5 million shares available for future grant and approximately 3.4 million options that were outstanding under the 2005 Equity Incentive Plan, or 2005 Plan. In December 2007, the Board amended the 2005 plan to increase the number of shares reserved for future issuance by 0.7 million shares. This amendment was approved by the stockholders at the 2008 Annual Meeting of Stockholders' held on February 1, 2008.

In October 2007, the Company granted 0.2 million performance-based Restricted Stock Units or RSUs to selected executives of the Company pursuant to the 2005 Plan. The performance-based RSUs cliff vest at the end of a two year requisite service period, constituting the Company's fiscal years 2008 and 2009, upon achievement of specified performance criteria established by the Compensation Committee of our Board of Directors. The award agreements for RSUs generally provide that vesting will be accelerated in certain events related to changes in control of the Company. Total compensation cost for these awards is based on the fair market value of the shares at the date of grant. The portion of the total compensation cost related to the performance-based awards is subject to adjustment each quarter based on management's assessment of the likelihood of achieving the two year performance criteria.

2000 Nonstatutory Equity Incentive Plan

As of March 31, 2008, there were approximately 0.4 million options outstanding under the 2000 Nonstatutory Equity Incentive Plan.

1999 Non-Employee Directors' Option Plan

As of March 31, 2008, there were approximately 0.2 million shares of common stock available for future grant and 0.2 million options that were outstanding under the 1999 Non-Employee Directors' Option Plan or Directors' Plan. In December 2007, the Board amended the Directors' Plan to incorporate the following changes:

1. expand the type of awards that may be granted under the Directors' Plan to allow Restricted Stock Awards (RSAs) and RSU awards; and
2. for fiscal year 2008 and thereafter, directors will be awarded RSAs instead of stock options for their annual and initial automatic Board service awards.

This amendment was approved by the stockholders at the 2008 Annual Meeting of Stockholders' held on February 1, 2008.

On February 1, 2008, the Company's Board members were granted 71,088 RSAs for their annual service award under the Directors' Plan. The RSAs cliff vest at the earlier of the date of the first anniversary of the most recent Annual Meeting or on the date of the next Annual meeting.

Stock Option Activity

The following table summarizes stock option, RSA, and RSUs activity under our stock option plans (in thousands, except per share data):

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

	Shares Available for Grant	Shares	Options Outstanding		Aggregate Intrinsic Value Closing Price at 3/31/2008 of \$6.03
			Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	
Balance at September 30, 2007	3,058	3,178	\$ 7.96		
Authorized	700	—	—		
Options granted	(1,037)	1,037	9.32		
Restricted stock awards granted	(71)	—	—		
Restricted stock units granted *	(52)				
Options exercised	—	(98)	6.24		
Cancellation of unvested restricted stock	—	—	—		
Options and awards cancelled/forfeited	102	(102)	9.39		
Authorized reduction in shares from existing plans	(9)	—	—		
Balance at March 31, 2008	2,795	4,015	\$ 8.31	7.97	\$ 1,164
Vested and expected to vest at March 31, 2008		3,103	\$ 8.16	7.70	\$ 1,128
Exercisable at March 31, 2008		1,791	\$ 7.53	6.72	\$ 1,076

* The number of RSUs granted is an estimate based upon management's assessment of the likelihood of achieving the two year performance criteria.

The following table summarizes information about stock options outstanding and exercisable at March 31, 2008 (in thousands, except exercise prices and contractual life data):

Range of Exercise Prices	Number Outstanding	Options Outstanding			Options Exercisable		
		Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	Aggregate Intrinsic Value Closing Price at 3/31/2008 of \$6.03	Number Exercisable	Weighted Average Exercise Price	Aggregate Intrinsic Value Closing Price at 3/31/08 of \$6.03
\$0.35 – 6.45	635	5.89	\$ 4.21	\$ 1,164	495	\$ 3.87	\$ 1,076
6.48 – 7.80	536	7.33	7.17	—	349	7.08	—
7.88 – 8.15	439	7.69	7.98	—	235	7.98	—
8.25 – 8.25	802	8.81	8.25	—	246	8.25	—
8.28 – 9.13	201	7.94	8.51	—	87	8.56	—
9.25 – 9.25	799	9.62	9.25	—	77	9.25	—
9.26 – 45.00	603	7.60	12.67	—	302	12.39	—

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\$0.35 – 45.00	4,015	7.97	\$	8.31	\$	1,164	1,791	\$	7.53	\$	1,076
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The aggregate intrinsic value in the preceding table represents the total intrinsic value, based on the Company's closing stock price of \$6.03 as of March 31, 2008, which would have been received by the option holders had all option holders exercised their options as of that date. The total intrinsic value of options exercised during the three and six months ended March 31, 2008 was less than \$0.1 million and \$0.7 million, respectively, and \$4.0 million and \$4.3 million for the three and six months ended March 31, 2007, respectively. The fair value of options vested was \$0.1 million and \$0.8 million for the three and six months ended March 31, 2008 and \$0.3 million and \$0.9 million for the three and six months ended March 31, 2007, respectively. As of March 31, 2008, total unrecognized compensation costs related to non-vested stock options was \$6.3 million, which is expected to be recognized as expense over a weighted-average period of approximately 2.8 years. As of March 31, 2007, total unrecognized compensation costs related to non-vested stock options was \$5.7 million, which was expected to be recognized as expense over a weighted-average period of approximately 1.5 years.

On February 1, 2008, the Company's Board members were granted 71,088 RSAs for their annual service award under the Directors' Plan. The Company had 0.1 million unvested RSAs as of March 31, 2008, which were excluded from the preceding tables. The total fair value of the unvested RSAs at grant date was \$0.6 million. Aggregate intrinsic value of the unvested RSAs at March 31, 2008 was \$0.4 million. During the three months ended March 31, 2008, zero shares vested related to RSAs. The weighted average fair value at grant date of the unvested RSAs was \$8.44 per share as of March 31, 2008. As of March 31, 2008,

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

total unrecognized compensation costs related to unvested RSAs was \$0.5 million which is expected to be recognized as expense over a weighted average period of approximately 0.8 year.

The Company had 0.1 million unvested RSAs as of March 31, 2007. The total fair value of the unvested RSAs at grant date was \$0.4 million. Aggregate intrinsic value of the unvested RSAs at March 31, 2007 was \$0.9 million. During the three and six months ended March 31, 2007, approximately 0.1 million and 0.2 million shares vested related to RSAs, respectively. There were no shares of restricted stock awarded during the three and six months ended March 31, 2007. The weighted average fair value at grant date of the unvested RSAs was \$5.25 as of March 31, 2007. As of March 31, 2007, total unrecognized compensation costs related to unvested RSAs was less than \$0.1 million which is expected to be recognized as expense over a weighted average period of approximately 0.3 years.

As of March 31, 2008, the total fair value and number of vested RSUs was zero. Based upon management's assessment of the likelihood of achieving the two year performance criteria, the Company has less than 0.1 million out of a maximum of 0.2 million of unvested RSUs with an average fair value of \$15.38 per unit. During the six months ended March 31, 2008, \$0.2 million of stock compensation expense related to the performance-based RSUs has been recognized. The total unrecognized compensation costs related to unvested RSUs was \$0.6 million which is expected to be recognized as expense over a weighted average period of approximately 18 months. If the maximum target of RSUs outstanding were assumed to be earned, total unrecognized compensation costs would be approximately \$3.1 million which would be expected to be recognized as expense over a weighted average period of approximately 18 months.

The Company settles stock option exercises, RSAs and RSUs with newly issued common shares.

Valuation and Expense Information under SFAS 123(R)

On October 1, 2005, the Company adopted SFAS 123(R), which requires the measurement and recognition of compensation expense for all share-based payment awards made to the Company's employees and directors including employee stock options, RSAs, RSUs and employee stock purchases related to the Employee Stock Purchase Plan based on estimated fair values. The following table summarizes stock-based compensation expense related to employee stock options, RSA and RSUs for the three and six months ended March 31, 2008 and 2007, respectively, which was allocated as follows (in thousands):

	Three Months Ended March 31,		Six Months Ended March 31,	
	2008	2007	2008	2007
Stock-based compensation expense:				
Cost of revenues, service	\$ 109	\$ 54	\$ 262	\$ 161
Sales and marketing	230	237	471	566
Research and development	144	168	343	262
General and administrative	498	434	1,081	880
Total stock-based compensation expense	\$ 981	\$ 893	\$ 2,157	\$ 1,869

The weighted-average estimated fair value of stock options granted during the three months ended March 31, 2008 and 2007 was \$2.96 and \$4.07 per share, respectively, and for the six months ended March 31, 2008 and 2007 was

\$4.30 and \$4.06, respectively, using the Black-Scholes model with the following weighted-average assumptions:

	Three Months Ended March 31,		Six Months Ended March 31,	
	2008	2007	2008	2007
Expected lives in years	3.7	3.5	3.5	3.5
Risk free interest rates	2.3%	4.8%	3.3%	4.7%
Volatility	61%	63%	60%	63%
Dividend yield	0%	0%	0%	0%

The fair value of each option award is estimated on the date of grant using the Black-Scholes option valuation model with the weighted-average assumptions for volatility, expected term, and risk free interest rate. With the adoption of SFAS 123(R) on October 1, 2005, the Company used the trinomial lattice valuation technique to determine the assumptions used in the Black-Scholes model. The trinomial lattice valuation technique was used to provide a better estimate of fair values and meet the fair value objectives of SFAS 123(R). The expected term of options granted is derived from historical data on employee exercises and post-vesting employment termination behavior. The risk-free rate is based on the U.S. Treasury rates in effect during the corresponding period of grant. The expected volatility rate is based on the historical volatility of our stock price.

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

As stock-based compensation expense recognized in the Condensed Consolidated Statements of Operations for the three and six months ended March 31, 2008 and 2007 is based on awards ultimately expected to vest, it has been reduced for estimated forfeitures. SFAS 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Our estimated forfeiture rate for the three and six months ended March 31, 2008 and 2007 was based on our historical forfeiture experience.

Accuracy of Fair Value Estimates

The Company uses third-party analyses to assist in developing the assumptions based on a trinomial lattice valuation technique used in the Black-Scholes model. The Company is responsible for determining the assumptions used in estimating the fair value of share-based payment awards.

Our determination of fair value of share-based payment awards on the date of grant using an option-pricing model is affected by the Company's stock price as well as assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to the Company's expected stock price volatility over the term of the awards, and actual and projected employee stock option exercise behaviors. Because the Company's employee stock options have certain characteristics that are significantly different from traded options, and because changes in the subjective assumptions can materially affect the estimated value, in management's opinion, the existing valuation models may not provide an accurate measure of the fair value of the Company's employee stock options and RSAs. Although the fair value of employee stock options and RSAs is determined in accordance with SFAS 123(R) and SAB 107 using an option-pricing model, that value may not be indicative of the fair value observed in a willing buyer/willing seller market transaction.

NOTE 13—SEGMENT INFORMATION

Our chief operating decision maker reviews financial information presented on a consolidated basis, accompanied by desegregated information about revenues by geographic regions for purposes of making operating decisions and assessing financial performance. Accordingly, the Company has concluded that the Company has one reportable segment.

The following table summarizes license revenue by product emphasis (in thousands):

	Three Months Ended March 31,		Six Months Ended March 31,	
	2008	2007	2008	2007
License Revenue:				
Enterprise solutions	\$ 3,870	\$ 12,619	\$ 10,084	\$ 16,164
Marketing solutions	579	1,268	1,293	2,257
Decision management solutions	358	4,995	2,237	7,623
Total	\$ 4,807	\$ 18,882	\$ 13,614	\$ 26,044

The following table summarizes service revenue consisting of consulting implementation and integration, consulting customization, training, post-contract customer support services, or PCS and certain reimbursable out-of-pocket expenses by product emphasis (in thousands):

	Three Months Ended March 31,	Six Months Ended March 31,
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	2008	2007	2008	2007
Service Revenue:				
Enterprise solutions	\$ 13,439	\$ 10,147	\$ 28,649	\$ 22,346
Marketing solutions	3,070	2,903	6,188	5,508
Decision management solutions	3,400	833	5,399	1,806
Total	\$ 19,909	\$ 13,883	\$ 40,236	\$ 29,660

25

Table of Contents

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

Foreign revenues are based on the country in which the customer order is generated. The following is a summary of total revenues by geographic area (in thousands):

	Three Months Ended March 31,		Six Months Ended March 31,	
	2008	2007	2008	2007
North America	\$ 14,671	\$ 9,473	\$ 30,262	\$ 22,694
Europe	10,045	23,292	23,588	33,010
Total	\$ 24,716	\$ 32,765	\$ 53,850	\$ 55,704

Included in foreign revenue results for Europe is revenue from the United Kingdom of \$6.0 million and \$12.1 million for the three and six months ended March 31, 2008 and \$9.5 and \$15.8 million for the three and six months ended March 31, 2007, respectively.

Net property and equipment information is based on the physical location of the assets. The following is a summary of net property and equipment by geographic area (in thousands):

	March 31, 2008	September 30, 2007
North America	\$ 2,519	\$ 2,346
Europe	1,232	1,292
Total	\$ 3,751	\$ 3,638

NOTE 14—STOCK REPURCHASE

On February 28, 2008, the Company's Board of Directors authorized a program to repurchase up to \$25 million of the Company's common stock over a one year period, or 2008 Repurchase Plan, starting on March 4, 2008. In conjunction with the 2008 Repurchase Plan, the Company entered into a written trading plan with a broker under Rule 10b5-1 of the Securities Exchange Act of 1934, as amended, to effect the repurchases. Repurchased shares are immediately retired and will resume the status of authorized but unissued shares. As of March 31, 2008, the Company had repurchased 1.5 million shares of our common stock for \$9.3 million at an average price of \$6.10 per share. The Company terminated the 2008 Stock Repurchase Plan as of April 30, 2008. Subsequent to March 31, 2008, through April 30, 2008, the Company had repurchased an additional 1.8 million shares of our common stock for \$9.3 million at an average price of \$5.09 per share. As of April 30, 2008, the Company had repurchased a total of 3.4 million shares of our common stock for \$18.6 million at an average price of \$5.55 per share.

NOTE 15—SUBSEQUENT EVENT

On May 1, 2008, the Company committed to a cost reduction plan intended to align its resources and cost structure with expected future revenues. The plan anticipates a re-allocation of employee resources between functional groups. The plan includes an immediate reduction in positions equal to approximately ten percent of the Company's worldwide

workforce. We notified employees on May 1, 2008.

As a result of the cost-cutting measures, the Company estimates that it will record pre-tax operating charges in the third quarter of fiscal year 2008 of approximately \$0.4 million for severance costs.

26

Table of Contents

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

This discussion and analysis should be read in conjunction with our Condensed Consolidated Financial Statements and accompanying Notes included in this report and the 2007 Audited Financial Statements and Notes thereto included in our Annual Report on Form 10-K for the year ended September 30, 2007 filed with the SEC. Operating results are not necessarily indicative of results that may occur in future periods.

The following discussion and analysis contains forward-looking statements. These statements are based on our current expectations, assumptions, estimates and projections about our business and our industry, and involve known and unknown risks, uncertainties and other factors that may cause our or our industry's results, levels of activity, performance or achievement to be materially different from any future results, levels of activity, performance or achievements expressed or implied in or contemplated by the forward-looking statements. Words such as "believe," "anticipate," "expect," "intend," "plan," "will," "may," "should," "estimate," "predict," "guidance," "potential," "continue" or such terms or other similar expressions, identify forward-looking statements. Our actual results and the timing of events may differ significantly from those discussed in the forward-looking statements as a result of various factors, including but not limited to, those discussed under the subheading "Risk Factors" and those discussed elsewhere in this report, in our other SEC filings and under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations" in our 2007 Form 10-K. Chordiant undertakes no obligation to update any forward-looking statement to reflect events after the date of this report.

Overview

As an enterprise software vendor, we generate substantially all of our revenues from the banking, insurance, healthcare, telecommunications, and retail industries. Our customers typically fund purchases of our software and services out of their lines of business and information technology budgets. As a result, our revenues are heavily influenced by our customers' long-term business outlook and willingness to invest in new enterprise information systems and business applications.

For the three months ended March 31, 2008, total revenues decreased 25% and backlog increased 19% as compared to the same period of the prior year. For the three months ended March 31, 2008, backlog decreased \$2.5 million or 3% compared to the balance at December 31, 2007. This decrease in backlog is primarily related to a reduction of license and support and maintenance deferred revenue balances at the end of the quarter.

Software Industry Consolidation and Possible Increased Competition

The enterprise software industry continues to undergo consolidation in sectors of the software industry in which we operate. In 2007 and 2008 IBM acquired Cognos, DataMirror and Watchfire Corporation; Oracle completed its acquisition of Hyperion and Moniforce and has entered into an agreement to purchase BEA Systems; Sun Microsystems has entered in an agreement to purchase MySQL and SAP acquired BusinessObjects, YASU Technologies and Pilot Software. While we do not believe that Cognos, DataMirror, Watchfire Corporation, Hyperion, Moniforce, BEA Systems, MySQL, BusinessObjects, YASU Technologies, or Pilot Software have been significant competitors of Chordiant in the past, the acquisition of these companies by IBM, Oracle, Sun Microsystems and SAP may indicate that we will face increased competition from larger and more established entities in the future.

Financial Trends

Backlog. Our revenues have primarily been derived from large customer transactions. For some of these transactions, the associated professional services provided to the customer can span over a period greater than one year. If the services delivery period is over multiple quarters, it will cause the associated backlog to be recognized as revenue over

a similar period of time. As of March 31, 2008 and 2007, we had approximately \$93.5 million and \$78.6 million in backlog, respectively, which we define as contractual commitments by our customers through purchase orders or contracts. Backlog at March 31, 2008 includes approximately \$26.1 million relating to a large telecommunications customer commitment. For the period ended March 31, 2008 as compared to the previous period ended December 31, 2007, aggregate deferred revenue balances decreased \$2.0 million due to a decrease of \$2.2 million in long-term deferred revenue offset by an increase of \$0.2 million in short-term deferred revenue. Backlog is comprised of:

• software license orders for which the delivered products have not been accepted by customers or have not otherwise met all of the required criteria for revenue recognition. This component includes billed amounts classified as deferred revenue;

- deferred revenue from customer support contracts; and,

• consulting service orders representing the unbilled remaining balances of consulting contracts not yet completed or delivered, plus deferred consulting revenue where we have not otherwise met all of the required criteria for revenue recognition.

Table of Contents

Backlog is not necessarily indicative of revenues to be recognized in a specified future period. There are many factors that would impact Chordiant's conversion of backlog as recognizable revenue, such as Chordiant's progress in completing projects for its customers, Chordiant's customers' meeting anticipated schedules for customer-dependent deliverables and customers increasing the scope or duration of a contract causing license revenue to be deferred for a longer period of time.

Chordiant provides no assurances that any portion of its backlog will be recognized as revenue during any fiscal year or at all, or that its backlog will be recognized as revenues in any given period. In addition, it is possible that customers from whom we expect to derive revenue from backlog will default and as a result we may not be able to recognize expected revenue from backlog.

Implementation by Third Parties. Over time as our products mature and system integrators become more familiar with our products, our involvement with implementations has diminished on some projects. If this trend continues, certain agreements with customers may transition from a contract accounting model (SOP81-1) to a more traditional revenue model whereby revenues are recorded upon delivery (SOP 97-2).

Service Revenue. Service revenue as a percentage of total revenues were 81% and 42% for the three months ended March 31, 2008 and 2007, respectively, and 75% and 53% for the six months ended March 31, 2008 and 2007, respectively. While the composition of revenue will continue to fluctuate on a quarterly basis, we expect that service revenue will represent between 50% and 60% of our total revenues in the future.

Revenues from International Customers versus North America Revenues. For all periods presented, revenues were principally derived from customer accounts in North America and Europe. For the three months ended March 31, 2008 and 2007, international revenues were \$10.0 million and \$23.3 million, or approximately 41% and 71% of our total revenues, respectively. For the six months ended March 31, 2008 and 2007, international revenues were \$23.6 million and \$33.0 million, or approximately 44% and 59% of our total revenues, respectively. The decrease in international revenue for the three and six months ended March 31, 2008 was primarily due to a decrease in license revenue. During the March 31, 2007 quarter, a large customer transaction was recognized as revenue. International revenues were favorably impacted for the three months ended March 31, 2008, as compared to the three months ended March 31, 2007, as both the British Pound and the Euro increased in average value by approximately 1% and 14%, respectively, as compared to the U.S. Dollar.

For the three months ended March 31, 2008 and 2007, North America revenues were \$14.7 million and \$9.5 million, or approximately 59% and 29% of our total revenues, respectively. For the six months ended March 31, 2008 and 2007, North America revenues were \$30.3 million and \$22.7 million, or approximately 56% and 41% of total revenues, respectively. We believe North America revenues will continue to represent a significant portion of our total revenues in the foreseeable future.

Gross Margins. Management focuses on license and service gross margin in evaluating our financial condition and operating performance. Gross margins on license revenues were 94% and 97% for the three months ended March 31, 2008 and 2007, respectively, and 95% and 96% for the six months ended March 31, 2008 and 2007. The 1% decrease for the quarter ending March 31, 2008 is primarily a function of the fixed periodic amortization costs associated with capitalized software being divided by a smaller license amount quarter-over-quarter. We expect license gross margin on current products to range from 95% to 97% in the foreseeable future. The margin will fluctuate with the mix of products sold. Historically, the enterprise solution products have higher associated third party royalty expense than the marketing solution products and decision management products.

Gross margins on service revenue were 57% and 60% for the three months ended March 31, 2008 and 2007, respectively and 58% and 56% for the six months ended March 31, 2008 and 2007, respectively. The decrease in gross margins for the three months period ending March 31, 2008 is primarily due to the mix of consulting revenue versus support revenue. Consulting revenue, which has a lower gross margin than support revenue, increased to a larger percentage of total service revenue reducing the overall gross margin. We expect that gross margins on service revenue to range between 55% and 60% in the second half of fiscal year 2008.

Costs Related to Stock Option Investigation. For the three and six months ended March 31, 2007, significant professional service costs are included in general and administrative expense associated with the Company's stock option investigation which began in July 2006 and was completed during the quarter ended March 2007. This issue is more fully described in the Note 2 of the Consolidated Financial Statements in our 2006 Form 10-K. For the three and six months ended March 31, 2007, these costs were \$0.8 million and \$1.8 million, respectively. We have not incurred any additional costs since the quarter ended March 31, 2007 and do not expect to incur such costs in the future periods.

Cost to Amend Eligible Options. In July 2006, our Board of Directors, or the Board, initiated a review of our historical stock option grant practices and appointed the Audit Committee to oversee the investigation. The Audit Committee determined that the correct measurement dates for a number of stock option grants made by us during the period 2000 to 2006, or Review

Table of Contents

Period, differed from the measurement dates previously used to account for such option grants. The Audit Committee identified errors related to the determination of the measurement dates for grants of options where the price of our common stock on the selected grant date was lower than the price on the actual grant date which would permit recipients to exercise these options at a lower exercise price. As such, these affected stock options are deemed, for accounting purposes, to have been granted at a discount. Based on the determination made for accounting purposes, the discounted options (for accounting purposes) may now be deemed to have been granted at a discount for tax purposes, which may expose the holders of these impacted stock option grants to potentially adverse tax treatment under Section 409A of the Internal Revenue Code and state law equivalents. As more fully described on Form SC TO-I filed with the SEC on March 29, 2007, Chordiant offered certain optionees the opportunity to increase the exercise price of the discounted options to limit the potential adverse personal tax consequences that may apply to those stock options under Section 409A of the Internal Revenue Code and state law equivalents. On April 26, 2007, eligible optionees finalized their elections under the offer and were awarded a future cash payment equal to the price differential of the Amended Options. These payments were treated as bonus payments. These cash payments were approximately \$0.3 million and were paid out in January 2008.

Reduction in Workforce. In October 2006, we initiated a restructuring plan intended to align our resources and cost structure with expected future revenues. The restructuring plan included a balancing of services resources worldwide, an elimination of duplicative functions internationally, and a shift in the U.S. field organization toward a focus on domain-based sales and pre-sales teams.

The restructuring plan included an immediate reduction in positions of slightly more than ten percent of our workforce, the consolidation of our European facilities, and the closure of our France office. A majority of the positions eliminated were in Europe. The plan was committed to on October 24, 2006, and we began notifying employees on October 25, 2006.

We initially recorded a pre-tax cash restructuring expense of \$6.5 million as calculated using the net present value of the related costs as required by SFAS 146. The expense was composed of costs for severance and exiting excess facilities. During the three months ended March 31, 2007, we incurred an additional charge of \$0.1 million for employee severance costs associated with the closure of our France office. Also during the three months ended March 31, 2007, we negotiated an early termination of the France office lease associated with its closure, resulting in a \$0.2 million reduction in the excess facility liability. This reduction was recorded as an offset to restructuring expense in the period. In November 2007, we negotiated a break clause in the lease allowing for an early termination of the United Kingdom facility which released us from any future rent liabilities subsequent to January 2008. All termination payments have now been made.

In July 2005, we undertook an approximate 10% reduction in our workforce. In connection with this action, we incurred a one-time cash expense of approximately \$1.1 million in the fourth quarter ended September 30, 2005 for severance benefits. As of March 31, 2008, \$0.1 million of the cash charges remains outstanding.

During fiscal year 2002, we restructured several areas of the Company to reduce expenses and improve revenues. As part of this restructuring, we closed an office facility in Boston, Massachusetts and recorded an expense associated with the long-term lease which expires in January 2011. During the three months ended March 31, 2007, we completed a new sublease with a sub-lessee for the remaining term of our lease at a rate lower than that which was forecasted when the original restructuring expense was recorded in 2002. This change in estimate resulted in a \$0.3 million restructuring expense for the year ended September 30, 2007.

Past Results may not be Indicative of Future Performance. We believe that period-to-period comparisons of our operating results should not be relied upon as indicative of future performance. Our prospects must be considered given the risks, expenses and difficulties frequently encountered by companies in early stages of development,

particularly companies in rapidly evolving businesses. There can be no assurance we will be successful in addressing these risks and difficulties. Moreover, we may not achieve or maintain profitability in the future.

Critical Accounting Estimates

Our discussion and analysis of our financial condition and results of operations are based upon our Condensed Consolidated Financial Statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities.

On an on-going basis, we evaluate the estimates, including those related to our allowance for doubtful accounts, valuation of stock-based compensation, valuation of goodwill and intangible assets, valuation of deferred tax assets, restructuring expenses, contingencies, vendor specific objective evidence, or VSOE, of fair value in multiple element arrangements and the estimates associated with the percentage-of-completion method of accounting for certain of our revenue contracts. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities and the recognition of revenue and expenses that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Table of Contents

We believe the following critical accounting judgments and estimates are used in the preparation of our Condensed Consolidated Financial Statements:

Revenue recognition, including estimating the total estimated time required to complete sales arrangements involving significant implementation or customization essential to the functionality of our products;

Estimating valuation allowances and accrued liabilities, specifically the allowance for doubtful accounts, and assessment of the probability of the outcome of our current litigation;

- Stock-based compensation expense;
- Accounting for income taxes;
- Valuation of long-lived and intangible assets and goodwill;
- Restructuring expenses; and
- Determining functional currencies for the purposes of consolidating our international operations.

Revenue Recognition. We derive revenues from licenses of our software and related services, which include assistance in implementation, customization and integration, post-contract customer support, training and consulting. The amount and timing of our revenue is difficult to predict and any shortfall in revenue or delay in recognizing revenue could cause our operating results to vary significantly from quarter to quarter and could result in operating losses. The accounting rules related to revenue recognition are complex and are affected by interpretation of the rules and an understanding of industry practices, both of which are subject to change. Consequently, the revenue recognition accounting rules require management to make significant estimates based on judgment.

Software license revenue is recognized in accordance with the AICPA's Statement of Position No. 97-2 "Software Revenue Recognition," as amended by Statement of Position No. 98-9 "Software Revenue Recognition with Respect to Certain Arrangements", or collectively SOP 97-2.

For arrangements with multiple elements, we recognize revenue for services and post-contract customer support based upon the fair value VSOE of the respective elements. The fair value VSOE of the services element is based upon the standard hourly rates we charge for the services when such services are sold separately. The fair value VSOE for annual post-contract customer support is generally established with the contractual future renewal rates included in the contracts, when the renewal rate is substantive and consistent with the fees when support services are sold separately. When contracts contain multiple elements and fair value VSOE exists for all undelivered elements, we account for the delivered elements, principally the license portion, based upon the "residual method" as prescribed by SOP 97-2. In multiple element transactions where VSOE is not established for an undelivered element, we recognize revenue upon the establishment of VSOE for that element or when the element is delivered.

At the time we enter into a transaction, we assess whether any services included within the arrangement related to significant implementation or customization essential to the functionality of our products. For contracts for products that do not involve significant implementation or customization that is essential to the product functionality, we recognize license revenues when there is persuasive evidence of an arrangement, the fee is fixed or determinable, collection of the fee is probable and delivery has occurred as prescribed by SOP 97-2. For contracts that involve significant implementation or customization essential to the functionality of our products, we recognize the license and professional consulting services revenue using either the percentage-of-completion method or the completed

contract method as prescribed by Statement of Position No. 81-1, "Accounting for Performance of Construction-Type and Certain Product-Type Contracts", or SOP 81-1.

The percentage-of-completion method is applied when we have the ability to make reasonably dependable estimates of the total effort required for completion using labor hours incurred as the measure of progress towards completion. The progress toward completion is measured based on the "go-live" date. We define the "go-live" date as the date the essential product functionality has been delivered or the application enters into a production environment or the point at which no significant additional Chordiant supplied professional service resources are required. Estimates are subject to revisions as the contract progresses to completion. We account for the changes as changes in accounting estimates when the information becomes known. Information impacting estimates obtained after the balance sheet date but before the issuance of the financial statements is used to update the estimates. Provisions for estimated contract losses, if any, are recognized in the period in which the loss becomes probable and can be reasonably estimated. When we sell additional licenses related to the original licensing agreement, revenue is recognized upon delivery if the project has reached the go-live date, or if the project has not reached the go-live date, revenue is recognized under the percentage-of-completion method. We classify revenues from these arrangements as license and service revenue based upon the estimated fair value of each element using the residual method.

Table of Contents

The completed contract method is applied when we are unable to obtain reasonably dependable estimates of the total effort required for completion. Under the completed contract method, all revenue and related costs of revenue are deferred and recognized upon completion.

For product co-development arrangements relating to software products in development prior to the consummation of the individual arrangements where we retain the intellectual property being developed and intend to sell the resulting products to other customers, license revenue is deferred until the delivery of the final product, provided all other requirements of SOP 97-2 are met. Expenses associated with these co-development arrangements are accounted for under SFAS 86 and are normally expensed as incurred as they are considered to be research and development costs that do not qualify for capitalization or deferral.

Revenue from subscription or term license agreements, which include software and rights to unspecified future products or maintenance, is recognized ratably over the term of the subscription period. Revenue from subscription or term license agreements, which include software, but exclude rights to unspecified future products and maintenance, is recognized upon delivery of the software if all conditions of recognizing revenue have been met including that the related agreement is non-cancelable, non-refundable and provided on an unsupported basis.

For transactions involving extended payment terms, we deem these fees not to be fixed or determinable for revenue recognition purposes and revenue is deferred until the fees become payable and due.

For arrangements with multiple elements accounted for under SOP 97-2 where we determine we can account for the elements separately and the fees are not fixed or determinable due to extended payment terms, revenue is recognized in the following manner. If the undelivered element is PCS, or other services, an amount equal to the estimated value of the services to be rendered prior to the next payment becoming due is allocated to the undelivered services. The residual of the payment is allocated to the delivered elements of the arrangement.

For arrangements with multiple elements accounted for under SOP 81-1 where we determine we can account for the elements separately and the fees are not fixed or determinable due to extended payment terms, revenue is recognized in the following manner. Amounts are first allocated to the undelivered elements included in the arrangement, as payments become due or are received, the residual is allocated to the delivered elements.

We recognize revenue for post-contract customer support ratably over the support period which ranges from one to five years.

Our training and consulting services revenues are recognized as such services are performed on an hourly or daily basis for time and material contracts. For consulting services arrangements with a fixed fee, we recognize revenue on a percentage-of-completion method.

For all sales we use either a signed license agreement or a binding purchase order where we have a master license agreement as evidence of an arrangement. Sales through our third party systems integrators are evidenced by a master agreement governing the relationship together with binding purchase orders or order forms on a transaction-by-transaction basis. Revenues from reseller arrangements are recognized on the "sell-through" method, when the reseller reports to us the sale of our software products to end-users. Our agreements with customers and resellers do not contain product return rights.

We assess collectibility based on a number of factors, including past transaction history with the customer and the credit-worthiness of the customer. We generally do not request collateral from our customers. If we determine that the collection of a fee is not probable, we recognize revenue at the time collection becomes probable, which is generally

upon the receipt of cash.

Allowance for Doubtful Accounts. We must make estimates of the uncollectability of our accounts receivables. We specifically analyze accounts receivable and analyze historical bad debts, customer concentrations, customer credit-worthiness and current economic trends when evaluating the adequacy of the allowance for doubtful accounts. Generally, we require no collateral from our customers. Our gross accounts receivable balance was \$26.2 million (including long-term accounts receivable of \$0.1 million) with an allowance for doubtful accounts of \$0.2 million as of March 31, 2008. Our gross accounts receivable balance was \$28.5 million (including long-term accounts receivable of \$1.0 million) with an allowance for doubtful accounts of \$0.2 million as of September 30, 2007. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances would be required. To date, bad debts have not been material and have been within management's expectations.

Stock-based Compensation Expense. Upon adoption of SFAS 123(R) on October 1, 2005, we began estimating the value of employee stock awards on the date of grant using the Black-Scholes model. Prior to the adoption of SFAS 123(R), the value of each employee stock award was estimated on the date of grant using the Black-Scholes model for the purpose of the pro forma financial disclosure in accordance with SFAS 123. The determination of fair value of share-based payment awards on the date of grant using an option-pricing model is affected by our stock price as well as assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to the expected stock price volatility over the term of the awards, and actual and projected employee stock option exercise behaviors.

Table of Contents

With the adoption of SFAS 123(R) on October 1, 2005, we used the trinomial lattice valuation technique to determine the assumptions used in the Black-Scholes model. The trinomial lattice valuation technique was used to provide better estimates of fair values and meet the fair value objectives of SFAS 123(R). The expected term of options granted is derived from historical data on employee exercises and post-vesting employment termination behavior. The expected volatility is based on the historical volatility of our stock.

As stock-based compensation expense recognized in the Condensed Consolidated Statement of Operations is based on awards ultimately expected to vest, it has been reduced for estimated forfeitures. SFAS 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Forfeitures were estimated based on historical experience.

If factors change and we employ different assumptions in the application of SFAS 123(R) in future periods, the compensation expense that we record under SFAS 123(R) may differ significantly from what we have recorded in the current period. The estimated value of a stock option is most sensitive to the volatility assumption. Based on the March 31, 2008 variables, it is estimated that a change of 10% in either the volatility, expected life or interest rate assumption would result in a corresponding 8%, 5% or 1% change, respectively, in the estimated value of the option being valued using the Black-Scholes model.

As stock-based compensation expense attributable to performance restricted stock units, or RSUs, is based on management's assessment of the likelihood of achieving certain criteria, the amount of expense that is recorded in a period is dependent on the accuracy of management's estimates. It is estimated that a 5% change in management's achievement estimates would result in a corresponding 52% change in the stock compensation expense recorded for the period. The RSUs granted vest at the end of fiscal year 2009 if certain specified performance criteria are achieved. It is expected that estimates will become more accurate leading up to September 30, 2009.

Accounting for Income Taxes. As part of the process of preparing our Condensed Consolidated Financial Statements we are required to estimate our income taxes in each of the jurisdictions in which we operate. This process involves estimating our actual current tax exposure together with assessing temporary differences resulting from differing treatment of items, such as deferred revenue, for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within our Condensed Consolidated Balance Sheets. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income and to the extent we believe that recovery is not likely, we must establish a valuation allowance. To the extent we establish a valuation allowance or increase this allowance in a period, we must include an expense within the tax provision in the Statement of Operations.

We have recorded a valuation allowance equal to 100% of the deferred tax assets as of March 31, 2008, due to uncertainties related to our ability to utilize our net deferred tax assets, primarily consisting of certain net operating loss carryforwards, research and development credits and temporary differences relating to deferred revenue. Deferred tax assets have been fully reserved for in all periods presented.

Effective October 1, 2007, the Company adopted Financial Accounting Standards Interpretation, No. 48 "Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109" or FIN 48. FIN 48 prescribes a recognition threshold and measurement guidance for the financial statement reporting of uncertain tax positions taken or expected to be taken in a company's income tax return. The application of FIN 48 is discussed in Note 11 to the Condensed Consolidated Financial Statements.

Valuation of Long-lived and Intangible Assets and Goodwill. We assess the impairment of identifiable intangibles and long-lived assets whenever events or changes in circumstances indicate that the carrying value may not be

recoverable. Furthermore, we assess the impairment of goodwill annually. Factors we consider important which could trigger an impairment review include the following:

- Significant underperformance relative to expected historical or projected future operating results;
 - Significant changes in the manner of our use of the acquired assets or the strategy for our overall business;
 - Significant negative industry or economic trends;
 - Significant decline in our stock price for a sustained period;
 - Market capitalization declines relative to net book value; and
- A current expectation that, more likely than not, a long-lived asset will be sold or otherwise disposed of significantly before the end of its previously estimated useful life.

Table of Contents

When one or more of the above indicators of impairment occurs we estimate the value of long-lived assets and intangible assets to determine whether there is impairment. We measure any impairment based on the projected discounted cash flow method, which requires us to make several estimates including the estimated cash flows associated with the asset, the period over which these cash flows will be generated and a discount rate commensurate with the risk inherent in our current business model. These estimates are subjective and if we made different estimates, it could materially impact the estimated fair value of these assets and the conclusions we reached regarding impairment. To date, we have not identified any triggering events noted above. While the recent decline in our stock price and negative economic trends have lowered our market capitalization at March 31, 2008, our market capitalization is still at the levels significantly higher than our book value.

We are required to perform an impairment review of our goodwill balance on at least an annual basis. This impairment review involves a two-step process as follows:

Step 1—We compare the fair value of our reporting units to the carrying value, including goodwill, of each of those units. For each reporting unit where the carrying value, including goodwill, exceeds the unit's fair value, we proceed on to Step 2. If a unit's fair value exceeds the carrying value, no further work is performed and no impairment charge is necessary.

Step 2—We perform an allocation of the fair value of the reporting unit to our identifiable tangible and non-goodwill intangible assets and liabilities. This derives an implied fair value for the reporting unit's goodwill. We then compare the implied fair value of the reporting unit's goodwill with the carrying amount of the reporting unit's goodwill. If the carrying amount of the reporting unit's goodwill is greater than the implied fair value of its goodwill, an impairment charge would be recognized for the excess.

We determined that we have one reporting unit. We completed a goodwill impairment review for the period ending September 30, 2007 and performed Step 1 of the goodwill impairment analysis required by SFAS 142, "Goodwill and Other Intangible Assets," and concluded that goodwill was not impaired as of September 30, 2007 using the methodology described above. Accordingly, Step 2 was not performed. We will continue to test for impairment on an annual basis and on an interim basis if an event occurs or circumstances change that would more likely than not reduce the fair value of our reporting units below their carrying amount.

Restructuring Expenses. In the past five years, we have implemented cost-reduction plans as part of our continued effort to streamline our operations to reduce ongoing operating expenses. These plans resulted in restructuring expenses related to, among others, the consolidation of excess facilities. These charges relate to facilities and portions of facilities we no longer utilize and either seek to terminate early or sublease. Lease termination costs and brokerage fees for the abandoned facilities were estimated for the remaining lease obligations and were offset by estimated sublease income. Estimates related to sublease costs and income are based on assumptions regarding the period required to locate and contract with suitable sub-lessees and sublease rates which can be achieved using market trend information analyses provided by a commercial real estate brokerage retained by us. Each reporting period we review these estimates and to the extent that these assumptions change due to new agreements with landlords, new subleases with tenants, or changes in the market, the ultimate restructuring expenses for these abandoned facilities could vary by material amounts.

Determining Functional Currencies for the Purpose of Consolidation. We have several foreign subsidiaries that together account for a significant portion of our revenues, expenses, assets and liabilities.

In preparing our Condensed Consolidated Financial Statements, we are required to translate the financial statements of the foreign subsidiaries from the currency in which they keep their accounting records, generally the local currency,

into United States dollars. This process results in exchange gains and losses which, under the relevant accounting guidance are either included within the Condensed Consolidated Statement of Operations or as a separate part of our net equity under the caption "Accumulated Other Comprehensive Income." Under the relevant accounting guidance, the treatment of these translation gains or losses is dependent upon our management's determination of the functional currency of each subsidiary. The functional currency is determined based on management's judgment and involves consideration of all relevant economic facts and circumstances affecting the subsidiary. Generally, the currency in which the subsidiary conducts a majority of its transactions, including billings, financing, payroll and other expenditures would be considered the functional currency but any dependency upon the parent and the nature of the subsidiary's operations must also be considered.

If any subsidiary's functional currency were deemed to be the local currency, then any gain or loss associated with the translation of that subsidiary's financial statements would be included in cumulative translation adjustments. However, if the functional currency were deemed to be the United States dollar then any gain or loss associated with the translation of these financial statements would be included within our Condensed Consolidated Statement of Operations. If we dispose of any of our subsidiaries, any cumulative translation gains or losses would be recognized in our Condensed Consolidated Statement of Operations. If we determine that there has been a change in the functional currency of a subsidiary to the United States dollar, any translation gains or losses arising after the date of change would be included within our Condensed Consolidated Statement of Operations.

Table of Contents

Based on our assessment of the factors discussed above, we consider the relevant subsidiary's local currency to be the functional currency for each of our international subsidiaries. Accordingly, foreign currency translation gains and losses are included as part of Accumulated Other Comprehensive Income within our Condensed Consolidated Balance Sheets for all periods presented.

The magnitude of these gains or losses is dependent upon movements in the exchange rates of the foreign currencies in which we transact business against the United States dollar. These currencies include the United Kingdom Pound Sterling, the Euro and the Canadian Dollar. Any future translation gains or losses could be significantly larger or smaller than those reported in previous periods. At March 31, 2008, approximately \$41.7 million of our cash and cash equivalents were held by our subsidiaries outside of the United States.

Recent Accounting Pronouncements

See Note 2 to the Condensed Consolidated Financial Statements under section "Recent Accounting Pronouncements" for detailed information regarding status of new accounting standards that are not yet effective for us.

Table of Contents

Results of Operations

The following table sets forth, in dollars and as a percentage of total revenues, unaudited Condensed Consolidated Statements of Operations data for the periods indicated. This information has been derived from the Condensed Consolidated Financial Statements included elsewhere in this Quarterly Report (in thousands, except percentages):

	Three Months Ended March 31, 2008		2007		Six Months Ended March 31, 2008		2007	
Statements of Operations								
Data:								
Revenues:								
License	\$ 4,807	19%	\$ 18,882	58%	\$ 13,614	25%	\$ 26,044	47%
Service	19,909	81	13,883	42	40,236	75	29,660	53
Total revenues	24,716	100	32,765	100	53,850	100	55,704	100
Cost of revenues:								
License	283	1	583	2	617	1	1,037	2
Service	8,532	35	5,622	17	17,010	32	13,088	23
Amortization of intangible assets	303	1	303	1	606	1	606	1
Total cost of revenues	9,118	37	6,508	20	18,233	34	14,731	26
Gross profit	15,598	63	26,257	80	35,617	66	40,973	74
Operating expenses:								
Sales and marketing	7,400	30	8,314	25	16,303	30	15,578	28
Research and development	6,381	26	7,296	23	13,106	24	13,592	24
General and administrative	4,019	16	5,295	16	9,022	17	10,906	20
Restructuring expense	—	—	255	1	—	—	6,727	12
Total operating expenses	17,800	72	21,160	65	38,431	71	46,803	84
Income (loss) from operations	2,202	(9)	5,097	15	(2,814)	(5)	(5,830)	(10)
Interest income, net	613	3	492	2	1,448	2	796	2
Other income, net	350	1	180	—	485	1	165	—
Income (loss) before income taxes	(1,239)	(5)	5,769	17	(881)	(2)	(4,869)	(8)
Provision for (benefit from) income taxes	(80)	—	794	2	73	—	905	2
Net income (loss)	\$ (1,159)	(5)%	\$ 4,975	15%	\$ (954)	(2)%	\$ (5,774)	(10)%

Comparison of the Three and Six Months Ended March 31, 2008 and 2007 (Unaudited)

Revenues

Total revenues decreased \$8.0 million, or 25%, to \$24.7 million for the three months ended March 31, 2008 compared to \$32.8 million for the three months ended March 31, 2007. This decrease was primarily due to a \$14.1 million or 75% decrease in license revenue offset by an increase of \$6.0 million or 43% in service revenue. Total revenues decreased \$1.9 million, or 3%, to \$53.8 million for the six months ended March 31, 2008 compared to \$55.7 million for the six months ended March 31, 2007. This decrease was primarily due to \$12.4 million or 48% decrease in license revenue offset by an increase of \$10.5 million or 36% in service revenue.

The following summarizes the components of our total revenues:

License Revenue

The increase or decrease of license revenue occurring within the three different product emphases is dependent on the timing of when a sales transaction is completed and whether a license transaction was sold with essential consulting services. License revenue sold with essential consulting services is recognized under percentage-of-completion method of accounting. The timing and amount of revenue for those transactions being recognized under the percentage-of-completion is influenced by progress of work performed relative to the project length of customer contracts and the dollar value of such contracts. These orders typically involve consulting services that are essential to functionality of the respective licenses. The following table sets forth our license revenue by product emphasis for the three and six months ended March 31, 2008 and 2007 (in thousands, except percentages):

Table of Contents

	Three Months Ended March 31,				Six Months Ended March 31,			
	2008	2007	Change	%	2008	2007	Change	%
License Revenue:								
Enterprise solutions	\$ 3,870	\$ 12,619	\$ (8,749)	(69)%	\$ 10,084	\$ 16,164	\$ (6,080)	(38)%
Marketing solutions	579	1,268	(689)	(54)	1,293	2,257	(964)	(43)
Decision management solutions	358	4,995	(4,637)					