

I2 TECHNOLOGIES INC
Form 10-K
March 15, 2006
Table of Contents

Index to Financial Statements

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

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 December 31, 2005

or

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

For the transition period from _____ to _____

Commission file number 0-28030

i2 Technologies, Inc.

(Exact Name of Registrant as Specified in Its Charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

One i2 Place
11701 Luna Road

Dallas, Texas

75-2294945
(I.R.S. Employer Identification No.)

75234
(Zip code)

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(Address of principal executive offices)

Registrant's telephone number, including area code: **(469) 357-1000**

Securities registered pursuant to Section 12(b) of the Act: **None**

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

Common Stock, \$0.00025 par value

Preferred Share Purchase Rights

(Title of Class)

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not 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.

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer (as defined in Rule 12b-2 of the Act).

Large accelerated filer Accelerated filer Non-accelerated filer

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

The aggregate market value of the common equity held by non-affiliates (Affiliates being, for these purposes only, directors, executive officers and holders of more than 5% of the Registrant's Common Stock) on June 30, 2005, was \$94.4 million.

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As of March 1, 2006, the Registrant had approximately 20,702,325 outstanding shares of Common Stock.

DOCUMENTS INCORPORATED BY REFERENCE

Selected designated portions of the Registrant's definitive Proxy Statement to be filed on or before April 30, 2006 in connection with the Registrant's 2006 Annual Meeting of stockholders are incorporated by reference into Part III of this Annual Report.

Table of Contents

Index to Financial Statements

i2 TECHNOLOGIES, INC.

ANNUAL REPORT ON FORM 10-K

TABLE OF CONTENTS

	Page
	<u> </u>
PART I	
Item 1.	<u>Business</u> 3
Item 1A.	<u>Risk Factors</u> 10
Item 1B.	<u>Unresolved Staff Comments</u> 20
Item 2.	<u>Properties</u> 20
Item 3.	<u>Legal Proceedings</u> 20
Item 4.	<u>Submission of Matters to a Vote of Security Holders</u> 22
PART II	
Item 5.	<u>Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u> 23
Item 6.	<u>Selected Financial Data</u> 26
Item 7.	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> 29
Item 7A.	<u>Quantitative and Qualitative Disclosures About Market Risk</u> 46
Item 8.	<u>Financial Statements and Supplementary Data</u> 46
Item 9.	<u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u> 47
Item 9A.	<u>Controls and Procedures</u> 47
Item 9B.	<u>Other Information</u> 49
PART III	
Item 10.	<u>Directors and Executive Officers of the Registrant</u> 50
Item 11.	<u>Executive Compensation</u> 50
Item 12.	<u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u> 50
Item 13.	<u>Certain Relationships and Related Transactions</u> 50
Item 14.	<u>Principal Accountant Fees and Services</u> 50
PART IV	
Item 15.	<u>Exhibits and Financial Statement Schedules</u> 51
<u>SIGNATURES</u>	

Table of Contents

Index to Financial Statements

The disclosures set forth in this report are qualified by Item 1A, Risk Factors, and by the section captioned Forward-Looking Statements in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, as well as other cautionary statements set forth elsewhere in this report.

References in this report to the terms optimal and optimization and words to that effect are not necessarily intended to connote the mathematically optimal solution, but may connote near-optimal solutions, which reflect practical considerations such as customer requirements as to response time, precision of the results and other commercial factors.

All references to common stock and per share amounts for periods prior to February 17, 2005 have been retroactively restated to reflect the 1-for-25 reverse stock split we implemented February 16, 2005. See Item 5, Market For Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity.

ITEM 1. BUSINESS

Nature of Operations. We are a provider of multi-enterprise supply chain management solutions, including various supply chain software and service offerings. We operate our business in one business segment. Supply chain management is the set of processes, technology and expertise involved in managing supply, demand and fulfillment throughout divisions within a company and with its customers, suppliers and partners. The goals of our solutions include increasing supply chain efficiency and enhancing customer and supplier relationships by managing variability, reducing complexity, improving operational visibility, increasing operating velocity and integrating planning and execution. We also offer master data management technology, which is designed to collect, synthesize and distribute critical reference data by leveraging a service oriented architecture. Our offerings help customers improve efficiency in relation to sourcing, supply, demand, fulfillment and logistics performance. Our application software is often bundled with other offerings we provide such as business optimization and technical consulting, training, solution maintenance, software upgrades and development.

Globally, we have more than 500 customers in a variety of industries including:

Technology

Computer & Electronics

Telecommunications Equipment and Service

Semiconductor

Consumer Electronics & Consumer Durables

Contract Manufacturers

Automotive and Industrial

Automotive Original Equipment Manufacturers

Suppliers

Industrial Manufacturers

Process Industries

Metals

Energy & Chemicals

Consumer Goods & Retail

Retailers

Table of Contents

Index to Financial Statements

Consumer Packaged Goods

Soft Goods (Textiles/Apparel & Footwear)

No individual customer accounted for more than 10% of our total revenues during 2005, 2004 or 2003.

i2 was founded in 1988 and incorporated in Delaware in 1989. Our executive offices are located at One i2 Place, 11701 Luna Road, Dallas, Texas 75234, and our telephone number is (469) 357-1000.

Industry Background

Today's competitive business environment has led many companies in diverse industries to seek ways to make their businesses more agile and offer greater operating efficiency while improving flexibility and responsiveness to changing market conditions. In addition to facing higher competitive standards with respect to meeting customer demands for product quality, variety and price, businesses also recognize the need to improve asset utilization, reduce the cost of goods, reduce inventories, shorten lead times and reduce the cost of fulfilling orders. Furthermore, a company's extended supply chain may span multiple continents, requiring suppliers in one part of the world to collaborate with a plant in another to serve customers in yet a third location. These forces are prompting companies to collaborate with a broad range of suppliers and customers to improve efficiencies across multi-enterprise supply chains.

We believe that traditional enterprise resource planning (ERP) systems fail to provide both the forward visibility across divisions or enterprises and the high-speed decision-support capabilities that we believe are necessary to quickly plan and execute decisions. To increase competitiveness, we believe companies are looking for solutions that can be integrated with their existing systems to provide tools for managing the variability in their supply chains, allowing them to monitor events in order, inventory and transportation, to evaluate tradeoffs for fast and accurate decision-making and to execute their plans across the critical processes in their supply chains.

The growth of the Internet and the proliferation of software applications have accelerated many companies' efforts to increase efficiencies by leveraging information technology based on open standards. We believe this has prompted demands for a dynamic, open and integrated environment among customers, suppliers and designers. In response to these evolving market forces, many companies have sought to re-engineer their business processes to reduce manufacturing cycle times, shift from mass production to order-driven manufacturing, increase the use of outsourcing and share information more readily with vendors and customers.

Integration has become an increasingly important issue for enterprises to lower costs and realize value from their diverse environment of applications and distributed systems. Customers seek integration at several levels—business process, applications, user interface, data and technology. A wide variety of companies are pursuing the integration market opportunity, including ERP companies, leading Independent Software Vendors (ISVs), Enterprise Application Integration (EAI) vendors, Systems Integrators (SIs) and other information technology (IT) services organizations, but no single company has demonstrated a complete solution to the various requirements sought by customers. i2 provides an integration framework utilizing service oriented architecture—the Agile Business Process Platform.

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Leading software and technology companies are developing offshore (global) workforces, in part to take advantage of the technical talent and lower costs of human resources in India, China and other locations. This has led many companies to initiate their own offshore operations or outsource some run and maintain processes, as well as development and implementation activities, to Offshore IT Services (OIS) firms.

Table of Contents

Index to Financial Statements

Development of the i2 Solutions

Advanced Planning and Scheduling. We have offered a set of supply chain management solutions since our company was founded nearly 18 years ago. Our founders, Sanjiv Sidhu and Ken Sharma, sought to expand enterprise application software beyond traditional ERP systems, which were basically transaction accounting and processing systems that did not consider production constraints or offer more sophisticated monitoring, decision-support and execution capabilities. We took the first step beyond ERP with the development of an advanced planning and scheduling application that took into account actual constraints to improve the flow of materials within a factory. That solution, i2 Factory Planner, has assisted many of our customers in improving the efficiency and profitability of their factories while reducing their materials and inventory costs.

Supply Chain Planning/Supply Chain Management. Our applications evolved into solutions for supply chain planning that encompassed constraint-based planning and scheduling for multiple factories, distribution centers and warehouses. With the addition of supply chain design and execution capabilities for logistics, demand planning and fulfilment, we became a leader in enterprise solutions for supply chain management.

Supplier Relationship Management. We continued to expand our product base by applying our solutions for the extended supply chain to the supplier relationship processes and functions. To facilitate cost-effective sourcing and product design, we acquired and developed technologies that help customers to more efficiently source, negotiate the pricing of and procure materials and components from suppliers, thereby enabling them to make design decisions while cognizant of the effect on the supply chain of existing products and the total product portfolio.

Distributed Fulfilment and Revenue Management. Our distributed order execution technology has enabled us to develop integrated, closed-loop planning and execution solutions. We continue to invest in this technology, which provides a scalable and flexible framework for creating new solutions and is used by our customers across multiple entities for transaction processing, visibility and event management capabilities. We have also invested in solutions that help customers optimize merchandising, revenue and pricing.

Supply and Demand Synchronization. i2's next-generation supply chain management solutions focus on the multi-echelon value chain, encompassing the customer's customer and the supplier's supplier. Our next-generation solutions are designed to enable businesses to manage and tune their supply chains simultaneously so that they can quickly change parameters to meet their dynamic business needs. These solutions are built on the i2 Agile Business Process Platform, a unique service-oriented architecture (SOA) that includes a layer of technology services for integration and data management, user interface development and a visual business process workflow engine. The platform is business process management (BPM) compliant and been designed to interoperate with legacy, ERP and other enterprise architectures.

Products

Our solutions—bundles of software products and technology services—are designed to help customers address various supply chain problems and opportunities, including:

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Linking certain aspects of planning and decision-making to execution of such plans and the monitoring of changing conditions across the supply chain

Improving current business processes, return on assets and profitability

Creating an environment for continuous process improvement

Improving customer service levels and delivering on commitments to customers

Enhancing competitive advantage

Table of Contents

Index to Financial Statements

Increasing market share

Enhancing time to value for process redesign and acquisition integration

Our primary products are focused on optimizing the following business processes: supply and demand management; execution and collaboration; transportation and distribution management; supplier relationship management; as well as data management and analytics. Our products are complemented by our business process consulting and our technology and services.

Supply and Demand Management: i2 solutions for supply and demand management help businesses coordinate the production and distribution of goods and materials throughout the supply chain to final delivery to the customer. They also help businesses analyze their revenues with merchandising, planning and pricing tools.

Solutions for supply planning are designed to provide multi-enterprise visibility, collaboration, decision-support and execution capabilities. Using these tools, a business may estimate future demand for its products to help planners more accurately estimate future supply needs. As a result, businesses can make better decisions about how much of what products to make, when to make them, and what parts to utilize to make those products. Solutions for supply planning include i2 Factory Planner, i2 Supply Chain Planner, i2 Inventory Optimization and various scheduling products.

Solutions for demand management provide tools designed to forecast and continuously manage demand, plan merchandising strategies, manage markdowns and promotions pricing, and optimize price quoting. Using these products, companies can begin to optimize their revenues by selling products at prices set by analytic products. Demand management products include i2 Demand Manager, i2 Markdown Optimizer and i2 Merchandise Planner. i2 Inventory Optimization, i2 Sales and Operations Planning, i2 Merchandise Financial Planning, i2 Buying and Assortment Management, and i2 Allocation and Replenishment.

Transportation and Distribution Management: Solutions for transportation and distribution management help businesses optimize the flow of goods between suppliers, enterprise supply chain locations and customers. These tools provide integrated products for planning and executing transportation and distribution activities, as well as tools for strategic supply chain design and transportation modeling. Using i2 solutions, a business can procure, plan, execute and monitor freight movements across multiple modes, borders and enterprises. As a result, businesses can make better decisions about where and how to ship products, reducing their transportation costs while executing supply chain plans and achieving customer service objectives. Transportation and distribution management products include i2 Supply Chain Strategist, i2 Transportation Bid Collaboration, i2 Transportation Planner, i2 Transportation Modeler and i2 Transportation Manager.

Execution and Collaboration: Solutions to optimize plan execution and collaboration help businesses integrate the planning and execution processes, creating a closed-loop environment. These solutions provide tools designed to stage inventory, plan replenishment, manage orders and provide visibility to lower fulfilment costs, improve on-time delivery performance and enhance customer satisfaction. The i2 Collaborative Supply Execution solution is designed to, provide inventory and plan collaboration, transaction processing, visibility, event management, integration and workflow capabilities. Other solutions in this category include i2 Supply Chain Visibility, i2 Customer Order Fulfilment, i2 Collaborative Replenishment and i2 Configurator.

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Supplier Relationship Management: Supplier relationship management solutions help companies and their suppliers collaborate on sourcing and procurement for supply management. This solution is designed to bridge product development, sourcing, supply planning and procurement across the supply chain, providing the ability to create, execute and sustain global sourcing strategies. Sourcing solutions provide decision-support and optimization tools that are designed to help companies improve decision-making on supplies and the parts to use in products. During product development, these products can help to optimize designs by considering sourcing and supply chain constraints, as well as allowing design collaboration when outsourcing manufacturing or

Table of Contents

Index to Financial Statements

custom parts. During procurement, supplier relationship management solutions help companies to define sourcing strategies to reduce supply risks and costs, negotiate terms and streamline the requisitioning and buying of materials. Sourcing products include i2 Strategic Sourcing, i2 Product Sourcing and i2 Negotiate.

Data Management and Analytics: We offer a data management solution that is designed to provide customers with the ability to manage data from multiple sources including legacy, ERP and other applications. i2 Master Data Management can be deployed: to create and maintain application-specific data; to consolidate data from multiple disparate sources; to cleanse, transform, synchronize and validate data; as well as to filter unwanted data. Solutions for analytics such as i2 Performance Manager enable companies to monitor all aspects of their supply chain.

Dispositions: On July 1, 2005, we completed the sale of Trade Service Corporation (TSC), which was operated as a part of our content and data services business and on December 1, 2005, we sold the remainder of our content and data service business. See *ITEM 7.*

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - Discontinued Operations and Note 15. *Discontinued Operations* in our Notes to Consolidated Financial Statements.

Product Development

We focus our ongoing product development efforts on meeting the requests of, and delivering on our commitments to, our current customers, enhancing our solutions and the underlying technology across our products, and developing or enhancing products that will enable us to enter new markets. In order to address customer recommendations, we have developed a User Enhancement Voting Process in collaboration with the i2 User Group. This process allows customers to provide input so that our solutions evolve to meet our customers' business challenges and opportunities. In addition, we invest in solutions that help us more fully complete our solution offerings and enable cross-product workflows. We have continued to invest in products and technologies that we anticipate will be important and differentiated in the future.

Our Solutions Operations activities are primarily conducted in North America and India. Most product management and product marketing employees are based in North America, but many development and services teams are based in India. The India location offers many benefits to i2, including centralization of development efforts and cost structure advantages. Our India-based Solutions Center provides services such as upgrades, implementations and development services that heavily leverage other organizations based in India. For the years ended December 31, 2005, 2004 and 2003, our research and development expense totaled approximately \$37.3 million, \$56.3 million and \$66.2 million, respectively.

Services and Maintenance

Our customer service and support program includes software maintenance, the delivery of functional enhancements and updates, and around-the-clock availability for high severity issues.

We maintain a technical support team that operates through our service and support centers located in North America, Latin America, Greater Asia Pacific, Europe and Africa. Our customer service and support activities consist of the following:

Consulting Services. We offer our customers both on-site and off-site consulting services for assisting in the implementation of our products and services and integration with the customers' existing systems. We and our customers also use third-party consulting firms.

Development Services. Customers may also contract with us for services to provide custom development of our applications. In some cases, the modifications or additions to the software may be incorporated into future releases of our products.

Table of Contents

Index to Financial Statements

Training. We offer education and training programs for our customers and third-party implementation providers with classes offered at our offices or at customer locations. We also offer web-based and self-paced learning programs. These classes focus on the fundamental principles of our software products as well as their implementation and use.

Maintenance and Product Updates. We provide ongoing support services for our products. Maintenance contracts are typically sold to customers at the time of the initial license and may be renewed for additional periods. Our maintenance agreements with our customers provide the right to receive most product updates and enhancements to the products purchased by the customer, as well as telephone and online support. Our support services are packaged into three tiers (silver, gold and platinum), which offer customers the ability to choose the level of service they desire.

Sales and Marketing

We sell our software and services through a direct customer-facing organization that is augmented by other sales channels, including systems consulting and integration firms and other industry-related partners. Our direct customer-facing organization consists of account representatives and client managers that are supported by a team of personnel that includes solution and industry specialists.

We currently have joint marketing agreements with software vendors and other industry-related firms such as IBM and Microsoft. Additionally, we have alliances with top global and regional systems consulting and integration, hardware, software, and other relevant services firms including Accenture, IBM Global Services, Infosys and Tata Consulting Services, among others. These joint-marketing agreements and alliances generally provide the vendors with the ability to market our products and access our marketing materials and product training. By using these indirect sales channels, we seek to capitalize on the installed base of other companies and obtain favorable product recommendations from the business partners, thereby increasing the market coverage of our products.

Competition

The markets in which we operate are highly competitive. Our competitors are diverse and offer a variety of solutions targeting various segments of the extended supply chain as well as the enterprise as a whole. Some competitors compete with suites of applications, while most offer solutions designed specifically to target particular functions or industries. We believe our principal competitors are as follows:

ERP Software Vendors. These include companies such as Oracle and SAP, who have added or are attempting to add capabilities for supply chain planning or collaboration to their transaction system products. In addition, both companies are engaged in a multi-year effort to re-deploy their solutions on a Services Oriented Architecture platform.

Other Software Vendors. These include companies such as Adexa and Manugistics who compete principally with our production, logistics and fulfilment optimization products; companies such as Manugistics who compete with our transportation and distribution management products; companies such as JDA Software who compete primarily with our retail applications; and companies such as Manhattan Associates and Kinaxis who compete principally with our fulfilment and certain of our demand optimization products.

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Custom and Offshore Development. We also compete with independent developers of enterprise application software such as Infosys, Satyam, Wipro and other entities in countries with relatively low wage structures and, increasingly, internal development efforts by corporate information technology departments.

Table of Contents

Index to Financial Statements

Proprietary Rights and Licenses

We regard our trademarks, copyrights, patents, trade secrets, technology and other proprietary rights as critical to our business. To protect our proprietary rights, we primarily rely on a combination of copyright, patent, trademark and trade secret laws, confidentiality procedures and contractual provisions. We license our software products in object code (machine-readable) format to customers under license agreements and we generally do not sell or otherwise transfer title to our software products to our customers. Our non-exclusive license agreements generally allow the use of our software products solely by the customer for specified purposes without the right to sublicense or transfer our software products.

Trademarks are important to our business as we use them in our marketing and promotional activities as well as with the delivery of our software products. Our registered trademarks include i2, i2 and design and PLANET.

We hold a number of U.S. patents that predominantly relate to planning, scheduling optimization, demand fulfilment, collaboration, e-commerce and data management and reporting. These patents expire at various times through 2021. We also depend on trade secrets and proprietary know-how for certain unpatented aspects of our business. To protect our proprietary information, we enter into confidentiality agreements with our employees, consultants and licensees, and generally control access to and distribution of our proprietary information. We sublicense some software that we license from third parties and incorporate in, or license in conjunction with, our products.

International Operations

We have international offices in Australia, Belgium, Canada, China, Finland, France, Germany, India, Japan, Korea, Netherlands, Singapore, South Africa, Taiwan and the United Kingdom. Total assets related to our international operations accounted for 37%, 32% and 26% of our total consolidated assets as of December 31, 2005, 2004 and 2003. International revenue totalled \$158.2 million, or 47% of total revenue in 2005; \$144.8 million, or 40% of total revenue, in 2004; and \$166.3 million, or 36% of total revenue, in 2003. See *Note 14 Segment Information, International Operations and Customer Concentrations* in our Notes to Consolidated Financial Statements.

Employees

At December 31, 2005, we had approximately 1,250 full-time employees, including approximately 410 employees engaged in research and development activities primarily located in India and the U.S. and approximately 135 employees engaged in sales and marketing activities. Our future success depends in significant part upon the continued service of our key technical, sales and managerial personnel and our ability to attract and retain highly qualified technical, sales and managerial personnel. Our employees in Germany are represented by a Worker's Council; however, none of our employees is represented by a collective bargaining agreement and we have never experienced a work stoppage. We believe employee relations to be satisfactory.

Seasonality

We typically experience higher demand for our products and services during the second and fourth quarter of the year.

Available Information

We make available, free of charge, through our investor relations web site, our reports on Forms 10-K, 10-Q and 8-K, and amendments to those reports, as soon as reasonably practicable after they are filed with the Securities and Exchange Commission (SEC). The address for our investor relations web site is <http://www.i2.com/investor>.

Table of Contents

Index to Financial Statements

The information contained on our website is not part of, and is not incorporated in, this or any other report we file with or furnish to the SEC.

In June 2003, we adopted a Code of Business Conduct and Ethics. The Code of Business Conduct and Ethics applies to, among others, our Chief Executive Officer and Chief Financial Officer. The full text of the Code of Business Conduct and Ethics is available at our investor relations web site, <http://www.i2.com/investor>. We intend to disclose any amendment to, or waiver from, a provision of the Code of Business Conduct and Ethics that applies to our Chief Executive Officer or Chief Financial Officer on our investor relations web site.

Item 1A. Risk Factors

Any investment in our company will be subject to risks inherent to our business. Before making an investment decision, you should carefully consider the risks described below together with all of the other information included in this report. The risks and uncertainties described below are not the only ones facing our company. Additional risks and uncertainties that we are not aware of or focused on or that we currently deem immaterial may also impair our business operations. This report is qualified in its entirety by these risk factors.

If any of the following risks actually occur, they could have a material adverse effect on our business, financial condition, cash flow or results of operations. In that case, the trading price of our securities could decline and you may lose all or part of your investment.

Risks Related To Our Business

We Have Experienced Substantial Negative Cash Flows And May Continue To Experience Such Negative Cash Flows, Which Would Have A Further Significant Adverse Effect On Our Business, Impair Our Ability To Support Our Operations And Adversely Affect Our Liquidity.

We have experienced substantial negative cash flows during the five years ended December 31, 2005, primarily due to sharp declines in our revenues and our inability to reduce our expenses to a level at or below the level of our revenues. Additionally, in 2005 we disposed of operations that generated positive income and cash flow. We used the proceeds from these disposals to pay down existing debt. Although we implemented restructuring activities in early 2005 focused on, among other things, further reducing our workforce and decreasing continued development of the functionality of certain of our products, a failure to maintain expense levels, stabilize or grow revenues, achieve positive cash flows and obtain additional equity or debt financing as needed will impair our ability to support our operations, adversely affect our liquidity and threaten our ability to repay our debts when they come due, which would have a material adverse effect on our business, results of operations, cash flow and financial condition as well as our stock price. Additionally, we continue to be obligated to pay approximately \$5.6 million annually in interest on our \$111.3 million face value of convertible notes, which includes the additional \$7.5 million of notes issued in January 2006 pursuant to the exercise of the over-allotment option. Continued negative cash flows and the adverse market perception associated therewith may continue to negatively affect our ability to sell our products and maintain existing customer relationships and may adversely affect our ability to obtain additional debt or equity financing on advantageous terms. There can be no assurance that we will be successful in obtaining or maintaining an adequate level of cash resources and we may be forced to act more aggressively in the future in the area of expense reduction in order to conserve cash resources.

Table of Contents

Index to Financial Statements

We Have A Negative Net Working Capital Balance Which May Require Additional Private Or Public Debt Or Equity Financing To Meet Working Capital Needs And To Repay Our Existing Debt When It Becomes Due. This May Have A Substantial Dilutive Effect On The Holdings Of Existing Stockholders. Such Financing May Only Be Available On Disadvantageous Terms, Or May Not Be Available At All. We Have \$25 million of 5.25% Convertible Subordinated Notes That Are Due In December 2006 And Our Working Capital May Be Insufficient To Repay These Notes.

At December 31, 2005, we had a negative net working capital balance of \$34.3 million. Our cash position may continue to decline in the future, primarily due to cash outflows associated with our operations, our debt service obligations and our prior restructuring activities. Unless we are able to maintain expense levels, stabilize or grow revenues and achieve consistent positive cash flows, our ability to support our operations and our liquidity may be further impaired. We may not be successful in obtaining or maintaining an adequate level of cash resources. We have \$25.0 million of debt that matures in December 2006.

We may be required to seek additional private or public debt or equity financing in order to support our operations and repay our outstanding indebtedness. However, we may not be able to obtain debt or equity financing on satisfactory terms or at all, and any new financing will likely have a substantial dilutive effect on our existing stockholders.

Our 5% Senior Convertible Notes Contain Covenants That Restrict Our Ability To Incur Additional Indebtedness.

Our 5% senior convertible notes contain financial covenants that, among other things, place restrictions on the amount and type of additional indebtedness that we can incur. Based on certain conditions we are limited to additional unsecured borrowings of \$25 million and limitations of secured borrowings based on EBITDA levels.

Our Financial Results Have Varied And May Continue To Vary Significantly From Quarter To Quarter And We May Again Fail To Meet Expectations, Which Might Negatively Impact The Price Of Our Stock.

Our operating results have varied significantly from quarter to quarter in the past, and we expect our operating results to continue to vary from quarter to quarter in the future due to a variety of factors, many of which are outside of our control. Although our revenues are subject to fluctuation, significant portions of our expenses are not variable in the short term, such as our lease and purchase commitments and debt servicing expense. If we cannot reduce expenses quickly to respond to decreases in revenues, a revenue shortfall is likely to adversely and disproportionately affect our operating results. These factors have caused our operating results to be below the expectations of securities analysts and investors in the past and may do so again in the future. Our failure to meet or exceed analyst and investor expectations might negatively affect the price of our common stock.

Continued Decreased Levels Of Demand For Our Enterprise Products And Services Could Significantly Reduce Our Revenues.

Historically, we have derived a substantial portion of our revenues from licenses of our enterprise products and related services. Our enterprise products principally include solutions to address supply and demand management, transportation and distribution management, execution and collaboration, supplier relationship management, as well as data management and analytics. We expect software solution revenues and

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maintenance and consulting contracts related to our enterprise products to continue to account for a substantial portion of our revenues for the foreseeable future. We have experienced a sharp decrease in the demand for our enterprise products and related services due to a number of factors, including sales execution, product competitiveness and questions regarding our viability, which have led to a decline in our revenues. Other factors, such as competition and technological change and the existing and potential litigation and other proceedings against us, could also adversely impact demand for, or market acceptance of, these applications.

Table of Contents

Index to Financial Statements

If We Are Unable To Develop And Generate Demand For Our Products, Additional Serious Harm Could Result To Our Business.

We have invested significant resources in developing and marketing our products and services. The demand for, and market acceptance of, our products and services are subject to a high level of uncertainty. Adoption of software solutions, particularly by those individuals and enterprises that have historically relied upon traditional means of commerce and communication, requires a broad acceptance of substantially different methods of conducting business and exchanging information. Our products and services are often considered complex and may involve a new approach to the conduct of business by our customers. As a result, intensive marketing and sales efforts may be necessary to educate prospective customers regarding the uses and benefits of these products and services in order to generate demand. The market for our products and services may continue to weaken, competitors may develop superior products and services or we may fail to develop acceptable solutions to address new market conditions. Any one of these events could have a material adverse effect on our business, results of operations, cash flow and financial condition.

We May Not Be Competitive, And Increased Competition Could Seriously Harm Our Business.

Relative to us, many of our competitors have one or more of the following advantages:

Longer operating history.

Greater financial, technical, marketing, sales and other resources.

Consistent positive cash flows.

Historical profitable operations.

Superior product functionality in certain areas.

Greater name recognition.

A broader range of products to offer.

Better software performance.

A larger installed base of customers.

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Current and potential competitors have established, or may establish, cooperative relationships among themselves or with third parties to enhance their products, which may result in increased competition. In addition, we expect to experience increasing price competition as we compete for market share. We understand that some competitors are offering enterprise application software at no charge as components of product bundles. Further, traditional enterprise resource planning vendors have focused more resources on the development and marketing of enterprise application software, particularly in the product and industry segments in which we compete and, increasingly, corporate information technology departments are undertaking internal development efforts. As a result of these and other factors, we may be unable to compete successfully with our existing or new competitors.

We Have Been And Continue To Be Subject To Claims Pertaining To The Quality Of Our Products And Services, And Questions Regarding Our Financial Viability, Which Claims And Perceptions, If Unresolved Or Not Addressed, Could Continue To Seriously Harm Our Business And Our Stock Price.

From time to time, customers make claims pertaining to the quality and performance of our software and services, citing a variety of issues. Our recent operating performance, our historic negative net cash position, the long-term decline in our stock price, and the existing and potential litigation and other proceedings against us have led to questions in the market regarding our financial viability. Whether customer claims regarding the quality and performance of our products and services or concerns about our financial viability are founded or unfounded, if such claims and perceptions are not resolved in a manner favorable to us, they may continue to

Table of Contents

Index to Financial Statements

adversely impact customer demand and affect the market perception of our company, our products and our services. Any such damage to our reputation could have a material adverse effect on our business, results of operations, cash flow and financial condition and could negatively affect the price of our stock.

We Face Risks Related To Ongoing Governmental Investigations And Litigation That Could Have A Material Adverse Effect On Our Relationships With Customers And Our Business, Results Of Operations, Cash Flow and Financial Condition And We May Face Additional Litigation In The Future That Could Also Harm Our Business.

In March 2003, the SEC issued a formal order of investigation to determine whether there had been violations of the federal securities laws by us and/or others involved with us in connection with matters relating to the 2003 restatement of our consolidated financial statements. The settlement of the SEC enforcement proceedings, announced on June 9, 2004 and described in *Note 7 Commitments and Contingencies* in our Notes to Condensed Consolidated Financial Statements, covers the company only. On July 15, 2005, the SEC filed a civil action against three former officers of the company: Gregory A. Brady, William M. Beecher and Reagan L. Lancaster. The complaint relates to events that occurred prior to the restatement of the company's financial statements in 2003. We continue to cooperate with the staff of the SEC and we are also cooperating with the U.S. Attorney's Office for the Northern District of Texas, which has also been investigating certain matters relating to our restatement.

We currently face a lawsuit recently brought against us by Kmart and a potential assessment by the Internal Revenue Service relating to the timing of the company's remittance of withholding taxes associated with the exercise of stock options by employees in the 2000 tax year. We may face additional litigation in the future that could harm our business and impair our liquidity.

We are generally obligated, to the extent permitted by law, to indemnify our current and former directors and officers who are named as defendants in some of these lawsuits. Defending against existing and potential litigation and other proceedings may continue to require significant attention and resources of our management. We cannot assure you that the significant time and effort spent will not adversely affect our business, results of operations, cash flow and financial condition.

The Loss Of Certain Of Our Key Personnel And Any Future Potential Losses Of Key Personnel Or Our Failure To Attract Additional Personnel Could Seriously Harm Our Company.

We rely upon the continued service of a relatively small number of key technical, sales and senior management personnel. We have lost a number of key personnel as a result of our performance and our restructurings, among other reasons, and we believe our voluntary attrition rate is generally higher than the software industry's average. Our workforce reductions have impacted employees directly responsible for sales, which may affect our ability to close revenue transactions with our customers and prospects, and consulting, which may affect customer satisfaction. Our future success depends on retaining our key employees and our ability to retain, attract and train other highly qualified technical, sales and managerial personnel, which may be increasingly difficult given our recent financial performance and employee layoffs.

Additional changes to our organizational structure may result in further voluntary and involuntary attrition and loss of key personnel. Our employees can typically resign with little or no prior notice. Our loss of any more of our key technical, sales and senior management personnel, and the intellectual capital that they possess, or our inability to retain, attract and train additional qualified personnel could have a material adverse effect on our business, results of operations, cash flow and financial condition.

Table of Contents

Index to Financial Statements

Restructuring and Reorganization Initiatives Have Been Executed, And Such Activities Pose Significant Risks To Our Business.

Restructuring initiatives were recently executed by us in an effort to achieve our profitability objectives. This restructuring involved, among other things, reducing our workforce and decreasing continued development of functionality for certain of our products. These activities pose significant risks to our business, including the risk that terminated employees will disparage the company, file legal claims against us related to their termination of employment, become employed by competitors or share our intellectual property or other sensitive information with others and that the reorganization will not achieve targeted efficiencies. The failure to retain and effectively manage our remaining employees or achieve our targeted efficiencies through the reorganization could increase our costs, adversely affect our development efforts and impact the quality of our products and customer service. If customers become dissatisfied with our products or service, our maintenance renewals may decrease, our customers may take legal action against us and our sales to existing customers could decline, leading to reduced revenues. Additionally, during 2005, we announced the reorganization of our sales and services operating structure from primarily geographic to primarily industry-focused field groups. Failure to achieve the desired results of our strategic initiatives would harm our business, results of operations, cash flow and financial condition.

Because Our Software Products Are Intended To Work Within Complex Business Processes, Implementation Or Upgrades Of Our Products Can Be Difficult, Time-Consuming And Expensive, And Customers May Be Unable To Implement Or Upgrade Our Products Successfully Or Otherwise Achieve The Benefits Attributable To Our Products. This May Result In Customer Dissatisfaction, Harm To Our Reputation And Cause Non-Payment Issues.

Our products typically must integrate with the many existing computer systems and software programs of our customers. This can be complex, time-consuming and expensive, and may cause delays in the deployment of our products. As a result, some customers may have difficulty implementing our products successfully or otherwise achieving the benefits attributable to our products. Delayed or ineffective implementation or upgrades of our software and services may limit our sales opportunities, result in customer dissatisfaction and harm to our reputation, or cause non-payment issues.

Failure To Complete Development Projects As Planned Could Harm Our Operating Results And Create Business Distractions And Negative Publicity That Could Harm Our Business.

Risks associated with our software solutions and other development projects include, but are not limited to:

Customers may withhold cash payments or cancel contracts if we fail to meet our delivery commitments, the customers have financial difficulties or change strategy, or the functionality delivered is not acceptable to the customers. We are particularly susceptible to this with respect to arrangements where payments are scheduled to occur later in the engagement.

The cancellation or scaling back of one or more of our larger software solutions and other development projects could have a material adverse impact on future software solution revenues.

We may be unable to recognize revenue associated with software solutions and other development projects in accordance with expectations. We generally recognize revenue from software solutions and other development projects over time using the contract method of accounting. Failure to complete project phases in accordance with the overall project plan can create variability in our

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expected revenue streams if we are not able to recognize revenues related to particular projects because of delays in development.

Many of our software solutions and other development projects are fixed-price arrangements. If we fail to accurately estimate the resources required for a fixed-price project or the customer attempts to change the scope of the project, the profit, if any, realized from the project would be adversely affected to the extent that we have to add additional resources to complete the project.

Table of Contents

Index to Financial Statements

If We Fail To Adequately Protect Our Intellectual Property Rights Or Face A Claim Of Intellectual Property Infringement By A Third Party, We Could Lose Our Intellectual Property Rights Or Be Liable For Significant Damages.

We rely primarily on a combination of copyright, trademark and trade secret laws, confidentiality procedures and contractual provisions to protect our proprietary rights. However, unauthorized parties may attempt to copy aspects of our products or to obtain and use information that we regard as proprietary. Policing unauthorized use of our products is difficult, and we cannot be certain that the steps we have taken will prevent misappropriation of our intellectual property. This is particularly true in India, where a significant portion of our Solutions Operations are located, and other foreign countries such as China and Russia where the laws do not protect proprietary rights to the same extent as the laws of the United States and may not provide us with an effective remedy against piracy. The misappropriation or duplication of our intellectual property could disrupt our ongoing business, distract our management and employees, reduce our revenues and increase our expenses. Any litigation to defend our intellectual property rights could be time-consuming and costly.

There has been a substantial amount of litigation in the software industry regarding intellectual property rights. As a result, we may be subject to claims of intellectual property infringement. Although we are not aware that any of our products infringe upon the proprietary rights of third parties, third parties may claim infringement by us with respect to current or future products. Any infringement claims, with or without merit, could be time-consuming, result in costly litigation or damages, cause product shipment delays or the loss or deferral of sales, or require us to enter into royalty or licensing agreements. If we enter into royalty or licensing agreements in settlement of any litigation or claims, these agreements may not be on terms favorable to us. Unfavorable royalty and licensing agreements could have a material adverse effect on our business, results of operations, cash flow and financial condition.

Certain Of Our Customers Purchase Our Software, But Delay Or Terminate Its Implementation. If This Type Of Activity Becomes Significant, It Could Harm Our Ability To Sell To Existing Customers And Impact Our Maintenance and Services Revenues.

Certain of our existing customers delay or terminate implementations of our software due to budgetary constraints related to economic uncertainty, dissatisfaction with product quality, the difficulty of prioritizing a surplus of information technology projects, changes in business strategy, personnel or priorities or for other reasons. Such customers may be less likely to invest in additional software in the future and to continue to pay for software maintenance. Since our business relies to a large extent upon sales to existing customers and since maintenance and services revenues are key elements of our revenue base, any reduction in these sales or these maintenance and services payments could have a material adverse effect on our business, results of operations, cash flow and financial condition.

Our Software May Contain Errors Which Could Result In The Loss Of Customers And Reputation, Adverse Publicity, Loss Of Revenues, Delays In Market Acceptance, Diversion of Development Resources And Claims Against Us By Customers.

Our software programs may contain errors. Although we conduct testing and quality assurance through a release management process, we may not discover errors until our customers install and use a given product or until the volume of services that a product provides increases. On occasion, we have experienced delays in the scheduled introduction of new and enhanced products because of errors. Errors could result in loss of customers and reputation, adverse publicity, loss of revenues, delays in market acceptance, diversion of development and consulting resources and claims against us by customers.

Table of Contents

Index to Financial Statements

Failure Or Circumvention Of Our Controls And Procedures Or Failure To Comply With Regulations Related To Controls And Procedures Could Seriously Harm Our Business.

Over time, we have made significant changes in and may consider making additional changes to our internal controls, our disclosure controls and procedures, and our corporate governance policies and procedures. Any system of controls, however well designed and operated, is based in part on certain assumptions and can provide only reasonable, and not absolute, assurances that the objectives of the system are met. Any failure of our controls, policies and procedures could have a material adverse effect on our business, results of operations, cash flow and financial condition.

We May Have Difficulty Obtaining And Maintaining Cost-Effective Insurance, Which May Have A Material Adverse Effect On Our Business, Results Of Operations, Cash Flow and Financial Condition.

We obtain insurance to cover a variety of potential risks and liabilities. In the future, it may become more difficult to maintain insurance coverage at reasonable levels, or if such coverage is available, the cost to obtain or maintain it may increase substantially. This may result in our being forced to bear the burden of an increased portion of risks for which we have traditionally been covered by insurance, which could have a material adverse effect on our business, results of operations, cash flow and financial condition.

We May Not Be Successful In Convincing Customers To Migrate To Current Or Future Releases Of Our Products, Which May Lead To Reduced Consulting And Maintenance Revenues And Less Future Business From Existing Customers.

Our customers may not be willing to incur the costs or invest the resources necessary to complete upgrades to current or future releases of our products. This may lead to our loss of consulting and maintenance revenues and future business from customers that continue to operate prior versions of our products or choose to no longer use our products.

If We Fail To Derive Benefits From Our Existing And Future Strategic Relationships, Our Business Will Suffer.

From time to time, we have collaborated with other companies in areas such as marketing, distribution or implementation. Maintaining these and other relationships is a meaningful part of our business strategy. However, some of our current and potential strategic partners are either actual or potential competitors, which may impair the viability of these relationships. In addition, some of our relationships have failed to meet expectations and may fail to meet expectations in the future. A failure by us to maintain existing strategic relationships or enter into successful new strategic relationships in the future could have a material adverse effect on our business, results of operations, cash flow and financial condition.

Serious Harm To Our Business Could Result If Our Encryption Technology Fails To Ensure The Security Of Our Customers Online Transactions.

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The secure exchange of confidential information over public networks is a significant concern of consumers engaging in on-line transactions and interaction. Some of our software applications use encryption technology to provide the security necessary to affect the secure exchange of valuable and confidential information. Advances in computer capabilities, new discoveries in the field of cryptography or other events or developments could result in a compromise or breach of the algorithms that these applications use to protect customer transaction data. If any compromise or breach were to occur, it could have a material adverse effect on our business, results of operation and financial condition.

Table of Contents

Index to Financial Statements

We Are Dependent On Third-Party Software That We Incorporate Into And Include With Our Products And Solutions And Impaired Relations With These Third Parties, Defects In Third-Party Software Or The Inability To Enhance Their Software Over Time Could Harm Our Business.

We incorporate and include third-party software into and with certain of our products and solutions. Additionally, we may incorporate and include additional third-party software into and with our products and solutions in future product offerings. The operation of our products could be impaired if errors occur in the third-party software that we utilize. It may be more difficult for us to correct any defects in third-party software because the development and maintenance of the software is not within our control. Accordingly, our business could be adversely affected in the event of any errors in this software. There can be no assurance that these third parties will continue to make their software available to us on acceptable terms, to invest the appropriate levels of resources in their products and services to maintain and enhance the software capabilities, or to remain in business.

Further, it may be difficult for us to replace any third-party software if a vendor seeks to terminate our license to the software or our ability to license the software to customers. Any impairment in our relationship with these third parties could have a material adverse effect on our business, results of operations, cash flow and financial condition.

We Face Risks Associated With International Sales And Operations That Could Harm Our Company.

International revenues accounted for approximately 47% of our total revenues during 2005, and we expect to continue to generate a significant portion of our revenues from international sales in the future. Our international operations are subject to risks inherent in international business activities, including the tendency of markets outside of the U.S. to be more volatile and difficult to forecast than the U.S. market. Any of the following factors, among other things, could adversely affect the success of our international operations:

Difficulties and costs of staffing and managing geographically disparate operations.

Extended accounts receivable collection cycles in certain countries.

Compliance with a variety of foreign business practices, laws and regulations.

Overlap of different tax structures and regimes.

Meeting import and export licensing requirements.

Trade restrictions.

Changes in tariff rates.

Changes in general economic and political conditions in international markets.

The Expansion Of Our Operations In India Poses Significant Risks That Could Impair Our Ability To Develop Our Products, Implement Our Products Or Put Our Products At A Competitive Disadvantage.

We have shifted a large portion of our software solutions and other development and services capacity to India. However, we may not fully achieve the cost savings and other benefits that we anticipate from this program and we may not be able to attract or retain sufficient numbers of developers and consultants with the necessary skill sets in India to meet our needs. The distributed nature of our development and consulting resources could create further operational challenges and complications. Additionally, we have a heightened risk exposure to changes in the economic, security and political conditions of India. Operational issues, recruiting and retention issues, ability to obtain work permits, economic and political instability, military actions and other unforeseen occurrences in India could impair our ability to develop and introduce new software applications and functionality in a timely manner, or hinder our ability to provide cost-competitive services, either of which could put our products at a competitive disadvantage and cause us to lose existing customers or fail to attract new customers.

Table of Contents

Index to Financial Statements

We May Not Successfully Integrate The Products, Technologies Or Businesses From, Or Realize The Intended Benefits Of, Acquisitions, And We May Make Future Acquisitions Or Enter Into Joint Ventures That Are Not Successful, Which Could Seriously Harm Our Business.

Historically, we have acquired technology or businesses to supplement and expand our product offerings. In the future, we could acquire additional products, technologies or businesses, or enter into joint venture arrangements for the purpose of complementing or expanding our business. Negotiation of potential acquisitions or joint ventures and our integration of acquired products, technologies or businesses could divert management's time and resources. Future acquisitions could cause us to issue equity securities that would dilute your ownership of us, incur debt or contingent liabilities, amortize intangible assets, or write off in-process research and development and other acquisition-related expenses that could have a material adverse affect on our business, results of operations, cash flow and financial condition. We may not be able to properly integrate acquired products, technologies or businesses with our existing products and operations, train, retain and motivate personnel from the acquired businesses, or combine potentially different corporate cultures. Failure to do so could deprive us of the intended benefits of those acquisitions. In addition, we may be required to write-off acquired research and development if further development of purchased technology becomes unfeasible, which may adversely affect our business, results of operations, cash flow and financial condition.

Changes In The Value Of The U.S. Dollar, As Compared To The Currencies Of Foreign Countries Where We Transact Business, Could Harm Our Operating Results.

To date, our international revenues have been denominated primarily in U.S. Dollars. However, the majority of our international expenses, including the wages of approximately 63% of our employees, have been denominated in currencies other than the U.S. Dollar. Therefore, changes in the value of the U.S. Dollar as compared to these other currencies may adversely affect our operating results. We have implemented limited hedging programs to mitigate our exposure to currency fluctuations affecting international accounts receivable, cash balances and intercompany accounts, but we do not hedge our exposure to currency fluctuations affecting future international revenues and expenses and other commitments. For the foregoing reasons, currency exchange rate fluctuations have caused, and likely will continue to cause, variability in our foreign currency denominated revenue streams and our cost to settle foreign currency denominated liabilities.

We May Become Subject To Product Liability Claims That Could Seriously Harm Our Business.

Our software products generally are used by our customers in mission-critical applications where component failures could cause significant damages. To mitigate this exposure, our license agreements typically seek to limit our exposure to product liability claims from our customers. However, these contract provisions may not preclude all potential claims. Additionally, our insurance policies may be inadequate to protect us from all liability that we may face. Product liability claims could require us to spend significant time and money in litigation or to pay significant damages. As a result, any claim, whether or not successful, could harm our reputation and have a material adverse effect on our business, results of operations, cash flow and financial condition.

We May Not Be Able to Fully Realize The Benefits Of Our Deferred Tax Assets.

If we do not achieve sufficient domestic federal taxable income in future years to utilize all or some of our net operating loss carryforwards, they will expire, and we will be unable to fully realize the benefits of our deferred tax assets.

Table of Contents

Index to Financial Statements

Risks Related To Our Industry

If Our Products Are Not Able To Deliver Fast, Demonstrable Value To Our Customers, Our Business Could Be Seriously Harmed.

Enterprises are requiring their application software vendors to provide faster time to value on their technology investments. We must continue to improve the speed of our implementations and the pace at which our products deliver value or our competitors may gain important strategic advantages over us. If we cannot successfully respond to these market demands, or if our competitors do so more effectively than we do, our business, results of operations, cash flow and financial condition could be materially and adversely affected.

Releases Of And Problems With New Products May Cause Purchasing Delays, Which Would Harm Our Revenues.

Our practice and the practice in the industry is to periodically develop and release new products and enhancements. As a result, customers may delay their purchasing decisions in anticipation of our new or enhanced products, or products of competitors. Delays in customer purchasing decisions could seriously harm our business and operating results. Moreover, significant delays in the general availability of new releases, significant problems in the installation or implementation of new releases, or customer dissatisfaction with new releases could have a material adverse effect on our business, results of operations, cash flow and financial condition.

Risks Related To Our Stock

Our Stock Price Historically Has Been Volatile, Which May Make It More Difficult To Resell Common Stock At Attractive Prices.

The market price of our common stock has been highly volatile in the past, and may continue to be volatile in the future. The following factors could significantly affect the market price of our common stock:

Negative cash flows.

Additional equity or debt financing transactions.

Continued quarterly variations in our results of operations.

The market or system on which our common stock trades.

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Announcement of new customers, new products, product enhancements, joint ventures and other alliances by our competitors or us.

Technological innovations by our competitors or us.

Stock valuations or performance of our competitors.

General market conditions, geopolitical events or market conditions specific to particular industries.

Perceptions in the marketplace of performance problems involving our products and services.

In particular, the stock prices of many companies in the technology and emerging growth sectors have fluctuated widely, often due to events unrelated to their operating performance. These fluctuations may harm the market price of our common stock.

If We Are Unsuccessful In Maintaining The Listing Of Our Common Stock On The NASDAQ National Market, Our Business Reputation May Be Harmed and Our Ability To Raise Funds In The Capital Markets Might Be Adversely Affected.

On July 21, 2005, our common stock was re-listed by The NASDAQ Listing Qualifications Panel and began trading on The NASDAQ National Market. In the future, our common stock price may decline to levels that

Table of Contents

Index to Financial Statements

would again cause us not to comply with NASDAQ listing standards. Any failure to maintain the listing of our common stock on The NASDAQ National Market might harm our general business reputation and be a consideration for investors when considering an investment in us, which could have a material adverse effect on our business, results of operations, cash flow and financial condition.

Our Executive Officers And Directors, In Particular Sanjiv Sidhu And An Affiliate Of Q Investments, Have Significant Influence Over Stockholder Votes.

As of March 1, 2006, our current executive officers and directors together beneficially owned approximately 31.2% of the total voting power of our company, approximately 26.6% of which was beneficially owned by Sanjiv Sidhu, our current Chairman and former Chief Executive Officer and President, and entities that he controls. Further, an affiliate of Q Investments beneficially owns approximately 22.9% of the voting power of the company, and has the right to appoint two directors to our Board of Directors. Accordingly, Mr. Sidhu, the Q Investments affiliate and our officers and directors holding or controlling holdings of stock in our company have had and will have significant influence in determining the composition of our Board of Directors and other significant matters requiring stockholder approval or acquiescence, including amendments to our certificate of incorporation, a substantial sale of assets, a merger or similar corporate transaction or a non-negotiated takeover attempt. Such concentration of ownership may discourage a potential acquirer from making an offer to buy our company that other stockholders might find favorable, which in turn could adversely affect the market price of our common stock.

Our Charter And Bylaws Have Anti-Takeover Provisions And We Have A Stockholder Rights Plan Which, In Combination, Effectively Inhibit A Non-Negotiated Merger Or Business Combination.

Provisions of our certificate of incorporation and our bylaws, Delaware law and our stockholder rights plan could make it more difficult for a third party to acquire us, even if doing so would be beneficial to our stockholders. We are subject to the provisions of Section 203 of the Delaware General Corporation Law, which restricts certain business combinations with interested stockholders. The combination of these provisions effectively inhibits a non-negotiated merger or other business combination.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

Our corporate headquarters is located in Dallas, Texas and is held under an operating lease contract that expires in 2010. This facility houses our executive and administrative staff as well as sales, marketing, research and development and consulting personnel. We also lease space for our other offices in the U.S., Australia, Belgium, Canada, China, Finland, France, Germany, India, Japan, Korea, Netherlands, Singapore, South Africa, Taiwan and the United Kingdom primarily to provide sales, customer support, consulting services and research and development activities. We consider our properties suitable and adequate for our present needs and do not anticipate leasing any significant additional properties at this time.

ITEM 3. LEGAL PROCEEDINGS

Governmental Investigations and Actions

Beginning in the fall of 2001, we and certain members of our Board of Directors received a series of communications from a former officer containing a variety of allegations generally related to revenue recognition and financial reporting, among other things. Our Board of Directors directed our Audit Committee to conduct an internal investigation of these allegations. In November 2002, we reported to the SEC and publicly disclosed the results of that investigation, as well as certain related allegations made during the fall of 2002 by the former

Table of Contents

Index to Financial Statements

officer and another former officer. Thereafter, the staff of the SEC opened an informal inquiry into these allegations and other matters relating to our financial reporting.

In January 2003, our ongoing investigation turned up information that persuaded management and the Audit Committee that material adjustments to our previously issued financial statements might be required and that our consolidated financial statements for the years ended December 31, 2001 and 2000 should be re-audited. The cumulative impact of the revenue adjustments required by the re-audit was to reduce revenue by \$359.7 million, which was comprised of \$127.3 million of revenue that was reversed and \$232.4 million of revenue that was deferred for possible recognition in the future. In March 2003, we were advised that the SEC had issued a formal order of investigation to determine whether there had been violations of the federal securities laws by the company and/or others involved with the company in connection with matters relating to the restatement of our consolidated financial statements.

On June 9, 2004, the company settled the SEC enforcement proceedings. Without admitting or denying the SEC's substantive findings against it, the company consented to a cease-and-desist order requiring future compliance with specific provisions of the federal securities laws and paid a \$10.0 million civil penalty.

The settlement of the SEC enforcement proceedings covers the company only. On July 15, 2005, the SEC filed a civil action against three former officers of the company: Gregory A. Brady, William M. Beecher and Reagan L. Lancaster. The complaint relates to events that occurred prior to the restatement of the company's financial statements in 2003. The SEC's investigation continues as to other individuals and entities. We continue to cooperate with the staff of the SEC and we are also cooperating with the U.S. Attorney's Office for the Northern District of Texas, which is also investigating certain matters relating to our restatement.

Customer Litigation

On September 30, 2004, we were served with a complaint in a suit filed in the District Court of Dallas County, Texas by Kmart Corporation against the company, Sanjiv Sidhu, our current Chairman and former Chief Executive Officer and President, and Gregory Brady, our former Chief Executive Officer and President. The complaint alleges fraudulent inducement, breach of contract, breach of fiduciary duty, rescission and unjust enrichment in relation to the license agreement, dated as of September 29, 2000, between our company and Kmart. Certain of the allegations in Kmart's complaint are purportedly similar to the subject of the cease-and-desist order entered into by the company in connection with the June 9, 2004 settlement of the SEC enforcement proceedings related to the company's 2003 restatement as well as the allegations made by the SEC in the subsequent civil action brought against three former officers of the company on July 15, 2005. The complaint states that Kmart paid in excess of \$40.0 million for software and technology and in excess of \$10.0 million for implementation services in connection with the license agreement. The prayer for relief requests rescission of the license agreement, actual and punitive damages, fees, costs and other disbursements. We are vigorously defending the company against this action.

Indemnification Agreements

We have entered into indemnification agreements with certain of our officers, directors and employees that may require us, among other things, to indemnify such officers, directors and employees against certain liabilities that may arise by reason of their status or service as directors, officers or employees and to advance their expenses incurred as a result of any proceeding against them as to which they could be indemnified. Pursuant to these agreements, we have advanced fees and expenses incurred by certain current and former directors, officers and employees in

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connection with the governmental investigations and actions related to the 2003 restatement of our consolidated financial statements and other matters and may continue to do so in the future.

We have also entered into agreements regarding the advancement of costs with certain officers and employees. Pursuant to these agreements, we have advanced fees and expenses incurred by such officers and employees in connection with the governmental investigations and actions related to the 2003 restatement of our consolidated financial statements and other matters and may continue to do so in the future.

Table of Contents

Index to Financial Statements

The maximum potential amount of future payments we could be required to make under these indemnification agreements and the agreements for the advancement of costs is unlimited. Additionally, our corporate by-laws allow us to choose to indemnify any employee for certain events or occurrences while the employee is, or was, serving at our request in such capacity. We incurred approximately \$4.9 million, \$4.5 million and \$1.4 million of expense for legal fees and expenses for current and former employees during 2005, 2004 and 2003, respectively.

Internal Revenue Service Audit

We currently are being examined by the Internal Revenue Service (IRS) regarding matters relating to the timing of the company's remittance of withholding taxes, which were previously remitted, associated with the exercise of certain stock options by employees in the 2000 tax year. The company has filed a protest regarding the IRS's position on the matter and the protest is being reviewed by the IRS. The IRS has not issued an assessment with respect to any monetary penalties claimed to be owed by the company and the company presently intends to seek a full statutory abatement of any such penalties which might be assessed. The amount of such assessment could be significant.

India Tax Assessments

On March 29, 2005, we were notified by the Office of the Addl. Commissioner of Income-Tax in India of tax and interest assessments of approximately \$2.4 million and \$0.9 million, respectively, related to transfer pricing adjustments between our affiliated companies for the Indian statutory fiscal year ended March 31, 2002. The Office of the Addl. Commissioner of Income-Tax has asserted that intercompany charges from our Indian subsidiaries to our U.S. and Dutch subsidiaries were understated during this period. The company was required to pay, and has paid, the assessed tax during the appeals process. The future assessment of a penalty, in addition to the tax and interest, in an amount up to \$2.4 million is possible, but not probable, and no amount has been accrued at December 31, 2005.

On February 15, 2006, we were notified of similar adjustments related to the Indian statutory fiscal year ended March 31, 2003. We have not received formal assessments related to these adjustments, but we estimate that additional tax and interest assessments of approximately \$0.7 million and \$0.3 million, respectively, may be forthcoming.

We believe the Indian tax authorities' position regarding our intercompany transactions to be without merit and that all intercompany transactions were conducted at appropriate pricing levels.

Japan Tax Examination

In January 2006, we closed the tax examination by the National Tax Agency in Japan regarding withholding taxes on intercompany payments made by our subsidiary in Japan. No assessment was made.

Certain Accruals

We have accrued for estimated losses in the accompanying consolidated financial statements for matters where we believe the likelihood of an adverse outcome is probable and the amount of the loss is reasonably estimable. We are subject to various claims and legal proceedings that arise in the ordinary course of our business from time to time, including claims and legal proceedings that have been asserted against us by former employees and certain customers, and have been in negotiations to settle certain of those contingencies. The adverse resolution of any one or more of those matters or the matters described in this Item 3 over and above the amount, if any, that has been estimated and accrued in our consolidated financial statements could have a material adverse effect on our business, financial condition, results of operations or cash flows.

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

None.

Table of Contents**Index to Financial Statements****PART II****ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES**

Our common stock trades on the NASDAQ National Market under the ticker symbol ITWO. During the period from May 9, 2003 to July 25, 2005, our common stock was quoted on the over-the-counter Pink Sheets under the ticker symbol ITWH.PK.

The following table lists the high and low per share intra-day sales prices for our common stock as reported by The NASDAQ National Market or as quoted in the over-the-counter Pink Sheets, as applicable, for the periods indicated. All references to common stock and per share amounts for periods prior to February 17, 2005 have been retroactively restated to reflect the 1-for-25 reverse stock split we implemented on February 16, 2005.

	<u>High</u>	<u>Low</u>
2005		
Fourth quarter	\$ 22.25	\$ 10.83
Third quarter	24.88	7.80
Second quarter	8.80	6.75
First quarter	17.50	7.77
2004		
Fourth quarter	\$ 18.75	\$ 15.00
Third quarter	23.00	15.00
Second quarter	33.75	19.50
First quarter	61.25	25.00

As of March 1, 2006, there were approximately 20,702,325 shares of our common stock outstanding held by approximately 396 holders of record.

Dividends

We have never declared or paid cash dividends on our common stock. We currently intend to retain any earnings for use in our business and do not anticipate paying any cash dividends in the foreseeable future. Future dividends, if any, will be determined by our Board of Directors.

Table of Contents**Index to Financial Statements***Stock Option Plans*

Information regarding stock-based compensation awards (including both stock options and stock rights awards) outstanding and available for future grants as of December 31, 2005, segregated between stock-based compensation plans approved by stockholders and stock-based compensation plans not approved by stockholders, is presented in the table below. Included in the table are stock options granted to former employees of acquired companies that were assumed by us. We do not intend to grant additional stock options under any of the assumed plans of acquired companies. See *Note 10 Employee Benefit Plans*, in our Notes to Consolidated Financial Statements. While our stockholders approved certain of our acquisitions of the companies from which these plans were assumed, our stockholders have not approved any of the assumed plans (in thousands, except per share amounts):

Plan Category	Number of Shares to be Issued Upon Exercise of Outstanding Awards	Weighted-Average Price of Outstanding Awards	Number of Shares Available for Future Grants
Plans approved by stockholders:			
1995 Plan	4,853	\$ 76.49	2,619
Plans not approved by stockholders:			
2001 Plan	383	89.84	411
Assumed plans of acquired companies	25	324.36	619
Total	5,261	\$ 78.66	3,649

Stock Rights Plan

On January 17, 2002, our Board of Directors approved adoption of a stockholder rights plan and declared a dividend of one preferred share purchase right for each outstanding share of common stock. Each share of common stock has attached to it (after adjusting for our recent 1-for-25 reverse stock split) one right to purchase 25 units of one one-thousandth of a share of Series A junior participating preferred stock at a price of \$75.00 per unit. The rights, which expire on January 17, 2012, will only become exercisable upon distribution. Distribution of the rights will not occur until ten days after the earlier of (i) the public announcement that a person or group has acquired beneficial ownership of 15.0% or more of our outstanding common stock or (ii) the commencement of, or announcement of an intention to make, a tender offer or exchange offer that would result in a person or group acquiring the beneficial ownership of 15.0% or more of our outstanding common stock.

Shares of Series A preferred stock purchasable upon exercise of the rights are not redeemable. Each share of Series A preferred stock will be entitled to a dividend of 40 times the dividend declared per share of common stock. In the event of liquidation, each share of Series A preferred stock will be entitled to a payment of the greater of (i) 40 times the payment made per share of common stock or (ii) \$1,000. Each share of Series A preferred stock will have 40 votes, voting together with the common stock. Finally, in the event of any merger, consolidation or other transaction in which shares of common stock are exchanged, each share of Series A preferred stock will be entitled to receive 40 times the

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amount received per share of common stock. Because of the nature of the dividend, liquidation and voting rights, the value of the 25 units of Series A preferred stock purchasable upon exercise of each right should approximate the value of one share of common stock.

If, after the rights become exercisable, we are acquired in a merger or other business combination transaction, or 50% or more of our consolidated assets or earning power are sold, proper provision will be made so that each holder of a right will thereafter have the right to receive upon exercise that number of shares of common stock of the acquiring company having market value of two times the exercise price of the right.

Table of Contents

Index to Financial Statements

If any person or group becomes the beneficial owner of 15.0% or more of the outstanding shares of common stock, proper provision will be made so that each holder of a right, other than rights beneficially owned by the acquiring person (which will thereafter be void), will have the right to receive upon exercise that number of shares of common stock or units of Series A preferred stock (or cash, other securities or property) having a market value of two times the exercise price of the right.

The rights have significant anti-takeover effects by causing substantial dilution to a person or group that attempts to acquire us on terms not approved by our Board of Directors. The rights should not interfere with any merger or other business combination approved by the Board of Directors since the rights may be redeemed by us at the redemption price of \$0.25 per right prior to the occurrence of a distribution date. Additional details of this stock rights plan are presented in *Note 9 Stockholders Equity (Deficit) and Income (Loss) per Common Share* in our Notes to Consolidated Financial Statements.

Convertible Debt

As of December 31, 2005, we had approximately \$103.75 million in face value of outstanding indebtedness that is convertible into shares of our common stock, including \$25.0 million of our 5.25% convertible notes that are due in December 2006. Details of this debt are presented in *Note 6 Borrowings and Debt Issuance Costs* in our Notes to Consolidated Financial Statements included elsewhere in this report. On November 28, 2005, we called \$235.0 million of our \$260.0 million of our 5.25% convertible subordinated notes due December 15, 2006. We settled this debt on December 28, 2005. In September and October of 2005, we retired \$50.0 million of our 5.25% convertible subordinated notes due on December 15, 2006.

Table of Contents**Index to Financial Statements****ITEM 6. SELECTED FINANCIAL DATA**

The following table presents selected consolidated financial data for the periods indicated. The selected consolidated financial data set forth below should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and related notes included elsewhere in this report. Amounts shown are in thousands, except per share data. The revenue amounts have been reclassified from previously reported amounts. See *Note 2 Reclassification of Certain Revenue and Expense*.

	Years Ended December 31,				
	2005	2004	2003	2002	2001
Consolidated Statement of Operations:					
Revenues:					
Software solutions	\$ 89,937	\$ 54,155	\$ 61,115	\$ 68,034	\$ 166,032
Services	103,792	118,731	141,953	146,770	222,820
Maintenance	100,612	116,765	136,097	144,718	151,943
Contract	42,526	72,877	126,488	514,602	300,916
Total revenues	336,867	362,528	465,653	874,124	841,711
Costs and expenses:					
Cost of revenues:					
Software solutions	14,720	20,137	23,939	9,890	26,379
Services and maintenance	103,758	121,504	150,560	129,857	244,905
Contract	1,575	4,718	11,844	147,522	75,202
Amortization of acquired technology		369	579	15,156	43,861
Sales and marketing	51,727	74,946	87,928	194,964	401,251
Research and development	37,337	56,279	66,236	157,226	268,934
General and administrative	61,117	71,646	105,713	65,446	108,511
Amortization of intangibles		39	540	11,222	63,060
Write-off of in-process research and development					12,700
Impairment of intangibles and goodwill				37,662	7,385,734
Restructuring charges and adjustments	11,269	2,688	4,797	111,524	111,235
Total costs and expenses	281,503	352,326	452,136	880,469	8,741,772
Operating income (loss)	55,364	10,202	13,517	(6,345)	(7,900,061)
Non-operating expense, net:					
Interest income	7,697	4,179	4,942	13,926	35,948
Interest expense	(16,315)	(17,873)	(20,641)	(23,839)	(21,997)
Realized gains (losses) on investments, net	10,144	79	370	1,895	(68,640)
Foreign currency hedge and transaction losses, net	(4,217)	(3,212)	(424)	(2,203)	(2,817)
Gain on early repayment of debt obligation	(3,017)	2,223	3,435		
Other expense, net	(1,547)	(1,069)	(2,200)	(1,783)	(2,279)
Total non-operating expense, net	(7,255)	(15,673)	(14,518)	(12,004)	(59,785)
Income (loss) before income taxes	48,109	(5,471)	(1,001)	(18,349)	(7,959,846)
Provision (benefit) for income taxes	4,664	(674)	5,462	889,296	(237,433)
Income (loss) from continuing operations	\$ 43,445	\$ (4,797)	\$ (6,463)	\$ (907,645)	\$ (7,722,413)

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Income from discontinued operations, net of taxes	\$ 43,884	\$ 3,445	\$ 6,978	\$ 8,713	\$ 3,551
Net income (loss)	\$ 87,329	\$ (1,352)	\$ 515	\$ (898,923)	\$ (7,718,862)
Preferred stock dividend and accretion of discount	\$ 3,020	\$ 1,720	\$	\$	\$
Net income (loss) applicable to common shareholders	\$ 84,309	\$ (3,072)	\$ 515	\$ (898,932)	\$ (7,718,862)
Net income (loss) per common share applicable to common shareholders:					
Total					
Basic	\$ 3.50	\$ (0.17)	\$ 0.03	\$ (52.42)	\$ (465.16)
Diluted	\$ 3.45	\$ (0.17)	\$ 0.03	\$ (52.42)	\$ (465.16)
Discontinued operations					
Basic	\$ 1.82	\$ 0.19	\$ 0.40	\$ 0.50	\$ 0.21
Diluted	\$ 1.80	\$ 0.19	\$ 0.40	\$ 0.50	\$ 0.21
Continuing operations including preferred stock dividend and accretion of discount					
Basic	\$ 1.68	\$ (0.36)	\$ (0.37)	\$ (52.92)	\$ (465.37)
Diluted	\$ 1.65	\$ (0.36)	\$ (0.37)	\$ (52.92)	\$ (465.37)
Weighted-average common shares outstanding:					
Basic	24,084	18,004	17,331	17,150	16,594
Diluted	24,469	18,004	17,331	17,150	16,594
Balance Sheet Data:					
Cash, cash equivalents, restricted cash, short-term and long-term investments	\$ 117,655	\$ 285,522	\$ 309,354	\$ 457,245	\$ 753,747
Working capital (deficit)	\$ (34,336)	\$ 101,152	\$ 10,130	\$ (68,192)	\$ 145,144
Total assets	\$ 202,445	\$ 390,673	\$ 430,374	\$ 633,223	\$ 2,026,370
Total long-term debt	\$ 75,691	\$ 316,800	\$ 356,800	\$ 350,000	\$ 410,930
Total stockholder s equity (deficit)	\$ (70,654)	\$ (173,033)	\$ (296,938)	\$ (302,025)	\$ 581,843

Table of Contents**Index to Financial Statements**

The following tables set forth unaudited consolidated quarterly statements of operations data for the years ended December 31, 2005 and 2004. Amounts shown are in thousands, except per share data. For details of significant events and transactions in the quarter ended December 31, 2005, see *Note 6 Borrowings and Debt Issuance Costs* and *Note 15 Discontinued Operations*, in the Notes to Consolidated Financial Statements.

	Three Month Period Ended			
	March 31, 2005	June 30, 2005	September 30, 2005	December 31, 2005
	(unaudited)	(unaudited)	(unaudited)	(unaudited)
Revenues:				
Software solutions	\$ 25,409	\$ 23,489	\$ 18,048	\$ 22,991
Services	27,627	27,534	23,272	25,359
Maintenance	25,818	25,496	24,268	25,030
Contract	3,057	15,343	899	23,227
Total revenues	81,911	91,862	66,487	96,607
Costs and expenses:				
Cost of revenues:				
Software solutions	4,927	3,459	3,013	3,321
Services and maintenance	28,685	26,656	24,445	23,972
Contract		1,575		
Sales and marketing	18,368	15,155	8,035	10,169
Research and development	11,800	9,085	8,281	8,171
General and administrative	25,643	11,592	12,138	11,744
Restructuring charges and adjustments	11,848	(235)	(256)	(88)
Total costs and expenses	101,271	67,287	55,656	57,289
Operating income (loss)	(19,360)	24,575	10,831	39,318
Non-operating income (expense), net	(4,760)	5,979	(2,964)	(5,510)
Income before income taxes	(24,120)	30,554	7,867	33,808
Income tax expense (benefit)	1,582	1,825	2,436	(1,179)
Income (loss) from continuing operations	(25,702)	28,729	5,431	34,987
Income from discontinued operations, net of taxes	1,210	3,496	3,960	35,218
Net income (loss)	(24,492)	32,225	9,391	70,205
Preferred stock dividend and accretion of discount	743	749	764	764
Net income (loss) applicable to common shareholders	(25,235)	31,476	8,627	69,441
Net income (loss) per common share applicable to common shareholders:				
Total				
Basic	\$ (1.09)	\$ 1.36	\$ 0.34	\$ 2.76

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Diluted	\$ (1.09)	\$ 1.33	\$ 0.33	\$ 2.69
Discontinued operations				
Basic	\$ 0.05	\$ 0.15	\$ 0.16	\$ 1.40
Diluted	\$ 0.05	\$ 0.15	\$ 0.15	\$ 1.36
Continuing operations including preferred stock dividend and accretion of discount				
Basic	\$ (1.14)	\$ 1.21	\$ 0.18	\$ 1.36
Diluted	\$ (1.14)	\$ 1.18	\$ 0.18	\$ 1.33
Weighted-average common shares outstanding:				
Basic	23,105	23,160	25,063	25,119
Diluted	23,105	23,638	25,958	25,824

Table of Contents**Index to Financial Statements**

	Three Month Period Ended			
	March 31, 2004	June 30, 2004	September 30, 2004	December 31, 2004
	(unaudited)	(unaudited)	(unaudited)	(unaudited)
Revenues:				
Software solutions	\$ 10,111	\$ 12,429	\$ 15,540	\$ 16,075
Services	29,676	30,077	31,728	27,250
Maintenance	31,005	29,798	27,742	28,220
Contract	5,970	31,970	29,130	5,807
Total revenues	76,762	104,274	104,140	77,352
Costs and expenses:				
Cost of revenues:				
Software solutions	7,324	1,672	5,250	5,891
Services and maintenance	33,251	31,766	29,288	27,199
Contract	106	1,025	2,079	1,508
Amortization of acquired technology	145	134	90	
Sales and marketing	19,281	20,544	18,139	16,982
Research and development	16,149	15,255	13,130	11,745
General and administrative	25,461	12,753	17,253	16,179
Amortization of intangibles	39			
Restructuring charges and adjustments	576	3,670	(670)	(888)
Total costs and expenses	102,332	86,819	84,559	78,616
Operating income (loss)	(25,570)	17,455	19,581	(1,264)
Non-operating expense, net	(5,087)	(4,374)	(1,775)	(4,437)
Income before income taxes	(30,657)	13,081	17,806	(5,701)
Income tax expense (benefit)	809	1,296	1,176	(3,955)
Income (loss) from continuing operations	(31,466)	11,785	16,630	(1,746)
Income from discontinued operations, net of taxes	1,490	371	1,236	348
Net income (loss)	(29,976)	12,156	17,866	(1,398)
Preferred stock dividend and accretion of discount		247	742	731
Net income (loss) applicable to common shareholders	(29,976)	11,909	17,124	(2,129)
Net income (loss) per common share applicable to common shareholders:				
Total				
Basic	\$ (1.72)	\$ 0.62	\$ 0.75	\$ (0.09)
Diluted	\$ (1.72)	\$ 0.61	\$ 0.75	\$ (0.09)
Discontinued operations				
Basic	\$ 0.09	\$ 0.02	\$ 0.05	\$ 0.02
Diluted	\$ 0.09	\$ 0.02	\$ 0.05	\$ 0.02

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Continuing operations including preferred stock dividend and accretion of discount

Basic	\$ (1.81)	\$ 0.60	\$ 0.70	\$ (0.11)
Diluted	\$ (1.81)	\$ 0.59	\$ 0.70	\$ (0.11)
Weighted-average common shares outstanding:				
Basic	17,378	19,223	22,686	22,980
Diluted	17,378	19,682	22,764	22,980

Table of Contents

Index to Financial Statements

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

Forward-Looking Statements

This report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. All statements other than statements of historical or current facts, including, without limitation, statements about our business strategy, plans, objectives and future prospects, are forward-looking statements. Such forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from these expectations, which could have a material adverse effect on our business and thereby cause our stock price to decline. Such risks and uncertainties include, without limitation, the following:

We have experienced substantial negative operating cash flows in recent years and we may not achieve a sustained return to positive cash flow. A failure to continue to control expenses, stabilize or grow revenues and achieve sustained positive cash flows will eventually impair our ability to support our operations and adversely affect our liquidity.

Our \$25.0 million of 5.25% convertible subordinated notes mature in December 2006. Although our current cash balances are sufficient to repay this debt, significant cash outflows in 2006 could impair our ability to do so.

Our 5% Senior Convertible Notes contain financial covenants that impact our ability to obtain certain types of new financing.

Our financial results have varied and may continue to vary significantly from quarter to quarter and we may fail to meet expectations, which could negatively impact the price of our stock. Our limited analyst coverage, which can result in wide variations in earnings estimates, can amplify this impact.

We may not benefit from increased demand in the market for information technology and an improving macroeconomic environment if we are unable to maintain or grow our market share, which would negatively impact our revenues and stock price.

We may not be competitive and increased competition could seriously harm our business. Our strategy to sell next-generation solutions may not be successful.

We have been and continue to be subject to claims pertaining to the quality of our products and services, and questions regarding our financial viability. These claims and perceptions, if unresolved or not addressed, could seriously harm our business and our stock price.

We face risks related to ongoing governmental investigations and litigation that could have a material adverse effect on our relationships with customers and our business, financial condition and results of operations. We may face additional litigation in the future that could also harm our business and impair our liquidity.

Further loss of key personnel, including customer-facing employees, may negatively affect our operating results and revenues and seriously harm our company.

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Restructuring initiatives have been executed recently, and such activities pose risks to our business.

Other risks indicated in Item 1A. Risk Factors and in our other filings with the SEC.

Many of these risks and uncertainties are beyond our control and, in many cases, we cannot accurately predict the risks and uncertainties that could cause our actual results to differ materially from those indicated by the forward-looking statements. When used in this document, the words believes, plans, expects, anticipates, intends, continue, may, will, should or the negative of such terms and similar expressions relate to us, our customers or our management are intended to identify forward-looking statements.

Table of Contents

Index to Financial Statements

Overview

We are a provider of enterprise supply chain management solutions, including various supply chain software and service offerings. We operate our business in one business segment. Supply chain management is the set of processes, technology and expertise involved in managing supply, demand and fulfillment throughout divisions within a company and with its customers, suppliers and partners. The goals of our solutions include increasing supply chain efficiency and enhancing customer and supplier relationships by improving agility, managing variability, reducing complexity, improving operational visibility, increasing operating velocity as well as integrating planning and execution. Our offerings help customers maximize efficiency in relation to sourcing, supply, demand, fulfillment and logistics performance. Our application software is often licensed in conjunction with other offerings we provide such as business optimization and technical consulting, training, solution maintenance, software upgrades and development.

Application of Critical Accounting Policies and Accounting Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and judgments related to the application of certain accounting policies.

While we base our estimates on historical experience, current information and other factors deemed relevant, actual results could differ from those estimates. We consider accounting estimates to be critical to our reported financial results if (i) the accounting estimate requires us to make assumptions about matters that are uncertain and (ii) different estimates that we reasonably could have used for the accounting estimate in the current period, or changes in the accounting estimate that are reasonably likely to occur from period to period, would have a material impact on our financial statements.

We consider our policies for revenue recognition to be critical due to the continuously evolving standards and industry practice related to revenue recognition, changes to which could materially impact the way we report revenues. Accounting policies related to: allowance for doubtful accounts, deferred taxes, goodwill and intangible assets, loss contingencies, and restructuring charges are also considered to be critical as these policies involve considerable subjective judgment and estimation by management. Critical accounting policies, and our procedures related to these policies, are described in detail below. Also, see *Note 1 Summary of Significant Accounting Policies* and *Note 2 Reclassification of Certain Revenue and Expense* in our Notes to Consolidated Financial Statements.

Revenue Recognition. We derive revenues from licenses of our software and related services, which include assistance in implementation, integration, customization, maintenance, training and consulting. We recognize revenue for software and related services in accordance with *Statement of Position (SOP) 81-1, Accounting for Certain Construction Type and Certain Production Type Contracts*, *SOP 97-2, Software Revenue Recognition*, as modified by *SOP 98-9, Modification of SOP 97-2, Software Revenue Recognition with Respect to Certain Transactions*, and *SEC Staff Accounting Bulletin (SAB) 101, Revenue Recognition*, and *SAB 103, Update of Codification of Staff Accounting Bulletins*.

Software Solutions Revenue. Recognition of software solutions revenue occurs under SOP 81-1 and under SOP 97-2, as amended.

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Software solutions revenue recognized under SOP 81-1 includes both fees associated with licensing of our products, as well as, any fees received to deliver the licensed functionality (for example, the provision of essential services). Essential services involve customizing or enhancing the software so that the software performs in accordance with specific customer requirements. Arrangements accounted for under SOP 81-1 follow either the percentage-of-completion method or the completed contract method. The percentage-of-completion method is used when the required services are quantifiable, based on the estimated number of labor

Table of Contents

Index to Financial Statements

hours necessary to complete the project, and under that method revenues are recognized using labor hours incurred as the measure of progress towards completion but is limited to revenue that has been earned by the attainment of any milestones included in the contract. We do not capitalize costs associated with services performed where milestones have not been attained. The completed contract method is used when the required services are not quantifiable, and under that method revenues are recognized only when we have satisfied all of our product and/or service delivery obligations to the customer. Similar to the treatment of milestones, we do not capitalize or defer costs associated with services performed on contracts recognized under the completed contract method that have not been completed.

30.1

Table of Contents

Index to Financial Statements

Under SOP 97-2, software license revenues are generally recognized upon delivery, provided persuasive evidence of an arrangement exists, fees are fixed or determinable and collection is deemed probable. We evaluate each of these criteria as follows:

Evidence of an arrangement: We consider a non-cancelable agreement signed by the customer to be evidence of an arrangement.

Delivery: Delivery is considered to occur when media containing the licensed programs is provided to a common carrier or, in the case of electronic delivery, the customer is given access to the licensed programs. Our typical end user license agreement does not include customer acceptance provisions.

Fixed or determinable fee: We consider the fee to be fixed or determinable if the fee is not subject to refund or adjustment and the payment terms are within our normal established practices. If the fee is not fixed or determinable, we recognize the revenue as amounts become due and payable.

Collection is deemed probable: We conduct a credit review for significant transactions at the time of the arrangement to determine the credit-worthiness of the customer. Collection is deemed probable if we expect that the customer will pay amounts under the arrangement as payments become due. If we determine that collection is not probable, we defer the revenue and recognize the revenue upon receipt of cash. Based on our collections history in certain countries, we apply a cash-basis recognition requirement for software solutions agreements in those countries.

Revenue for software solution arrangements that include one or more additional elements (i.e., services and maintenance) to be delivered at a future date is generally recognized using the residual method as set forth in SOP 98-9. Under the residual method, the fair value of the undelivered element(s) is deferred, and the remaining portion of the arrangement fee is recognized as license revenue. If fair values have not been established for the undelivered element(s), all revenue associated with the arrangement is deferred until all element(s) have been delivered or the fair value of the undelivered elements has been determined. Fair value for an individual element within an arrangement may be established when that element, when contracted for separately, is priced in a consistent manner. Fair value for our maintenance and consulting services has been established based on our maintenance renewal rates and consulting billing rates, respectively. Arrangements that include a right to unspecified future products are accounted for as subscriptions and recognized ratably over the term of the arrangement. Software solution license fees from reseller arrangements are generally based on the sublicenses granted by the reseller and recognized when the license is sold to the end customer. Licenses to our content databases were recognized over the term of the content database license. Such amounts are reflected in discontinued operations.

Services Revenue. Services revenue is primarily derived from fees for implementation, integration, consulting and training services as well as fees received to customize or enhance a previously purchased licensed product that resulted from arrangements negotiated and executed subsequent to the license arrangement. Also included are reimbursable expense revenue representing travel expenses incurred by our consultants and billed to our customers for reimbursement pursuant to a signed agreement. Services revenue is generally recognized when services are performed. Contractual terms may include the following payment arrangements: fixed fee, full-time equivalent, milestone, and time and material. In order to recognize service revenue, the following criteria must be met:

Signed agreement The agreement must be signed by the customer.

Fixed Fee The signed agreement must specify the fees to be received for the services.

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Delivery has occurred Delivery is substantiated by time cards and where applicable, supplemented by an acceptance from the customer that milestones as agreed in the statement of work have been met.

Collectibility is probable We conduct a credit review for significant transactions at the time of the engagement to determine the credit-worthiness of the customer. We monitor collections over the term of each project, and if a customer becomes delinquent, the revenue may be deferred.

Table of Contents

Index to Financial Statements

Maintenance Revenue. Maintenance revenue consists of fees generated by providing software maintenance, upgrades and support to customers, such as telephone support and new releases of software and updated user documentation. A customer typically prepays maintenance and support fees for an initial period, and the related revenue is deferred and generally recognized over the term of such initial period. Maintenance is renewable by the customer on an annual basis thereafter. Rates for maintenance, including subsequent renewal rates, are typically established based upon a specified percentage of net license fees as set forth in the contract.

Contract Revenue. Contract revenue consists of fees generated from license, services and maintenance revenue attributable to those transactions for which we determined to change the accounting from revenue recognition under SOP 97-2 to contract accounting under SOP 81-1 in connection with the 2003 restatement of our consolidated financial statements for the years ended December 31, 2001 and 2000 and the first three quarters of 2002. As of December 31, 2005, \$7.6 million of revenue deferred as a result of the restatement remains on our balance sheet as deferred revenue.

Royalties and Affiliate Commissions. Royalties paid for third-party software products integrated with our technology are expensed when the products are shipped. Commissions payable to affiliates in connection with sales assistance are generally expensed when the commission becomes payable. Accrued royalties payable totalled \$2.1 million and \$2.9 million as of December 31, 2005 and 2004, respectively, while accrued affiliate commissions payable totalled \$0.4 million and \$0.8 million as of December 31, 2005 and 2004, respectively.

Concurrent Transactions. We occasionally enter into transactions which are concluded at or about the same time as other arrangements with the same customer. These concurrent transactions are accounted for under Accounting Principles Board (APB) Opinion No. 29, *Accounting for Non-monetary Transactions*, as interpreted by EITF 01-02 *Interpretations of APB Opinion No. 29*. Generally, the recognition of a gain or loss on the exchange is measured based on the fair value of the assets involved to the extent that the fair value can be reasonably determined. A transaction that is not a culmination of the earnings process is based on the net book value of the asset relinquished.

Warranty. We generally warrant that our products will function substantially in accordance with documentation provided to customers. We accrue for warranty claims on a case-by-case basis; however, due to the unique nature of each claim and lack of a settlement history, estimating the necessary accrual involves an element of uncertainty.

Allowance for Doubtful Accounts. The allowance for doubtful accounts is a reserve established through a provision for bad debts charged to expense and represents our best estimate of probable losses resulting from non-payment of amounts recorded in the existing accounts receivable portfolio. In estimating the allowance for doubtful accounts, we consider our historical write-off experience, accounts receivable aging reports, the credit-worthiness of individual customers, economic conditions affecting specific customer industries and general economic conditions, among other factors. Should any of these factors change, our estimate of probable losses due to bad debts could also change, which could affect the level of our future provisions for bad debts.

Table of Contents

Index to Financial Statements

Deferred Taxes. Deferred tax assets and liabilities represent estimated future tax amounts attributable to the differences between the carrying amounts of assets and liabilities in the consolidated financial statements and their respective tax bases. These estimates are computed using the tax rates in effect for the applicable period. Realization of our deferred tax assets is, for the most part, dependent upon our U.S. consolidated tax group of companies having sufficient federal taxable income in future years to utilize our domestic net operating loss carry-forwards before they expire. We adjust our deferred tax valuation allowance on a quarterly basis in light of certain factors, including our financial performance.

Goodwill. On January 1, 2002, in accordance with Statement of Financial Accounting Standard (SFAS) No. 142 Goodwill and Intangible Assets, we ceased amortizing goodwill and adopted a new policy for measuring goodwill for impairment. No goodwill impairment was recorded in conjunction with the adoption of the new accounting standard. Under our policy, we test for impairment once annually or more frequently if an event occurs or circumstances change that may indicate that the fair value of our reporting unit is below its carrying value. Goodwill is tested for impairment using a two-step approach. The first step is to compare the fair value of the reporting unit to its carrying amount, including goodwill. If the fair value of the reporting unit is greater than its carrying amount, goodwill is not considered impaired and the second step is not required. If the fair value of the reporting unit is less than its carrying amount, the second step of the impairment test measures the amount of the impairment loss, if any. The second step of the impairment test is to compare the implied fair value of goodwill to its carrying amount. If the carrying amount of goodwill exceeds its implied fair value, an impairment loss is recognized equal to that excess. The implied fair value of goodwill is calculated in the same manner that goodwill is calculated in a business combination, whereby the fair value of the reporting unit is allocated to all of the assets and liabilities of that unit (including any unrecognized intangible assets) as if the reporting unit had been acquired in a business combination and the fair value of the reporting unit was the purchase price. The excess purchase price over the amounts assigned to assets and liabilities would be the implied fair value of goodwill.

As stated above, we currently operate as a single reporting unit and all of our goodwill is associated with the entire company. Accordingly, we generally assume that the minimum fair value of our single reporting unit is our market capitalization, which is the product of (i) the number of shares of common stock issued and outstanding and (ii) the market price of our common stock.

Loss Contingencies. There are times when non-recurring events occur that require management to consider whether an accrual for a loss contingency is appropriate. Accruals for loss contingencies typically relate to certain legal proceedings, customer and other claims and litigation. As required by SFAS No. 5, we determine whether an accrual for a loss contingency is appropriate by assessing whether a loss is deemed probable and can be reasonably estimated. We analyze our legal proceedings, warranty and other claims and litigation based on available information to assess potential liability. We develop our views on estimated losses in consultation with outside counsel handling our defense in these matters, which involves an analysis of potential results assuming a combination of litigation and settlement strategies. The adverse resolution of any one or more of these matters over and above the amounts that have been estimated and accrued in the current consolidated financial statements could have a material adverse effect on our business, results of operations and financial condition.

Restructuring Charges. We recognize restructuring charges consistent with applicable accounting standards. We reduce charges for obligations on leased properties with estimated sublease income. Furthermore, we analyze current market conditions, including current lease rates in the respective geographic regions, vacancy rates and costs associated with subleasing, when evaluating the reasonableness of future sublease income. The accrual for office closure and consolidation is an estimate that assumes certain facilities will be subleased or the underlying leases will otherwise be favorably terminated prior to the contracted lease expiration date. Significant subjective judgment and estimates must be made and used in calculating future sublease income. While the current accrual represents our best estimate of our expected costs to exit these obligations, variances between our expected and actual sublease income may result in significant restructuring charge adjustments in future periods.

Table of Contents**Index to Financial Statements**

Reclassification of Certain Revenue and Expense. During the fourth quarter of 2005, the company underwent an internal review of its revenue classifications. As a result of this review, the company has implemented an alternative classification of revenue previously reported as development services to more closely reflect the presentation of revenue by our peers and consistent with our sales model.

Fees associated with licensing of our products, as well as any fees received to deliver the licensed functionality (for example, the provision of essential services) are classified under software solutions revenue along with core license and recurring license revenue. Fees received to customize or enhance a previously purchased licensed product that result from arrangements negotiated and executed subsequent to the license arrangement are classified as services revenue. Similarly, the previously reported cost of development services are reclassified such that the cost is allocated to cost of software solutions and cost of services, as appropriate.

Our presentation of reimbursable expense revenue has also changed. Historically, we have stated the related revenue and expense amounts separately on our income statements. Beginning with the fourth quarter of 2005, we have adopted the industry practice of including reimbursable expense revenue in services revenue, and the related costs in cost of services.

The following charts illustrate the previous and current classifications of revenue and costs of revenue:

	December 31,		
	2005	2004	2003
Revenue			
Previous Classification			
Software licenses	\$ 46,176	\$ 33,392	\$ 39,084
Development services	50,325	30,672	26,782
Contract	42,526	72,877	126,488
Services	87,236	98,370	123,628
Reimbursable expense	9,992	10,451	13,574
Maintenance	100,612	116,766	136,097
Total Revenue	\$ 336,867	\$ 362,528	\$ 465,653
Current Classification			
Software solutions	\$ 89,937	\$ 54,155	\$ 61,115
Services	103,792	118,731	141,953
Maintenance	100,612	116,765	136,097
Contract	42,526	72,877	126,488
Total Revenue	\$ 336,867	\$ 362,528	\$ 465,653
Costs of Revenue			
Previous Classification			
Software licenses	\$ 5,694	\$ 7,645	\$ 3,702
Development services	13,369	18,041	23,261
Contract	1,575	4,718	11,844

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Amortization of acquired technology		369	579
Reimbursable expense	9,992	10,451	13,574
Services and maintenance	89,423	105,504	133,962
	<u> </u>	<u> </u>	<u> </u>
Total Costs of Revenue	\$ 120,053	\$ 146,728	\$ 186,922
	<u> </u>	<u> </u>	<u> </u>
Current Classification			
Software solutions	\$ 14,720	\$ 20,137	\$ 23,939
Services and maintenance	103,758	121,504	150,560
Contract	1,575	4,718	11,844
Amortization of acquired technology		369	579
	<u> </u>	<u> </u>	<u> </u>
Total Costs of Revenue	\$ 120,053	\$ 146,728	\$ 186,922
	<u> </u>	<u> </u>	<u> </u>

Table of Contents**Index to Financial Statements**

	For the Three Months Ended			
	March 31, 2005	June 30, 2005	September 30, 2005	December 31, 2005
Revenue				
Previous Classification				
Software Licenses	\$ 6,780	\$ 9,029	\$ 12,213	\$ 18,154
Development Services	20,064	16,828	7,193	6,240
Contract	3,057	15,343	899	23,227
Services	23,558	22,028	19,876	21,774
Reimbursable Expense	2,634	3,139	2,038	2,181
Maintenance	25,818	25,495	24,268	25,031
Total Revenue	\$ 81,911	\$ 91,862	\$ 66,487	\$ 96,607
Current Classification				
Software Solutions	\$ 25,409	\$ 23,489	\$ 18,048	\$ 22,991
Services	27,627	27,534	23,272	25,359
Maintenance	25,818	25,496	24,268	25,030
Contract	3,057	15,343	899	23,227
Total Revenue	\$ 81,911	\$ 91,862	\$ 66,487	\$ 96,607
Costs of Revenue				
Previous Classification				
Software Licenses	\$ 1,790	\$ 1,543	\$ 843	\$ 1,518
Development Services	4,601	3,318	3,002	2,448
Contract		1,575		
Reimbursable Expense	2,634	3,139	2,038	2,181
Services and Maintenance	24,587	22,115	21,575	21,146
Total Costs of Revenue	\$ 33,612	\$ 31,690	\$ 27,458	\$ 27,293
Current Classification				
Software solutions	\$ 4,927	\$ 3,459	\$ 3,013	\$ 3,321
Services and Maintenance	28,685	26,656	24,445	23,972
Contract		1,575		
Total Costs of Revenue	\$ 33,612	\$ 31,690	\$ 27,458	\$ 27,293

Table of Contents**Index to Financial Statements**

	For the Three Months Ended			
	March 31, 2004	June 30, 2004	September 30, 2004	December 31, 2004
Revenue				
Previous Classification				
Software Licenses	\$ 5,966	\$ 6,071	\$ 10,924	\$ 10,431
Development Services	6,617	9,191	7,510	7,354
Contract	5,970	31,970	29,130	5,807
Services	24,520	24,181	26,376	23,293
Reimbursable expense	2,685	3,063	2,459	2,244
Maintenance	31,004	29,798	27,741	28,223
Total Revenue	\$ 76,762	\$ 104,274	\$ 104,140	\$ 77,352
Current Classification				
Software solutions	\$ 10,111	\$ 12,429	\$ 15,540	\$ 16,075
Services	29,676	30,077	31,728	27,250
Maintenance	31,005	29,798	27,742	28,220
Contract	5,970	31,970	29,130	5,807
Total Revenue	\$ 76,762	\$ 104,274	\$ 104,140	\$ 77,352
Costs of Revenue				
Previous Classification				
Software Licenses	\$ 2,317	\$ (642)	\$ 3,007	\$ 2,963
Development Services	6,606	4,045	3,352	4,038
Contract	106	1,025	2,079	1,508
Amortization of acquired technology	145	134	90	
Reimbursable expense	2,685	3,063	2,459	2,244
Services and Maintenance	28,967	26,972	25,720	23,845
Total Costs of Revenue	\$ 40,826	\$ 34,597	\$ 36,707	\$ 34,598
Current Classification				
Software solutions	\$ 7,324	\$ 1,672	\$ 5,250	\$ 5,891
Services and maintenance	33,251	31,766	29,288	27,199
Contract	106	1,025	2,079	1,508
Amortization of acquired technology	145	134	90	
Total Costs of Revenue	\$ 40,826	\$ 34,597	\$ 36,707	\$ 34,598

Discontinued Operations. On July 1, 2005, we completed the sale of Trade Service Corporation (TSC), which was operated as a part of our content and data services business, for approximately \$3.0 million. This transaction led to a gain on sale, net of write-offs of associated assets and liabilities, of approximately \$2.2 million. The sale was to a group of investors led by TSC's then-current management team.

On December 1, 2005 and December 16, 2005, respectively, i2 and i2 Technologies Software Private Limited, an India corporation and a subsidiary of i2, sold to IHS Parts Management, Inc. (IHS) certain assets associated with our subsidiary's content and data services business

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(CDS). In addition, we agreed to license to IHS certain software and patents associated with CDS. In consideration of the transaction, IHS agreed to pay us approximately \$30 million in cash and assume certain liabilities associated with CDS.

As part of the transaction, IHS agreed to sublease certain office space located in India from our subsidiary. In addition, we agreed to perform certain transition and hosting services for IHS to assist in the transition of CDS to IHS.

Table of Contents**Index to Financial Statements**

Due to the two sales transactions, the historical operating results of TSC and CDS, including the gain on the sale of TSC, have been reported as discontinued operations in our financial statements. Income from discontinued operations was \$43.9 million in 2005, \$3.4 million in 2004 and \$7.0 million in 2003. See *Note 15 Discontinued Operations in our Notes to Consolidated Financial Statements*. The analysis presented below excludes all revenues and expenses from discontinued operations.

Revenues

The following table sets forth revenues and the percentages of total revenues of selected items reflected in our Consolidated Statements of Operations. The year-to-year comparisons of financial results are not necessarily indicative of future results.

Total revenues decreased \$25.7 million, or 7%, in 2005 and \$103.1 million, or 22%, in 2004. Details of our revenues are presented below:

	<u>2005</u>	<u>Percent of Revenue</u>	<u>2004</u>	<u>Percent of Revenue</u>	<u>2003</u>
SOP 97-2 recognition	\$ 25,736	8%	\$ 18,075	5%	\$ 27,295
SOP 81-1 recognition and other recurring revenue	64,201	19%	36,080	10%	33,820
Total software solutions	89,937	27%	54,155	15%	61,115
Services	103,792	31%	118,731	33%	141,953
Maintenance	100,612	30%	116,765	32%	136,097
Contract	42,526	12%	72,877	20%	126,488
Total revenues	\$ 336,867	100%	\$ 362,528	100%	\$ 465,653

Software Solutions. Software solutions revenue includes core license revenue, recurring license revenue, and fees received to develop the licensed functionality. Software solutions revenue increased \$35.8 million, or 66%, in 2005 and decreased \$7.0 million, or 11%, in 2004.

Software solutions revenue recognized under SOP 97-2 increased \$7.7 million, or 42%, in 2005 and decreased \$9.2 million, or 34%, in 2004. We have experienced variability in the timing of recognition of revenue from software solutions under SOP 97-2 and expect this variability to continue. This variability is caused by the timing of contract execution, sales execution, delivery of localized versions of software solutions, and cash receipts for arrangements where significant uncertainty exists regarding collectibility of license fees. In addition, as we continue licensing our new products and determine that they can be implemented without essential services, those solution licenses are eligible for recognition under SOP 97-2 subject to consideration of the specific terms of each arrangement.

Software solutions revenue recognized under SOP 81-1 and other recurring revenue increased \$28.1 million, or 78%, in 2005 and \$2.3 million, or 7%, in 2004. We have also experienced variability in the timing of recognition of revenue from software solutions under SOP 81-1 and other recurring revenue and expect this variability to continue. This variability is caused by the timing of development and delivery of licensed functionality, achievement of contractual milestones, cash receipts for arrangements where significant uncertainty exists regarding collectibility

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of fees, and the timing of signing new and renewal recurring revenue agreements. Another source of variability for software solutions revenue is our focus on selling new products, because there is a high likelihood of providing essential services associated with the new products. License fees received for these arrangements, together with fees for the essential services, are recognized under SOP 81-1 over the period in which the services are performed instead of being recognized upon delivery of the software. In 2005, we achieved numerous contractual milestones, some of which pertained to agreements signed in prior periods, which resulted in the recognition of revenue under SOP 81-1.

Table of Contents**Index to Financial Statements**

Services. Services revenue is primarily derived from fees for implementation, integration, consulting and training services and is generally recognized when services are performed. In addition, service revenue includes fees received from arrangements to customize or enhance previously purchased licensed software. Services revenue also includes reimbursable expense revenue, with the related costs of reimbursable expenses included in cost of services. Services revenue decreased \$14.9 million, or 13%, in 2005 and \$23.2 million, or 16%, in 2004. The decreases in services revenue primarily related to the lower volume of license sales, which led to fewer implementations. Our volume of upgrade projects has also declined as many of our customers have already migrated to the newest version of our products.

Maintenance. Maintenance revenue decreased \$16.2 million, or 14%, in 2005 and \$19.3 million, or 14%, in 2004. The decrease in maintenance revenue during 2005 and 2004 resulted from a continuing decline in both the number and dollar amount of maintenance renewals, mainly due to cost cutting efforts by our customers, less favorable renewal terms and lower volumes and dollar amounts of software solutions bookings. In addition, we concluded four supply chain leader transactions in 2004, which were being recorded as subscription revenue. These transactions were executed with customers who were previously utilizing our software through perpetual license agreements with annual maintenance contracts. There can be no assurance that maintenance revenues will improve or even remain at current levels.

Contract. Contract revenue decreased \$30.4 million, or 42%, during 2005 and \$53.6 million, or 42%, during 2004. Contract revenue is not indicative of our current business performance, as it reflects the recognition of deferred revenues for which cash was collected in prior periods. The decrease in contract revenue during 2005 was a result of the lower amount of remaining deferred contract revenue, the decreased number of deferred transactions and the occurrence of fewer events that allow the recognition of this revenue. As of December 31, 2005, the deferred contract revenue balance was \$7.6 million, consisting of two transactions. In the future, we expect contract revenue to continue to fluctuate on a quarterly basis due to the timing of events allowing recognition of this remaining deferred revenue.

International Revenue. Our international revenues, included in the categories discussed above, primarily are generated from customers located in Europe, Asia and Canada. International revenue totalled \$158.2 million, or 47% of total revenue, in 2005; \$144.8 million, or 40% of total revenue, in 2004; and \$166.3 million, or 36% of total revenue, in 2003. During 2005, we saw an increase in international revenue due to increased sales in EMEA. The increase of international sales as a percentage of total sales is due to an overall increase in international sales of 9.3% and a decrease in U.S. sales of 18.0%. The decrease in the amount of international revenue during 2004 was the result of declining demand for our enterprise application software, uncertainties related to our financial condition following the 2003 restatement of our consolidated financial statements, reductions in customer-facing employees, sales execution issues and increased competition, among other factors.

Customer Concentration. No individual customer accounted for more than 10% of annual revenues in 2005, 2004 or 2003.

Costs of Revenues

The following table sets forth cost of revenues and the gross margins of selected items reflected in our Consolidated Statements of Operations. The year-to-year comparisons of financial results are not necessarily indicative of future results.

<u>2005</u>	<u>Gross Margin</u>	<u>2004</u>	<u>Gross Margin</u>	<u>2003</u>	<u>Gross Margin</u>
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Software solutions	\$ 14,720	84%	\$ 20,137	63%	\$ 23,939	61%
Services and maintenance	103,758	49%	121,504	48%	150,560	46%
Contract	1,575	96%	4,718	94%	11,844	91%
Amortization of acquired technology			369		579	
	<u> </u>		<u> </u>		<u> </u>	
Total cost of revenues	\$ 120,053		\$ 146,728		\$ 186,922	
	<u> </u>		<u> </u>		<u> </u>	

Table of Contents

Index to Financial Statements

Cost of Software Solutions. Cost of software solutions consists of:

Commissions paid to non-customer third parties in connection with joint marketing and other related agreements. Such commissions are generally expensed when they become payable.

Royalty fees associated with third-party software utilized with our technology. Such royalties are generally expensed when the products are shipped; however, royalties associated with fixed cost arrangements are generally expensed over the period of the arrangement.

Costs related to product user documentation.

Costs related to reproduction and delivery of software.

Provisions for estimated costs related to service customer claims. We accrue for customer claims on a case-by-case basis.

Salaries and other related costs of employees who provide essential services to customize or enhance the software for the customer.

Cost of software solutions decreased \$5.4 million, or 27%, in 2005 and \$3.8 million, or 16%, in 2004. These decreases are due to renegotiated prepaid third-party royalty agreements resulting in a lower expense run rate and a reversal in 2004 of \$3.2 million in costs related to customer claim accruals that were no longer necessary. Also included in cost of software solutions during 2004 was \$2.3 million of costs related to a large project that involved a customer dispute. The dispute was resolved and the related revenues that had been deferred in 2004 were recognized in 2005

Cost of Services and Maintenance. Cost of services and maintenance includes expenses related to implementation, training, and customization and enhancement of previously licensed software solutions, as well as providing telephone support, upgrades and updated user documentation. The total cost of services and maintenance decreased \$17.7 million, or 15%, in 2005 and \$29.1 million, or 19%, in 2004. Services and maintenance headcount decreased 25% in 2005 and 11% in 2004, which contributed to a significant decrease in compensation-related expenses incurred by the services and maintenance organization. In addition, our increased utilization of India-based personnel to provide services and maintenance support also caused a decrease in this expense.

Cost of Contract. Cost of contract decreased \$3.1 million, or 67%, in 2005 and decreased \$7.1 million, or 60%, in 2004. Because contract expenses are recorded when the corresponding revenue is recognized, we expect cost of contract to vary. As of December 31, 2005, we had \$0.3 million remaining in deferred contract costs.

Amortization of Acquired Technology. In connection with our acquisitions in 2001 and 2000, we acquired developed technology that we offer as a part of our solutions. In accordance with applicable accounting standards, the amortization of acquired technology is included as a part of our cost of revenues because it relates to software products that are marketed to potential customers. As of December 31, 2004, all of our acquired technology was fully amortized.

Table of Contents**Index to Financial Statements****Operating Expenses**

The following table sets forth our operating expenses and their relative percentage of total revenue for these operating expenses as reported in our Consolidated Statements of Operations. The year-to-year comparisons of financial results are not necessarily indicative of future results:

	<u>2005</u>	<u>Percent of Revenue</u>	<u>2004</u>	<u>Percent of Revenue</u>	<u>2003</u>	<u>Percent of Revenue</u>
Sales and marketing	\$ 51,727	15%	\$ 74,946	21%	\$ 87,928	19%
Research and development	37,337	11%	56,279	16%	66,236	14%
General and administrative	61,117	18%	71,646	20%	105,713	23%
Amortization of intangibles			39		540	
	<u> </u>		<u> </u>		<u> </u>	
Total operating expenses	\$ 150,181		\$ 202,910		\$ 260,417	
	<u> </u>		<u> </u>	 		