AGILE SOFTWARE CORP
Form 10-K
July 14, 2004
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C.

FORM 10-K

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended April 30, 2004

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 000-27071

AGILE SOFTWARE CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**77-0397905**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

6373 San Ignacio Avenue, San Jose, California 95119-1200

(Address of principal executive office)

(408) 284-4000

(Registrant s telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

None

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, $0.001 par value

(Title of class)

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Securities Exchange Act of 1934). Yes x No ¨

The aggregate market value of Agile Software Corporation Common stock, $0.001 par value, held by non-affiliates as of October 31, 2003 was $393,005,768 based upon the last sales price reported for such date on the NASDAQ National Market on October 31, 2003. For purposes of this disclosure, shares of Common Stock held by persons who held more than 5% of the outstanding shares of Common Stock and shares held by officers and directors of the registrant, have been excluded in that such persons may be deemed to be affiliates. Share ownership information of certain persons known by the Registrant to own greater than 5% of the outstanding Common Stock for purposes of the preceding calculation is based solely on information on Schedule 13F or 13G filed with the Securities and Exchange Commission and is as of October 31, 2003. The determination of affiliate status is not necessarily a conclusive determination for other purposes.

The number of shares of Common Stock of Agile Software Corporation issued and outstanding as of June 30, 2004 was 52,501,741.

DOCUMENTS INCORPORATED BY REFERENCE

The registrant has incorporated by reference into Part III of this Form 10-K portions of its proxy statement for the registrant s Annual Meeting of Stockholders to be held on September 21, 2004, which definitive proxy statement will be filed with the Securities and Exchange Commission within 120 days after the fiscal year to which this Report relates.

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AGILE SOFTWARE CORPORATION

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APRIL 30, 2004

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PART I

ITEM 1. BUSINESS

Overview

We develop and sell an integrated suite of product lifecycle management (PLM) software products and offer related business consulting and implementation services. Our solutions enable our customers to accelerate their time-to-market and revenue, reduce costs, improve product quality, ensure regulatory compliance and drive innovation throughout the product lifecycle. Alcatel, Boeing Service Company, Dell Computer Products, Flextronics International, Hitachi Corporation, LeapFrog Enterprises, Lockheed Martin Missile and Fire Control, Magna Steyr, Siemens A&D, QUALCOMM Corporation and ZF are among the nearly 1200 customers that have licensed Agile PLM solutions.

We focus solely on providing PLM solutions to companies in the electronics and high technology, industrial products, life sciences and other industries. Our strategy is to deliver business-ready solutions to streamline the information and process flow within a company s product operation, that are easy to implement and maintain, and that provide measurable results. Our strategy is industry-focused with product capabilities tailored to the requirements of our target industries. We sell our product through a direct sales channel and distributors.

Since late 2002, in addition to deploying additional sales and support coverage throughout the world and enhancing our core product line, we have chosen to expand our product offerings and increase our revenues by acquiring complementary businesses and technologies. We have closed four acquisitions since then. oneRev was acquired in December 2002, providing component technology to facilitate the process of product information exchange between disparate business systems across the global supply chain. ProductFactory, a company offering program planning and execution solution, was acquired in March 2003. We acquired Tradec, a provider of direct materials cost and performance management solutions, in October 2003 to fill out the Agile Product Cost Management solution. In August 2003, we acquired Eigner, a Product Lifecycle Management solutions provider focused primarily on the industrial products, including automotive supply chain, aerospace and defense and machinery market. This acquisition broadened the base of solutions we offer customers in the industrial products market and provided us with a strong European sales, support, and research and development presence. As opportunities to acquire additional companies, technology, and resources arise, we may consider additional acquisitions in the future.

Industry Background

For product-oriented companies, delivering products to market is increasingly complex. As companies move to global, outsourced design, manufacturing and service operations, and face increasing regulatory compliance concerns, the processes that people must follow to complete their work can no longer be handled with paper or inefficient information technology approaches. There are several business processes that companies struggle to modernize to remain competitive and address the regulatory and other compliance requirements. These include:

New Product Development and Introduction. The lifecycles of many products are very short. In order to compete effectively, companies need to be able to introduce new or enhanced products quickly and cost effectively. Products that are late to market, do not satisfy market requirements or have quality problems can severely impact the business, market share and financial results of companies.

Customer Needs Management. Understanding what the customer wants, whether for mass-produced products or small quantity, engineered-to-order products, is critical to gaining customer acceptance of a company s products. Manufacturers that cannot manage customer needs will suffer market share erosion, costly project overruns and liability for contract non-compliance.

Direct Materials Sourcing. As manufacturers outsource more and more of their production requirements, including in many cases engineering activities, to third-party suppliers, they no longer have direct control over the internal procedures used to design and build their products. To insure high quality,

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cost effective and timely availability of products, product information and changes must be communicated effectively across a very complex, global supply chain.

Volume Production and Product Changes. As a product transitions during its lifecycle from proof-of-concept and prototype to volume production, it is critical to link the proper design and planning information with production systems to build physical products. Communication of pending changes and quality trends across the enterprise is needed to ensure the right products are being built per customer, market and engineering requirements.

Product Serviceability. High quality customer service is an important differentiator for manufacturers. Not only is it important to capture and incorporate field service feedback in the development of new and improvement of existing products, but it is also important to communicate effectively product changes to service organizations for equipment that requires repair or overhaul.

Compliance. Whether driven by regulatory agencies such as the Federal Drug Administration or Department of Defense, industry standards like STEP, customer requirements or internal policies, companies need to comply with regulations and policies and be able to provide proof of compliance on demand. Clear, auditable records of what and why product decisions were made, by whom, and when are critical elements necessary to satisfy product compliance.

Recently, awareness of the impact that operational improvements in the business areas listed above can have on companies profitability, product innovation, market acceptance of their products, compliance, and quality has increased. A market category called ***Product Lifecycle Management (PLM)*** has emerged over the past several years that describes the investments made by companies in the strategy, business process change and technology underlying their products as well as in the organizations responsible for manufacturing products in order to improve operational efficiency.

Companies, both large and small, domestic or global, face similar challenges. Companies in industries such as electronics and high technology, industrial products, life sciences and other industries, have made investments in PLM solutions and strategies.

The Agile PLM Solution

At the core of the Agile PLM solution is the product record, the complex set of information that uniquely defines all aspects of a product at each stage of its lifecycle.

The product record includes the data about the product that manufacturers conceptualize, design, plan, build, sell, service and dispose of, including program plans, portfolio performance, design databases, configuration changes, planned and actual costs, decision documentation and problem reports. The product record also includes the processes by which companies manage their product operation such as change control procedures, direct materials sourcing, corrective and preventive action and compliance auditing. In total, the product record is the key asset underlying products that, when managed well, can significantly improve the productivity of a company allowing it to get products to market faster, improve profitability, and be sure their products and processes comply with applicable regulations.

Described below are the principal software products we offer. Many of these products are tightly integrated and may be purchased and used as combined solution set.

Agile Product Collaboration / Product Data Management. Agile Product Collaboration manages product information including bills of material, documentation, engineering and manufacturing changes, configurations, and mechanical, electrical and software design and analysis databases, providing visibility to this information throughout the extended enterprise and streamlining the product development and delivery process.

Agile Product Portfolio Management. Agile Product Portfolio Management manages program, project and product information across the product lifecycle. This enables organizations to optimize resource allocation,

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product investment and program execution decisions by assessing key performance indicators such as schedule, cost and past portfolio financial performance.

Agile Product Cost Management. Agile Product Cost Management provides product cost intelligence between internal design and sourcing functions on the one hand and external supplier and partners on the other hand, and is used to streamline the direct materials sourcing process. Using Agile Product Cost Management, customers can plan and manage critical cost, commercial terms and other key product information early and throughout the product lifecycle. This enables users to achieve product total cost goals by promoting the use of preferred suppliers, aggregating demand across multiple organizations for greater buying power, and sharing product information across the supply chain.

Agile Product Service & Improvement. Agile Product Service & Improvement integrates customer, product, quality and regulatory information with the product record in order to track and rapidly address product quality issues. Using Agile Product & Service Improvement, customers are able to drive proactive product quality improvement and lower the costs (warranty and service expenses) associated with quality issues.

Agile Product Governance & Compliance. Agile Product Governance & Compliance enables organizations to manage product and program compliance against internal and external standards and regulatory requirements, providing assurance of effective compliance throughout the product lifecycle.

Agile Product Catalog. Agile Product Catalog provides a central repository for storing and aggregating technical product information, including specifications, parts, documents and CAD files, and product attributes. Through components classification, information can be classified, making easy to find and reuse for initiatives such as data exchange between customers and suppliers or developing marketing and sales programs and collateral.

Agile Requirements Management. Agile Requirements Management facilitates the requirements management and product planning processes by linking customers, sales, marketing, engineering, and manufacturing more closely, and providing a single, unified environment to capture and manage product requirements and data. Agile Requirements Management helps companies ensure that the actual product meets the specifications of the original product plan.

Agile Configuration Management. Agile Configuration Management extends core configuration management capabilities by providing configuration control linked to serial numbers that is integrated with the change identification and management process. Agile Configuration Management enables manufacturers of complex, heavily regulated or highly customizable products, such as Aerospace & Defense suppliers, to ensure that the product delivered meets the customer s exact specifications. It also ensures that each unique configuration can be tracked and identified.

Agile Maintenance Repair & Overhaul. Agile Maintenance Repair and Overhaul enables manufacturers to plan and execute maintenance, repair and overhaul activities, providing an electronic audit trail between the as-delivered product and the current in-service configuration. Fully integrated with Agile PLM solutions, Agile Maintenance Repair & Overhaul links change activities and facilitates feedback between engineering, production, sales/marketing and field service personnel.

Agile Engineering Collaboration. Agile Engineering Collaboration manages the complex design databases created by mechanical CAD, electronic CAD and design automation, software configuration management, and document authoring tools within the context of the Product

Record ensuring that the correct version of the product design is being used at all times across the organization. Moreover, rich product information is made available to people outside of engineering through easy-to-use visualization and collaboration tools eliminating the need for paper drawings and documentation.

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The Agile PLM Platform

Agile currently offers products based on two technology platforms. The latest version of the Agile PLM platform (upon which the recently released Agile 9 product suite operates) includes the element described below. Agile PLM e5.1 (formerly Eigner PLM) has a separate but similar set of platform features. Going forward, we intend to migrate the product families onto a common platform.

Agile User Interface Framework. The Agile UI Framework leverages configurable, prepackaged portlets to deliver content or services within customer portals. Portlets expose key services and user interface components in the Agile PLM platform as standard services that can be embedded seamlessly into a corporate or exchange portal. These portlets comply with industry standards and are certified with leading portal technologies, including IBM Websphere, to enable plug and play integration.

Agile Integration Framework. The Agile Integration Framework provides a comprehensive set of capabilities to enable integration between Agile PLM applications and other applications including MRP, ERP, CRM and internally developed business systems. Leveraging Internet standards such as XML and messaging as the primary vehicle for system-to-system communication enables rapid deployment of integrations and also reduces the overhead associated with ongoing maintenance. Standard adapters for systems such as SAP and J.D. Edwards are available and with partners offering several of their own system adaptors.

Agile Analytics Framework. Agile Analytics Framework provides a single point of access for all reporting functionality, including ad-hoc querying of the product record. Users can generate new reports from within Agile PLM without requiring a separate reporting application. Agile roles and discovery privileges enforce robust access control and data security.

Agile Content Framework. The Agile Content Framework links the product record in real-time to component information dispersed throughout the supply chain enabling evaluation and consolidation of manufacturer, enterprise and supplier information obtained from dispersed sources for optimal decision making throughout the product lifecycle. Component, Bill of Material and Approved Manufacturer / Vendor List data can be analyzed, cleansed, and mapped to consolidate product information coming from multiple sources like component catalogs into a usable asset for the engineering and sourcing organizations.

Agile Common Services. Agile PLM solutions are built on a common services oriented architecture (Agile Common Services), which offers tremendous flexibility and ease of administration. The use of common services minimizes configuration and maintenance and provides consistency across applications. Key components of the services architecture are electronic workflow, event subscription and notification, directory service integration (e.g., LDAP), advanced document handling, full text search, advanced security, and support for global localization requirements.

The Agile Strategy

Key elements in our strategy for achieving success are:

Focus on Customer Success Our top objective is to have 100% of our customers successfully implement and receive measurable financial benefits and operating improvements from their Agile PLM solutions. According to study by AMR Research, Inc., an independent research company, in fiscal 2003, our clients had the highest level of satisfaction in terms of product performance and capabilities, sales experience, and service and support provided during the implementation and upgrading.

Solutions Focused We are focused on helping companies improve the efficiency of their product operations by providing targeted solutions, with built in best practices. Rather than providing just technology we focus on delivering solutions that measurably improve our customers product operations and, as a result, their financial performance.

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Rapid Time To Benefit our research and development activities and implementation methodologies are specifically aimed at creating solutions that can be rapidly deployed by our customers in even the largest and most complex situations. Many of our customers have implemented our software solutions in 90 to 120 days.

Guaranteed Business Results Under this unique program, purchases by our customers of our software solutions are tied to results. Customers demand low risk, high impact, and cost effective solutions. The Guaranteed Business Results program allows customers to mitigate project risk by tying purchases of our software licenses to the achievement of previously agreed business results that are base on measurable metrics. This program demonstrates our commitment to solving our customer s critical business problems by sharing risks and aligning our interests.

Focused Acquisition We have and expect to continue to more rapidly expand our product footprint and our customer base through acquisition of companies and complementary technologies. Consistent with this strategy, we have acquired four companies or businesses as described in more detail elsewhere in this annual report.

Customers

To date, we have licensed our products to nearly 1,200 customers. No customer accounted for more than ten percent of our total revenues for fiscal 2004, 2003, or 2002.

We target our sales efforts to customers in four market categories:

> *Electronics & High Technology*. This category includes companies in the following businesses: computers and peripherals; consumer electronics; networking and telecommunications equipment; semiconductor equipment; and contract manufacturing services.
>
> *Industrial Products.* This category includes companies in the following businesses: automotive supply chain; aerospace and defense; and machinery and heavy equipment.
>
> *Life Sciences.* This category includes companies in the following businesses: biotechnology; pharmaceutical; and medical devices.
>
> *Others.* This category includes companies in the following businesses: consumer packaged goods and products; apparel; and software.

The following is a representative list of current customers in our targeted market categories:

Electronics & High Technology	Industrial Products
Brocade Communications System	Alps Automotive, Inc.

Celestica, Inc.	Ballard Power Systems
Dell Computer Products	Ball Aerospace & Technologies Corp
Flextronics International	BE Aerospace Business Jet Division
Foxconn (Hon Hai Precision Industry)	Boeing Service Company
Hitachi Corporation	Dana Corporation
Jabil Circuit, Inc.	ESCO, Inc.
Lucent Technologies	Harley Davidson/Buell Motorcycle Corporation Hartzell Propeller
Matsushita Electric Industrial	Heidenhain
Microsoft Xbox	Intertechnique
NEC Corporation	Keiper
Network Appliance	Lockheed Martin Missile and Fire Control
Qualcomm Corporation	Magna Steyr
Quanta Computers	Metaldyne, Inc.
Sanmina-SCI Systems	Saturn Electronics and Engineering, Inc.
Siemens	Siemens A&D
Solectron Corporation	ZF
TiVo	
ViaSat, Inc.	

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Life Sciences	**Others**
Draeger Medical AG and Co	Chantelle
GE Medical Systems	ETA
GlaxoSmithKline Plc.	International Paper Evergreen Packaging
Hill-Rom Company, Inc.	LeapFrog Enterprises
Hologic, Inc.	National Weather Service
Invitrogen Corporation	Playtex, Inc.
Johnson & Johnson	Rock-Tenn Alliance Group
Medtronic, Inc.	

Sales and Marketing

We market and sell our products primarily through our direct sales force. Our sales force is based at our headquarters in San Jose, California, and at regional and local sales offices in the United States. Internationally, we maintain sales offices in Austria, Germany, Japan, Taiwan, Switzerland and the United Kingdom. We also complement our direct sales force through additional distribution channels, including non-exclusive distributors, systems integrators and consulting partners.

To support our direct sales efforts and to actively promote our Agile brand, we engage in a variety of marketing activities. These include co-marketing strategies with our existing business partners, targeting additional strategic relationships, managing and maintaining our web site content, advertising in industry and other publications, conducting public relations campaigns and establishing and maintaining relationships with recognized industry analysts. We also actively participate in trade shows and host Agility, our annual user conference.

An element of our sales strategy is to establish marketing alliances to promote sales and marketing of our products, as well as to increase product interoperability. We also pursue services alliances with consulting and integration firms to implement our software, provide customer support services, create customized customer presentations and demonstrations and endorse our products during the evaluation stage of the sales cycle. We currently have relationships with Deloitte Consulting, PRTM, BearingPoint, Hewlett Packard, Domain Systems, Inc., Sierra Atlantic and Strategic Information Group, Inc. for the implementation of our solutions.

Customer Care

Customer Care is a collection of services where we offer assistance in planning, managing, implementing and supporting our solutions, as well as helping ensure the long-term success of our customer relationships. The services that we offer include solution delivery, customer support, and training.

Solution Delivery. We offer services, on a time and materials or fixed price basis, to assist in implementation planning, product installation, implementation assistance, legacy data loading and effectiveness audits. To facilitate and enhance the integration of our products, we have both developed internal capabilities and expertise and entered into alliances to enable integration of our products with existing design, manufacturing, finance and supply chain systems. This approach allows us to focus on our core competencies and leverage our partners domain knowledge, which helps reduce time to market, both for our customers and us.

Customer Support. We believe that responsive technical support is a requirement for our continued growth. We provide technical support and unspecified product upgrades on a when-and-if available basis through our annual maintenance program. Customers generally purchase the first year of maintenance and support at the time they initially license one of our products. After the initial term of the license is complete, the customer may renew support, generally for a term of one year. Customer support is offered by telephone, email and fax and we also offer an Internet-based support that features frequently asked questions, technical alerts, product upgrades and updates, problem reporting and analysis, and self-help through our on-line knowledge base. In addition, in some cases our consulting and implementation partners provide customer support and maintenance.

Training. We offer a variety of classes and related materials to train our customers on system administration, upgrades and new releases. These classes are also available as part of our Train the Trainer program. Training classes are offered at our headquarters in San Jose, California, at our development center in Karlsruhe, Germany, at customer sites, and at other locations. To improve access to our explanatory materials, we offer on-line documentation contained on the compact discs for our products and from our web site for all our products. We also offer on-line help for the majority of our products. Customers can purchase additional documentation via our web site.

Product Development

Our product development objectives are to:

- Develop innovative solutions focused on the streamlining the flow of information and work processes across product operations of the extended manufacturing enterprise and supply chain;
- Develop solutions that are easy to use, implement, maintain, and upgrade and that focus on delivering the highest return on investment to our customers; and
- Utilize industry and technology standards where appropriate.

Our software development staff is divided into teams consisting of software engineers, architects, software quality assurance engineers, technical writers, and product and program managers. Working closely with our marketing department, we determine product functionality based upon market requirements, customer feedback, technical support and business consulting. We also try to incorporate standard technologies where possible to minimize research and development costs and ensure interoperability with other business solutions employed by our customers.

In January 2004, we formally released Agile PLM 9 for general availability to our customers. The major enhancements provided by this release focused on:

- Increasing the scalability of the product line through utilization of web technologies such as J2EE, commercial application server support, web services and XML;
- Integrating components acquired over the previous year including technology acquired from ProductFactory, Eigner, oneRev and Tradec; and
- Introducing new solutions to expand the solution footprint including the Agile Analytics Framework, Agile Integration Framework, Agile Product Governance & Compliance, Agile Product Portfolio Management, and Engineering Collaboration CAD Connectors. Additionally, several hundred enhancements were made to the core product modules.

In April 2004, we introduced Agile PLM e5.1 (formerly Eigner PLM) with the following major enhancements:

Support for the latest releases of technology components such as Oracle RDBMS;

Alignment of the product under the Agile brand;

Integration with Agile Product Portfolio Management; and

Enablement of web-based view, redline and markup.

We maintain global development operations and have development centers in San Jose, California, Karlsruhe, Germany, Bangalore, India, and Suzhou, China.

Product Technology and Architecture

Our PLM software is supported by a scalable technology platform that ensures that the applications are scalable, reliable and extensible. The n-tier, standards-based architecture of the Agile platform uses technologies such as J2EE, XML and commercial components to manage the product record across Agile s solutions, and

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integrates that information with other applications within the customer enterprise. The result is a cost-effective, easy to maintain enterprise business application suite that minimizes the need for complex custom or in-house software development. Key features of our technology platform include:

- Support for commercial component technologies including Oracle RDBMS and Oracle Application Server, BEA WebLogic Application Server, and IBM Websphere Portal Server;

- End user client access via HTML through Microsoft Internet Explorer or Netscape Navigator, a Java client or a Windows client;

- Integration with other systems of record in use by manufacturing enterprises such as MRP, ERP, and CRM as well as custom and internally developed business applications. Common commercial solutions that can be integrated with Agile PLM include SAP, Oracle Applications, J.D. Edwards, and Peoplesoft.

In addition, many of the Agile solutions are enabled for both single-byte and double-byte localization, and have been localized for English, Chinese, Japanese and German languages. We intend to provide localization for additional languages as market needs dictate.

We have entered into platform alliances to ensure that our products are based on industry standards and to enable us to take advantage of current and emerging technologies, including alliances with BEA, Sun Microsystems, Oracle and Microsoft. To promote development, definition, adoption, promotion and implementation of open standards that can be leveraged by our solutions, we work with several industry standards organizations such as the National Institute of Standards and Technology, National Electronics Manufacturing Initiative, Institute for Interconnecting and Packaging Electronic Circuits, RosettaNet, and World Wide Web Consortium.

Competition

The market for PLM solutions is relatively new, fragmented, rapidly changing and consolidating, and becoming increasingly competitive. We expect competition to persist and intensify, which could result in price reductions, reduced gross margins and loss of market share, any one of which could seriously harm our business. Competitors vary in size and in the scope and breadth of the products and services offered.

Principally we compete with the following:

- In-house and out-sourced custom development efforts by potential customers;

- Vendors of engineering information management software, such as Dassault Systems S.A., UGS, MatrixOne, Inc., and Parametric Technology Corporation;

- Vendors offering related enterprise software (e.g. ERP) who seek to extend the functionality of their products, such as Oracle Corporation and SAP;

- Niche and new-to-the market vendors that provide partial PLM solutions such as IDE and Arena Systems; and

- Vendors that are focused in regional markets.

We believe our solutions are differentiated from our competitors for the following reasons:

- Our research and development and marketing resources are focused on delivering PLM solutions that solve very specific business problems for our customers in the industries we serve;

- Our sales and services organizations are focused on achieving customer success and rapid time-to-benefit when using our solutions; and

- We provide cost-effective solutions that are easy to sell, implement, and maintain by our customers over the lifetime of deployment.

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We believe that our ability to compete depends on many factors both within and beyond our control, including:

- The performance, functionality, price, reliability and speed of implementation of our solutions;
- The timing and market acceptance of new products and product enhancements to our solutions;
- The quality of our customer service; and
- The effectiveness of our sales and marketing efforts.

Proprietary Rights

Our success and ability to compete depend upon our proprietary technology. We rely on patent, copyright, trade secret and trademark law to protect our proprietary information. As of June 30, 2004, we had one issued patent and 26 patent applications pending in the United States. In certain cases we have filed corresponding patent applications in other jurisdiction. We also typically enter into agreements with our employees, consultants and customers to control their access to and distribution of our software, documentation and other proprietary information. Nevertheless, a third party could copy or otherwise obtain our software or other proprietary information without authorization, or could develop software competitive to ours. Our means of protecting our proprietary rights may not be adequate and our competitors may independently develop similar technology, duplicate our products or design around patents that may be issued to us or our other intellectual property. In addition, the laws of some foreign countries do not protect our proprietary rights to as great an extent as do the laws of the United States of America, and we expect that it will become more difficult to monitor the use of our products if we increase our international presence.

We utilize third-party technology that is integrated with our products. Some of these products are re-sold directly by Agile or may be procured directly from the third party. We attempt to negotiate favorable contracts and obtain product infringement indemnification protection in contracts when we integrate third-party products and technology into our products. Third-party software may not continue to be available on commercially reasonable terms. If we cannot maintain licenses to this third-party software at an acceptable cost, shipments of our products could be delayed until equivalent software could be developed or licensed and integrated into our products. We do not believe that our business could be considered to be substantially dependent on any one of these license agreements, and none of these licenses are responsible for a significant amount of our revenues.

There has been a substantial amount of litigation in the software industry regarding intellectual property rights. It is possible that, in the future, third parties may claim that we, or our current or potential future products, infringe their intellectual property rights. We expect that software product developers and providers will increasingly be subject to infringement claims as the number of products and competitors in our industry segment grows and the functionality of PLM products begins to overlap with other software applications. Any claims, with or without merit, could be time-consuming, result in costly litigation, cause product shipment delays or require us to enter into royalty or licensing agreements. If our products were found to infringe a third party s proprietary rights, we could be required to enter into royalty or licensing agreements in order to continue to be able to sell our products. Royalty or licensing agreements, if required, may not be available on terms acceptable to us or at all, which could seriously harm our business.

Employees

As of April 30, 2004, we had a total of 527 employees. Of this total, 194 were in engineering, 143 were in sales and marketing, 132 were in professional services, including technical support and customer training, and 58 were in IT, finance and administration. We also retain independent contractors to support activities such as our professional services and product development. None of our employees are represented by a collective bargaining unit, and we have never experienced a work stoppage. We consider our relations with our employees to be good.

Available Information

We make available, free of charge, by link from our website at *www.agile.com* our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and any amendments to those reports as soon as reasonably practicable after we have electronically filed or furnished such materials to the Securities and Exchange Commission. Information contained on our website is not part of this report. In addition, our filings with the Securities and Exchange Commission maybe accessed through the Securities and Exchange Commission s EDGAR system at www.sec.gov. All statements made in any of our securities filings, including all forward-looking statements or information, are made as of the date of the document in which the statement is included, and we do not assume or undertake any obligation to update any of those statements or documents unless we are required to do so by law.

ITEM 2. PROPERTIES

Our headquarters are currently located in an 82,000 square foot facility in San Jose, California under a lease that expires in 2009. We lease offices for sales and service personnel in various locations in the United States of America as well as in Salzburg, Austria, Braknell, United Kingdom, Tokyo, Japan, Taipei, Taiwan and various locations in Germany. We also lease office space for our development centers in Bangalore, India, Suzhou, China and Karlsruhe, Germany. We own land (approximately 16,600 square feet) and an office building (approximately 5,400 square feet) for sales and service personnel in Egerkingen, Switzerland.

We believe our current facilities will be adequate to meet our needs for the foreseeable future.

ITEM 3. LEGAL PROCEEDINGS

On or around October 25, 2001, a class action lawsuit was filed in the Southern District of New York against Agile Software Corporation, Bryan D. Stolle and Thomas P. Shanahan (collectively the Agile Defendants) and several investment-banking firms that served as underwriters of our initial public offering and secondary offering. The case is now captioned *In re Agile Software, Inc. Initial Public Offering Securities Litigation*, 01 CIV 9413 (SAS), *related to In re Initial Public Offering Securities Litigation*, 21 MC 92 (SAS). The operative amended complaint is brought purportedly on behalf of all persons who purchased our Common Stock from August 19, 1999 through December 6, 2000. It alleges liability under Sections 11 and 15 of the Securities Act of 1933 and Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, on the grounds that the registration statement for the offerings did not disclose that: (1) the underwriters had agreed to allow certain customers to purchase shares in the offerings in exchange for excess commissions paid to the underwriters; and (2) the underwriters had arranged for certain customers to purchase additional shares in the aftermarket at predetermined prices. The amended complaint also alleges that false analyst reports were issued. No specific damages are claimed.

Similar allegations were made in other lawsuits challenging over 300 other initial public offerings and follow-on offerings conducted in 1999 and 2000. The cases were consolidated for pretrial purposes and all defendants moved to dismiss. On February 19, 2003, the Court dismissed the claims under the Securities Act of 1933 with respect to our initial public offering, but not the secondary offering. The Court denied the motion to dismiss the Section 10(a) claim against us, but granted the motion as to the individual defendants.

We have accepted a settlement proposal presented to all issuer defendants. In this settlement, plaintiffs will dismiss and release all claims against the Agile Defendants, in exchange for a contingent payment by the insurance companies collectively responsible for insuring the issuers in all of the IPO cases, and for the assignment or surrender of certain claims we may have against the underwriters. The Agile Defendants will not be required to make any cash payments in the settlement, unless the *pro rata* amount paid by the insurers in the settlement exceeds the amount of the insurance coverage, a circumstance which we do not believe will occur. The settlement will require approval of the Court, which cannot be assured, after class members are given the opportunity to object to the settlement or opt out of the settlement.

We are also subject to various other claims and legal actions arising in the ordinary course of business. While the outcome of these proceedings and claims cannot be predicted with certainty, we do not believe that the ultimate disposition of these matters will have a material effect on our business, financial condition or results of operations.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of security holders during the fourth quarter of fiscal 2004.

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PART II

ITEM 5. MARKET FOR THE REGISTRANT S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Our Common Stock is traded on the NASDAQ National Market under the symbol AGIL. The price range per share reflected in the table below represents the high and low closing sales prices for our stock for the periods set forth, as reported by the NASDAQ National Market.

	High	Low
Fiscal 2004:		
Quarter Ended April 30, 2004	$ 10.82	$ 7.55
Quarter Ended January 31, 2004	$ 12.19	$ 9.21
Quarter Ended October 31, 2003	$ 11.30	$ 8.18
Quarter Ended July 31, 2003	$ 10.55	$ 6.40
Fiscal 2003:		
Quarter Ended April 30, 2003	$ 7.60	$ 5.88
Quarter Ended January 31, 2003	$ 9.14	$ 6.15
Quarter Ended October 31, 2002	$ 7.47	$ 5.11
Quarter Ended July 31, 2002	$ 8.60	$ 5.41

At June 30, 2004, we had 210 stockholders of record. The number of beneficial stockholders of our shares is greater than the number of stockholders of record. The last reported sale price of our Common Stock on June 30, 2004 was $8.75. Our present policy is to retain earnings, if any, to finance future growth. We have never paid cash dividends and have no present intention to pay cash dividends.

We did not repurchase any of our equity securities during the fourth quarter of fiscal 2004.

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ITEM 6. SELECTED CONSOLIDATED FINANCIAL DATA

	Fiscal Year Ended April 30,				
	2004	2003	2002	2001	2000
	(in thousands, except per share amounts)				
Consolidated Statement of Operations Data:					
Revenues:					
License	$ 36,293	$ 30,699	$ 45,141	$ 64,978	$ 21,463
Service	60,012	39,810	32,630	22,081	10,735
Total revenues	96,305	70,509	77,771	87,059	32,198
Cost of revenues:					
License	3,694	2,790	3,107	3,830	1,451
Service	28,993	18,151	13,921	11,861	6,228
Stock compensation (recovery)	240	37	(47)	663	562
Acquisition-related compensation	595				
Amortization of intangible assets	709				
Total cost of revenues	34,231	20,978	16,981	16,354	8,241
Gross margin	62,074	49,531	60,790	70,705	23,957
Operating expenses:					
Sales and marketing:					
Other sales and marketing	38,302	41,840	56,318	61,951	26,657
Stock compensation	3,158	2,227	220	7,294	5,820
Research and development:					
Other research and development	23,147	26,357	33,491	26,451	9,411
Stock compensation (recovery)	206	232	(189)	4,346	3,281
General and administrative:					
Other general and administrative	8,954	6,927	7,386	6,255	3,411
Stock compensation	678	136	298	3,749	2,182
Acquisition-related compensation	1,091				
Amortization of intangible assets	2,092		756	35,974	14,911
Acquired in-process research and development	500	400			1,300
Restructuring and other charges	9,201	7,836	6,257		
Merger-related expenses (benefit)			(835)	4,985	
Impairment of goodwill and other intangible assets				55,224	
Total operating expenses	87,329	85,955	103,702	206,229	66,973
Loss from operations	(25,255)	(36,424)	(42,912)	(135,524)	(43,016)
Other income (expense):					
Interest and other income, net	3,093	4,900	10,158	18,749	7,823
Loss from foreign currency translation	(639)				
Impairment of investments		(3,673)	(1,446)	(8,561)	
Loss before provision for income taxes	(22,801)	(35,197)	(34,200)	(125,336)	(35,193)
Provision for income taxes	1,294	934	343		

Net loss	$ (24,095)	$ (36,131)	$ (34,543)	$ (125,336)	$ (35,193)
Net loss per share:					
Basic and diluted	$ (0.48)	$ (0.75)	$ (0.73)	$ (2.74)	$ (1.14)
Weighted average shares	50,191	48,495	47,451	45,703	30,967

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	As of April 30,				
	2004	2003	2002	2001	2000
Consolidated Balance Sheet Data:					
Cash, cash equivalents and investments	$ 238,221	$ 256,967	$ 285,549	$ 300,525	$ 299,875
Working capital	149,801	243,181	267,706	293,705	294,251
Total assets	314,637	290,950	319,064	355,191	430,801
Long-term obligations	5,382				1,015
Stockholders equity	261,494	256,246	286,631	313,640	412,646

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ITEM 7. MANAGEMENT S DISCUSSION & ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This annual report includes forward-looking statements (within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended). Such statements are based upon current expectations that involve risks and uncertainties, and we undertake no obligation to publicly release any revisions to the forward-looking statements or reflect events or circumstances after the date of this report. Any statements contained herein that are not statements of historical fact may be deemed to be forward-looking statements. For example, words such as may, will, should, estimates, predicts, potential, continue, strategy, believes, anticipates, plans, expects, intends, and similar expressions are inte forward-looking statements. Our actual results and the timing of certain events may differ materially from those reflected in the forward-looking statements. Factors that might cause or contribute to such differences include, but are not limited to, those discussed in the Risk Factors section included below in this Annual Report on Form 10-K. The following discussion should be read in conjunction with the Consolidated Financial Statements and notes thereto appearing elsewhere in this Annual Report on Form 10-K. Our fiscal year ends on April 30 of each year.

Business Overview

We develop and sell an integrated suite of product lifecycle management (PLM) software products and offer related business consulting and implementation services. Substantially all of our revenues are derived from the license of software products under software license agreements and from the delivery of associated professional and maintenance services. Our solutions enable our customers to accelerate their time-to-market and revenue, reduce costs, improve product quality, ensure regulatory compliance and drive innovation throughout the product lifecycle.

We believe that understanding the following key developments is helpful to an understanding of our operating results for fiscal 2004.

Increased Product Breadth

We sold our first PLM product in 1996. At that time, our offering consisted of a single product. Over time, we have added features and functionality to our existing products as well as new products, both through internal development and acquisition. In January 2004, we began shipping Agile 9, our most comprehensive PLM product offering to date. Agile 9 provides extensive new features and capabilities, as well as an enterprise technology platform providing customers a broader, deeper PLM solution. As of April 30, 2004, we have licensed products to nearly 1,200 companies worldwide.

Expanded Industry Focus

We were initially focused on solutions targeted principally for customers operating in the electronics and high technology and, to a lesser extent, medical device industries. As we have grown our business and expanded our product suite, we have also expanded our industry focus. While the electronics and high technology industry still represent the single largest industry for us, we now have significant customers in all of the following industries:

- Electronics and high technology;

Industrial products;

Life sciences; and

Others.

Improved Geographic Balance

We have made significant strides toward growing our international business and reducing our operating expenses by establishing our offshore development centers:

Revenues. For fiscal 2004, revenues from customers located outside of North America represented 37% of total revenues, which compares to 25% for fiscal 2003 and 14% for fiscal 2002. While we expect this mix to vary from period to period, we will continue to seek to derive revenues from customers in North America as well as internationally, in order to achieve a reasonably balanced geographic distribution of revenues in future periods.

Product Development. In addition to our development activities in San Jose, we established development centers in India and China in fiscal 2003 and, as a result of our acquisition of Eigner US Inc. in fiscal 2004 (as discussed below), we now have a development center in Germany.

Acquisitions

Our strategy has been, and continues to be, to expand our business both organically and through acquisitions of complementary products, technologies and companies. We have made the following acquisitions since December 2002:

oneRev, Inc., acquired in December 2002;

ProductFactory, Inc., acquired in March 2003;

Eigner US Inc., acquired in August 2003; and

TRADEC, Inc., acquired in September 2003.

Through the acquisition of ProductFactory, Inc. we acquired what is now our Product Portfolio Management product. Through the acquisition of Eigner we acquired what is now our Product Catalog, Requirements Management, Configuration Management, Engineering Collaboration and Maintenance, Repair and Overhaul products. Eigner also provided us with a stronger presence in the automotive supply chain, industrial equipment, aerospace and defense industries, as well as in certain geographic markets such as the Central European region. The acquisition of oneRev, Inc. and TRADEC, Inc. provided additional functionality to our existing products as well as new customers. The results of all of these acquisitions are included in our statements of operations beginning as of the respective acquisition date.

Restructurings

We have taken a number of actions to reduce our expenses to better align our operations and cost structure with current and anticipated market conditions, as follows:

During the fourth quarter of fiscal 2002, we recorded restructuring and other charges of $6.3 million, primarily related to the reduction of 75 employees, the consolidation of excess facilities, the impairment of certain non-refundable prepaid license fees, and the abandonment of certain property and equipment;

Throughout the first half of fiscal 2003, we continued to evaluate the economic conditions and initiated a further restructuring of our operations. During the second quarter of fiscal 2003, we recorded restructuring and other charges of $7.8 million, primarily related to the consolidation of additional excess facilities, the abandonment of additional property and equipment and the further impairment of certain non-refundable prepaid license fees;

During the second quarter of fiscal 2004, in connection with our move to our new headquarters in San Jose, California, we recorded restructuring and other charges of $7.5 million, primarily related our outstanding lease commitments for properties that we vacated in September 2003 and the abandonment of certain long-lived assets;

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During the second quarter of fiscal 2004, in connection with our acquisition of Eigner, we recorded additional restructuring and other charges of $1.7 million primarily related to a reduction of 33 employees, to eliminate duplicative activities and reduce the cost structure of the combined company (see Note 8 Restructuring and Other Charges to our consolidated financial statements); and

Also during the first quarter of fiscal 2005, we terminated approximately 77 employees, consolidated our facility in Tokyo, Japan and consolidated our Chinese development centers by closing our development center in Hong Kong, China, with the projected restructuring and other charges ranging from $2.0 to $3.0 million (See Note 14 Subsequent Event to our consolidated financial statements).

Overview of Our Results

We derive revenues from the license of software products under software license agreements and from the delivery of associated professional and maintenance services. Our license revenues are comprised of fees charged for the use of our products licensed under perpetual or term-based arrangements. Our service revenue are comprised of fees charged for implementation services and fees charged for post-contract customer support (i.e., technical support and product updates). Our implementation services are typically provided over a period of three to six months subsequent to the signing of a software license arrangement. Post-contract customer support is generally purchased at the time of initial license purchase, and renewed annually thereafter. Post-contract customer support revenue is recognized ratably over the support period, generally 12 months.

Throughout fiscal 2004, 2003 and 2002, the primary factor that has impacted our operations and financial performance has been weak demand for enterprise software resulting from the continuing weakness of the global and U.S. economies. Weak economic conditions persisted through most of fiscal 2004, but beginning in fourth quarter of fiscal 2004, we began to see early evidence of strengthening demand for our products. While it is still too early to determine if this slow improvement in demand will continue, we believe that demand may be stabilizing and may be showing signs of returning to positive growth later in the fiscal year.

Although our operations and financial performance were directly and adversely impacted by the economic factors described above, and despite the difficult economic challenges we faced during fiscal 2004, we were able to achieve the following results:

We recorded record fiscal year total revenues of $96.3 million, a 37% increase from total revenues of $70.5 million in fiscal 2003, and a 24% increase from total revenues of $77.8 million in fiscal 2002. Our record revenues were achieved on the strength of a modest improvement in our license revenue and a significant in service revenue.

Our net loss for fiscal year 2004 was $24.1 million, a 33% decrease from net loss of $36.1 million in fiscal 2003, and a 30% decrease from net loss of $34.5 million in fiscal 2002.

We maintained cash and investments balance as of April 30, 2004 of $238.2 million.

We completed our integration of Eigner operationally across all functional areas, and several of our customers have begun to implement integrated Agile/Eigner solutions.

In January 2004, we delivered our most comprehensive product release to-date, Agile 9. This product release provides extensive new features and capabilities, as well as an enterprise technology platform providing customers a broader, deeper PLM solution.

Use of Estimates and Critical Accounting Policies

We have prepared our consolidated financial statements in accordance with accounting principals generally accepted in the United States of America. In preparing our financial statements, we make estimates, assumptions and judgments that can have a significant impact on our reported revenues, loss from operations, and net loss, as well as on the value of certain assets and liabilities on our balance sheet. These estimates, assumptions and

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judgments about future events and their effects on our results cannot be determined with certainty, and are made based upon our historical experience and on other assumptions that are believed to be reasonable under the circumstances. These estimates may change as new events occur or additional information is obtained, and we may periodically be faced with uncertainties, the outcomes of which are not within our control and may not be known for a prolonged period of time. The discussion and analysis of our financial condition and results of operations are based upon these statements. While there are a number of accounting policies, methods and estimates affecting our financial statements, areas that are particularly significant include revenue recognition, allowance for doubtful accounts and sales returns, investments, prepaid software license fees, restructuring reserves, stock options and warrants, and business combinations and acquired intangible assets, which are described below. In addition, please refer to Note 1 of our consolidated financial statements for further discussion of our significant accounting policies.

We have identified the policies below as critical to our business operations and understanding of our financial condition and results of operations. A critical accounting policy is one that is both material to the presentation of our financial statements and requires us to make difficult, subjective or complex judgments that could have a material effect on our financial condition and results of operations. These policies may require us to make assumptions about matters that are highly uncertain at the time of the estimate, and different estimates that we could have used, or changes in the estimate that are reasonably likely to occur, may have a material impact on our financial condition or results of operations.

In addition to the estimates and assumptions that we use to prepare our historical financial statements, we monitor our sales pipeline in order to estimate the timing and amount of future revenues. If we are unable to properly estimate the timing and amount of revenues, our future operations could be significantly impacted. Our sales pipeline may not consistently result in revenues in a particular period, as the data upon which the assumptions and estimates made by us may change. For example, the recent economic slowdown discussed above resulted in reduced information technology spending that caused customers to delay purchasing decisions during fiscal years 2002, 2003 and to some extent into fiscal 2004. In addition, it has remained more difficult and continues to take longer to close contracts with customers, the size of the transactions continues to be smaller than in previous years prior to the economic slowdown, and many of our license contracts are signed in the last weeks of the quarter, making it difficult for us to forecast revenues for the quarter. These factors have resulted in difficulty adjusting spending to respond to variations in revenue growth during the quarter, all of which has adversely affected our business, financial condition and results of operations.

Revenue Recognition

We recognize our software license revenue in accordance with Statement of Position (SOP) 97-2, Software Revenue Recognition, as amended by SOP 98-9 Software Revenue Recognition with Respect to Certain Arrangements. We recognize license revenues when all of the following criteria are met: persuasive evidence of an arrangement exists, the fee is fixed or determinable, collection of the related receivables is reasonably assured, delivery of the product has occurred and the customer has accepted the product (including the expiration of any acceptance period set forth in the contract) if the terms of the contract include an acceptance requirement. In the event that we grant a customer the right to specified upgrades and vendor-specific objective evidence of fair value exists for such upgrades, we defer license revenue in an amount equal to this fair value until we have delivered the specified upgrade. If vendor-specific objective evidence of fair value does not exist, then we defer recognition of the entire license fee until we deliver the specified upgrade. If professional services are essential to the functionality of the other elements of the arrangement, we defer recognition of revenue until we have satisfied our professional services obligations. To date, professional services have not been essential to the functionality of the other elements, and thus have been accounted for separately.

We consider a non-cancelable agreement signed by the customer and us to be evidence of an arrangement. Delivery is considered to occur when media containing the licensed programs is provided to a common carrier, or the customer is given electronic access to the licensed software. Our typical end user license agreements do not

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contain acceptance clauses. We consider the fee to be fixed or determinable if the fee is not subject to refund or adjustment. If the fee is not fixed or determinable, we recognize revenue as the amounts become due and payable. Reasonable assurance of collection is based upon our assessment of the customer s financial condition through review of their current financial statements or credit reports. For follow-on sales to existing customers, prior payment history is also used to evaluate probability of collection. If we determine that collection is not reasonably assured, we defer the revenue and recognize the revenue upon cash collection.

When our software licenses contain multiple elements, we allocate revenue to each element based on the relative fair values of the elements. Multiple-element arrangements generally include post-contract support (PCS or maintenance), software products, and in some cases, other professional services. Revenue from multiple-element arrangements is allocated to undelivered elements of the arrangement, such as PCS, based on the relative fair values of the elements specific to us, and we must analyze each license arrangement carefully to ensure that all of the individual elements have been identified, along with the fair value of each element. Our determination of fair value of each element in multiple-element arrangements is based on vendor-specific objective evidence, which is generally determined by sales of the individual element to third parties or by reference to a renewal rate specified in the related arrangement.

Where vendor-specific objective evidence of fair-value exists for all undelivered elements, but evidence does not exist for one or more delivered elements, we account for the delivered elements in accordance with the Residual Method prescribed by SOP 98-9. Under the residual method, the fair value of the undelivered elements is deferred and the remaining portion of the arrangement fee is recognized as revenue. In most cases, the bundled multiple elements include PCS and the software product. In such cases, when vendor-specific objective evidence of fair value exists for all of the undelivered elements (most commonly PCS), the residual or remaining amount is recognized as revenue and the PCS is recognized ratably over the PCS term, which is typically 12 months.

Revenues from professional services consist of training and implementation services. Training revenues are recognized as the services are performed. Professional services are not considered essential to the functionality of the other elements of the arrangement and are accounted for as a separate element. Professional services are recognized as the services are performed for time and materials contracts or upon achievement of milestones on fixed-price contracts. A provision for estimated losses on fixed-price professional services contracts is recognized in the period in which the loss becomes known.

Customers typically prepay maintenance fees for the first 12 months and the related maintenance revenues are recognized ratably monthly over the term of the maintenance contract. Maintenance contracts include the right to unspecified upgrades on a when-and-if available basis, and ongoing support.

Deferred revenues include amounts received from customers for which revenue has not yet been recognized that generally results from deferred maintenance, consulting or training services not yet rendered and license revenue deferred until all requirements under SOP 97-2 are met. Deferred revenue is recognized upon delivery of our products, as services are rendered, or as other requirements requiring deferral under SOP 97-2 are satisfied.

Allowance for Doubtful Accounts and Sales Returns

We maintain an allowance for doubtful accounts to reduce amounts to their estimated realizable value. A considerable amount of judgment is required when we assess the realization of accounts receivables, including assessing the probability of collection and the current credit-worthiness of each customer. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, an additional provision for doubtful accounts may be required. We initially record a provision for doubtful accounts based on our historical experience, and then adjust this provision at the end of each reporting period based on a detailed assessment of our accounts receivable and allowance for doubtful accounts. In estimating the provision for doubtful accounts, we consider (i) the aging of the accounts receivable; (ii) trends within and ratios involving the age of the accounts receivable; (iii) the customer mix in each of the aging categories and the nature of the receivable, such as whether it derives from license, professional services or maintenance revenue; (iv) our historical provision for doubtful accounts; (v) the credit worthiness of the customer; and (vi) the economic conditions of the customers industry as well as general economic conditions, among other factors.

Should any of these factors change, the estimates that we make may also change, which could impact our future provision for doubtful accounts. For example, if the financial condition of our customers were to deteriorate, affecting their ability to make payments, an additional provision for doubtful accounts could be required.

Our license agreements do not offer our customers the unilateral right to terminate or cancel the contract and receive a cash refund. In addition, the terms of our license agreements do not offer customers price protection. However, we provide for sales returns reserve based upon estimates of potential future credits related to current period revenues. We analyze historical credits, current economic trends, average deal size, changes in customer demand and acceptance of our products when evaluating the adequacy of the sales returns reserve. Revenue for the period is reduced to reflect the provision of our reserve for sales returns.

Stock Options

In connection with certain employee restricted Common Stock and stock option grants, we have recorded unearned stock compensation totaling $39.4 million through April 30, 2004, which represents an increase of $3.4 million over the balance as of April 30, 2003 due to options granted with exercise price below fair market value and restricted common stock granted to our employees. At April 30, 2004, the unamortized balance of the unearned stock compensation was $1.1 million. Unearned stock compensation, a component of stockholders equity, represents the fair value of the unvested portion of restricted Common Stock and the difference between the exercise price of the option and the fair value of our Common Stock on the date of grant. Unearned stock compensation is amortized through charges to operations over the vesting period of the options, which is generally five years, using the accelerated method of amortization as described in Financial Accounting Standards Board Interpretation (FIN) No. 28, Accounting for Stock Appreciation Rights and Other Variable Stock Option Award Plans. Stock compensation expense, less recoveries, for employees and consultants was $4.3 million, $2.6 million and $282,000 for fiscal 2004, 2003 and 2002, respectively.

Stock compensation expense related to stock options granted to non-employees is recognized as earned, over the applicable vesting period of the options, using the accelerated method of amortization prescribed by FIN 28. At each reporting date, we recalculate the value of the stock option using the Black-Scholes option pricing model and record changes in fair value for the unvested portion of the option. As a result, the stock compensation expense fluctuates with the movement in the fair market value of our Common Stock. Amortization of stock compensation for non-employees was $207,000, $892,000 and $760,000 for fiscal 2004, 2003 and 2002, respectively.

Business Combinations and Acquired Intangible Assets

We account for our purchases of acquired companies in accordance with Statement of Financial Accounting Standards (SFAS) No. 141, Business Combinations, and account for the related acquired intangible assets in accordance with SFAS No. 142, Goodwill and Other Intangible Assets. In accordance with SFAS No. 141, we allocate the cost of the acquired companies to the identifiable tangible and intangible assets acquired and liabilities assumed, with the remaining amount being classified as goodwill. Certain intangible assets, such as developed technologies, are amortized to expense over time, while in-process research and development costs (IPR&D), if any, are immediately expensed in the period the acquisition is completed. Identifiable intangible assets are currently amortized over a weighted-average of one to three years using the straight-line method.

The majority of entities we acquire do not have significant tangible assets and, as a result, a significant portion of the purchase price is typically allocated to intangible assets and goodwill. Our future operating performance will be impacted by the future amortization of intangible assets, potential charges related to IPR&D

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for future acquisitions, and potential impairment charges related to goodwill. Accordingly, the allocation of the purchase price to intangible assets and goodwill has a significant impact on our future operating results. The allocation of the purchase price of the acquired companies to intangible assets and goodwill requires us to make significant estimates and assumptions, including estimates of future cash flows expected to be generated by the acquired assets and the appropriate discount rate for these cash flows. Should different conditions prevail, material write-downs of intangible assets and/or goodwill could occur.

Under SFAS No. 142, goodwill is no longer subject to amortization. Rather, we evaluate goodwill for impairment at least annually or more frequently if events and changes in circumstances suggest that the carrying amount may not be recoverable. Impairment of goodwill is tested at the reporting unit level by comparing the reporting unit s carrying value, including goodwill, to the fair value of the reporting unit. The fair values of the reporting units are estimated using a combination of the income, or discounted cash flows, approach and the market approach, which utilizes comparable companies data. If the carrying amount of the reporting unit exceeds its fair value, goodwill is considered impaired and we then compare the implied fair value of the goodwill to its carrying amount to determine the impairment loss, if any. Annual goodwill impairment testing will be performed, at a minimum, during the fourth quarter of each fiscal year.

Accounting for income taxes

As part of the process of preparing our consolidated financial statements, we are required to estimate our income tax expense in each of the jurisdictions in which we operate. This process involves us 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 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.

Significant management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities, and any valuation allowance recorded against our net deferred tax assets. We have recorded a valuation allowance for the entire portion of the net operating losses related to the income tax benefits arising from the exercise of employees stock options. In the event that actual results differ from these estimates or we adjust these estimates in future periods, we may need to adjust our valuation allowance as well.

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Results of Operations

The following table sets forth selected consolidated financial data for the periods indicated, expressed as a percentage of total revenues.

	Fiscal Year Ended April 30,		
	2004	2003	2002
Revenues:			
License	38%	44%	58